Productivity Commission Rail Inquiry Submission

Capricorn Capital Limited

and

The Austrac Group

Capricorn Capital Limited (ACN 077 566 413), Level 3, 9-11 Castlereagh St, Sydney, NSW 2000, p 02 9279 1070, f 02 9279 1073

1. Introduction

1.1. Scope

i. Austrac Group and Capricorn Capital Limited (section 1).

ii. Transport infrastructure expenditure and cost recovery (section 2).

iii. Rail freight industry reform (section 3).

1.2. Austrac Group

i. Austrac is a private company operating in locomotive maintenance since 1995 and as a rail freight provider in NSW since October 1997. It is based in Junee in Southern NSW. Its primary business focus is agricultural freight from the surrounding Riverina region, and prospectively other equivalent NSW regions. Austrac runs trains between Melbourne and Sydney (in partnership with V/Line) which link with Riverina branchline services. It also runs a metropolitan shuttle train in Sydney linking terminals and ports.

ii. Regional freight is typically for export, sourced from customers on branchlines, is of low to moderate volumes, and is of medium to high densities. Typical cargoes include wine, stockfeed, frozen meat, magnesite, grain, and timber.

iii. The Riverina area was virtually abandoned by the incumbent intra-state rail service provider and Austrac's developing business is being won almost exclusively from road transport. Service frequency, reliability and flexibility are important to these customers.

1.3. Capricorn Capital Limited

i. Capricorn has provided Austrac with early stage funding and advisory assistance including strategic planning and micro-economic modeling.

1.4. Costs

i. Austrac provides for the operating cost data for an efficient private rail freight company at an early stage of marketplace development. Modeling has been used to establish pricing, plan capital expenditure, assess the viability of investment in track infrastructure, and assess the relative competitiveness of road and rail on specific freight tasks.

ii. Detailed modeling of rail costs demonstrates that under current track access pricing, rail transport is an effective competitor to road transport. For a range of typical agricultural freight tasks rail is more efficient than road transport by between 30 and 70 per cent. Determining task factors include:

a) base load volume;

b) level of road congestion at origin/destination (e.g. at ports);

c) cargo density;

d) distance to rail line of origin/destination; and

e) trip distance.

iii. Our assessment is that no direct subsidy is required to support rail freight service providers. Policy-makers should be aware that rail freight providers can be developed effectively from start-up – even in markets that incumbent providers had abandoned.

2. Infrastructure

2.1. A level playing field between road and rail

i. Current rail access charges in NSW are intended to cover the full cost of track maintenance. These charges currently represent about 20 per cent of rail freight operating costs.

ii. Competitive neutrality with road transport would require a similar basis to be created for road freight user charges. Full recovery of maintenance cost would require an estimated five-fold increase in charges. This would improve the relative competitiveness of rail to road for marginal freight tasks, for instance on moderate density cargo or when the distance of the origin/destination to the rail line is a significant factor.

iii. Australia's leading independent pavement deterioration experts suggest the relationship between vehicle mass and pavement damage is a quadratic function. This implies that a loaded B-Double (gross approx. 60 tonnes) causes 600,000 times the damage of a family car.

iv. Further gross load limit increases suggested by the road lobby should be strenuously resisted as a further 5 per cent increase in gross mass results in a 20 per cent increase in pavement damage.

2.2. New expenditure

i. Relatively small but targeted investments on the track infrastructure, for instance between Sydney and Melbourne, will have a significant impact on trip times and operating efficiency – i.e. achieve best bang for the infrastructure buck.

ii. The trip includes a number of features of particular concern including:

a) sections of track without constant electronic signaling (e.g. Wallendbeen-Harden and Medway-Exeter) result in significant delays;

b) bridges requiring refurbishment necessitate slow speed limits at hill bases increasing fuel costs and causing significant delay at following ascending track portions;

c) train path scheduling is haphazard, especially near metropolitan areas, causing delays of up to 4 hours; and

d) low load restrictions in Victoria between Shepparton and Wadonga, which reduce the overall capability of the Sydney to Melbourne line.

iii. Based on a 12 hour original trip-time and current crew, fuel, insurance and maintenance costs, a 2 hour reduction in the Sydney-Melbourne journey would result in an operating efficiency improvement of above 4 per cent. Consistent axle loadings would also generate an efficiency gain of an additional 4 per cent.

3. Competition

3.1. Current market situation

3.1.1. FreightCorp and NRC

i. Major government providers apparently operating without commercial discipline.

ii. Although aspects of their performance provide opportunities to competitors they are also capable of anti-competitive behaviour due to:

a) an ability to price below economic cost; and

b) control over unnecessary quantities of locomotives and rolling-stock and essential supporting assets including terminals.

iii. Sub-economic returns resulting from freight rates set by National Rail undermine the capability of start-ups like Austrac to raise equity.

3.2. Reform

3.2.1. Efficient Common-User Framework

i. The experience of Austrac has highlighted the extent to which the regulatory and technical framework of the rail industry has evolved in an environment of un-commercial monopoly producers.

ii. Establishment of an effective common-user market structure will require reform not only of the track access regime (already successfully achieved), but also of the systems, procedures and regulation by which rail freight providers interact with regulating agencies. Examples where improvements would significantly improve efficiency include insurance, communications, safety-related issues and scheduling. These improvements would amount to the development of service principles within the rail industry bureaucracy.

3.2.2. Inter-governmental regulation

i. Inconsistencies between state regulations inhibit cross border operations and therefore competition. An example of a banal but to-date prohibitive obstacle is the different radio requirements between NSW and Victoria.

3.2.3. Conversion of government equity to debt

i. One option which would enforce commercial behaviour in government-owned rail operators is conversion of government equity to debt, and subsequent privatisation of the debt. This is similar to the method used to achieve a level of commercial discipline over ANL.

3.2.4. Privatisation

i. SA, VIC and WA governments have attempted to maximise the sale price of their respective rail freight businesses by bundling assets. However, if the Federal Government and NSW Government adopt a similar strategy it will compromise optimal competitive development.

ii. National Rail and FreightCorp have extensive terminal, locomotive and rolling stock assets surplus to required capacity. Sale of excess standard gauge capacity and transfer of strategic terminal assets to access manager prior to privatisation will promote the development of regional players.

iii. The likely final form of the marketplace is of:

a) two major standard gauge providers operating nationally based around the current National Rail and FreightCorp assets; and

b) a small number of regional providers whose operations target agricultural rather than inter-state cargo.

iv. The regional players in alliance provide a capability to maintain competitive pressure on the larger operators.

Andrew Buckland

Executive Director

14 October 1998