

RAIL PRIVATISATION IN SOUTH AFRICA: WILL IT WORK?

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ABSTRACT

The 1990s saw the reintroduction of private rail operations in a number of developing countries across the globe where, without exception, all major railways had been under state control for more than half a century. By the end of 1997 fourteen developing countries had transferred varying degrees of responsibility for rail operations to the private sector.

Several of the so-called industrialised countries also privatised their national railways during the 1990s, notably Canada, the United Kingdom and New Zealand. The most common type of privatisation scheme has been the concession or franchise where a private operator provides rail transport services using publicly owned infrastructure.

Although South Africa's national rail operator, Spoornet, is actively involved in rail privatisation projects in no less than 20 foreign countries, private sector participation in local rail operations has been almost non-existent mainly due to opposition from the labour unions. This paper considers the achievements and failures of rail privatisation projects globally and comments on the viability of private sector involvement in the South African rail industry.

1. INTRODUCTION

Privatisation, according to Simon (1996:166), is 'the transfer of ownership of economic enterprises from the state to the private sector'. Thompson and Budin (2001) report that, with several railways exploring the possibilities of partnerships between governments and the private sector, the most common type of transaction to date has been the concession or franchise, where a private operator provides rail transport services using publicly owned infrastructure.

Data on private investment in railways reveal that 44 rail networks in 16 countries were concessioned or privatised during the 1990s and that another 7 railways in 7 countries were in the process of being concessioned by 2001. In most cases the rail infrastructure (track and other fixed assets) remained in government ownership, while managerial control of rail services was handed over to new, private entities. However, in the case of New Zealand Railways, the Canadian National Railways and the Northern Railway in Chile, the privatisation process included transferring full control over the infrastructure to the new owners. (Thompson, Budin and Estache 2001.)

Tynan (1999) expects that the current trend towards private contracting will continue and claims that in Latin America most of the concessioned rail services are showing improved performance under private management. He confirms that concessions have been more common than other forms of private participation, with most countries turning to the private sector, not only to improve the financial performance of loss-making rail services, but also to restore deteriorating rail infrastructure.

Reports about the progress (or lack of progress) with the privatisation of rail services in South Africa seem to be contradictory. The Railroad Association of South Africa claims that: 'Spoornet is now in the mid-stage of restructuring in preparation for outsourcing services and concessioning various lines' (Railroad Association 2004). On the other hand, a comprehensive media statement by Spoornet on the company's future plan of action, released by its Chief Executive on 13 May 2004, makes no mention about any concessioning and/or other privatisation endeavours (Spoornet is being re-born 2004).

2. FORMS OF PRIVATE SECTOR PARTICIPATION

A brief synopsis of various privatisation options is necessary before reviewing individual rail projects.

2.1 Railway Restructuring – a First Step Towards Privatisation

Historically most railways were fully integrated organisations where the railway enterprise provided all freight and passenger services, developed and managed its own infrastructure and performed most of the secondary functions needed by a railway internally. The modern trend however is to separate and re-organise the various rail businesses according to function. The so-called 'functional model' is very prominent in Europe where European Union policy requires rail operations to be separate from infrastructure control. (Harsh 1998.)

Separation or 'unbundling' of rail transport activities, according to Galenson and Thompson (1993), is a prerequisite for private sector participation in the rail industry as it:

- Liberates the railway from its base of fixed assets and long-term debt, allowing it to function commercially;
- Allows for the establishment of profit and cost centres, which in turn improves financial information and accountability; and
- Makes the railway structurally more like its competing modes.

Thompson and Budin (2001) also comment on the current tendency to separate infrastructure from operations, as well as on splitting the different operations into independent entities.

They call it the 'separation model' and claim that it:

- Allows each operator to focus on its core business;
- Relieves operators of the responsibility of managing and maintaining rail infrastructure; and
- Subdivides the railway enterprise into manageable components, some of which can be privatised or concessioned.

Galenson and Thompson (1993) mention decentralisation as another method of breaking up a large unyielding railway organisation, especially in the case of localised passenger services which often run at a loss, but which local governments may be willing to subsidise. They argue that, where a transport need is mostly at a local level,

decentralisation promotes greater accountability and opens the door for private sector participation through contract operation.

2.2 Concessioneing of Rail Services

Budin (1997) defines 'concessioneing' in the railway milieu as 'a partnership between the state and a private operator (the concessionaire) in which, while maintaining ownership of rail infrastructure, the state transfers railway operations to the concessionaire as spelt out in a concession agreement. Railway operations are handled by the concessionaire as a commercial activity, at its own expense and risk'. According to Galenson and Thompson (1993) a concession is a type of lease agreement in which the contractor undertakes to make certain fixed investments while retaining the use of the assets for a specified period.

Concessioneing, as stated earlier, has been the dominant form of privatisation in the rail industry to date. The majority of the concessions awarded have been for freight operations, with an average term of 30 years. The rationale behind the 30-year period is that it corresponds roughly with the lifespan of locomotives and wagons. (Thompson et al 2001.)

2.3 Service Contracts

Private sector involvement in a publicly owned railway can also be in the form of a service contract where activities such as catering, building maintenance, etc. are outsourced to the private sector (Galenson & Thompson 1993). This practise is well established in South Africa where Spoornet employs subcontractors to deliver a variety of non-core services, ranging from security to mechanised track maintenance.

2.4 Management Contracts

Management contracts, according to Galenson and Thompson (1993), range from what is essentially a form of technical assistance, where the contractor carries no financial risk, to more complex cases where compensation is based at least partly on results, which could include performance incentives. The contractor assumes responsibility for operations and maintenance of a particular activity, which could include running an entire railway.

Amtrak, the government-subsidised passenger rail service in the United States, provides commuter services in some major cities under contracts that provide for full cost repayment plus profit (Galenson and Thompson 1993).

2.5 Lease Agreements

In the case of leasing the contractor could be charged a fee for the use of fixed assets. Both Amtrak and VIA, the government-supported passenger rail service in Canada, pay to operate their trains over the tracks of other railway companies. Another form of leasing could be where a railway does not own locomotives and/or rolling stock, but leases them from a private entity. (Galenson and Thompson 1993.)

2.6 Full Private Ownership

Rail freight services in the United States (US) are fully privatised. Although the US rail transport market is dominated by large corporations such as Union Pacific, Burlington Northern Santa Fe and the CSX Corporation, freight services are also provided on more

than 500 privately-owned short lines, which is proof that smaller entrepreneurs can provide profitable rail services when they are unburdened by restrictive labour legislation. (Galenson and Thompson 1993.)

3. PRIVATE SECTOR INVOLVEMENT IN THE RAIL INDUSTRY – SELECTED CASE STUDIES

As a background to possible private sector involvement in the South African rail environment, it is necessary to focus on successes and failures of recent rail privatisations across the world.

In contrast to the rail privatisation difficulties experienced in Britain and New Zealand, some concessioned rail operations, notably those in Latin America, are yielding encouraging results. A recent case study of concessioned railways on four continents (Thompson et al 2001) revealed that traffic has increased after years of decline in most of the previously state-owned railways, labour productivity has improved significantly and tariffs have been reduced to the benefit of rail users.

3.1 Privatisation Pains in the United Kingdom (UK)

Simon (1996:167) points out that a study of the history of transport policies in many countries over the last century shows successive phases of regulation and deregulation and periodic shifts between private and public ownership. The best example of continuous fluctuation between private and public ownership of rail infrastructure and services is probably the UK.

Nock (1977:8-19) describes how the country's rail network was initially developed and operated by various private companies until nationalisation on 1 January 1948 with the formation of British Rail (BR). The BR-era ended on 1 April 1994 when individual elements of the national rail system were broken up into separate organisational and accountable business units. Train services were distributed amongst 25 operators who lease their rolling stock from individual leasing companies. Rail infrastructure was separated from train operations and came under ownership of a private company called Railtrack. (Faulks 1999:86.)

Railtrack, after suffering total financial collapse in 2001, was taken over by a government-supported company, Network Rail, in 2003 (Network Rail takes over in Britain 2002). The private company's poor financial performance was aggravated by four fatal rail disasters. The Southall train crash in 1997, with 7 fatalities, the collision at Ladbroke Grove in 1999, which claimed 31 lives, and the Hatfield crash in October 2000, which killed 4 people, (Railtrack in administration 2001) was followed by another accident at Potters Bar on 10 May 2002, in which 7 people were killed. In the latter case poor track maintenance by Railtrack was cited as the main cause of the accident. (Poor maintenance caused Potters Bar crash 2003.)

According to a report in the April/May 2003 edition of Railways Africa, privatisation in the UK has not been a complete success. It mentions that 6 of the 24 rail passenger franchises were operating at a loss (UK privatising headaches 2003). One of these returned to public ownership in November 2003 due to poor financial management (Connex hands back British franchise early 2003).

3.2 The Collapse of Privatised Rail Services in New Zealand

Government-owned New Zealand Railways was restructured during the 1980s prior to privatisation. It was then renamed Tranzrail with its sale to a private company in 1993. (Railroads 2004.)

Over a period of ten years Tranzrail had a succession of owners, but by 1993 the company was close to insolvency. New Zealand's 4 500 km rail network returned to public ownership in July 2004 when the government 'bought' back all fixed assets for a token amount of R3,90 from Toll Rail, the company responsible for the management of rail infrastructure. The intention now is to invest a substantial amount of government funds over a five-year period to upgrade the country's deteriorated rail system. (Kiwi rail system returns to state hands 2004.)

3.3 Rail Concessioneering in Argentina, a Success Story

An article in the October 1977 edition of the International Railway Journal describes how Argentina's rail system, the largest in South America, was grinding to a halt by early 1976. It mentions that numerous locomotives, passenger coaches and goods wagons were out of commission because of poor maintenance and lack of spares and that expenditure was more than double the income in fiscal 1976. (Argentina: Tough line brings results 1977.)

Nowadays, with private sector involvement, rail services are no longer a financial burden for the Argentine economy. The Argentine state railways was privatised during the 1990s by separating freight and passenger services and creating six freight and several passenger packages for concessioneering. By 1999 freight operations on the concessioneered lines were showing significant gains in productivity and revenue, while the subsidy cost of passenger services was decreasing under private management. (Tynan 1999.)

4. RAIL PRIVATISATION IN SOUTH AFRICA – WILL IT WORK?

Recent privatisation endeavours in the international arena confirm that restructuring of a state-owned rail utility is a prerequisite for private sector participation in rail operations. Spoornet, South Africa's national rail utility, has undergone several restructuring programmes since its formation in 1990. Most of these reshufflings, some of which never went beyond the planning stage, were based on recommendations made by successive foreign consultants. To date none of the changes have yielded satisfactory results.

4.1 Spoornet Restructuring – Quo Vadis?

The old South African Railways (SAR) was typical of the traditional large railway enterprise, which performed most of its functions internally. SAR, with a workforce of more than 230 000 in 1975, offered a countrywide road transport service to complement its train services and even managed its own catering department, railway police and travel and publicity department (This is South African Railways 1978).

Spoornet, a subsidiary of state-owned transport company Transnet, is more streamlined than its predecessor. Many of its ancillary functions have been outsourced to the private sector and by 2002 the staff complement had been reduced to about 34 000.

The rail utility is currently subdivided into six separate businesses:

- CoalLink, the coal export line from the Mpumalanga coal fields to Richard's Bay;
- Orex, the iron-ore export line from Sishen to Saldanha Bay;
- General Freight Business (GFB), also known as the Commercial Division;

- Shosholoza Meyl, responsible for the operation of long distance passenger trains;
- LuxRail, which operates the Blue Train; and
- International Joint Ventures.

The restructuring of rail services in South Africa into stand-alone entities has not contributed to an increase in freight tonnages, nor has it improved service delivery. GFB, the largest of the six business units in terms of revenue, customer accounts and staff complement, reported an operating loss of R469m for the 2001/02 financial year. Obsolete rolling stock, unfavourable tariff levels, a weak rand/dollar exchange rate and high maintenance costs are some of the reasons given in a 2003 Spoornet publicity brochure for GFB's poor financial performance.

While restructuring remains high on the agenda for Spoornet Management, there seems to be uncertainty as to how the company should be broken up into independent business units.

Various possibilities have been mentioned in recent media reports:

- The merger of CoalLink, Orex and the profitable GFB operations into a single rail freight company, with low-density rail lines managed as a separate entity (Creamer 2001).
- The merger of long-distance passenger rail services (Shosholoza Meyl), rail commuter services (Metro Rail) and the South African Rail Commuter Corporation into one operation (One rail service mooted for SA 2002).
- Splitting the rail utility into two divisions: rail operations and rail infrastructure (Singh 2005).

4.2 Is the Department of Public Enterprises Serious About Rail Privatisation in South Africa?

In 1999 a privatisation specialist, appointed by the Department of Public Enterprises (DPE), recommended that the profitable CoalLink and Orex lines be concessioned, while the loss-making GFB should remain in public ownership until it became financially viable (Von Holdt 2003). These recommendations were not acceptable to DPE and the ore lines remained under Spoornet control.

In a November 2000 address to the top 150 Spoornet customers the then Minister of Public Enterprises, Mr Jeff Radebe, stated that rail is a strategic government asset and will not undergo wholesale privatisation. Instead, private contractors will participate in rail operations through concessions and public-private partnerships. (Ministry of Public Enterprises 2000.)

The current thinking within DPE is to have a single freight business under Spoornet control, which will include CoalLink, Orex and GFB, while passenger services will be concessioned to the private sector (Loxton 2005).

Recent press releases by the DPE and by Spoornet have been rather vague about rail privatisation issues. There appears to be a lack of urgency to privatise any profitable parts of the national rail network in the immediate future. In addition, no visible steps have been taken about the possible concessioning of unprofitable low-density lines.

4.3 Opposition from the Trade Unions

The three railway trade unions in South Africa are opposed to privatisation, claiming that it would undermine the state's ability to provide affordable and efficient transport to meet socio-economic needs. They are also concerned that privatisation would place the future of rail transport in jeopardy with the closure of unprofitable lines and that high levels of retrenchment would be inevitable. (Von Holdt 2003.)

The labour unions' fear of job losses in the rail industry due to privatisation, are not unfounded. In some South American countries the concessionaires were given the freedom to employ only the labour force that they needed. Rail freight concessions in Argentina resulted in a reduction of the labour force by 92%, in Bolivia by 80% and in Brazil by 75%. (Thompson et al 2001.) In Canada, with the lease of British Columbia (BC) Rail by Canadian National, the aim was to cut BC Rail's 1 380 workforce by 30% through the offering of early retirement or severance packages (Canadian National to take over BC Rail 2003).

These are probably extreme examples and are an indication of how unproductive the workforce was while the railways were under state control. However, the question must be asked whether South Africa can afford further retrenchments, which will include the loss of skilled technical and administrative staff, in its rail sector.

Faulks (1999:103,125) talks about the possible effect of privatisation on staff motivation. He claims that with privatisation 'managements may become even more cost-conscious with a deterioration in pay and conditions and yet further staff reductions'. According to him this could demoralise employees, which, in turn, will jeopardise efficiency and loyalty to the service.

When talking to Spoornet personnel it is blatantly clear that the current uncertainty about restructuring and privatisation, in addition to rumours about possible retrenchments, are undermining staff morale. Perhaps the company's executives need to realise that without a motivated and productive workforce, it is unlikely that the rail utility will be transformed into a profitable, customer-orientated business within the foreseeable future.

4.4 Spoornet's Poor Performance – a Barrier to Private Sector Involvement

Spoornet recorded a R688m loss in the 2003/04 financial year, while in the first 6 months of the 2004/05 financial year up to the end of August 2004 losses had accumulated to R506m. Apart from poor financial performance, the company is also struggling with conflict amongst its managers, a shortage of skills, poor service records and ageing infrastructure. (Singh 2005.) These issues need to be addressed as they could inhibit private sector involvement in the rail industry. A loss-making business with a dwindling customer base will be written off as too much of a risk by many potential investors.

By offering severance packages, as part of a determined affirmative action drive, Spoornet has lost experienced personnel at both technical and managerial levels. While the need for transformation is undeniable, it could be argued that the manner in which it has been executed has impacted negatively on operational efficiency and service delivery. It is rather ironic that Ms Maria Ramos, the current CEO of Transnet, intends to fill the skills gap by seconding people from the private sector and/or recruitment from other countries (Singh 2005).

4.5 The Status of Low-Density Rail Lines

Until recently Spoornet has pursued a policy of terminating services on some of its unprofitable low-density lines, notably in the poorer provinces of the country. The company has also increased tariffs for the conveyance of agricultural produce and timber to levels that many rural rail customers cannot afford. The net result has been a further reduction of traffic on low-density lines and a shift of freight from rail to road.

To date several of these rail lines have been scrapped, depriving many remote rural communities of much-needed transportation infrastructure. Seymour, Hofmeyr, Tarkastad, Qamata and Jamestown are typical of towns in the Eastern Cape that are no longer connected to the country's rail system. While rail closures may have been part of Spoornet's strategy to become more market orientated, they have not been in compliance with government's socio-economic objectives.

President Mbeki, in a May 2004 speech in Parliament, confirmed that state-owned utilities like Spoornet 'would play a leading role in encouraging growth and development while at the same time eradicating poverty and underdevelopment' (Mbeki sees Transnet as a driving force in development 2004). In the Eastern Cape specifically there is renewed interest in the potential use of the remaining low-density lines to stimulate economic growth in rural areas. At least one, the 281 km Amabele-Umtata line, has been identified as a future corridor for economic development. This branch line will be upgraded to serve timber industries and farming communities in the former Transkei.

Branch lines serving poorer parts of the province may not be financially viable for concessionaires, as some of the rail services could be offered at sub-economic rates in support of small and medium enterprises. Private operators are profit-driven and will be hesitant to deliver such services without a guaranteed subsidy. There are, however, other low-density lines in the province that do have the potential to be concessioned. Typical examples are the Kirkwood Branch, which carries export citrus from the Sundays River Valley to the Port Elizabeth Harbour, and the narrow gauge Port Elizabeth-Avontuur railway.

The 285 km Port Elizabeth-Avontuur line is perhaps the most suitable candidate for concessioning or even full privatisation. Because of its narrower track gauge (610 mm) it is not linked to the rest of the country's standard 1 065 mm gauge rail network, and can thus be operated as an independent enterprise without impacting on other rail services. Current freight traffic is estimated at about 70 000 tons/annum and the potential for growth exists (Van der Mescht 2004). Privatisation or concessioning could probably be done without the need for retrenchments. With an increase in revenue-earning freight traffic it may even be necessary to employ additional staff.

5. THE WAY FORWARD

There is little merit in discussing rail privatisation in South Africa if it is government's intention to keep the country's entire rail system in public ownership. However, there appears to be some political will to allow for limited private sector participation in the rail industry. The most probable scenario is that Spoornet will retain its profitable freight operations, while some of the non-strategic low-density lines could be repositioned for concessioning.

At this stage rail infrastructure and other fixed assets on many of the low-density lines under Spoornet administration continue to deteriorate due to years of neglect, deferred maintenance and zero capital investment. It is crucial that those lines with commercial potential be offered to private entrepreneurs while their basic facilities are still intact.

The Port Elizabeth-Avontuur railway, despite its narrower track gauge and other inherent technical limitations, carries more freight than any of its normal gauge counterparts in the Eastern Cape. It has the capability to be operated as a profitable rail business and should therefore be fully privatised or concessioned without delay.

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