



---

# **Railway privatisation through concessions**

**The origins and effects of the  
experience in Latin America**

*A report for the International Transport Workers' Federation*

*Brendan Martin*

*With the research assistance of Ana Beatriz Urbano*

*Public World, 2002*

## **Table of contents**

<b>1. INTRODUCTION</b>	
1.1 The scope and purpose of this report	page 1
1.2 Summary of trends and of this report's findings	page 2
1.3 Patterns of structural change in railways	page 4
1.4 Problems of state ownership and driving forces of restructuring	page 5
1.5 The IMF, World Bank and structural adjustment	page 7
<b>2. CONCESSIONS: THE MAIN FORM OF RAILWAY PRIVATISATION</b>	
2.1 Why concessions are the main form of railway privatisation	page 9
2.2 Restructuring as the basis for concessions	page 10
2.3 The mechanics of concessions	page 11
2.4 Examples of concession contract arrangements	page 12
<b>3. THE EFFECTS OF CONCESSIONS</b>	
3.1 Impact on public finance and investments	page 13
3.2 Impact on freight and passenger services	page 15
3.3 Impact on safety	page 18
3.4 Impact on employment and workers	page 19
3.5 Impact on governance	page 21
<b>4. THE BRAZILIAN EXPERIENCE OF RAILWAY PRIVATISATION</b>	
4.1 Origins of the Brazilian railway	page 22
4.2 State ownership	page 23
4.3 The privatisation process	page 23
4.4 Investment and governance	page 25
4.5 Changes in freight and passenger loads	page 25
4.6 Safety on the railway	page 26
4.7 Employment, terms of employment and retrenchment	page 27
4.8 The future	page 28
<b>5. CONCLUSIONS AND LESSONS</b>	page 28
References	page 31

## **INTRODUCTION**

### **1.1 The scope and purpose of this report**

The 1990s were marked by 'the reemergence of private railway operation in developing countries after half a century of nationalization and public sector management,' declared a World Bank report in June 1999.<sup>i</sup> In countries which are World Bank clients, the predominant form of privatisation has been the transfer of responsibility for services and infrastructure investment to private businesses, on the basis of long-term concessions. The World Bank has itself been more responsible than any other international agency for the trend, both through its advocacy of the policy and its insistence upon its implementation as a condition of support for much-needed investment and restructuring in transport.

This report, commissioned by the International Transport Workers' Federation (ITF) in June 2001 following discussions at the ITF Railway Workers' Section Conference held in Durban, South Africa, in October 2000, focuses on the experience of such concessions in Latin America. It focuses on Latin America because it was there – in Argentina – that the first major modern experiment in railway concessioning in a 'developing'<sup>iii</sup> country was undertaken with World Bank support, and because other Latin American countries have followed the example to a greater degree than has occurred elsewhere.

As well as being the region where most of the rail concessions have taken place, Latin America is the region where the involvement of the World Bank in railway concessioning has been best documented, not least by the World Bank itself. However, the information in this report has significance for other parts of the world, not only because of a general global tendency towards policy convergence in the public services field – a convergence encouraged and engineered by international institutions, including the World Bank -- but also because the World Bank itself points to Latin American experience as a source of inspiration and knowledge for countries elsewhere.

The report examines the experience of Argentina and Brazil, and to a lesser extent that of Mexico, in some detail. It attempts to explore the positives as well as the negatives of privatisation through concessions, but concentrates on the negatives, since these have been relatively under-reported hitherto. The positives have already been widely discussed in and promoted through World Bank literature and in policy documents and reports from governments and private operators themselves. The intention in addressing the subject from a more sceptical point of view is not to provide an unbalanced picture but rather to contribute to the correction of the existing imbalance.

It is hoped that the report will help ITF affiliates not only in Latin American countries but also on other continents to evaluate the experience and develop their policies and strategies for dealing with the privatisation trend. The aim is to enable affiliates to engage with railway privatisation from a better informed standpoint and assist them in their efforts to encourage governments, employers and international institutions to work in partnership with railway workers and their unions to develop participatory approaches to the restructuring and modernization of railways.

The report seeks to build upon and complement an earlier Public World report for ITF, *Structural Adjustment and Railway Privatisation: World Bank policy and government practice in Ivory Coast and Ghana*, published in October 1997. This report does not supersede the earlier one, but is a companion to it. The experience explored and analysis undertaken in the earlier report remains of relevance to ITF affiliates, and especially to those in sub-Saharan Africa (although the experience of Latin American countries dealt with in this report probably has greater relevance for South Africa). The outline of World Bank policy provided in the earlier report is not repeated here, but remains pertinent to the subject.

In accordance with the limitations of the project's budget, this report draws mainly upon published sources, although some original material from union sources has also been used. Much of the information in the report is drawn from studies published by World Bank, which has not only facilitated much of the experience described but has also monitored and reported on the effects much more than any other official or academic institution has done.

## **1.2 Summary of trends and of this report's findings**

The past decade has witnessed a continuation of a worldwide trend towards privatisation of public services which began in the 1980s. In rail (and in utility services such as electricity and water supply), the predominant form of privatisation has been long-term concessions to private companies. These are, typically, consortia linking transnational (often US-owned) firms which specialize in the rail sector with banks and with local businesses. The latter, typically, are companies whose major interest is in products carried by rail. The concession terms typically pass to the private companies responsibility both for the development and maintenance of infrastructure and for service operation and billing, while formal ownership of fixed assets remains with the state.

Latin America has led the way internationally in railway privatisation through concessions, with Africa next. Eight Latin American countries – Argentina, Bolivia, Brazil, Chile, Costa Rica, Guatemala, Mexico and Peru – developed private rail concessions to one extent or another in the 1990s. 'Developing' countries have not been alone in taking the privatisation route. Japan, New Zealand and the United Kingdom are among Organisation for Economic Cooperation and Development (OECD) countries to have introduced private ownership and management into their railway in one form or another. In the European Union, the trend is likely to accelerate as the terms of the European Commission's Directive 91-440 take increasing effect, because they require national networks to be structurally separated between infrastructure, freight and passenger services and opened up to cross-border participation.

Even so, if the World Bank's 1999 report cited in the first paragraph of this report is followed ten years later by a survey of international developments during the present decade, the picture it presents is likely to be rather more complicated than simply a continuation of the 'reemergence' of private operation. Many concession contracts awarded during the 1990s are currently being renegotiated as governments, private operators, freight customers and passengers experience the mixed blessings of private finance and operation. The aim of reconciling the public interest with the commercial interests of the companies involved through contract design and regulation is proving far less straightforward to achieve in practice than on paper.

This is not least because the definition of the 'public interest' remains in dispute. The World Bank and other international institutions remain committed to the development of infrastructure services, such as the railway, as servants of an approach to economic and social development predicated on expansion of export-orientation in a context of increasingly liberalized world trade. That is the route to economic growth and poverty alleviation, they insist; national and local economies need to adapt to it, and the idea behind more market-orientated provision of rail services is to provide better infrastructure for such development. This involves giving priority to the provision of transport infrastructure and services suited to the needs of big transnational producers of main export commodities, rather than enabling small and medium-sized producers to develop local markets more effectively. This priority is reflected in the uneven results of privatisation through concessions.

There is no doubt that large-scale investments and significant efficiency improvements have followed privatisation in some cases, and that, in some countries, it has been possible, through the concessions, to renovate parts of the railway infrastructure while relieving governments and taxpayers of the burden of subsidizing continually loss-making operations. That has been by no means an invariable result, however, and even insofar as it has been achieved, the social cost has been a heavy one.

In particular, the experience so far is reinforcing the conventional wisdom that, while parts of railway networks can be run profitably, other parts (and networks as a whole) require public subsidy, whether or not services are privatised. The alternative is to allow loss-making but socially and/or economically valuable services to collapse, as has tended to happen with inter-city passenger services in Latin America, or to raise fares, as has tended to happen in urban commuter services. In general, while freight service concessions involve the payment of fees by the companies to the state, passenger service concessions require subsidies to be paid by the state.

Concessions have undoubtedly been associated with some cost reduction, mainly through job losses, which have occurred on a very large scale. In the Latin American countries which are the main focus of this report, direct railway employment has typically been reduced by 75 per cent, and World Bank finance has been decisive in enabling this to happen. Some new jobs have been created, but in the main these have been with contractors and sub-contractors. It is not clear to what extent these new jobs have compensated for the lost ones, or how the terms and conditions of employment have changed as a result of contracting-out. Those are among many important topics that would warrant a larger research project.

The impact on remaining railway workers appears to have varied, reflecting variety in availability of skills, union strength and other factors influencing labour market conditions. There is strong anecdotal evidence (supporting intuition as to what might be expected following such large-scale job losses) of intensification of workload, and of some decline in health and safety as a consequence. The impact of privatisation on safety in general appears, however, to have been variable; there are instances of improved safety thanks to better management systems and/or new technology, but there is also clear evidence in other cases of deterioration.

### 1.3 Patterns of structural change in railways

Although many railways began life under private ownership, most were state-run during the second half of the 20th Century, and for good reasons. Private ownership proved incapable of developing freight and passenger services in ways needed either to serve the economy as a whole or to meet social need. The scale and direction of the capital investment required and the natural monopoly character of the railway were among the factors leading to state ownership and operation as a condition of planned strategic development.

'The low rolling resistance of steel wheels on steel rails made railroad transportation extremely fuel efficient and relatively cheap,' according to one account, published by the World Bank, which adds: 'This allowed railroads to rapidly grow as the first mass transportation system, particularly for passengers, beginning in the years of the industrial revolution. For military and industrial reasons, most countries envisaged some form of public control, and many imposed their control by legal mandate.' This model of development having served the advanced industrial countries well, other countries emerging later from colonial rule and intent on establishing national economic as well as political independence tended to follow suit.

The same World Bank account continues: 'Public control over the rail industry occurred both with or without accompanying subsidies, public service obligations to transport providers in the form of compulsory (often unprofitable) routes, organized timetables, and particular services for strategic products or areas. The ultimate reason behind this control, which remains the same today, is that this industry is regarded as an integral mechanism to overcome geographical barriers in certain areas, to aid in the economic development of undeveloped zones, and even to guarantee minimum transport services for a particular segment of the population.'<sup>iii</sup>

The organizational structure through which the state has exercised its stewardship of the railway has varied. In some countries, the railway has been managed directly by a government department, while, in others, more or less autonomous enterprises, reporting to government, were established. 'During the past 50 years, the most common market structure in many countries' rail sectors was a single, state-owned firm, entrusted with the unified management of both infrastructure and services,' according to the World Bank account. 'Despite some differences in their degree of commercial autonomy, the traditional methods of regulation and control of this sort of company have been relatively homogeneous. In general, it was assumed that the monopoly power of the national company required price and service regulation to protect the general interest. In addition, the companies were obligated to meet any new demand at those prices. The closure of existing lines or the opening of new services required government approval. Thus competition was rare and often discouraged, and preservation of the national character of the industry was considered the key factor governing the overall regulatory system.'<sup>iv</sup>

In the 1990s, this began to change. Since Argentina's Rosario to Bahia Blanca line was turned over to a private concession in 1991, railway privatisation has occurred in at least 13 other 'developing' countries, as well as in the rest of Argentina's railway network. 'Another six rail projects reached financial closure during the first half of 1998, and the trend toward private contracting is expected to continue,' the World Bank forecast.<sup>v</sup>

Latin America leads the way, with Africa not far behind. The World Bank's Private Participation in Infrastructure (PPI) database shows that eight Latin American countries have awarded a total of twenty-six railway contracts to private companies, and this amounts to more than 80 per cent of the global total. 'One reason for Latin America's dominance in private railway projects is the region's positive experience with private participation in other infrastructure sectors,' says the World Bank, although the extent to which privatisation of water and electricity supply has been a 'positive' experience is certainly debatable. 'Many Latin American governments have gained experience in concessioning through private participation in electricity, telecommunications, and water and sanitation.'<sup>vi</sup>

Another study comments: 'After 1988, country after country in Latin America announced plans to privatise airlines, telephone companies, electric power companies, or gas and oil companies; more surprisingly, they implemented these plans at a mind-boggling pace. Within the five year period 1988-93, six of these countries privatised their telephone companies, nine divested their flag carriers, and between two and four privatised firms in the electric power, railroad, and water sectors. Argentina went the farthest in the shortest time.'<sup>vii</sup>

Although further privatisation projects have been initiated since 1998 – in Zambia and Zimbabwe, for examples – it is not clear that the trend will continue at the same pace as before. Indeed, judging by the evidence of the World Bank's PPI database, the trend has slowed down over the last three years, with fewer new projects during that period than in the three years before that. On the other hand, judging by the accounts of delegates to the ITF railway workers section conference in October 2000, it seems that an increasing number of governments is embarking on railway restructuring. Since privatisation through concessions is the predominant form of restructuring worldwide, it seems possible and even likely that the trend will accelerate again.

In any event, lessons will have to be learned from the experiences of the 1990s. If there has been something of an hiatus in the trend, it could well be because of some of the consequences in countries which took the privatisation route in the 1990s, some of which are described in this report. The results have been mixed, but it is fair to say that, while they have included many of the negative consequences for labour that were feared, they have not brought all the positive consequences for economic and social development that were promised.

If that is the case with the better examples, the truly catastrophic experience of rail privatisation in the United Kingdom, despite efforts on the part of privatisation advocates to explain it away as a good idea badly executed, might also have introduced a note of scepticism into the minds of policy makers in other countries. Many are asking whether privatisation really does provide the best and most cost-effective route to rehabilitation, efficiency and service quality claimed on its behalf, and, if it can, how the private operators can be regulated to make sure that they deliver in ways compatible with safety, local economic development, social amenity and other aspects of the public interest.

#### **1.4 Problems of state ownership and driving forces of restructuring**

It is by now well known that the role of the state in economic and social development came under increasing challenge following the oil price shocks of the 1970s and

development of financial, debt and budget deficit crises in many countries in the 1980s. These developments increased the dependence of many countries on international financial institutions and coincided with the emergence – especially in the United States, and, crucially, therefore, in the international institutions dominated by US policy – of an unprecedented faith in the capacity of neo-classical economics to provide the answer to any public policy challenge.

A policy package including cuts in public spending and privatisation of public services – elements of the so-called 'Washington Consensus'<sup>viii</sup> – became a standard component of the conditions which those institutions, chiefly the International Monetary Fund (IMF) and the World Bank, attached to the loans and other financial assistance offered to client countries. This contributed to chronic under-investment in railways, the effects of which – exacerbated by other trends, such as urbanization, which increased pressure on transport infrastructure in many fast-growing cities – helped to provide the rationale later for privatisation as the only affordable way to access the required investment and management skills to reverse the decline of railways.

Lack of investment and growing demand for transport services in cities were not the only problems faced by railways. In former colonial countries, they were also disadvantaged by the circumstances of their original design. The Argentine rail union Sindicato la Fraternidad has explained many of the problems of the railway in that country in terms of the colonial circumstances of their origin, an issue of relevance throughout Latin America and Africa. 'As can be imagined,' the union has pointed out, 'those British and French railways in Argentina, originally created as extractors of agricultural riches to be transferred to the markets of Europe, were structured from the port to the interior. The design of this industry never reflected the need for tracks to connect, unite and integrate the country's vast national production areas.'<sup>ix</sup>

The same union account points out that, from the 1960s onwards, there was insufficient investment to enable the Argentine railway to effectively carry out even the limited role for which they had been designed, and this, too, was an experience shared by other countries. Instead, investments were made in roads, and competition from other modes (air as well as roads in some countries) has been one of the factors in rail's loss of market share. The policies and corrupt practices of military dictatorships in Argentina and other countries featured in this report did not help matters. 'The background to the process of restructuring the railways in Argentina boils down to the typical syndrome of centralized bureaucratic superstructures in a country in which a lack of political objectives has been a characteristic feature since the mid-50s,' as the Argentine union puts it.<sup>x</sup>

As a result of these and other factors, Argentina's railway – and, again, this experience was shared by other countries -- had been in decline for more than two decades before they became, in 1991, the first model of rail privatisation engineered by the World Bank. From 1965 to 1990, there was a 25 per cent decline in inter-city passenger services, and a 35 per cent decline in the Buenos Aires metropolitan services. Freight services dropped even more, by half over the same period. Both passenger and freight services lost market share relative to other modes from 1970 to 1989, and for the last 15 years of that period, the wage bill alone of the state-owned enterprise concerned, Ferrocarriles Argentinos, exceeded its revenues.

This latter fact reflected the reality that, while governments became less and less able to invest in their railways, many also used them as a source of employment to avoid increasing social unrest and for patronage purposes. The strength and long histories of labour unions in railways was significant in dissuading governments from dealing with their problems by cutting rail labour forces, but neither did governments invest enough to make maximum use of the knowledgeable and experienced workforces they had built. By 1990 in Argentina, to persist with that important example, more than half of the total network was reported to have track in bad or fair condition only, and nearly half of the total locomotive fleet was out of service. Services were also heavily subsidized, and as governments sought ways to cut fiscal expenditure, their involvement with loss-making railways was bound to come under close scrutiny.

The World Bank has reported: 'Under this protective environment, most national rail companies incurred growing operating deficits during the 1970s and 1980s. Furthermore, social obligations to their staffs made it nearly impossible to reach any agreement on redundancies or even wage adjustments. In some countries, the companies were forced to finance their deficits by borrowing, so their accounts lost all resemblance to reality. The main problems associated with the traditional policies for rail were (a) increasing losses, which were usually financed by public subsidies; (b) a high degree of managerial inefficiency; and (c) business activities oriented exclusively towards production targets rather than commercial and market targets.'<sup>xi</sup>

In the end, the problems had to be tackled. Not only were their huge investment backlogs, but new technology (in the computing and telecommunications fields, as well as containers) was emerging with potential to greatly improve services and/or cut costs. These new possibilities remained beyond the reach of railway enterprises burdened by massive losses, while major business interests demanded faster, cheaper and more reliable freight services and commuter passengers demanded similar improvements. Clearly, in all the circumstances, something radical had to be done.

### **1.5 The IMF, World Bank and structural adjustment**

The nature of what has actually been done has been shaped in part by the fact that economic problems that produced the growing crises in railways in many countries also increased their dependence on the international financial institutions. IMF stabilisation programmes and World Bank structural adjustment programmes had contributed to the inability of governments to invest sufficiently in rail and other areas of public services, since they insisted that public expenditure should be cut rather than increased. Later, the same institutions insisted upon privatisation as a condition of their support in arranging investment to overcome the problems they had helped to create.

As one account has noted: 'At the same time, many Latin American countries were going through severe economic stabilisation and structural adjustment programs that required significant austerity measures and tight fiscal policies. As a result, expenditures on infrastructure development were slashed. By 1993, many of these countries were unable to provide for even the most urgent infrastructure needs. ... Therefore, for reasons of both improving efficiency and alleviating the pressure on public funds, many Latin American countries have chosen a privatisation-concession approach for infrastructure operations.'<sup>xii</sup>

According to the World Bank: 'Governments were keen to transfer the risk of this investment to the private sector, and private sponsors were willing to assume the risk under credible contractual arrangements of sufficient duration – ten to fifteen years where the operator invested only in rolling stock, but up to ninety years where the track required substantial restoration.'<sup>xiii</sup>

The World Bank's role has been not only to contribute to the problems which privatisation is supposed to solve and to enforce privatisation (thorough loan conditions) as the solution. 'Multilateral organizations were also a significant source of infrastructure financing in Latin America,' another account points out. 'Over the 1971-1993 period, the IADB (the Inter-American Development Bank) committed an annual average of US\$1.8 billion for infrastructure projects.' In the 1990s, the World Bank increasingly tied its assistance to privatisation: 'The IFC (International Finance Corporation), the private sector financing branch of the World Bank, also took an aggressive approach to private sector infrastructure investments. In 1993, its lending and investment in that sector worldwide grew to US\$330m, which was leveraged to finance up to US\$3.5 billion of infrastructure projects. ... Worldwide, IFC's investment projects represented between 15 per cent and 25 per cent of all private investment in infrastructure, which was estimated between \$14 and £20 billion a year.'<sup>xiv</sup>

This focus on privatisation-linked investment in infrastructure, including railways, grew throughout the 1990s. As another of the many World Bank accounts of the experience puts it: 'The 1990s saw a dramatic increase in the liberalization of transport policies and a strengthening of the role of private operators and investors in transport infrastructure worldwide. This increased private sector participation has often reflected changing ideologies about the role of the state and dissatisfaction with publicly provided services. The main driving force behind it, however, generally has been the pressure to look for private financing imposed on governments by lasting fiscal crises. This change in the financing of the sector is also providing an opportunity to restructure it in an attempt to improve its efficiency and sustain these improvements.'<sup>xv</sup>

Another World Bank study adds: 'Most of the railway projects are in countries with a long history of rail transport, often with early private involvement. Heavy financial losses and poor operating efficiency prompted governments to consider (or reconsider) private sector approaches. The deficiency in government investment led to interest among freight customers in taking over the networks, and the potential for reliable revenue encouraged sponsor support.'<sup>xvi</sup>

To realize that potential, however, the private 'sponsors' (a term which implies charitable rather than commercial interest, but the term by which the World Bank routinely refers to the companies which form concession consortia) need costs and, especially, workforces to be cut. That is why it has been in the railway sector that the World Bank has developed a new area of its technical assistance – the direct financing of workforce reductions in preparation for concessions. Without this, the 'sponsors' could not have been offered 'credible contractual arrangements'. In this and other respects, the extent to which the 'sponsors' have actually absorbed risk is limited. In reality, much of the financial burden has been left with the state.

## **2. CONCESSIONS: THE MAIN FORM OF RAILWAY PRIVATISATION**

### **2.1 Why concessions are the main form of railway privatisation**

Concessions are the chief form of railway privatisation. According to a World Bank account based on projects recorded in its PPI database: 'Concessions that are for managing and operating existing railways and involve major capital expenditure by private sponsors are the dominant form of contract for private participation in the rail sector, accounting for twenty-two of the thirty-seven projects (listed on the database).'<sup>xvii</sup>

Another World Bank study comments: 'Few railways have been truly privatised, beyond such recent examples as New Zealand, Canadian National, East Japan, Conrail in the United States, and the infrastructure and freight services of the old British Rail. Instead, most governments have preferred to concession (franchise) their railways. Why concessioning is usually preferred to privatisation is probably that governments believe that concessioning offers them the best of both worlds: they retain ultimate control over the infrastructure (at least in the political sense), while the private sector carries out the operating functions and competes for customers.'<sup>xviii</sup>

That explanation for the concession being the leading form of railway privatisation is unconvincing. Certainly, by retaining ownership of infrastructure, governments are able to claim that they retain control. They are thus better able to sell the policy politically to sceptical voters and rail workers, by claiming that it does not facilitate recolonisation of their countries' assets and that they remain in command. Some even maintain that concessions do not amount to privatisation at all, but rather to a partnership in which the advantages of state ownership can be combined optimally with those of the commercial incentives, access to investment capital and new technology, and management techniques of the private sector.

However, another compelling reason for privatisation being accomplished through concessions could be that the private sector does not actually wish to take over ownership of the assets concerned. If they did so, they would absorb much more risk than is the case with concessions, and the risks would include those associated with transferring to their balance sheets the value of assets in poor and uncertain condition. In general (the UK experience is the exception), ownership of fixed infrastructure has remained with the state, although concessions typically involve some private investment in parts of the infrastructure as well as privately operated services.

Another reason for the preference for concessions in the rail sector could be that there is a history of the arrangement in the sector. According to the World Bank: 'Rail concessioning is not new. Many railways were originally built and operated as concessions, and if not for the wave of public ownership (especially strong in countries undergoing decolonization) after World War II, many would never have been publicly operated.' That is clearly a tautology, but it has a purpose: to encourage the idea that public ownership has been a short-lived aberration and that the concessions trend means normality is returning.

However, the World Bank is by no means alone in regarding privatisation as inevitable. An International Labour Organisation (ILO) study has stated: 'The process of rail concessioning restarted in the early 1990s in Argentina and the UK, and in the early

measures taken by the European Commission. The success of these early attempts, combined with the lack of credible alternatives, has led to its rapid spread in Latin America. Concessioning is also beginning in Africa, the Middle East, and tentatively in Asia. A similar process, partly based on concessioning/franchising, and partly based on privatisation, has taken hold in several EU countries.<sup>xix</sup>

Another study published by the World Bank has suggested that the advantage of the concession arrangement is that it enables government regulation more effectively than do other privatisation approaches. 'Concession contracts allow the cushioning of some of the negative effects that may arise from the private company's actions,' it states. 'Thus, establishing maximum prices and minimum service levels, so that impact on equity can be minimized, is habitual.'<sup>xx</sup> It adds that concessions 'have been the favored form of restructuring because it allows the government to retain ultimate control over the assets, while the private sector carries out day-to-day operations according to prespecified rules devised in a contract, which transforms the problems associated with traditional regulation into issues of contract enforcement.'<sup>xxi</sup>

In that context, the fact that it has become the norm for concession contracts to be renegotiated at the companies' insistence two or three years into 30-year deals is clearly significant, since it undermines much of the original rationale for the arrangement.

## **2.2 Restructuring as the basis for concessions**

A prerequisite of rail concessions is the separation not only of infrastructure from operations but also of one type of service from another, so that they can be concessioned separately. One of the reasons for this is to enable profitable or potentially profitable services to be concessioned separately from loss-making services, which can also be concessioned but with guaranteed state subsidies. In preparation for concessioning, it has been particularly important to separate freight from passenger services and to divide passenger services between inter-city services and commuter services (the latter often including metro subway operations). In the main, responsibility for passenger services has been decentralized as part of the restructuring exercise, but the provinces or municipalities concerned usually lack the resources to subsidise them, with the result that many have collapsed.

A wide range of other restructuring measures have also been necessary preconditions to privatisation of all types, since private operators prefer the state to take much of the responsibility for, in particular, reductions in personnel. 'The changes have involved revising laws and other regulations affecting railways, reducing staff, dealing with pension issues, and deciding how much property the state should sell and how much it should retain. In addition, several arrangements for paying for unprofitable (but socially needed) train services were put into place, together with a precise definition of the concession contracts and their main terms.'<sup>xxii</sup>

Separation of infrastructure from operations, and disintegration of service networks into a number of separate corporate arrangements, can produce positive results by enabling costs to be more transparently visible and managerial authority to be decentralised. On the other hand, economies of scale and of scope can be lost, along with government capacity to develop rail as part of strategic transport development programmes. 'Often noted [as downsides of disintegration of networks] is that the relationship between the

services supplied and the rolling stock used, as well as the quality, quantity and technical characteristics of the infrastructure, is so close that both aspects need to be planned together,' one World Bank-published paper concedes.<sup>xxiii</sup>

Disintegration of railway networks can also impede passenger services by making through-ticketing more problematic and impose additional transaction costs through the contractual arrangements linking one inter-dependent company with another. Those disadvantages, and others, have certainly been experienced in the United Kingdom, where the approach to privatisation has indeed been unique, in that it has been the only example of both services and ownership of rail infrastructure having been privatised.

That represents one extreme end of the scale of restructuring that has taken place. In the 1980s, some countries restructured by passing responsibility to state-owned enterprises rather more at arms length from day-to-day political responsibility than when railways are managed directly by a government department. Many also divided their operations into cost- and profit-centres and some began to privatise delivery of some ancillary services, such as catering. Some went much further, contracting out (to companies which typically tend to sub-contract further) track maintenance and other operational activities which can have a major impact on delivery of the core service. This experience established examples of privatised management of services, a form of privatisation extended in some countries to the core service of running trains itself. That is the case with concessions, which in addition normally involve the private sector also in delivering infrastructure renewal on the basis of contracts with the state.

### **2.3 The mechanics of concessions**

The model for private participation in railways in Latin America involves separating passenger and freight services and awarding concessions either for both services or just for freight, with passenger services remaining with the state (but usually decentralized) in the latter case. Therefore, concessions are more common in freight than in passenger services and have normally been awarded to consortia linking domestic businesses – typically including major freight rail customers – with foreign (often US-owned) rail operators. The financial structure of the concession arrangements have varied. 'In most countries,' according to one account, 'almost all private infrastructure financing has been through direct equity participation, the placement of debt offshore, a few bank bridge loans, or occasional government guarantees.'<sup>xxiv</sup>

The concession arrangements have had both vertical (functional) and horizontal (geographic) dimensions. Argentina, Brazil, Colombia and Mexico set up regional companies; Chile set up four passenger companies and two freight companies with a separate infrastructure firm. The World Bank has noted, on the basis of information in its database, that 'in 76 percent of projects the government transferred the management of fixed assets and rolling stock to the private sector as a vertically integrated utility, introducing competition at the bidding stage,' while 'some governments have gone further, requiring concessionaires to open their network to competing operators.'<sup>xxv</sup>

The duration of concession contracts has also varied, with governments attempting to balance the greater competition and regulatory control enabled by short contracts (because of their earlier expiry) with the need for longer duration to encourage

investment. In Argentina, 30-year concessions were awarded for freight and 10 or 20 years for passenger services privatised later.

The nature of the process for evaluating rival bids has also varied. One factor in this has been that, while concessions for profitable services can be awarded on the basis of competition to pay the largest fee to the state, on loss-making services which governments choose to maintain because of their social or economic necessity or desirability, the competition is for the lowest subsidy. Sometimes the bidding process has been open, while in other cases some pre-selection of candidates has been preferred.

Criteria for selection can be led by priorities of government, attempting to balance wider objectives with financial factors. However, since pressures on public finance tend to dominate the reasons for privatisation, this consideration tends to influence selection of concessionaires and contract terms most strongly, even if other criteria are also taken into account. Argentina attempted to incorporate a wide range of objectives into the contracts and both quantitative and qualitative evaluation criteria. Bids for the six freight concessions were evaluated using the net present value of the fees to be paid to the government during the first 15 years of the concessions, the quality of business and investment plans, the staffing levels, the proposed track fee for passenger trains, and the share of Argentine interest in the consortium. When Argentina came to concession metro passenger services, the government simplified the award criteria substantially, focusing on minimizing subsidies. Similarly, 'Brazil successfully auctioned the six regional rail concessions to the highest bid above the government's minimum price. Concessionaires were required to make an up-front payment immediately after the auction, followed by a stream of predetermined payments over the life of the concession.'<sup>xxxvi</sup>

The obligations of concession companies to potential competitors or to other companies wishing to use the infrastructure managed by them have varied too. In Argentina, for example, while the freight concessionaires had exclusive freight rights on 'their' lines, they were obliged to make them available to state-run passenger services for an agreed fee. In other cases, concessions have begun with exclusive rights for the concessionaire on the basis of contracts enabling competitors to use the infrastructure after a certain number of years.

#### **2.4 Examples of concession contract arrangements**

Argentina's integrated network was broken up into three parts – freight, intercity passenger and metropolitan commuter rail (in Buenos Aires). The freight services were further divided into six regional vertically integrated franchises, more or less corresponding to the old private structure before nationalization in 1948. They were then concessioned to consortia linking Argentine and international businesses for 30 years.

The state remained owner of fixed assets – track and stations – and rolling stock, which were leased to the concessionaires as part of the contracts. Vertical integration meant that each of the six was responsible for all the activities involved – improvement and maintenance of fixed facilities such as stations and track, running train services themselves and marketing and financial control. In addition, the contracts required them to invest in upgrading the infrastructure in ways set out in the concession contracts. In return, the concessionaires were granted monopoly rights, except that, as mentioned

earlier, they were obliged to allow passenger services to run on 'their' track in return for a fee. They were allowed to run passenger services themselves, but not required to do so.

Intercity passenger services were transferred to provinces, which were given the option of either keeping services going with their own resources or closing them down. In reality, that has been no choice for provinces already under great budgetary pressure and most have been unable to sustain services, which have, therefore, been closed down. Those that did choose to keep services going had to enter into agreements with the freight concessions about track usage fees. Viability studies of the intercity passenger services had shown that only one corridor – that between the capital Buenos Aires and the popular seaside resort of Mar del Plata – could be run profitably.

Metropolitan services were concessioned through 10 year contracts (20 for the Buenos Aires subway system). Unlike the freight concessions, the award criteria were simple: the state specified the investment and rehabilitation plan required, and awarded the contract to the consortium that required the least subsidy in return. Unlike the freight concessions, therefore, under which the private companies paid fees to the state, these were so-called negative concessions, involving payments by the state to the concessionaires.

Argentina's concessions were all awarded by 1996, the year in which Mexico began splitting up its rail services into three regional companies, plus a fourth company serving the capital, and a few shorter lines. Each of the three regional concessions predominantly carry freight, and all were privatised by 1998. The state retained ownership of the infrastructure, but sold the three companies, with 50 year concessions which included responsibility for maintenance and future investment, and a 25 per cent stake each in the fourth company (the remaining 25 per cent being retained by the state).

The northeast concession was sold to a Mexican-US consortium called Transportacion Ferroviaria Mexicana (TFM) comprising the Mexican transport company TMM with Kansas City Southern of the US, which paid around US\$1.4 billion for the concession. The northwestern concession was also sold, for around US\$524 million, to a Mexican-US consortium, Ferrocarril Mexicano (Ferromex), comprising Grupo Mexico and Union Pacific. The smaller of the three was sold as Ferrocarril del Sueste (FerroSur) to a Mexican company, Grupo Tribasa, for around US\$322 million. Passenger services remained in state hands but have been drastically reduced. The major driving force of privatisation in Mexico has been to facilitate cross-border traffic at reduced cost in the context of the North American Free Trade Agreement (NAFTA), while forging international links has been a factor in driving privatisation elsewhere in Latin America too.

### **3. THE EFFECTS OF CONCESSIONS**

#### **3.1 Impact on public finance and investments**

According to statistics derived from the World Bank's database, the privatisations engineered through 37 projects in 14 developing countries up to 1998 involved plans for investment totaling US\$14 billion over the lifetime – up to 90 years – of the contracts. The extent to which concessions have delivered on such commitments has varied, and, so has the extent to which the public purse has been relieved of responsibility for providing investment finance.

In Mexico, according to a report of statements made at the Transporte Internacional conference held in Monterey, in that country, in 1999, the private operators soon 'began to invest hefty sums to improve infrastructure, operational procedures and information systems'.<sup>xxvii</sup> The head of one of the consortia said his company would invest US\$230m, concentrating especially on the development of intermodal yards in both Mexico and Texas (in a joint venture with Texas Mexican Railway, with which it is corporately linked). It is also investing in improved information management technology.

The other US-Mexican-owned consortium plans investment of \$218m, mainly in new equipment but also in infrastructure improvements, telecommunications and signals. It too has made a business decision to focus on intermodal capacity and improved information systems in response to the stated needs of its major freight customers.

However, things have not gone wholly according to plan in Mexico. One of the concession companies experienced financial difficulties very early on, requiring the state to increase the size of the residual stake it held in the business as a way of bridging the gap. Overall, however, the Mexican government estimates that its expenditure on rail has been reduced by US\$400m per annum.

A World Bank account of the Argentine experience records similarly mixed experience somewhat different from original stated intentions. 'The most immediate and painful change for the system as a whole was the reduction in employment from 92,000 workers to about 17,000 in 1998. Politically, this is still proving to be a tough sell mainly because the fiscal goals have not really been achieved as expected. In spite of the privatisation and reduction of the required public expenditures in the sector, the government is still spending US\$400 million/year in subsidies, in addition to a commitment to pay for US\$6 billion in investment over the next 20 years.'<sup>xxviii</sup>

However, the economic and financial crisis in Argentina has undermined the government's capacity to maintain subsidies, and this has hit the concessions' viability badly and contributed to their failures, in turn, to meet their obligations to the government. The Argentine freight concessions have, in fact, fallen behind with their payments of concession fees to the government, building up arrears of more than US\$15 million.

In Argentine passenger services, subsidies per passenger have fallen as passenger numbers have increased, but: 'The results are not that clear cut ... the mixed reviews have ended up in a 1998-99 renegotiation of most contracts. This stems from the fact that the extremely high expectations promoted at the time of privatisation have not been met.'<sup>xxix</sup> In addition: 'Private operators are asking for an increase in the current subsidy levels for the subway to cover operating expenses and some investment.'<sup>xxx</sup>

Some capital financing experts have pointed to intrinsic financial instabilities with concessions as sources of infrastructure finance. They point out that Latin American financial intermediaries have been geared almost exclusively to short-term lending, and rarely offer the long-term funds so essential for many infrastructure projects. Similarly, local capital markets are not developed enough to offer long-term funding. These factors have precluded a number of potential firms from participating in the process, thus

limiting competition. This in turn has driven up the price of capital, which is passed on in higher service prices.

As a result of these realities, most investment finance has been secured offshore in US dollars, exposing concessions (and, therefore, ultimately the state) to exchange rate risks. The difficulties this can cause have been thrown into sharp relief recently in Argentina, where the devaluation of the peso (which had previously been pegged to the dollar, on a one-to-one exchange rate) means that concessions whose fare revenue is in pesos are having to meet debt payments in dollars. This undermining of their financial position is sure to be passed on to the state – or else services will collapse as a result of bankruptcy - - although part of the rationale for privatisation is precisely to relieve the state of such burdens and risks.

### **3.2 Impact on freight and passenger services**

The incentives built into concessions mean that, unless subject to government subsidy, unprofitable services are abandoned. In the case of Mexico, for example, all 'less than full wagon-load' freight services were eliminated, as were entire routes with low volumes. The reduction in passenger numbers carried has been even more dramatic, as loss-makers disappeared. In Mexico, passenger numbers fell by 80 per cent in the first year.

The priority of the Mexican freight consortia has been to provide more efficient integrated transport facilities for large industrial customers – that is, in effect, the aim of the increased 'customer-orientation' urged on governments by the World Bank and other advocates of market-oriented restructuring approaches. For example, TFM, one of the US-Mexican-owned consortia in Mexico, claims to have increased daily capacity of an intermodal yard by more than double, and to have reduced transit times and speeds and reduced cargo thefts. The other major consortium in that country is making similar claims about the improvements its investments will achieve. What remains unclear is the impact these business decisions have had on smaller freight customers, but it is reasonable to suppose that they have lost out as a result of the re-orientation to the higher volume market sector.

Even so, some of the businesses the Mexican concessions are trying hardest to please appear not to be entirely pleased. According to Mexico's largest cement producer, CEMEX, privatisation was followed by 'interruptions in service, equipment shortages, and communications problems caused by software incompatibilities'. These problems became so severe that 'CEMEX was forced in many cases to divert shipments to barges and more expensive trucks'. In addition, there had been 'uncertainty in pricing', according to a senior CEMEX executive who was quoted as saying: 'Rates keep going up ... the railroads also keep changing their administrative and payment procedures ... we don't get notice of when the rates will go up, so we can't plan long term.'<sup>xxxix</sup>

He also reported problems arising from the break-up of the national network, pointing out that there was no consistency in the information systems between the private companies, which added to business customers' administrative costs.

Another large corporate customer agreed with the CEMEX verdict, according to the same source. An executive of one of Mexico's largest manufacturers of household appliances praised the private companies in some respects – highlighting improvements in transit

times – but criticized 'poor communications both internally and between railroads, slow response to customer requests, and insufficient attention to customers' needs'. He also mentioned equipment shortages and sudden rate increases as having caused problems.

World Bank studies acknowledge some such problems (though by no means all of them) but insist, nevertheless, that, on balance and overall, both financial efficiency and service quality have increased as a result of privatisation. One study of the Argentine experience supports its verdict with statistics produced by the country's economics ministry, which reveal steady growth in both usage and revenue after privatisation. (See Table 1.) The same account also refers to a survey which found that 85% of commuters believed services had improved after privatisation. 'Most service quality indicators have improved as demanded by the contracts,' says the study's report. 'The main outstanding issue is that many users are still unhappy with the stations ... but their improvement was not addressed that specifically by the contracts.'<sup>xxxii</sup>

**Table 1: Trends in metropolitan passenger numbers and revenue, Argentina**

<b>Line</b>	(millions of units)	<b>1993</b>	<b>1994</b>	<b>1995</b>	<b>1996</b>	<b>1997</b>
<b>Mitre</b>	Revenue (\$)	<i>34.41</i>	<i>38.29</i>	<i>53.48</i>	69.81	80.58
	Car-kms	<i>16.28</i>	<i>16.92</i>	<i>14.47</i>	21.70	24.16
<b>Sarmiento</b>	Revenue (\$)	<i>60.47</i>	<i>61.27</i>	<i>81.88</i>	99.37	111.51
	Car-kms	<i>20.28</i>	<i>20.68</i>	<i>17.92</i>	23.74	29.07
<b>Urquiza</b>	Revenue (\$)	<i>16.79</i>	<i>22.46</i>	<i>23.15</i>	24.72	24.95
	Car-kms	<i>8.53</i>	<i>9.24</i>	<i>9.68</i>	9.78	10.26
<b>Roca</b>	Revenue (\$)	<i>64.91</i>	<i>75.77</i>	<i>116.46</i>	136.02	147.03
	Car-kms	<i>25.97</i>	<i>33.80</i>	<i>38.90</i>	43.08	48.10
<b>San Martin</b>	Revenue (\$)	<i>21.68</i>	<i>29.33</i>	<i>38.03</i>	43.51	46.63
	Car-kms	<i>13.47</i>	<i>13.02</i>	<i>14.96</i>	15.62	16.78
<b>Belgrano N.</b>	Revenue (\$)	<i>11.81</i>	<i>14.78</i>	<i>25.37</i>	28.79	32.28
	Car-kms	<i>8.52</i>	<i>8.33</i>	<i>9.87</i>	10.53	12.96
<b>Belgrano S.</b>	Revenue (\$)	<i>2.02</i>	<i>4.10</i>	<i>8.32</i>	11.35	13.11
	Car-kms	<i>2.08</i>	<i>2.51</i>	<i>4.64</i>	6.35	6.88
<b>Subte</b>	Revenue (\$)	<i>145.32</i>	<i>171.15</i>	<i>187.22</i>	198.88	221.86
	Car-kms	<i>20.08</i>	<i>22.66</i>	<i>25.65</i>	26.76	30.02

*Source: Argentine economics ministry, as reproduced by Estache and Carbajo, 2000*

*Numbers in italics represent years in which the line in question remained state-run*

Analysis of the numbers in Table 1 suggests three reasons for caution in concluding from them that services have improved. Firstly, increased usage could be the product of commuters having little choice – despite the existence of bus services – but to use the services in question increasingly. After UK rail privatisation, usage also grew rapidly, but it did not represent passenger satisfaction so much as the effective monopoly status of the privatised services at a time of economic expansion and rising motoring costs.

Secondly, it is clear that revenue grew at a faster rate than usage, suggesting rapidly rising fares. And, thirdly, it should be noted that surveys of commuters are bound to exclude the verdict of others who have priced out of using rail services.

In fact, fares have risen by between 40% and 60% since the start of the concessions. 'From a financial point of view, private passenger services operations are having a clear impact. The burden of the costs is shifting from the government to the passengers,' as the

World Bank report has put it.<sup>xxxiii</sup> Again, the fact that more people were willing to pay higher fares could indicate the lack of real options rather than customer satisfaction.

In any event, the fact of the growth in demand has led the private operators to demand (successfully) higher fares and longer concessions. They say the latter are necessary in order to ensure they obtain a return on their investment, and they have had their contracts extended by up to 35 years as a result. In addition, they have been granted further fares increases of 80 per cent on average – between 50 and 100 per cent depending on the concession -- spread over four years. Compounded with the fares increases already enforced during the first five years of the concessions, this means that Argentina's metropolitan passengers will be paying around three times more for the same journey ten years into privatisation as they were paying when privatisation began.

As the World Bank drily notes: 'The process is hotly debated in Argentina and for the users exposed to the higher initial tariffs, the increase is likely to represent an increase in monthly travel costs significant enough to raise some concern.'<sup>xxxiv</sup> Certainly, according to the union Sindicato La Fraternidad, the rapid increases in fares has led to increasing numbers of fare dodgers.

In Argentina, freight carried by rail has shown a similar increase to that of passenger numbers, from 7.4 million tonnes carried in 1992 to 17 million in 1999. However, this again reflects in part general growth in economic activity over the period, a growth which has not been sustained more recently. Indeed, according to the economics ministry website, freight carried by rail declined by 7 per cent from 1999 to 2000, the latest comparison available, and the collapse of the Argentine economy since then would suggest a further sharp decline.

Even before the decline, the rail freight companies had failed to build their market share in comparison to other modes at the pace hoped for when the concessions began, failing to rise above 8% market share. Moreover, with only one exception out of the six concessions, the increases in freight carried were also below the commitments in the contracts. The concession process itself appears to have encouraged bidders to exaggerate what they would be able to achieve, as a World Bank study has acknowledged: 'The optimism in projecting demand levels, possibly induced by the bidding criteria used to award the concessions, may bear some responsibility for the gap between realized and expected traffic levels.'<sup>xxxv</sup>

As mentioned earlier, unlike in the case of the commuter passenger services, where consortia made their bids in relation to pre-specified levels of investments and service improvements to be carried out, in the case of freight the evaluation criteria invited them to compete with each other to promise more than their rivals. 'This criterion of selection undoubtedly may have induced the concessionaires to make demand projections and associated investment promises that were unrealistic but helped them obtain the concession,' the same World Bank study added.

With profits lower than anticipated, the concessionaires have failed to keep up payment of their financial obligations to the state under the contracts, and these have now been written off against new investment promises for the future. This is despite the fact that investment promises made at the time the concessions were awarded have also been broken.

It has not proved possible to obtain much information about the effect on inter-city passenger services in Argentina, not least because, as well as operational responsibility having passed from federal to provincial government level under the restructuring which accompanied privatisation, responsibility for monitoring and reporting on effects was also decentralised. In effect, national government simply washed its hands of responsibility for inter-city passenger rail travel. This has certainly placed considerable extra financial pressure on the provinces. Some have not been able to continue with services, which have therefore collapsed. Others have continued them but refused to pay the freight concessionaires the fees demanded from them on the grounds that the concessions have failed to meet their investment obligations.

As a World Bank study has noted: 'Passenger services need more maintenance than freight trains and freight concessionaires are reportedly not doing a particularly good job of maintaining the track at stipulated standards. In addition, the access fee that freight concessionaires charge the passenger trains may be too high compared to international standards (up to 10 times in some cases).' In effect, by refusing to pay so much, the provinces which have managed to maintain their inter-city services are passing financial responsibility back to national government level, since their non-payment of the access fees as demanded by the freight concessionaires is a factor (though by no means the only one) in the latter demanding renegotiation of their obligations to the state.

### **3.3 Impact on safety**

ITF affiliates have reported that safety often deteriorates after privatisation. In general, working conditions and health and safety have deteriorated, according to union representatives quoted in a report of a 1999 ILO symposium.<sup>xxxvi</sup> It was said that drivers were working longer hours for lower wages and that accident rates had increased because of fatigue. That verdict has been all too obviously and tragically borne out in the UK, whose catastrophes have been well documented and are beyond this report's scope. However, one of the reasons for the loss of safety in the UK system is important to mention here, since the causes stem from a structural change which has been replicated elsewhere.

In the UK, underneath the surface of 26 separate companies operating the infrastructure and service network following UK privatisation, the structure rests upon layers and layers of sub-contractors, each making money out of hiring the next down the food chain until, at the base – where the work is done and where the greatest strength is needed -- labour is casualised and individualised. So it is that, while it would appear that the privatised UK system has one infrastructure company, Railtrack, in fact it has more than 2,000, not including the self-employed labourers even further down the hierarchy.

The consequences of this casualisation and cheapening of labour – which was accompanied by a halving of the number of permanent staff employed in infrastructure maintenance – have been vividly described in the *Financial Times*: 'The first consequence was the breakdown of the old comradeship, which used to mean that problems were easily spotted, repairs made, and people could talk to each other. Track workers operated in gangs and knew their stretch of rails like their own back gardens. Instead, workers became nomadic, moving to the next job with little or no local knowledge and instructions not to talk to rival workers except via a supervisor miles away. The second big problem was a growing lack of control over the staff and their

work. There have been complaints of sub-contractors recruiting workers out of pubs to fill gaps on the night shift.<sup>xxxvii</sup>

It is ironic that a global business newspaper has addressed the relationship between employment standards and service quality and safety so vividly. Unions in Australia, Denmark and South Africa are among those to have reported similar problems to the ITF, albeit in less graphic terms. Their testimony shows, nevertheless, a clear relationship between increased use of contractors and deterioration in safety. Similarly, an Argentine rail union has noted that its members are reporting an increased number of workplace accidents because of inadequate qualifications and training. It points also to lack of company health and safety policies, and claims that the supervisory authority, which recently stated that 89% of companies do not comply with current legislation in this area, is 'largely powerless' to enforce standards.<sup>xxxviii</sup>

### **3.4 Impact on employment and workers**

The union testimony about the relationship between changes in status, terms and conditions of employment and changes in service safety and quality is supported by some business accounts. One of the complaints leveled at the privatised freight system in Mexico by its largest corporate customers, for example, was that too many personnel were inexperienced.<sup>xxxix</sup>

For the World Bank, very large cuts in railway employment and increased use of contract labour are not by-products but central aims of privatisation. Indeed, the increased use of contractor companies has been an aspect of the programmes the World Bank has funded to deal with the social cost of such large-scale retrenchments. In Argentina, for example, the World Bank-funded arrangements for retrenchments included provision of opportunities for rail workers to re-establish themselves as small businesses contracted to their former employers to provide various functions previously carried out by direct labour. In this way, what was in fact an imposed fundamental change in the status, terms and conditions of rail workers was dressed up as a socially benign project to soften the impact of job cuts. Moreover, such worker-run companies often do not last long following privatisation, because they are almost invariably under-capitalised and frequently lack the management skills to match their operational expertise.

The ILO has reported: 'Employment programmes for workers leaving the public sector did exist in Argentina but they were not always applied promptly. It was also true that there were some very imaginative solutions, particularly in rail transport where groups of workers were given repair workshops to repair machines. It was a way of outsourcing which started the autonomous workers off in a productive project.'<sup>xl</sup>

However, in practice, according to the union Sindicato La Fraternidad: 'The great majority first set themselves up in mini-undertakings which were unsuccessful because they were geared closely to the railways. This great majority is now unemployed. The state has never set up training programmes for workers who had been employed in the industry for 15 or 20 years. It is also true to say that what used to be a secure job is no longer secure, and that this has destroyed an identity in the case of our speciality, in which 70% of use were sons and grandsons of engine drivers.'

Such testimony must be taken into account when considering the extent to which the enormous job losses experienced in association with privatisation in Latin America have in fact been balanced by growth of employment opportunities with contractor companies and measures to enable retrenched personnel to find alternative employment.

As the ILO has noted: 'Railway restructuring has had a severe impact on the level of staffing of the companies involved ... For example, following the concessioning of Argentine Railways (FA), employment declined from 94,800 in 1989 to approximately 17,000 in 1997.<sup>xlii</sup> The impact has been felt particularly harshly in freight, according to an Argentine rail union, which has described the wider social impact in vivid terms. 'Many railway workers and other settlers have had to migrate to the major cities because the places they used to live in revolved around the railway lines. They have therefore become ghost towns, with closed schools, banks, shops, etc.'<sup>xliii</sup>

The scale of job loss associated with concessions in Argentina, enormous though it has been, is not untypical. In Chile, where there had already been a cut of 75 per cent in the railway labour force between the seizure of power by the Pinochet military junta in 1973 and 1990, the number was halved again in the course of privatisation from 1990 to 1995. Brazil's experience was similar (see Section 4 below), while in New Zealand, although traffic increased after privatisation, employment fell from 22,000 to 4,600.

Elsewhere, however, privatisation has been presented as a way of minimising the negative impact on labour of the decline of rail transport. In Kenya, for example, the preparatory phase for privatisation began in 1995 and involved a reduction from about 14,500 to 8,500 workers. 'Consequently the company was unable to sustain its fixed costs or to maintain its rolling stock,' an ILO report quoted the state-owned railway's managing director, Eric Nyamunga as telling a symposium. Cuts in employment had, thus, directly contributed to further decline, rather than revival, of the railway. 'As the government did not have money for subsidies, the railway had to privatise or face extinction,' the report went on. 'He (Nyamunga) understood that workers felt bad about the job losses, but those who had left the company had two assets – training and some money to start with. If the company was not privatised soon, it would fail and remaining 8,500 workers would lose their jobs.'<sup>xliiii</sup>

The impact of privatisation on earnings has been determined largely by labour market factors such as levels of supply of skills. Although privatisation has in some cases led to improved pay for some of the retained workforce (particularly if over-zealous employment reductions led to skills shortages), lower skilled workers or those with oversupplied skills have typically been casualised or suffered pay reductions. In Argentina, one union insists that wages, having failed to rise in the 10 years since the beginning of the privatisation process, have drastically lost purchasing power.

However, the full impact of variable labour market factors on the post-privatisation earnings of rail workers has been softened in cases where concession contracts imposed conditions about employment terms. According to the ILO: 'With regard to wages and other working conditions, employees do not necessarily lose since the wage rates of those employed before privatisation may be protected as one of the conditions of privatisation, e.g. through the negotiation of two-tier wage structures.'<sup>xliv</sup> In other words, lower wages are gradually phased in to overcome union resistance to privatisation, as occurred in Côte d'Ivoire.<sup>xlv</sup>

### 3.5 Impact on governance

The report by the Argentine Sindicato La Fraternidad, quoted earlier, to the effect that the regulatory authority there could not prevent companies ignoring health and safety regulations, highlights one of the principal flaws in the claim that the corporate interests of concessionaires can be reconciled with the public interest through the wording of contracts. Regulations, whatever their mechanics and their strengths on paper, are only ever as good as they are enforceable. Their enforceability is, in turn, a function of many factors, such as the extent to which investment is made in regulatory capacity, in terms of budgets, staff numbers, training, and so on. In addition, the World Bank literature acknowledges that, in rail, in Argentina in particular, there have been 'information asymmetries' between the companies and the state which have undermined regulatory enforcement. That is a technical way of saying that the companies deprive regulators of the information required to regulate them effectively.

A general increase in the use of commercial secrecy as a reason to deprive the state and society of information about railway company accounts has been noted by the *International Railway Journal*, which carries out an annual survey of investment. It introduces its latest attempt as follows: 'We have been publishing our unique World Polls of railway and rapid transit capital expenditure in one form or another since *IRJ* was first launched in 1960. We had hoped the World Poll would go from strength to strength with the collapse of the Iron Curtain and more recently with the advent of email and the internet. Unfortunately, railways are becoming more secretive, so despite bombarding them with faxes, emails and telephone calls, it has become more difficult to get the railways to respond.<sup>xlvi</sup> Research for the present report has been hampered by the same difficulty, which points to a growing loss of democratic accountability.

These information problems are contributing to a shift in the balance of power between concession companies and regulatory authorities, in favour of the former, and this is exacerbated by the very fact that privatisation is enabling companies to grow, while transferring much specialist knowledge out of the state into those companies. The balance of power shifts the more privatisation spreads. The ILO has noted: 'The last few years have also seen a rapid increase in the concentration of rail and road transport companies, as well as in the operation of transport concessions resulting from deregulation and/or privatisation. Transport companies are either investing in their own subsector and transforming themselves into multinational companies such as Wisconsin Central International, a railway company with operations in the US, Canada, NZ and the UK, or they are involved in various modes of transport, such as the British group Stagecoach, which runs bus, rail and airport operations. In 1997-8, it acquired bus and ferry operations in Australia and New Zealand and took a 49 per cent stake in the Virgin Rail Group. National Express is another British transport group acquiring interests in other parts of the world. Finally, "outsiders" have also demonstrated considerable interest in investing in transport operations. Virgin, ACCOR and VIVENDI can be cited as examples of this trend.<sup>xlvii</sup>

Yet, rather than helping to provide regulatory authorities with sufficient capacity to do their job effectively and ensuring that contracts are designed in such a way as to overcome the information gap, the World Bank urges renegotiation. 'Argentina's freight and passenger concessions have faced challenges despite their general success' states a

World Bank report. 'Initial demand projections proved too optimistic, and sponsors have been unable to fulfill their investment commitments. Argentina's experience highlights the importance of renegotiation or other adjustment mechanisms that allow concessionaires to remain in business without the government losing credibility.'<sup>xlvi</sup>

However, if it is true that contracts should be sufficiently flexible as to be renegotiable, it cannot also be claimed that the safeguards built into them at the time of privatisation can be regarded as reliable. The Brazil experience explored in the following section highlights that issue as well as many others raised so far in this report.

#### **4. THE BRAZILIAN EXPERIENCE OF RAIL PRIVATISATION**

##### **4.1. Origins of the Brazilian railway**

In common with other Latin American countries, Brazil's railway developed in the context of exploitation of natural resources for export in the late 19th and early 20th century. Having established its political independence from Portugal, 'during the 19th century, Brazil easily fitted into the world economic order dominated by Britain'<sup>xlvi</sup>. Brazil became, in fact, a 'typical example of such a country' in that its economy was dependent on one major primary export product (coffee) and a few others (sugar, cotton and cocoa), whilst being open to foreign (mainly British) manufactured products and foreign (mainly British) capital. That capital 'flowed into the country and was designed to build a financial, commercial and transport infrastructure that would link the country more efficiently into the nineteenth century world economic order'.<sup>1</sup>

However, the idea (promoted in some World Bank literature) that concessions rather than public ownership represent the natural and best order of things is undermined by the difficulties arising from the concession approach when railways were first developed. In Brazil, there were several concessions, most of which were awarded to British firms, and some of which went to French companies. It was a lucrative business: concession firms were paid subsidies by the state and they were also guaranteed rates of return. Consequently, there was considerable patronage involved in the choice of concessionaires.

The results of developing railways in this way included many problems. According to one account: 'Different lines were constructed with different gauges, they linked plantations to the port, and there was a tendency for many lines to meander instead of linking the interior with the port in the most efficient way. The resulting transportation system did not link the country into a more unified market.'<sup>li</sup>

These and other deficiencies, together with the financial burden of guaranteeing rates of return to their foreign owners, became increasingly onerous for the Brazilian state. 'It was felt that borrowing money abroad in order to buy a number of railroads would ultimately be less burdensome on the economy. Thus, in 1901 the Brazilian government contracted a large loan in order to nationalise some of the railroads. This process continued over the years. By 1929 close to half of the railroad network was in government hands, and by the 1950s this had grown to 94 per cent.'<sup>lii</sup>

## 4.2 State ownership

Most of the infrastructure thus inherited by the Brazilian state was institutionally unified in 1957 into RFFSA, Brazilian Federal Railway, comprising what had been 18 regional railways, consisting of 22 lines. In 1971, another state-owned company, FEPASA, was created by the merger of five railways in Sao Paulo state, converging on the port of Santos. By 1996, the network comprised 29,000 kilometres of lines carrying 40 million tons of freight a year.<sup>liii</sup> This amounted to one third of the total line length of the whole of South America, but carried six times as much freight as the rest of the South America's railways put together.<sup>liv</sup>

However, the railway was by then again an unsustainable burden on state finance. Brazil had been hit by the debt crisis and rising budget deficits in the 1980s for the same general reasons as other countries in Latin America and Africa -- deterioration in terms of trade for primary export products, the oil price shocks, the lending policies of international banks, and so on -- and these were exacerbated by more specific factors, such as the authoritarian and corrupt nature of the country's then dictatorship, which contributed to management inefficiency as well as other problems.

The impact on the economic viability of the railway was very serious. The whole network was carrying big losses, sustained by growing state subsidies. Parts of the network were cross-subsidising other parts (which is perfectly reasonable if the railway is seen as a developmental service, but the World Bank is strongly opposed to cross-subsidy because of its interference with market forces). Eight per cent of the lines were carrying 80 per cent of the traffic at one point, and increasing competition from road and air transport on the more profitable routes undermined the revenue required to sustain the network as a whole. Cargo tariffs were driven down by the competition, undermining the railway's revenue.

It did not help RFFSA's financial position that the network was also employing many more people than needed, a total of 160,000 at its peak. Labour unions were quite successful in protecting employment, but there were also other factors in low labour productivity. Rail had been used, as had other areas of state employment, in part to provide employment, and in some cases this was the product of political patronage rather than social considerations. The provision of patronage sinecures in turn resulted in top heavy management structures, further undermining efficiency. By 1991, the daily loss had soared to US\$1 million and accumulated debt stood at US\$1.2billion, a figure which rose by 1995 to US\$2.56billion.

According to the ILO, although Brazilian railway employment fell from 110,000 to 42,000 between 1975 and 1995, 'labour productivity remained low when compared with North American standards and those of other Latin American concessioned railways.'<sup>lv</sup>

## 4.3 The privatisation process

From the late 1980s onwards, some new lines were built as privately operated concessions, but restructuring and privatisation of state-owned lines originated in a 1993 decision to include RFFSA in the Brazilian government's general privatisation programme. The decision was motivated in part by the pioneering rail privatisations in Chile and, especially, Argentina. The outcome was that RFFSA was restructured into six

regional railways, each of which was to be concessioned out. Studies of the economic viability of each of the six were carried out to establish required investment levels and to plan employment reduction programmes.

By the end of 1997, all six had been privatised through 30 year concessions, with leases for operational assets. RFFSA retained ownership of the infrastructure but the private companies are responsible for running services and maintaining and renewing the infrastructure. In 1998, FEPASA was incorporated into the residual RFFSA but soon afterwards it too was concessioned. Responsibility for passenger services was retained by the state but decentralized to provinces, which in the main could not afford to keep them going.

The overall result is that there are now 11 private rail operators in Brazil, of which the largest six to have been privatised up to 2001 are:

- Ferrovias Sul-Atlântico, sold to a consortium of US-owned Railtex, the US investment group Ralph Partners and Brazilian investors. This railway carries 50 per cent of all the traffic previously carried by RFFSA.
- Ferrovias Centro-Atlântica (FCA), which was sold to Tacuma Consortium, a subsidiary of CVRD, the world's largest iron ore producer. CVRD also has cross shareholdings with CSN, a privatised steel company, and as a result CVRD directly and indirectly owns around 69 per cent of the country's steel production. Originally, this consortium also involved the US-owned Railtex, the Bank of Boston and the US investment group Ralph Partners, but in 2000 Railtex sold its shares to the CVRD pension fund.
- Ferrobán, which took over the old FEPASA, and was considered potentially the most profitable of the concessions because of its link to the port of Santos. The concession was sold to a consortium comprising railway operators, banks and investment companies. Again, CVRD is a major partner in the consortium.
- CFN, which was considered the least likely to profit, was concessioned to a Brazilian consortium, again led by CVRD.
- MRS Logística, which operates in the country's most industrially developed area and was taken over by a consortium consisting of mineral and steel companies providing most of its freight, and led by CSN, which has linked ownership with CVRD.
- Novoeste, acquired by a consortium of Brazilian and US investors, led by the US Noel Group.

A process of merger of the concessions is already underway. Novoeste and Ferrobán have already merged, for example -- increasing CVRD's dominance -- and further consolidation is in progress. One commentator with the business journal *Gazeta Mercantil* forecasts that only three or four separate companies will emerge from this merger process. There are also signs of cross-border mergers beginning to link ownership of the Argentine and Brazilian concessions.

#### **4.4 Investment and governance**

There has been no significant new track built as a result of privatisation (although, as already mentioned, some new lines were already under construction on the basis of concessions before rail was added to the privatisation programme), but there has been some investment in track improvement and, to a greater extent, new rolling stock.

The Ministry of Transport website states that although investment in rolling stock increased in the year following the beginning of the concessions, investment in other infrastructure decreased in that year. Most of the capital for investment is being mobilised through the state-owned investment bank, BNDES. The Ministry states that it is considering funding investments on one line itself because of the concession's failure to deliver as contracted.

In 2000, Brazil's 11 private operators had plans to invest US\$389.5 million. (It is not clear to what extent these plans have reached fruition). The company making the most investment is MRS Logistica, which has launched a US\$320m bond issue to finance its plans. It is significant that it is this company that is responsible for most of the investment, since its principal owner is the privatised steel production company which provides most of its cargo, and most of the investment it has made has been spent on new rolling stock to carry iron ore.

But this concession is causing concern for just that reason. Like others, it is dominated by CVRD -- iron ore and steel producers -- and it is feared that it will charge other customers uneconomically in order to finance its debt while benefiting its own transport costs. There have been complaints that the concession's accounts are insufficiently separate from those of its parent companies, making it difficult to establish transparency about costs. In general, the emergence of major customers of rail as major owners of concessions is causing concern because of the potential for conflicts of interest which could prevent the infrastructure from being as economically beneficial to other parts of the economy as to their owners' core businesses.

The September 2000 edition of the *International Railway Journal* claimed that railway privatisation in Brazil had been successful, despite acknowledging a decline in investment levels from 1999 to 2000. The journal claimed this was only an apparent decline, because the 1999 investment level had been distorted upwards by the very large investment involved in building an extension to the Ferrovia Norte-Sul (Feronorte) line (which was established in 1989 as a private concession, and was not one of those privatised by concession in the 1990s) during that year. However, even that investment surge was largely the product of public subsidy. Most of the capital came from the state (US\$500m), while private capital contributed \$400m, of which most (\$230m) came through BNDES.

#### **4.5 Changes in freight and passenger loads**

Rail has lost some cargo – especially fuel, as a result of deregulation of fuel transportation and the construction of pipelines – and gained some others, principally soy (which was the main purpose of the Feronorte line construction). The four main concessions in the industrial south-east region have increased their freight loads considerably, the government website claims, contributing to a total increase in freight

carried of 20 per cent, with billings up 75 per cent. Press accounts also suggest that a wider range of goods is being carried by rail than before, with more food and drink, paper and pulp and automobiles in particular.

Containers are also being used more than before, which might be putting small scale industry and agriculture (whose products might not be of sufficient volume to fill a container) at a disadvantage vis-à-vis larger competitors. The MRS Logistica concession claims that it increased transport of containers by 40% in one year, with iron ore, coal, cement and steel mill products among the freight carried more than before.

However, other concessions appear not to have grown freight volumes as planned. The concession contracts required that companies should increase freight transport carried in the first year by 5% per cent, but in some cases there has been a decline. It was reported, for example, that FCA carried 4.05 TKU (ton kilometre units) in the first year of privatisation, compared to 4.66 in the last year before privatisation and 4.75 in the year before that. FSA carried 5.48 TKU in the first year, slightly more than in the previous year (5.45) but less than the year before that (5.7).

The decline in passenger services is much more clear cut. As in Argentina, the privatisation process involved decentralization of these, and provincial government budgets have been unable, in the main, to maintain subsidies. Passenger kilometre units declined by more than half from 1995 to 1999.

#### **4.6 Safety on the railway**

The concessions were also supposed to bring about a reduction in accidents, but safety has certainly deteriorated in some cases and might have done so in others. According to the ministry of transport, overall accidents have declined by 12 per cent over the last five years, but in some cases there have been sharp increases.

For example, the accident rate on Novoeste increased by around 50 per cent in the year after the concession began as compared to the worst year in the six years before that. This rate takes account of the sharp increase in freight carried on that line over the same period, some of which is attributed to increased use of cheap labour for loading. It might be that the higher accident rate can be attributed also to those changes in labour practices. MRS Logistica's accident rate also increased, by around 20 per cent.

According to Jainina Fernandes, of the transport union CNTTT, three years into the privatisation process the government had failed to deliver on its promises that privatisation would lead to a reduction in accidents. She said also that it was proving very difficult to negotiate about this with the private concession companies, who were refusing to respond to union concerns. The same union has pointed out that the drive for lower costs through cuts in jobs and more use of sub-contractors has increased worker (and especially driver) fatigue and undermined skills and knowledge bases. The union also reports lack of training in accident prevention.<sup>lvi</sup>

#### **4.7 Employment, terms of employment and retrenchment**

The impact of the privatisation process on employment numbers in Brazil is clear. At the beginning of the process, RFFSA employed 42,000. This was roughly halved in preparation for the concessions over a three-year period that produced 4,000 voluntary redundancies and 18,000 others.

The World Bank provided financial assistance for a project with three aims: to cut the workforce; to increase productivity towards the levels in Chile and Argentina; and to minimise the social cost of the job losses. A study carried out in preparation for the project revealed that of the largely male workforce, the average worker was aged 41 with 18 years service, low educational qualifications and either few or highly specified skills. This meant that their chances of finding new jobs were low.

In preparation for privatisation, the number of people employed by RFFSA was reduced to around 21,000. At FEPASA, there was a reduction from 8,000 to 5,000 jobs. It was recognised that the statutory maximums for severance pay would be inadequate, and so a scheme was developed to soften the blow. Early retirement was made available to those over 50, while others were entitled to severance payments of between four and 12 months pay, in addition to what the law required, depending on length of service.

According to a World Bank report: ‘The privatisation team recognised that these targeted reductions in labour force were by no means final. Once all the regional areas had been privatised, the organisation of each system would probably change and would likely lead to additional reductions in staff, changes in skills mixes and improved productivity.’<sup>lvii</sup>

So it proved. The workforce was halved again, to a total of around 11,000, within a year of the concessions beginning, meaning that since the beginning of the privatisation process around 75 per cent of the jobs had been cut. The impact on the workload of those remaining is causing concern. Novoeste (now, like other concessions, controlled by CVRD, the iron and steel producers) is reported to have dismissed more than 1,000 workers since privatisation and the union says this has greatly increased workload among those remaining, especially loaders. Novoeste has been officially warned by the Ministry of Labour about the excessive hours being worked by its employees.

A central element of the World Bank staff reduction programme in Brazil was provision of retraining for retrenched workers. But the Bank admits that only a small minority actually received the promised training and that in one case the programme from which redundant workers were supposed to benefit did not even start until 18 months after they had been dismissed. The delays in beginning the training programmes is seen as one of the major reasons for their lack of success, but the delays in themselves could be seen as an expression of the limited commitment to the programmes by all concerned (including workers themselves, whose applications for retraining were lower in number than anticipated, perhaps reflecting their scepticism as to its practical value).

As part of the privatisation process, responsibility for honouring pension arrangements of former rail employees passed to the state, so that these obligations are not carried by the concessions.

#### **4.8 The future**

Brazil is already experiencing the same phenomenon seen earlier in Argentina, and, indeed, everywhere in connection with privatisation of this sort -- demands from the companies for renegotiation of the contracts. The companies are alleging that the commitments involved are too onerous, and that this could only have become clear with hindsight once they became more familiar with the state of the assets they took over. The government is reported to be resisting this, but information is lacking on the progress of negotiations.

There have also been reports of some concession companies defaulting on the payment of their instalments, just as occurred in Argentina.

#### **5. CONCLUSIONS AND LESSONS**

The point with which the last section ended emphasizes that it is too early to make a definitive judgement about the impact of railway privatisation through concessions in Latin America, not least because contracts are currently being renegotiated. The very fact that they are being renegotiated demonstrates the uncertainty intrinsic to the process, and the fact that it is the concession companies that have forced the renegotiation demonstrates the shift in authority to them from the state since the concessions began.

The signs are that the limited democratic control of the concessions built into the arrangements at the start is weakened by the dynamic of the concession process itself. This is at variance with the claims made by the World Bank about the capacity of concessions to marry the advantages claimed on behalf of the private sector – greater efficiency, new technology, greater access to capital and better customer focus – to the public interest defined through political processes. In practice, the wider economic and social responsibilities of the concessions are being subordinated to their development of infrastructure and services geared to the most profitable areas of their customer base, which means that further concentration of economic power is being promoted rather than ameliorated by this approach to railway restructuring and modernization.

According to some accounts, the concessions are not delivering effectively even to their major freight customers, much less to others. The robust verdict of Argentine rail union Sindicato La Fraternidad is that 'the transfer of the railway companies to the private sector

- Has not generated employment;
- Has not transformed industries with investment and technology;
- Has not reduced high accident rates;
- Has not met transport market expectations and needs;
- Has not expanded the networks sold off;
- Has not maintained its fixed infrastructures, nor its engine and rolling stock (except those incorporated with state capital arising from subsidies);
- Has reduced the areas of influence and territorial integration of the regional productive economies by abolishing branch lines.<sup>lviii</sup>

Even to the extent that so clear-cut a verdict can be challenged as being informed by sectional interest, its terms are justified by the extravagant claims made on privatisation's behalf at the outset. Clearly, there have been enormous reductions in rail workforces

while the economic expansion that was supposed to be the product of improved and cheaper rail services has failed to provide alternative employment opportunities for more than a few of those who lost their jobs or for the next generation of the national labour force.

More specifically, to the extent that there have been programmes, financed in part by the World Bank, to ameliorate the effects of workforce reductions, these have failed to produce training and new employment opportunities on anything like the scale required to deal with the social cost. Even to the extent that they have done so, the effect has been to engineer major labour restructuring away from secure employment towards less secure and, in general, less well remunerated contract employment. In addition, railways have been deprived of much invaluable institutional knowledge and memory through the loss of so many experienced and trained workers, and this has had some negative impact on service quality and safety standards.

On the other hand, to the extent that investments have been delivered – especially in new technology – efficiency, quality and, potentially at least, safety have increased in some cases. Volume of freight and passengers carried has increased in some cases while falling in others. Some inter-city passenger services have disappeared entirely, while fares have tended to rise, especially for commuter services.

That variety of outcome reflects the issue at the heart of the matter – the fact that privatisation has been designed primarily to gear railway development to global market forces, which finds expression in the investment and operational decisions of the concessions. The aim and the effect has been to develop transport infrastructure to suit it more to the requirements of international trade dominated by the richer countries. This is reflected in the investment decisions of the concession companies, both positively – in the form of increased investment in parts of the infrastructure serving export corridors and the commodities mainly carried on them, and intermodal capacity – and negatively, in that other parts of the economy, as well as social amenity, are not being so well served.

The future shape of investment remains unclear. A cause for concern is the shifting balance of power between the private businesses and the state reflected in the latter's failure to enforce investment obligations and its agreement to renegotiate contracts. These concerns are heightened by trends in the pattern of ownership of the concessions. While the involvement of major cargo customers as concession operators has undoubtedly benefited those customers, it might have done so at the expense of other areas of industry, and especially at the expense of small and medium-sized enterprises. It seems likely that the consequences of these trends will find political expression in growing pressure on governments to provide for the transport infrastructure and service needs of local and small scale economic development, and the whole of society, which concessions are not currently designed to do.

The World Bank points out that it is the 'interest among freight customers' allied to the 'potential for reliable revenue' that explains the nature of the ownership trend among the consortia which are securing rail concessions. The new companies are often alliances between major rail freight customers and transnational rail businesses. There are concerns that, while these interests can indeed bring much-needed capital investment, they do so in ways which distort the economic and social impacts of rehabilitation and development of infrastructure in favour of already entrenched economic powers.

The World Bank is not alarmed by this prospect, since it is consistent with the institution's overriding commitment to countries concentrating on export-led development in which they have 'comparative advantage' in the context of increasing international economic integration. However, development of that kind also increases the vulnerability of countries to changes in world markets for the products in which they are concentrating – a reliance which has contributed to the fiscal instability that caused earlier under-investment by the state. The concessions' reliance on foreign borrowing in dollars in a service which necessarily raises its revenue in local currency is adding to the financial burden, as Argentina has discovered, and this burden will be passed on to freight customers and passengers and/or back to the state.

Certainly, concessions are producing some unforeseen – or, at any rate, unforetold – consequences, especially in the trend (routine also in other utility privatisations, especially water) for contracts to be renegotiated. There is a paradox at the heart of this trend. On the one hand, it is right that governments and operators should enjoy sufficient flexibility to re-evaluate demand for services, supply of services and investment in corresponding infrastructure and operational capacity in accordance with changes in market and wider economic and social conditions. That would, indeed, be a great advantage in properly structured, adequately resourced and effectively managed state-run railways. In conditions of privatisation, however, where the public interest is supposed to be expressed in the contractual terms agreed with private companies, flexibility can lead to erosion of the original conditions and even the rationale for them, particularly since the private side of the arrangement is in a much stronger bargaining position once the concessions have started, and the state has shed its capacity and control.

There is a moral hazard inherent in the concession arrangement, therefore, in that there are incentives for private companies to make forecasts and commitments in advance, to beat off competition for the concession, only to revise their forecasts and seek renegotiation of commitments later, once both competitors and state-run capacity are out of the picture. It is not suggested that so cynical an intention informed any of the decisions mentioned in this report – there is no reason known to the author to suggest that any participant acted other than in good faith – but insofar as a trend has been established, there is certainly a danger that future decisions could manifest the tendency. Equally, however, it might be that future policy will be better informed by the experience, so that the same mistakes are avoided.

Again, the issue boils down to one of rival approaches to economic and social development and the role that restructuring and modernisation of railways can play in supporting each of them. Railway privatisation through concessioning is tending to meet the needs of large scale export producers rather than smaller scale and more local economic interests or wider social needs. That is hardly surprising given the pattern of ownership of the concession companies themselves and the greater profits to be made from shipping containerized cargo quickly between and through intermodal facilities than providing more complex services for smaller producers of a wider range of products, or carrying passengers in competition with other modes.

Perhaps the starting point for evaluating the success or otherwise of railway privatisation through concessions, therefore, is to open up a wider dialogue about how infrastructure and services need to develop to meet the needs of less powerful economic interests and

society. So long as the international institutions which are driving the trend remain prejudiced against alternative approaches such as restructuring based on social dialogue, effective comparisons and judgements will not be made.

As the ILO has pointed out: 'There seems to be a popular misconception that only the private sector can successfully implement marketing systems, policies and strategies – a misconception which may stem from the belief that public sector enterprises have no incentive to operate in a profit-maximizing way. However, there are numerous examples of publicly owned railway companies employing very effective marketing strategies to achieve profit or market share-maximizing objectives. In France, the state-owned railway organization (SNCF) has been able to win from the airlines a dominant share of the long-distance domestic travel market for its high-speed TGV services. Privatisation could result in a paradox whereby the profit-maximising strategies of a privatised railway actually work against the effective marketing of services.'<sup>lix</sup>

In that and other ways, the mixed results of privatisation through concessions suggests that the experience is producing the same distortions that resulted in the state taking over ownership and management of railways in the first place. The goals of sustainable, secure and socially just national economic and social development that private rail concessions failed to support in their earlier incarnation appear to be equally elusive in the context of privatisation today.

## REFERENCES

---

<sup>i</sup> 'Private Participation in the Rail Sector – recent trends', Nicola Tynan, in *Public Policy for the Private Sector*, World Bank, Washington, D.C., 1999.

<sup>ii</sup> The term 'developing' appears in quotation marks here because it refers to the quotation from the World Bank report cited in the first paragraph, and to indicate the author's belief that it is an unsatisfactory term in general, and even less appropriately applied to Argentina than to many other countries to which it is applied. However, this paper is not the place for a wider discussion of the nature of 'development'. For more general exploration of the relationship between World Bank structural adjustment programmes, privatisation, globalisation and 'development', please see *New Leaf or Fig Leaf? The Challenge of the New Washington Consensus*, Brendan Martin, Bretton Woods Project, 2000.

<sup>iii</sup> 'Railways', Javier Campos ad Pedro Cantos, in *Privatisation and Regulation of Transport Infrastructure: Guidelines for Policymakers and Regulators*, Antonio Estache and Gines de Rus, World Bank Institute, World Bank, Washington, D.C., 2000, p.175.

<sup>iv</sup> *ibid*, p.178.

<sup>v</sup> 'Private Participation in the Rail Sector – recent trends', Nicola Tynan, in *Public Policy for the Private Sector*, World Bank, Washington, D.C., 1999, p.1.

<sup>vi</sup> *ibid*, p.5.

<sup>vii</sup> *Privatising Monopolies: Lessons from the Telecommunications and Transport Sectors in Latin America*, Ravi Ramamurti (ed.), John Hopkins University Press, p.4.

<sup>viii</sup> For detail of the policy package dubbed the 'Washington Consensus', and discussion of the politics involved, please see *New Leaf or Fig Leaf? The Challenge of the New Washington Consensus*, Brendan Martin, Bretton Woods Project, 2000.

<sup>ix</sup> *Consequences for La Fraternidad Workers of the Process of Concessioning the Railways*, Sindicato La Fraternidad evidence to ITF, May 2001.

<sup>x</sup> *ibid*.

<sup>xi</sup> 'Railways', Javier Campos ad Pedro Cantos, in *Privatisation and Regulation of Transport Infrastructure: Guidelines for Policymakers and Regulators*, Antonio Estache and Gines de Rus, World Bank Institute, World Bank, Washington, D.C., 2000, p.178.

<sup>xiii</sup> 'Infrastructure Concession Design and Financing Issues', Juan Luis Guasch, in *Privatising Monopolies: Lessons from the Telecommunications and Transport Sectors in Latin America*, Ravi Ramamurti (ed.), John Hopkins University Press, p.367.

- <sup>xiii</sup> 'Private Participation in the Rail Sector – recent trends', Nicola Tynan, in *Public Policy for the Private Sector*, World Bank, Washington, D.C., 1999, p.3.
- <sup>xiv</sup> 'Infrastructure Concession Design and Financing Issues', Juan Luis Guasch, in *Privatising Monopolies: Lessons from the Telecommunications and Transport Sectors in Latin America*, Ravi Ramamurti (ed.), John Hopkins University Press, p.377.
- <sup>xv</sup> *Privatisation and Regulation of Transport Infrastructure: Guidelines for Policymakers and Regulators*, Antonio Estache and Gines de Rus, World Bank Institute, World Bank, Washington, D.C., 2000, p.1.
- <sup>xvi</sup> 'Private Participation in the Rail Sector – recent trends', Nicola Tynan, in *Public Policy for the Private Sector*, World Bank, Washington, D.C., 1999, p.3-4.
- <sup>xvii</sup> *ibid*, p.3.
- <sup>xviii</sup> 'Global Trend to Railway Concessions Delivering Positive Results', Louis S. Thompson and Karim-Jacques Budin, in *Public Policy for the Private Sector*, World Bank, Washington, D.C., December 1997.
- <sup>xix</sup> *Symposium on the Social and Labour Consequences of Technological Developments, Deregulation and Privatisation of Transport*, Background Paper, ILO, Geneva, 1999, p.15.
- <sup>xx</sup> 'Railways', Javier Campos ad Pedro Cantos, in *Privatisation and Regulation of Transport Infrastructure: Guidelines for Policymakers and Regulators*, Antonio Estache and Gines de Rus, World Bank Institute, World Bank, Washington, D.C., 2000, p.192.
- <sup>xxi</sup> *ibid*, p.193.
- <sup>xxii</sup> *ibid*, p.179.
- <sup>xxiii</sup> *ibid*, p.188.
- <sup>xxiv</sup> 'Infrastructure Concession Design and Financing Issues', Juan Luis Guasch, in *Privatising Monopolies: Lessons from the Telecommunications and Transport Sectors in Latin America*, Ravi Ramamurti (ed.), John Hopkins University Press, p.374.
- <sup>xxv</sup> 'Private Participation in the Rail Sector – recent trends', Nicola Tynan, in *Public Policy for the Private Sector*, World Bank, Washington, D.C., 1999, p.4.
- <sup>xxvi</sup> 'Railways', Javier Campos ad Pedro Cantos, in *Privatisation and Regulation of Transport Infrastructure: Guidelines for Policymakers and Regulators*, Antonio Estache and Gines de Rus, World Bank Institute, World Bank, Washington, D.C., 2000, p.196.
- <sup>xxvii</sup> 'Mexican railroads face a long, uphill climb', Toby B. Gooley, in *Logistics Management and Distribution Report*, Vol. 38, number 5.
- <sup>xxviii</sup> *Argentina's Transport Privatisation and Reregulation: Ups and Downs of a Daring Decade-long Experience*, Antonio Estache and Jose C. Carbajo, World Bank, 2000, p.9-10.
- <sup>xxix</sup> *ibid*, p.9.
- <sup>xxx</sup> *ibid*, p.11.
- <sup>xxxi</sup> 'Mexican railroads face a long, uphill climb', Toby B. Gooley, in *Logistics Management and Distribution Report*, Vol. 38, number 5.
- <sup>xxxii</sup> *Argentina's Transport Privatisation and Reregulation: Ups and Downs of a Daring Decade-long Experience*, Antonio Estache and Jose C. Carbajo, World Bank, 2000, p.10-11.
- <sup>xxxiii</sup> *ibid*, p.11.
- <sup>xxxiv</sup> *ibid*, p.12.
- <sup>xxxv</sup> *ibid*, p.13.
- <sup>xxxvi</sup> *Symposium on the Social and Labour Consequences of Technological Developments, Deregulation and Privatisation of Transport*, Final Report, ILO, Geneva, 2000.
- <sup>xxxvii</sup> 'Why an accident like Hatfield was waiting to happen', Juliette Jowit, *Financial Times*, February 22, 2001.
- <sup>xxxviii</sup> *Consequences for La Fraternidad Workers of the Process of Concessioneing the Railways*, Sindicato La Fraternidad evidence to ITF, May 2001.
- <sup>xxxix</sup> 'Mexican railroads face a long, uphill climb', Toby B. Gooley, in *Logistics Management and Distribution Report*, Vol. 38, number 5.
- <sup>xl</sup> *Symposium on the Social and Labour Consequences of Technological Developments, Deregulation and Privatisation of Transport*, Final Report, ILO, Geneva, 2000, p.20-21.
- <sup>xli</sup> *Symposium on the Social and Labour Consequences of Technological Developments, Deregulation and Privatisation of Transport*, Background Paper, ILO, Geneva, 1999, p.15.
- <sup>xlii</sup> *Consequences for La Fraternidad Workers of the Process of Concessioneing the Railways*, Sindicato La Fraternidad evidence to ITF, May 2001.
- <sup>xliii</sup> *Symposium on the Social and Labour Consequences of Technological Developments, Deregulation and Privatisation of Transport*, Final Report, ILO, Geneva, 2000, p.23.
- <sup>xliiv</sup> *Symposium on the Social and Labour Consequences of Technological Developments, Deregulation and Privatisation of Transport*, Background Paper, ILO, Geneva, 1999, p.20.

- 
- <sup>xlv</sup> See *Structural Adjustment and Railways Privatisation: World Bank policy and government practice in Ivory Coast and Ghana*, Brendan Martin and Marc Micoud, ITF, 1997.
- <sup>xlvi</sup> *International Railway Journal, Outlook 2001*, p.1.
- <sup>xlvii</sup> *Symposium on the Social and Labour Consequences of Technological Developments, Deregulation and Privatisation of Transport*, Background Paper, ILO, Geneva, 1999, p.8.
- <sup>xlviii</sup> 'Private Participation in the Rail Sector – recent trends', Nicola Tynan, in *Public Policy for the Private Sector*, World Bank, Washington, D.C., 1999, p.6.
- <sup>xliv</sup> *The Brazilian Economy: Growth and Development*, Werner Baer, Praeger, 1989, p.15.
- <sup>i</sup> *ibid*, p.16.
- <sup>ii</sup> *ibid*, p.19.
- <sup>iii</sup> *ibid*, p.239.
- <sup>liii</sup> Information from IPEA, the Economic Research Institute in Brazil.
- <sup>liv</sup> *International Railway Journal*, September 2000.
- <sup>lv</sup> *Symposium on the Social and Labour Consequences of Technological Developments, Deregulation and Privatisation of Transport*, Background Paper, ILO, Geneva, 1999, p.15.
- <sup>lvi</sup> *Symposium on the Social and Labour Consequences of Technological Developments, Deregulation and Privatisation of Transport*, Final Report, ILO, Geneva, 2000, p.23.
- <sup>lvii</sup> *Labor Redundancy, Retraining and Outplacement during Privatisation: the experience of Brazil's Federal Railway*, Antonio Estache, Jose Antonio Schmitt de Azevedo and Evelyn Sydenstricker, World Bank research paper, 2000.
- <sup>lviii</sup> *Consequences for La Fraternidad Workers of the Process of Concessioneing the Railways*, Sindicato La Fraternidad evidence to ITF, May 2001.
- <sup>lix</sup> *Symposium on the Social and Labour Consequences of Technological Developments, Deregulation and Privatisation of Transport*, Background Paper, ILO, Geneva, 1999, p.15.