Competitor Report German Railway 2010/2011

Netzwerk Privatbahnen

mofair
mobil und fair

supported by

bundes | arbeits | gemeinschaft
BAGSPNV
schienen | personen | nah | verkehr

Editor

supported by

mofair e. V.

Dr. Engelbert Recker
Managing Director

Nimrodstr. 28
13469 Berlin
Germany

phone: +49 (0)30 30 60 46 83
internet: www.mofair.de
email: e.recker@mofair.de

Netzwerk Privatbahnen – Vereinigung Europäischer Eisenbahngüterverkehrsunternehmen e. V.

Alexander Kirfel
Director

Friedrichstraße 186
10117 Berlin
Germany

phone: +49 (0)30 53 14 91 47 10
internet: www.netzwerk-privatbahnen.de
email: office@netzwerk-privatbahnen.de

Bundesarbeitsgemeinschaft der Aufgabenträger des SPNV e. V.

Susanne Henckel
Managing Director

Hardenbergplatz 2
10623 Berlin
Germany

phone: +49 (0)30 81 61 60 99-1
internet: www.bag-spnv.de
email: info@bag-spnv.de

This report was prepared by

KCW GmbH

Bernburger Straße 27
10963 Berlin
Germany

phone: +49 (0)30 40 81 768 -70
internet: www.kcw-online.de
email: info@kcw-online.de

Authors

Michael Holzhey (Red.), Felix Berschin, Ingo Kühl, René Naumann

Illustrations and layout

André Darmochwal, Marc-Oliver Wille

May 2011, 1. edition
ISBN 978-3-00-034680-4

V. i. S. d. P.: Dr. Engelbert Recker, mofair e. V., Alexander Kirfel, Netzwerk Privatbahnen e. V.


EWS

Summary

Rail competition is firmly on its way – and at the same time, with its flanks unprotected, it is in danger of being firmly stopped in its tracks. This sounds paradoxical. But it sums up the contradiction that rail competitors – seen relatively – are practically never out there. However, the further development of competition is overshadowed by significant uncertainty.

Since the Competitor Report 2008/2009 was published one can observe the following positive developments:

- For the first time in 2010 rail competitors were able to increase their market share of **rail freight transport** (in thousand kms) to past the 25 % mark. This is remarkable if one takes the economic crisis into account. One would normally have expected that, following their serious slump in volume, market leader DB Schenker Rail would have, also as a counter movement, gained more than the industry average.

  Against expectations, however, the number of competitors not only increased during the crisis but also thereafter (from 24.6 % in 2009 to 25.1 % in the following year). They are the drivers of growth in freight transport. The absolute increase of DB AG's transport services proves that competition doesn't cannibalise but rather can increase the performance of all participants on the market for the benefit of all.

  One should also emphasise that, in the meantime, competitors have been able to enter more market areas than two years ago, for example automotive, wood/cellulose or grain/feed grain.

- Competition dynamics can be evaluated a little less but it is still positive for **regional rail transport**. In 2010, rail competitors were able to expand their share of transport services (passenger km) to 12.5 %. In operating performance (train km) they are approaching a quarter of the market with 24.1 % in the current timetable year 2011.

  The decision of the **Federal Court of Justice** in February 2011 is particularly encouraging – regional rail transport contracts **must be awarded in a competition**. After eight years of uncertainty the law is now clear, which opens up new perspectives for passengers and tax payers alike. One continues to hope that the law will not loosen the reigns by allowing direct awards through the back door.

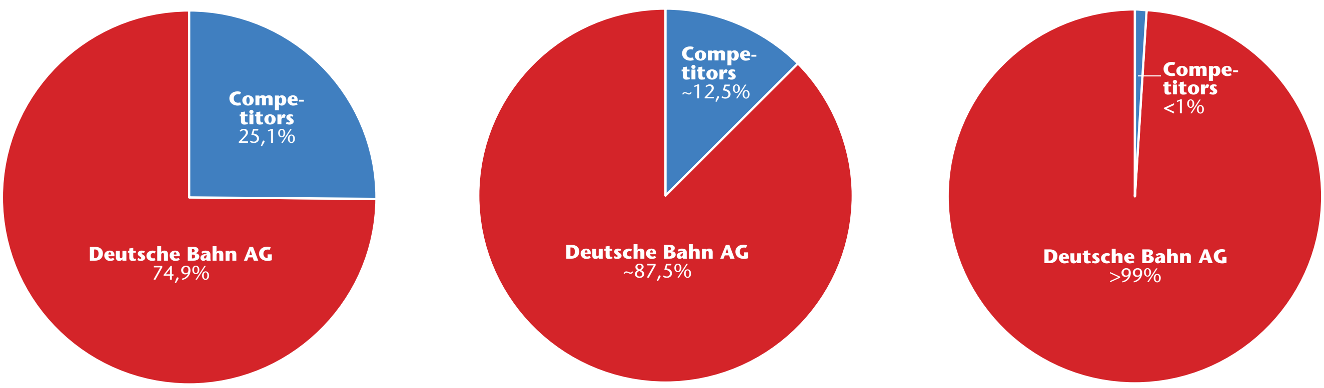
  Independent of the legal questions, transport authorities have backed competitions more than ever before. An award volume of 51 m train km in 2009 and the record value of 61 m train km in 2010 set a level that is to be expected in a «tuned-in competition«.

  One can state that a positive effect for **companies** is that new operators or shareholders liven up the scene. The Danish state rail DSB went on board with Vias, Arriva Deutschland went to the Italian FS Trenitalia following a short «parking position« at DB AG, private city rail (EGP) successfully managed to

Figure 1: Market shares of rail freight (left), regional rail passenger transport (center) and long-distance rail passenger transport (right) in Germany

in % of ton km (left) and in % of passenger km (center, right)

Source: own calculation



enter the market in Saxony and international heavyweight National Express is interested in the S-Bahn tender in Frankfurt/Main.

- Even **long-distance rail transport**, the tail-light of the three transport segments, is making a few positive headlines. From autumn 2011 onwards, DB long-distance transport will for the first time, have serious competition from a privately initiated line – the **Hamburg Cologne Express (HKX)**. Three train pairs per day, almost the same journey time and a high degree of travel comfort – this is supposed to catch the attention of passengers in the northwest.

  One awaits similar impulses following the **liberalisation of long-distance bus transport** which the Federal Government will announce in the second half of the year. The opening up of the market offers the opportunity to curb DB AG's high price policy which they have practiced for years in rail transport. Furthermore, the idea is that increasing pressure from competition will motivate the quasi monopolist DB Fernverkehr to consider creative alternatives.

  The argument that long-distance bus transport would kill off the long-distance rail branch, which is in less demand, is not convincing. DB AG themselves spurred on the reduction of long-distance transport services without any bus competition. In fact competition on the long-distance bus market awakens hopes to gain new customers in public transport, namely those who up until now prefer the car.

Despite these positive examples there is a long way to go to accomplish the transfer from monopoly to competition. Reality hits when one looks at the market shares in Fig. 1 on page 4. The fact that DB AG dominate with a margin of at least 75 % and in long-distance transport even have a market share of more than 99 % is a clear indicator that, even in its 18th year following the rail reform, rail transport is far from at a normal level. Significant branches of freight transport (single wagon transport, market areas such as ore, coal/coke, sand/soda) are as far away from competition as still 50 % of the total volume in regional rail transport is away from its first awards – not to mention long-distance rail transport, which is as good as free of all competition.

The Europe-wide trend towards **renationalisation** of rail companies brings particular economical concerns. Triggered by DB AG's push for expansion, which lastly lead to the purchase of British company Arriva, the large European state rail companies have entered a buying race, which absorbs more and more private medium-sized businesses.

From a competitive perspective this upgrading process could, at least in the short-term, be advantageous if it means that more European rail companies with strong financial backing meet at the same level. However, this requires the state rail companies to continue intensive competition via their foreign shareholdings. This will only succeed if they maintain their decentralised, sleek organisational structures which are moulded by medium-sized companies. Added value for the acquired companies would then stem from the additional financial strength from the parent company.

The long-term perspective of the takeover of private companies is nonetheless worrying because their market behaviour suggests critical expectations for future market parameters. The following **obstacles to competition**, which either already exist today or which threaten to in the future, show us that this is not without justification:

- In **rail freight transport** competitor rail companies are still at a significant disadvantage when it comes to obtaining **rail electricity**. The cause is too high delivery fees and the discount system, which is biased in being tailored to companies the size of DB Schenker Rail and therefore distorts competition. The Federal Government intends to regulate rail electricity by putting it under the shelter of a commission for misuse, which offers cause for hope.

  For smaller and medium-sized freight rail companies, which are of particular importance for market dynamics, the flood of **European standards** and above all their interpretation at national level present a business risk. Thus, for example, the **security management specification** has proven to be a bureaucratic monster. Due to lacking specifications from the Federal Railway Authority and a sluggish processing of applications, by the due date at the end of 2010 so few certificates had been issued that had they been strict, many rail companies would have had to shut down their services. This was only prevented by a mass issue of one-year certificates at the last minute.

Large rail companies belonging to the state also suffer under bureaucracy. However, what for them is only a nuisance from a financial standpoint can put smaller companies in jeopardy. It is incomprehensible why in Germany, according to market players, one has to pay up to 70.000 Euros for consultancy costs and fees while other EU states charge a mere 20 Euros for the official stamp.

- Very different dangers lie in wait for competitors in **regional rail transport**. Participants can expect a **wave of awards** with up to 100 m train km p. a. which challenges not only those who order regional rail services but in particular the companies as contractors.

The last two award intensive years have shown that even large players like Veolia Transdev, Netinera (FS Trenitalia, ex Arriva Deutschland), BeNEX or Keolis only took part in half the bids at most. Subsequently the average number of bidders per award dropped to 2.9 in 2009 and even 2.4 in 2010. In eleven large bids with a total volume of approximately 75 m train km only one competitor made a bid aside from DB Regio.

Since large, internationally active companies do not voluntarily forgo possible business there must be serious reasons to prevent them from bidding. Aside from the virulent financial crisis in 2009, the effects of which continue today, it is the lack of capacity to put bids together which is the limiting factor. This in turn comes from many years of experience where up until 2009 the volume of awards always remained below the long-term forecast values. Competitors now need to adjust and react to the doubling of train km per year to 60 m – more to be expected in future – and this takes time. Thus the reliability of forecast tender volumes becomes all the more important.

Over the next five years contractors must be prepared not only to aggressively woo the «rare species« bidders, in other words to maintain the market, but above all to be confronted with the **topic of vehicles**. Aside from the financial aspect there are signs of a shortage for competitors on three out of four vehicle markets. What is surprising is that **second-hand diesel vehicles** are becoming scarce. The cause is the increase in consecutive awards which are often bundled into larger bids so that the whole fleet needs to be replaced.

Whether or not regional rail transport can continue its success story with the expansion of services on offer depends mainly on how much the Federal Authority continues to permit DB AG to **skim off regional funds** via their rail infrastructure companies. These days the track system and passenger stations of DB AG skim approximately 450 m Euros more than in 2002 off the system – for the same if not qualitatively worse service in return. Translated into profit figures, in 2010 for regional rail transport, DB AG earned not only the transparent 729 m Euros (EBIT) for Regio, but a further rough 400 m Euros via their infrastructure sector. If their EBIT shoots up to 1.2 bn Euros (approx. 750 m Euros of that comes from regional rail transport) as forecast until 2015 then the devaluation of the purchasing power of regional funds will very soon lead to a reduction in services offered. This is a harbinger of current train cancellations in Saxony.

- On the **long-distance rail transport** market competition continues a shadowy existence and the entrance of KHX onto the market will not make much difference. If one is to assume that DB AG's high-speed transport continues to be closed to third parties, then one asks oneself what potential lies in the remaining network where DB AG have **radically thinned out** their long-distance transport services on offer over the last ten years in the name of profit maximisation.

Thus an analysis of the number of national railway stations between the timetable years 1999 and 2010 shows us **that services on offer in towns and places of interest to tourists outside**

the core network have declined by 48%. Thirteen regional centres (e.g. Krefeld, Heilbronn, Bremerhaven, Salzgitter, Gera) have completely lost their long-distance transport connection, the same applies to a further ten towns of between 40,000 and 100,000 residents. Even cities which in principle are well connected have had to take huge reductions of services on board, e.g. Magdeburg -62%, Regensburg -55%, Darmstadt -36%, Bonn (incl. Siegburg) -35% and Dresden -33%. Meanwhile whole regions such as the Eifel, Mosel, Black Forest, Lake Constance, Alps, northern Bavaria, Brandenburg and Mecklenburg-West-Pomerania have no long-distance transport or only have the odd «alibi» trains.

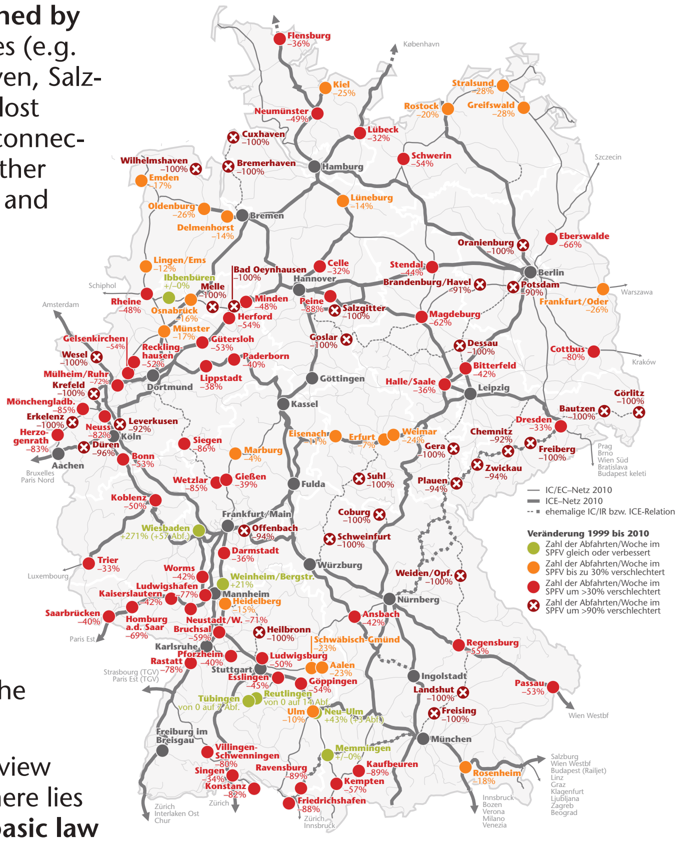


Figure 2: Development of long-distance connections from cities with more than 40,000 inhabitants 1999-2010

based on the number of departures per week

Sources: DB Netz; own observations

The Federal Authority must review how far the decline outlined here lies within the **definition under basic law of a service to the public** having to also provide long-distance transport services. As long as competition is blocked from entering the market by the barriers put up – above all the non-existent independence from the network operator, but also the structure of the **framework agreements** on the securing of tracks, it is hard to estimate the potential. If anything, a market test of transport services in competitions would end up with a large part of the cancelled long-distance transport services being operated with a small subsidy.

The overall picture clearly shows that politicians would be well advised to promote rail competition. In this respect the **interim balance** of the black-yellow coalition government has room for growth. Two of the goals set in the coalition contract, with regard to rail politics, have been as good as implemented but they are of little significance. Six further goals earn a yellow at the traffic lights. In particular liberalising long-distance bus transport which, in a legal sense is in its preparation phase, strengthening the Federal Network Agency by establishing a ruling chamber and introducing regulation criteria »cost efficient operation of services« (as on the energy market) are the right steps. Also, forming a commission to control misuse in the rail electricity field is overdue.

However, **the determining flaw remains the inactivity of the Federal Government in making rail infrastructure companies more independent from DB AG.** Following DB AG's successful intervention neither the capping of the control and profit-pooling contract with the holding nor the ban on dual mandates will be implemented. However, both these measures are **central** in effectively boosting rail competition. It seems that competitors have to bank on the verdict of the European Court of Justice regarding the independence of the network operator.

Given the successes gained by competitors despite the suboptimal framework conditions, one gets an idea of how much more could be possible if the network operator were independent. The time has come to expand the potential.

Rail transport in Germany – Overview

Topic	*SPNV*	*SPFV*	*SGV*
Market volume 2010	ca. 8,6 bn Euro	ca. 3,6 bn Euro	ca. 4,3 bn Euro
Rail transport performance 2010	46,6 bn passenger km	36,0 bn passenger km	107,3 bn tonne km
Ratio of tenders to rail transport performance 2010	ca. 12,5 %	< 1 %	25,1 %
Train mileage 2010	636 m train km	149 m train km	ca. 250 m train km
Ratio of tenders to train mileage 2010/11	24,1 % (2011)	< 1 % (2010)	ca. 25 % (2010)
Track access charges 2010	ca. 2.700 m Euro	ca. 780 m Euro	ca. 600 m Euro
Biggest market players besides DB AG	1. Veolia Transdev 2. Netinera (FS Trenitalia) 3. BeNEX 4. AVG 5. Keolis (SNCF)	not relevant	1. SNCF Geodis 2. SBB Cargo Deutschland 3. FS Trenitalia 4. HGK