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Competition in the railway passenger market in the Czech Republic

Zdeněk Tomeš [a,*,1], Martin Kvizda [a], Tomáš Nigrin [b], Daniel Seidenglanz [c]

[a] Department of Economics, Masaryk University Brno, Czech Republic
[b] Institute of International Studies, Charles University Prague, Czech Republic
[c] Department of Geography, Masaryk University Brno, Czech Republic

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ABSTRACT

This paper describes the development of competition in the Czech railway passenger market. The vertical separation of infrastructure and services occurred in 2003. Open access for commercial passenger services is allowed, and it was utilised in 2011 when the incumbent on the key rail route Prague–Ostrava was challenged by a new operator; a third operator entered the route at the end of 2012. This resulted in an intensive on-track competition with tariff declines and service improvements. With the exception of the Prague–Ostrava route, the operation of other passenger lines is classified as a public service obligation and is subsidised from public budgets. Long-distance services are organised by the Ministry of Transport, and the usual form of procurement used to be a direct awarding of services to the incumbent. However, this is changing as competitive tendering is being used more frequently. Competitive tendering is also theoretically possible in regional transport, but in 2009, regional transport authorities decided to directly award all contracts to the incumbent for 10–15 years, effectively closing regional markets for that period.

1. Introduction

The Czech railway passenger market has progressively been liberalised. The initiation of liberalisation was the unbundling of infrastructure and services in 2003. An independent manager of infrastructure was created, and the entrance of other operators on the railway infrastructure enabled. Competition in the freight railway market developed substantially, and the market share of non-incumbent operators was 23.8% in 2011.[2] However, the development of competition in the passenger market has been much slower, and the market is still dominated by the incumbent operator, České Dráhy, with the market share of non-incumbent operators as low as 1.4% in 2011.[3] However, this situation is changing because of the recent emergence of two private open-access operators on the main railway route (Prague–Ostrava) and the government's effort to proceed with competitive tendering for subsidised services. The existence of different competitive regimes poses challenges in reconciling on-track competition in the backbone route with the financial sustainability of public service obligations in the rest of the network. The aim of this article is to describe the development of competition in different segments of the railway passenger sector and to obtain more detailed information about the degree of liberalisation in the Czech Republic than it is possible to obtain from single indices such as IBM (2011). In Section 2 we review relevant literature, Section 3 describes the unbundling of infrastructure and services, Section 4 describes the development of competition in long-distance services, Section 5 describes the development of competition in regional transport and in Section 6 we consider implications and recommendations for transport policy.

2. Literature review

The progressive liberalisation of the European railway markets has resulted in varying outcomes. In a number of countries, there have been strong developments in competition; however, in other countries, there have been no developments in this regard, and the market is still dominated by the incumbent (IBM, 2011; RMMS, 2012). Moreover, there is a wide variety of competition structures and regulatory approaches in the European countries. The experiences with the introduction of competition in the major European countries, such as the UK, Germany, France, Italy, Spain and Sweden, are well documented in the comparative (Beria, Quinet, de Rus,

* Corresponding author. Department of Economics, Faculty of Economics and Administration, Masaryk University, Brno, Lipova 41a, Czech Republic. Tel.: +420 549498146.
E-mail address: tomes@econ.muni.cz (Z. Tomeš).
[1] Presenting author.
[2] Train-kilometres (SŽDC, 2011).
[3] Train-kilometres (SŽDC, 2011).

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& Schulz, 2012; Finger, 2014; Nash, Nilsson, & Link, 2013) and single-country case studies (Alexandersson & Rigas, 2013, Link, 2012; Preston & Robins, 2013); however, the experiences of the smaller and, especially, Eastern European countries have largely not been analysed, and we know little regarding the effect of liberalisation on the development of competition in these markets. There are several comparative studies for the Eastern European railways, but these investigations concentrated on the freight rail competition (Friebel, Guriev, Pittman, Shevyakhova, & Tomova, 2007; Pittman, Diaconu, Šip, Tomová, & Wronka, 2007), infrastructure (Tanczos & Bessenyei, 2009) and reform progress (Carbajo & Sakatsume, 2004). Therefore, there is a need to document the development of passenger railway competition in these countries.

The Czech case is particularly interesting because since the year 2011, there has been open-access passenger competition between the three operators on the major railway route Prague–Ostrava. The impact of open-access competition on the development of markets has been analysed thus far in the cases of niche market entries in the UK (Griffiths, 2009) and Germany (Séguret, 2009). However, in the last number of years, a new pattern of open-access competition has emerged. In Italy (Cascetta & Coppola, 2014), Austria and the Czech Republic, new entrants have not targeted the niche markets but rather the principal railway routes with a clear aim to directly challenge the incumbent. There are theoretical and simulation studies that attempt to predict the outcomes of such direct competition (Ivaldi, 2005; Johnson & Nash, 2012; Preston, Whelan, & Wardman, 1999) but almost none that analyse its real functioning. This paper attempts to fill that gap.

This paper is a case study analysing the development of competition in the passenger railway sector in the Czech Republic. The previous studies analysing the Czech railway market are Otáhal and Pospíšil (2009), which focused on railway financing; Beneš, Březina, Bulíček, and Mojžiš (2008), on the intermodal competition, Šíp (2006), on the freight railway competition; and Havlíček (1999), on the railway output.

3. Vertical unbundling

The formal opening of the railway passenger market went into effect as early as 1994 as a result of the Railway Act (266/1994), which put pressure on the integrated incumbent to open its railway infrastructure to other operators. However, the real market opening was only possible after the vertical unbundling of railway infrastructure and services in January 2003 as a result of the Railway Transformation Act (77/2002), which split the old integrated railway company into a new independent manager of infrastructure (Správa železniční dopravní cesty, or SŽDC) along with the incumbent operator (České Dráhy, or ČD). However, the transformation of the railway sector in 2003 was incomplete. The infrastructure manager acquired possession of railway infrastructure and became responsible for its build-up and maintenance. However, the incumbent ČD retained possession of railway stations and the facilities for infrastructure maintenance, management and operation. This situation forced the infrastructure manager to rely on the services of the incumbent for many activities. In the period of 2003–2008, the infrastructure manager paid the incumbent ČD for infrastructure maintenance, timetabling and traffic control. This situation changed somewhat in 2008 when the infrastructure manager bought from the incumbent the part of the company that handled infrastructure maintenance and timetabling. The price of purchase was 11.852 billion CZK[4] (approximately 475 million EUR) (ČD, 2009). This purchase was widely criticised because the infrastructure manager bought (with the help of state subsidies) something from the incumbent that the incumbent had received for free during the transformation of 2003. The incumbent should have used this money to finance rolling stock renewal, but it was mostly used to finance operational losses. The second change occurred in 2011 when there was a transfer of the operational and traffic control activities from the incumbent to the infrastructure manager. The increasing role of SŽDC in infrastructure management can be traced in the gradual increase in the number of its employees (Table 1).

It took 5 years to transfer infrastructure maintenance and 8 years to transfer traffic control from the incumbent to the infrastructure manager. Between 2003 and 2008, the infrastructure manager had little control over infrastructure costs, while between 2003 and 2011 the incumbent was in charge of network operation. This state of affairs slowed the progress of competition because it gave a competitive advantage to the incumbent. The institutional situation of the Czech railway sector from 2003 to 2011 resembled the organisational setup in France (Deville & Verduyn, 2012).

However, the incumbent maintains possession of railway stations even today, which causes problems in enforcing fair competition rules. The incumbents' competitors argue that the ownership situation regarding railway stations favours the ČD and that they have problems with gaining fair access to railway station facilities. Conversely, the incumbent states that the operation of railway stations is highly unprofitable and that it would like to charge fees to other operators for using the facilities that are the sources of the dispute. There are plans to transfer the ownership of stations to the infrastructure manager, but it is unclear whether it should be for a price or free of charge, and a final solution have not yet been found. The incumbent's competitors argue that the transfer should be free of charge because railway stations constitute part of the infrastructure, but the incumbent opposes this, arguing that it has to take care of its property and cannot give it up without adequate payment. There is also the problem of the rolling stock's repairing and washing facilities, which have also remained with the incumbent. New operators are reporting that they are having problems accessing them.

The transformation of the Czech railway sector included the incumbent's debt clearance in 2003. The total debt of České Dráhy in December of 2002 was 58 billion CZK (ČD, 2003). In January 2003, the debt was cleared off from the incumbent's balance sheet and handed over to the infrastructure manager, SŽDC. Because SŽDC was unable to repay it from its own sources, this debt had to be paid from the public budgets at an average rate of 4–5 billion CZK per year, with an estimated total public subsidy of 45 billion CZK between 2003 and 2011 (SŽDC, 2012). The infrastructure manager is in a precarious financial situation because infrastructure charges are low, especially for passenger transport, and they were repeatedly decreased during the recession of 2008–2011. Therefore, the high costs of old debts, infrastructure maintenance and ambitious modernisation programmes are financed almost exclusively by public subsidies. Additionally, the incumbent's financial situation has progressively gotten worse. The freight division was hardly hit by the economic recession and passenger division has been under increasing amounts of pressure from competition (Table 2).

The regulatory institutions for the newly emerging competitive structure of the railway industry are Drážní inspekce (Railway Inspection) and Drážní úřad (Railway Office). Drážní inspekce is entrusted with the safety aspects of railway operations. Drážní úřad is the state administration body, which issues railway licensing, and regulates capacity allocation and infrastructure charges. However, the maximum level of infrastructure charges is regulated by the

[4] CZK = Czech koruna.