



HIT BY A BUS: EUROPEAN PASSENGER RAIL

WESTERN EUROPE IS in the midst of a sweeping deregulation of intercity motor coach markets – Sweden, Finland, Germany, Italy, and France have all recently opened these services to competition. The result is a new class of low-cost competitors that are putting pressure on long-distance passenger rail services and rapidly gaining market share. Rail operators will need to move quickly to counter this existential threat.

HERE COMES THE BUS

The intercity buses of today offer train-like comforts (such as luxury seats, restrooms, wi-fi, snacks, and beverages) but at a fraction of the price of rail on high-density routes. We

believe that new bus operators have lured up to 20 percent of customers away from some rail services in just a couple of years, thanks to aggressive marketing tactics, a smart route network, and large seating capacities.

Consider the popular Hamburg-Berlin route. Rail service is more frequent and faster, but bus fares are much less. The rail operator does offer some deeply discounted tickets at \$20, but that's still, on average, twice the price of the lowest-cost bus ticket. And aggressive bus companies are slicing fares even more on routes where they compete with rail.

By offering comparable or even better quality service, bus operators are attracting middle-income passengers and business

customers. This is especially true for routes between cities that are poorly served by train (low speeds, limited frequencies, or limited on-board comfort).

As a result, two competitive scenarios are emerging for passenger rail: On routes operated with very high-speed trains (300 kmh versus 100 kmh for bus), rail operators will continue to benefit from their huge travel time advantage. Rail companies also can deploy economic models to help limit their market share erosion on such routes, such as a low-fare offering from France's SNCF called OUIGO. But on traditional rail routes with lower speeds and a less modern fleet (meaning buses can compete head on), market share erosion for rail operators is just beginning.

UPPING RAIL'S APPEAL

We recently surveyed European travelers and found that while rail still clearly wins on comfort and enjoyment (for now), travelers consider bus a better value. Buses also win in areas where rail ought to have the advantage, such as innovation and service orientation. Attempts by rail companies to retain customers with isolated price reductions and promotions have had a limited impact on market share erosion thus far and are unlikely to be successful over the long term.

Bus fleets are structurally much cheaper and more flexible to operate than trains, so rail operators won't be successful competing purely on price. Instead, they will need to figure out how to best capitalize on their strengths: national and dense networks, strong brands, loyal customer bases, committed staff, and well-appointed stations.

A comparable lesson is the emergence of low-cost airlines in the 1990s, which traditional European airlines didn't immediately perceive as a paradigm shift. The new entrants offered lower prices, but they also operated in ways that changed customers' expectations and behaviors. Several traditional airlines foundered when they were unable to learn from these up-and-comers and adapt.

Passenger rail services in bus-competitive lanes now face the same peril if they fail to rethink their product and service offerings and adapt their business designs. Fending off market share erosion will require not only

Comparison of rail and bus services for Hamburg-Berlin

	RAIL	BUS
Frequency	Every 30 minutes	Every 75 minutes
Journey time	1 hour and 38 minutes	3 hours
One-way fare	\$42-\$85, limited discount prices from \$20 and up	\$8-\$18

lower prices, but innovation – improving the entire door-to-door mobility chain in terms of transparency, ease of use, and interconnectedness – and aligning product offerings with what customers are willing to pay. In some cases, rail operators may need to adjust capacity while refocusing investments on enriched offerings. Stations also could be utilized to profit from evolving generational changes, such as charging stations for e-cars, upgraded work and play/rest areas, even drop-in “maker spaces.”

Finally, rail operators may want to consider diversifying, by taking a position in the low-cost intercity bus market themselves. Some already have: German railway Deutsche Bahn runs a low-cost luxury bus service on routes to/from Germany that are not well served by trains. A rail operator already possesses

the core competencies necessary to operate buses and could even use its data on customer journeys and travel preferences to build targeted bus and linked rail-bus offers.

THE TIP OF THE ICEBERG

Passenger railroads are facing an uncertain future as part of a broadening and diversifying mobility market that includes not only new bus services but also car sharing, integrated mobility solutions, and autonomous cars. Understanding these trends, anticipating their associated risks and opportunities, and being willing to adapt flexibly and rapidly can ensure rail operators make good investment decisions and maintain a strong position in this market.

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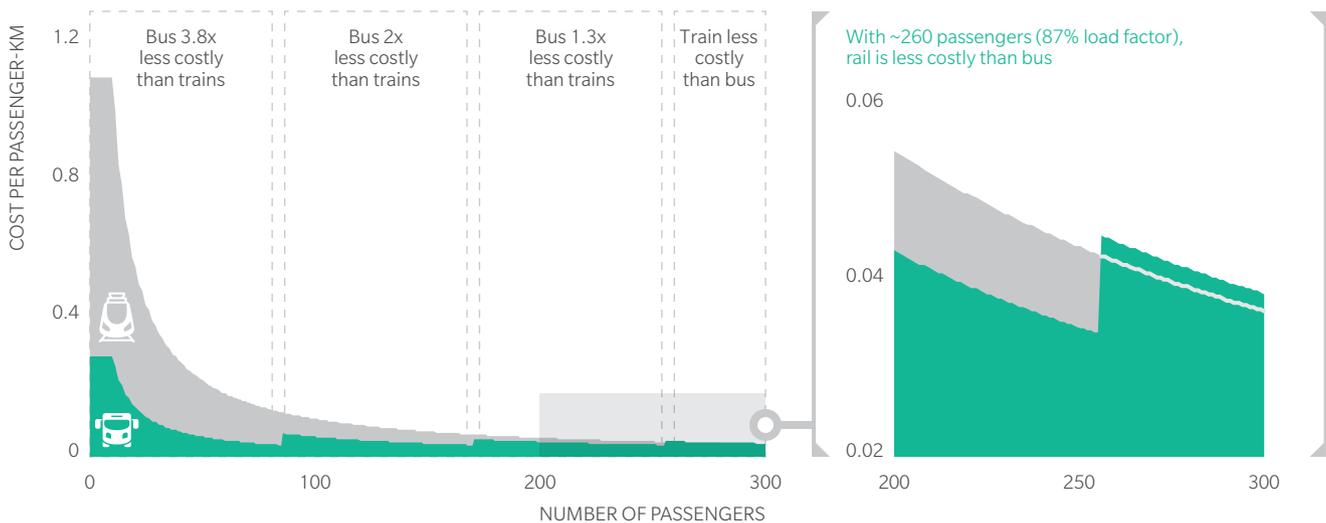
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EUROPEAN INTERCITY PASSENGER BUS VERSUS RAIL COST STRUCTURE



Note Assumes double-decker with 85 seats, \$3.26 per bus-km; train with 300 seats, \$12.38 per train-km
 Source Oliver Wyman analysis