Peer Review of:

ORR's PR13 Efficiency Benchmarking of Network Rail using LICB

I was asked to independently review the ORR's analysis of the cost efficiency of Network Rail in the above document. I have been given the opportunity to comment on a number of drafts of this document. This note gives my opinion of the process of arriving at the estimates of Network Rail's efficiency gap based on an international comparison with comparable European railways.

The ORR has undertaken a substantial data quality assurance exercise which looks very comprehensive. In particular their choices of which countries and which years to include or exclude in the analysis look sensible. It is also correct to make a steady state adjustment for track renewals and there are well justified adjustments for exchange rates and inflation.

The final model specification (Explanatory variables: TRACK; PASSDT; FRDT; SING; TIME; TIME2) of the cost function is clearly arrived at. I note that ORR has managed to justify simplifying the specification relative to the previous regulatory review, PR08 (Explanatory variables: ROUTE; PASSDR; FRDR; SING; ELEC; TIME; TIME2). This is to be commended as there can be a tendency for regulators to complicate specifications of costs over time in a way that is unhelpful to the transparency of regulation.

The model analysis starts out with 21 models and reduces these to 4. The 21 models certainly cover the range of models that are in use in regulatory benchmarking, though, if anything, this was too many models to consider. For instance, the class of models (i.e. FEI, PL and PLM) that do not allow for time varying inefficiency is inappropriate for regulatory benchmarking of a network industry in the UK, since the intended consequence of regulation is to improve regulated company performance over time. These models do not require consideration. The final four models (COLS, CUESTAL, CUESTAN, CSSRE) are sensible models to report the results of.

The attempt to undertake Monte Carlo sensitivity analysis to provide error bounds on the efficiency scores represents a welcome development in the reporting of the estimates of efficiency scores.

Overall, I believe the analysis conducted by the ORR represents a best practice attempt by a UK regulatory authority to compare the efficiency of a national infrastructure monopoly, by undertaking international benchmarking. The quality of analysis compares very favourably with regulatory practice in other countries and in other comparable sectors (such as electricity transmission) and exhibits a further development of the good practice exhibited in the international benchmarking undertaken by ORR for PR08.

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