

COMMENT : IS THE PRICE RIGHT FOR GNER ON THE

GNER has won the right to run train services on the east coast mainline for at least another seven years – but at what cost? Alan Whitehouse looks at the finances and tries to assess if it has paid over the odds for the UK's most prestigious rail route

Nothing should surprise us any more about the franchising process. It has thrown up so many shocks and upsets down the years that the only lesson for harassed bid managers and chief executives is that anything can happen.

Even so, the Intercity East Coast Franchise result still contained enough surprises to raise collective eyebrows.

Shock one: it was won by the incumbent, Great North Eastern Railway. Anyone with half an ear to the industry grapevine over the past 12 months would have been switching bets around all four short-listed bidders. Even as late as February, First Group was still being touted as the likely winner.

When you take into account what happened at Anglia and ScotRail, GNER's achievement seems all the more noteworthy. Few people would be willing to bet their house on the outcome of the competition for the Greater Western or Cross Country franchises when they come up for auction.

Shock two: GNER won, at least partly, because of the eye-watering annual premiums it has signed up to. Over the 10-year life of the franchise it will pay a staggering £1.3bn to the Treasury. Set against the £22m it paid in 2003-04, that looks like a very steep hill to climb.

The commitment brought an immediate warning from the RMT union that the premium payments would not be paid for out of rail workers' jobs, pay or conditions. Equally, GNER went out of its way to stress that fare increases will not be used to foot the bill either because it competes with cars, coaches and aircraft. So where will the money come from?

GNER's chief operating officer, Jonathan Metcalfe, has a simple answer: 'We will do it



by growing the business,' he said.

'Our annual turnover is around £450m-£500m a year, so we are a big business. Every one per cent increase in turnover is worth an extra £4.5m-£5m. If you look at what we have been achieving over the past couple of years, we have been growing at around 8.5 per cent.

'So all we have to do is keep growing at about that rate. It is nothing radical, and nothing we have not been doing already.'

Metcalfe believes there is plenty of space for growth. The load factor, spread across all GNER services, is around 50 per cent, so there are plenty of empty seats which can be marketed. In addition, the franchise commitment includes leasing in three additional HST sets, one to provide extra maintenance and breakdown cover, the other two to beef up the King's Cross-Leeds

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EAST COAST?



service to half-hourly right through the day with an additional 13 services in all.

This will happen by December 2007 when completion of the Allington chord will free up capacity on the east coast main line (ECML) north of Grantham, by separating Nottingham-Boston-Skegness services from ECML services.

GNER's biggest challenge will be to persuade more people to travel off-peak. The average load factor may be 50 per cent, but the peak trains often suffer from overcrowding. The southern end of the ECML becomes more like a commuter route each year with tidal flows of business traffic into and out of London.

And what happens if the economy catches a cold? The first 10 years of rail privatisation has coincided with continuous economic growth, low unemployment and general

stability, which has been reflected in a significant (and largely unexpected) increase in passenger numbers.

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GNER looks to have anticipated that possibility by cannily negotiating a deal that would see the Government protect the company's revenue from year five of the franchise. According to GNER, if revenues fall to less than 94 per cent of target, the deficit is shared 20 per cent to GNER and 80 per cent to the Government. Between 94 per cent and 98 per cent it is shared 50-50. To balance this up, the Treasury will receive 40 per cent of revenues over 102 per cent of target and 60 per cent of anything in excess of 106 per cent.

Even allowing for this, GNER's Metcalfe will not rule anything in or out on the jobs front. 'No business can ever do that,' he said.

He insists that no swingeing cuts are planned and that he wants serious talks with the unions about productivity gains rather than a sweeping round of redundancies. But his comments leave GNER with an escape route if the going gets tougher than anticipated.

Leeds has emerged as a winner in the franchise deal, because **shock three** is GNER's commitment to electrify the 'missing link' between Leeds Neville Hill and the ECML at Colton Junction.

The company says it will benefit in two ways: Leeds will cease to be an electrification 'dead end' and this will create a useful diversionary route between York and Doncaster. It also allows King's Cross to Leeds services to be routed via Hambleton Junction, entering Leeds from the east rather than the current route via Wakefield.

GNER describes the Leeds-London route as the biggest long-distance rail market in the UK; passenger numbers have risen by 30 per cent in the last two years. Rail journey times are very competitive when set against either road or air travel. Having an alternative route into Leeds, bypassing the congested Doncaster-Wakefield-Leeds route, will allow an expansion of services that would otherwise not be possible.

When GNER first won the East Coast franchise nearly nine years ago, it ran 37 services between Leeds and London every

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weekday. The figure today is 53 and in two years it will have gone up again to 66. With the creation of a new electrified route into Leeds GNER confidently predicts it could run up to 80 trains per weekday.

Overall, this is an eye-catching package. But it had to be. The Government is clearly bent on making the profitable parts of the industry pump as much cash as possible back into the parts that aren't making money.

For GNER this starts to look like a real culture change. Its reputation has been built on excellent customer care and on-board service (its punctuality record at around 75 per cent is certainly nothing to shout about). The trick has been to create a perception amongst customers that it is doing a great job even on those occasions when things go wrong.

But now with payments to the Treasury averaging out at £100m a year for the next 10 years, it really has to raise its game. Having got the 'soft' issues right over the past nine years, GNER faces some serious financial discipline to make these numbers crunch.

Alan Whitehouse is Transport Correspondent for BBC North

