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Fares and rail financing

Prepared for the Campaign for Better Transport, December 2013

Introduction

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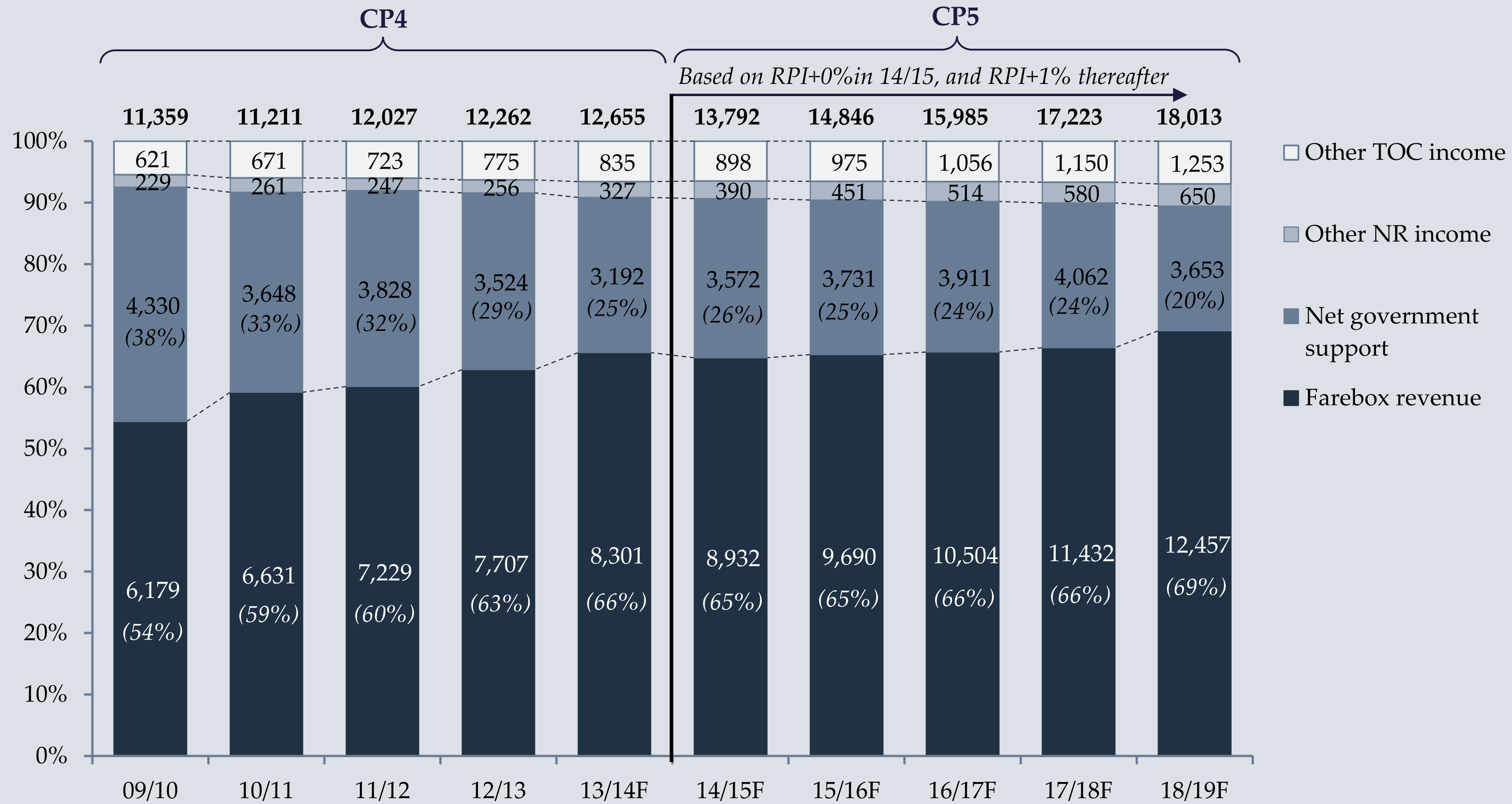
- This report has been prepared by Credo Business Consulting LLP ("Credo") for the Campaign for Better Transport. It is intended to provide preliminary analysis of the potential impacts of different fare regulation structures during the next control period, and help the Campaign for Better Transport stimulate the debate about the appropriate funding structure for the rail industry.

- The report has been prepared by Credo using publicly available sources of data published by, inter alia, the Department for Transport, the Office of the Rail Regulator and Network Rail. Credo has not carried out any assessment on the accuracy of this information.

- Figures relate to franchised passenger rail operations (they do not include Open Access operators). Our analysis assumes that underlying journey growth is similar to the last five years. The impact of changes in fares have been modelled using fare elasticities based on PDFH v4.0.

Farebox revenue has increased from 54% of financing in 2009/10 to 66% today, and we forecast its share to grow to 69% by 2018/19 if RPI+1% resumed from 2015. Net government funding would fall to c. 20%

Components of financing* to the railway, 2009/10-18/19F (nominal prices - £m)

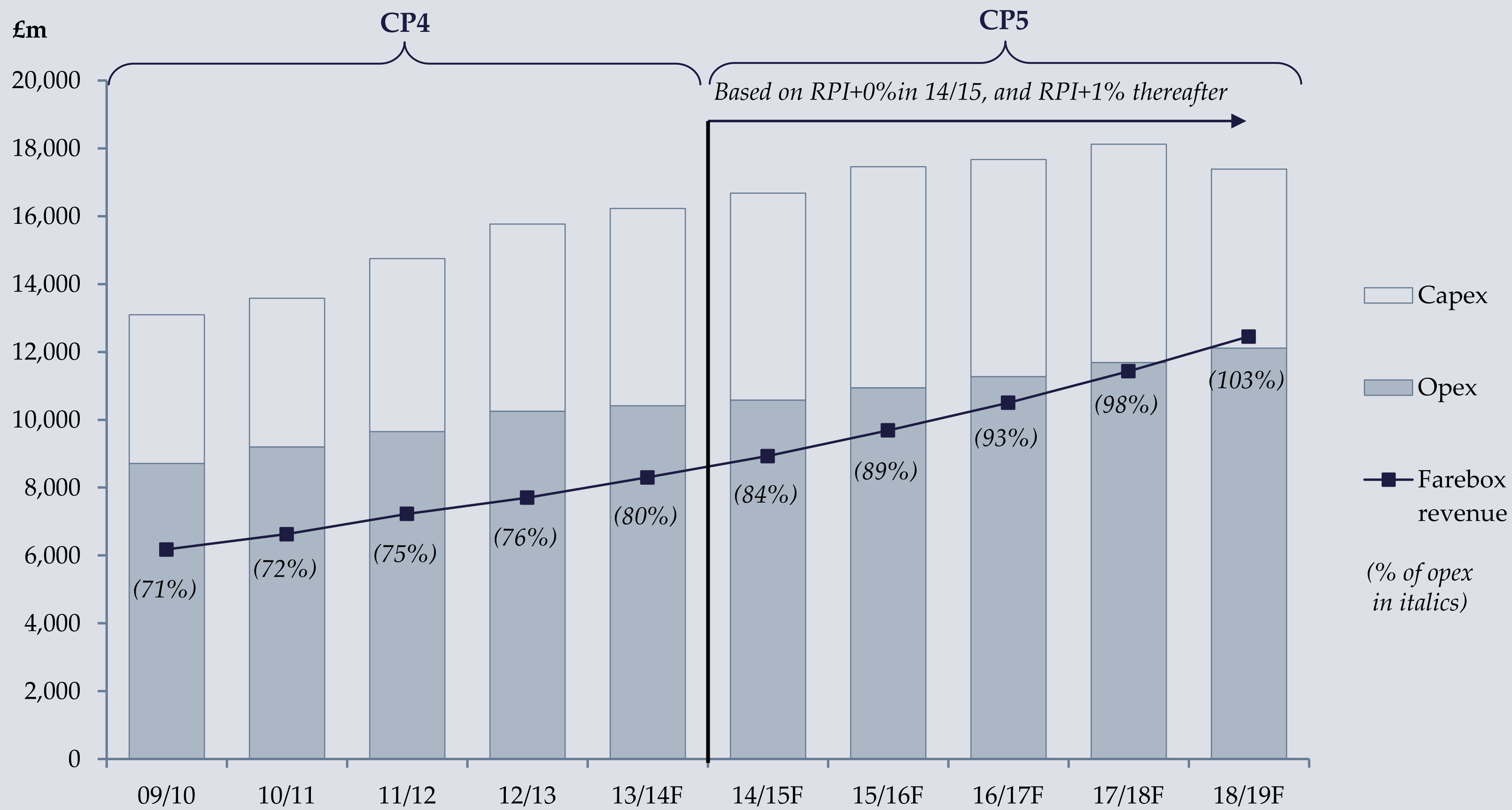


Notes on forecasts: Farebox based on modelled journeys growth in response to fare change according to PDFH elasticities; government support to NR according to CP5 Final Determination assessment; grants to PTEs held constant at 2012/13 level; other NR income (incl. property and commercial) grown according to CP5 Final Determination assessment; TOC other income kept at historic percentage of farebox

* Excludes NR borrowing

This means that fares would be covering over 100% of opex by 2018/19 (versus 80% today)

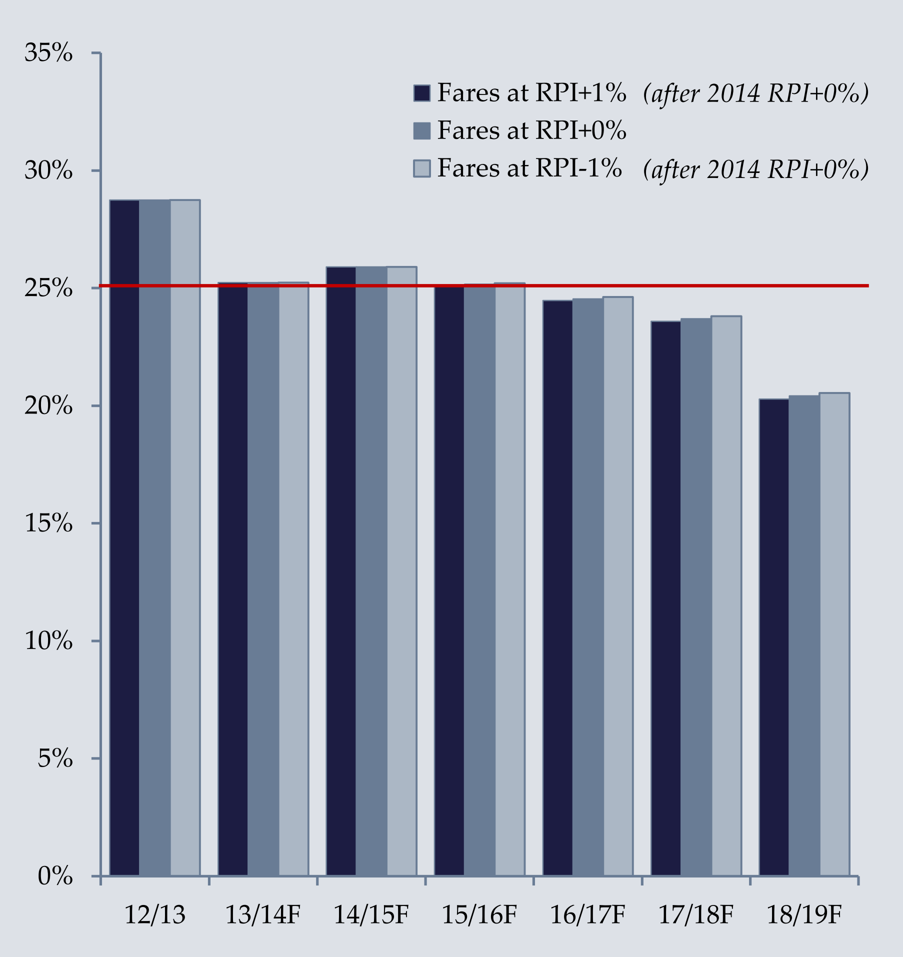
Farebox revenue vs. expenditure, 2009/10-18/19F (nominal prices)



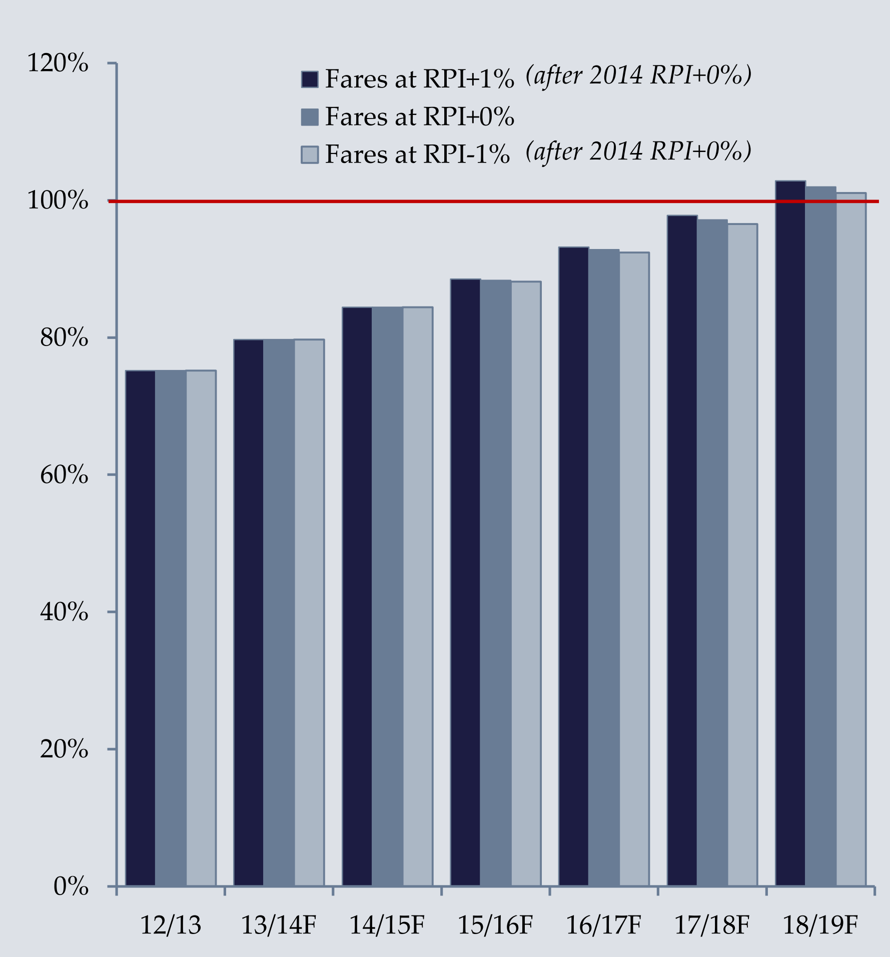
Notes on forecasts: Opex – CP5 Final Determination for Network Rail; grown in line with historic rate for TOCs' staff and rolling stock costs. Capex: – CP5 Final Determination Assessment for Network Rail, is grown according to CP5 Final Determination; grown in line with historic rate for private investment

If fares are frozen in real terms or even cut by RPI-1%, government share of financing will still fall below 25% and fares revenue will cover more than 100% of opex by 2018/19

Government share of rail financing

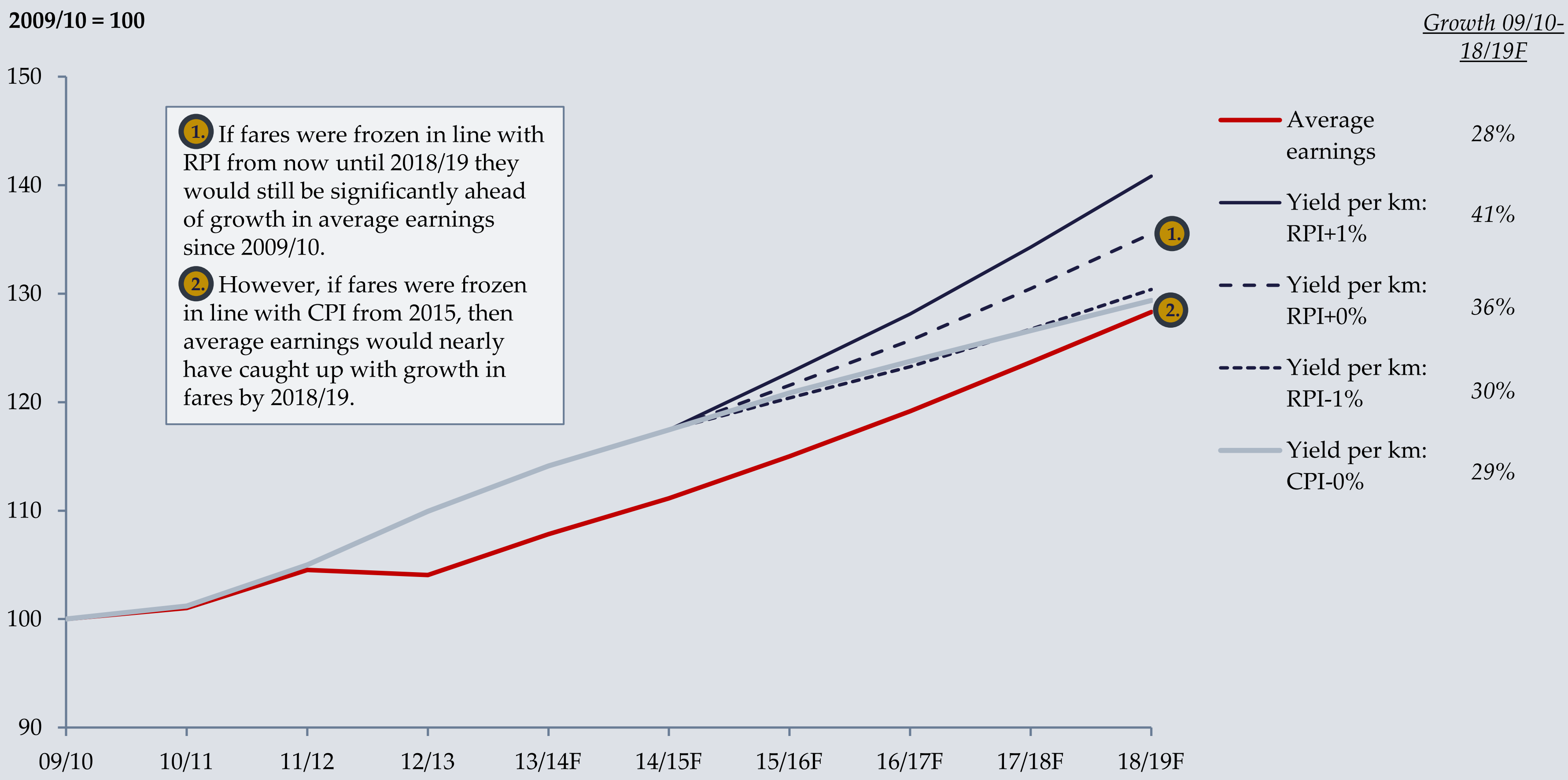


Farebox contribution to opex



Freezing or cutting fares would be fairer for passengers who have experienced fare increases above growth in average earnings. Pegging fares to CPI+0% would have a more positive impact than RPI-1%

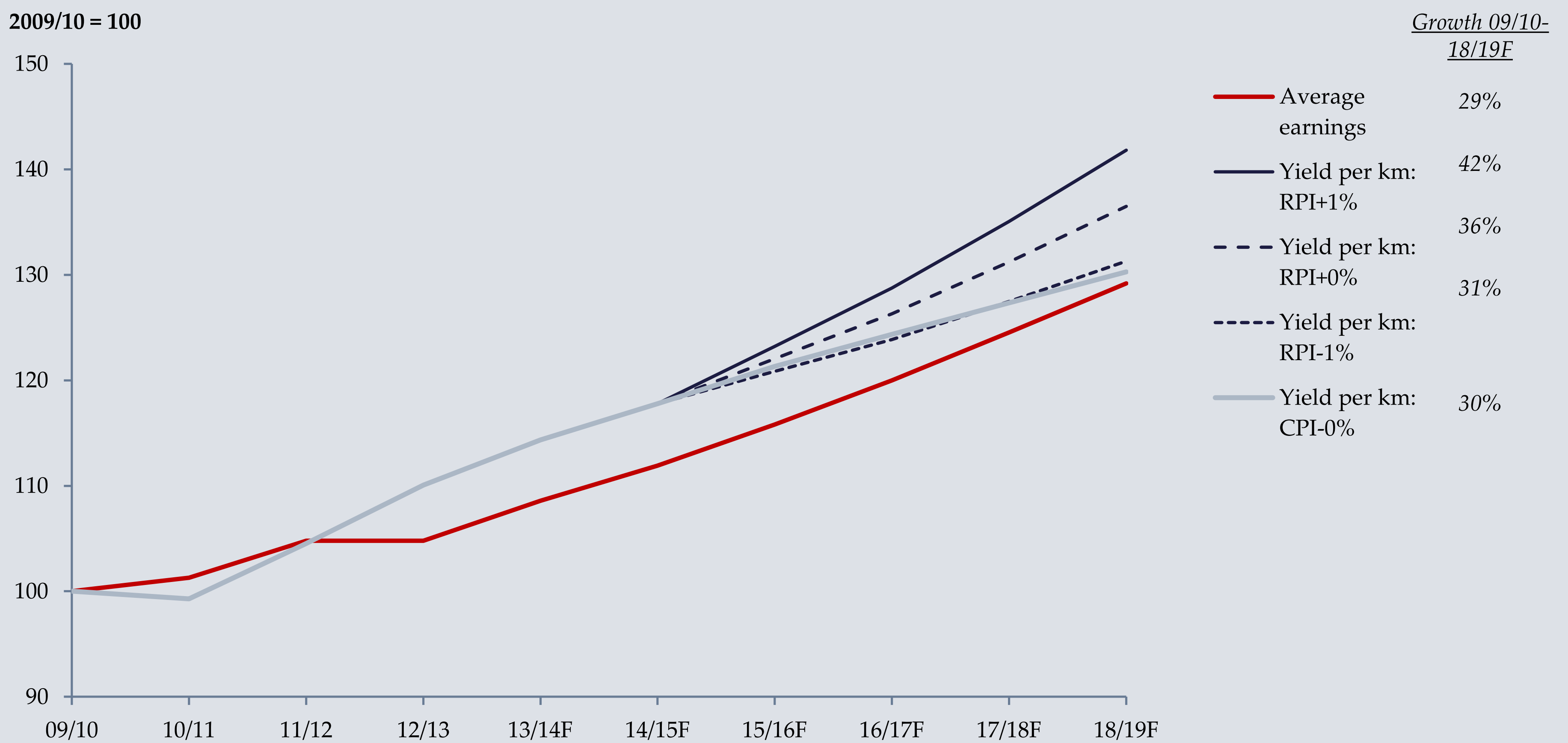
Yield per km vs. average earnings, 2009/10-18/19F (indexed, nominal prices)



Note on forecast: Average earnings come from the OBR's *Supplementary Economic Tables, December* 2013

This picture can also be considered for particular combinations of sector and ticket type

Yield per km vs. average earnings, 2009/10-18/19F (indexed, nominal prices) – *LSE season tickets*



Notes on forecast: Average earnings come from the OBR's *Supplementary Economic Tables*, December 2013; data for LSE season tickets based on estimated mapping between Ticket type and Sector

Increases in season tickets have meant that an even larger share of take home pay is being spent on transport costs (e.g. over 20% for a worker on average London earnings commuting from Reading)

Season ticket as share of take home pay

- Between 2008 and 2013 the cost of a weekly season ticket from Reading to London (incl. Travelcard) has increased by 25% while average take home pay has risen by just 9%
  - This is based on average London earnings in 2013 of £34,895, resulting in take home pay of £26,539
- This means someone on average London salary and commuting from Reading would now be paying 22% of their take home pay in transport
  - 18% of this is to and from Paddington
  - 4% is the cost of travel within London

Above a certain threshold the cost of transport could be considered 'unaffordable' for commuters

Pursuing an RPI-1% or CPI+0% rather than RPI+1% policy during CP5 would provide significant help to passengers for only limited revenue downside for the industry

Modelling of revenue and journeys (2013/14F - 2018/19F)

		13/14F (base yr)	CP5 14/15F	15/16F	16/17F	17/18F	18/19F	TOTAL CP5
RPI+1%	**Farebox**	£8,301m	£8,932m	£9,690m	£10,504m	£11,432m	£12,457m	£53,014m
	Journeys	1,547m	1,603m	1,652m	1,703m	1,757m	1,812m	8,528m
RPI+0%	**Farebox**	£8,301m	£8,932m	£9,668m	£10,458m	£11,358m	£12,351m	£52,768m
	Journeys	1,547m	1,603m	1,661m	1,722m	1,785m	1,852m	8,622m
RPI-1%	**Farebox**	£8,301m	£8,932m	£9,647m	£10,413m	£11,285m	£12,247m	£52,524m
	Journeys	1,547m	1,603m	1,670m	1,740m	1,814m	1,893m	8,720m
CPI+0%	**Farebox**	£8,301m	£8,932m	£9,656m	£10,422m	£11,283m	£12,226m	£52,519m
	Journeys	1,547m	1,603m	1,666m	1,736m	1,815m	1,901m	8,722m
Difference: RPI+1% vs RPI-1%	*Farebox*	-	-	*£42m*	*£91m*	*£147m*	*£210m*	*£491m*
	Journeys	-	-	*(18m)*	*(37m)*	*(58m)*	*(80m)*	*(192m)*
Difference: RPI+1% vs CPI+0%	*Farebox*	-	-	*£34m*	*£82m*	*£149m*	*£230m*	*£496m*
	Journeys	-	-	*(14m)*	*(33m)*	*(59m)*	*(88m)*	*(194m)*

- Cutting fares by RPI-1% rather than increasing them by RPI+1% over the four years 2015/16F-18/19F would mean farebox generating an estimated £491m less in revenue over CP5 (equivalent to just 1.1% of forecast farebox revenue from 2015/16-2018/19)
- It would also mean an extra 88m journeys across the UK by the final year, equivalent to approximately 20,000 each morning 3 hour peak in London (assuming 13%[1] of LSE journeys are morning peak arrivals in London, spread over 250 days)
  - Investment in capacity will mean an additional 119,000 London morning seats will be provided by the end of CP5

Note: [1] This is based on their being 536,000 journeys in the morning peak in 2012
(Source: DfT, *Rail Passenger Numbers and Crowding Statistics 2012)*

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