Annual efficiency and finance assessment of Network Rail 2025

3. Future financial risks and opportunities

3.1 Network Rail faces heightened financial pressures as it navigates reduced risk funding, ongoing inflationary pressures and the need to deliver core renewals within tighter budgetary constraints and the need to close the funding gap. This chapter examines the challenges surrounding risk funding and the funding gap. It also covers other matters such as R&D and Industry Performance Improvement Fund which may provide Network Rail with opportunities to make further performance improvements and efficiency savings, and Network Rail's financial flexibilities withing the Government's budgetary processes.

Risk funding

3.2 The financial challenges faced by Network Rail during CP6, such as managing input price risk and other unplanned costs, highlight the importance of allocating funding appropriately to efficiently manage unforeseen financial risks over a five-year control period. In our PR23 final determination, we required Network Rail to set aside £1.7 billion (cash prices) for risk funding (£1.5 billion for England and Wales and £0.2 billion for Scotland) to help manage such pressures.

3.3 Network Rail has drawn down and allocated 55% of its CP7 risk fund to address unexpected cost pressures that it has identified across the control period. These include increased National Insurance Contributions, higher input prices from increases in construction costs in excess of CPI inflation and Schedule 8 payments related to lower train performance (Years 1 and 2 only). As a result, only 45% (£760 million) of risk funding remains uncommitted within Network Rail budget as it enters Year 2.

3.4 Network Rail's reduced risk fund comes when it is facing significant financial risks including performance challenges (which affects Schedule 8 payments), high inflation and a funding gap in its England & Wales delivery plan (see next section).

Funding gap

3.5 Our assessment of Network Rail's CP7 delivery plan identified a gap in funding for core asset requirements for England & Wales. At the start of CP7 we wrote to Network Rail to ask it to resolve the funding gap without compromising the delivery of essential core renewals and maintenance activities. Over the course of the year significant effort has been made to reduce the gap down to £488 million. However, further inflationary pressures have made this more difficult and the remaining gap at the end of March 2025 remains a concern.

3.6 As outlined in our January 2025 letter to Network Rail on the funding gap, we recognise the scale of the financial challenge and have acknowledged that time is needed to make the right decisions. However, the combination of reduced risk funding and a remaining funding gap presents a threat to delivery confidence. Without decisive action, there is a risk that Network Rail may be forced to scale back or delay core renewals work, compromising long-term asset sustainability and reliability.

3.7 We will continue to engage with Network Rail to ensure that the funding gap is closed and that Network Rail looks at all available options for resolving the funding gap before it considers cutting back on planned renewals for core assets.

Research and development expenditure

3.8 Our PR23 determination included £165 million of funding (£147 million in England & Wales and £18 million in Scotland) for Network Rail to spend on research and development (R&D) activities in CP7.

3.9 Network Rail spent £31 million on R&D in Year 1 of CP7, £4 million less than planned. This investment supports the development of innovations and new approaches that are expected to deliver efficiency improvements. Through its CP7 R&D programme, Network Rail has identified £223 million of potential efficiency savings across the control period with additional further savings being explored.

3.10 Third party funding is used to support the R&D programme alongside the direct funding of £165 million set at PR23. Network Rail secured an additional £8 million of third-party funding over the year and aims to raise a further £66 million over the control period. While the use of third-party funding can generate cost savings, these are not recorded as part of routes' and regions' efficiency savings.

3.11 At the end of Year 1, Network Rail had 65 projects at different stages of readiness for deployment, with 10 projects deploying on the network.

3.12 We remain concerned about Network Rail's ability to use the R&D fund effectively. The limited information and assurance provided this year has added to these concerns. While there are clear opportunities for innovation and savings, the challenge lies in getting new technologies adopted across regions. This issue was evident in CP6, where promising projects were not fully adopted, and the expected cost savings were not realised. We believe this issue could persist in CP7. We suggest that Network Rail's R&D team continues to work closely with the regions to encourage uptake and simplify the process of embedding new technologies, which many regions find challenging.

Industry Performance Improvement Fund

3.13 Recognising the importance of improving performance our PR23 determination included £40 million (cash prices) of funding for an industry Performance Improvement Fund in the CP7 plans (for England and Wales). As examined in our Network Rail Annual Assessment, progress to date has been good.

3.14 Network Rail Scotland's CP7 plan includes £53 million (cash prices) for a targeted performance fund. Good progress has been made with setting up this fund, which has attracted proposals from the industry with allocated funding. See Chapter 4 for further details.

Budget flexibility

3.15 Network Rail is classified as an arm's length public sector body which means that it is subject to the Government's resource (operating) and capital departmental expenditure limits ('RDEL' and 'CDEL'). These expenditure limits restrict Network Rail's ability to reprofile expenditure across years within a control period and limit the extent to which spending can be switched between resource and capital budgets.

3.16 For CP7, the UK Government has confirmed that the same budgetary processes that applied in CP6 will continue.

3.17 No budget rollover was permitted for England and Wales as of 31 March 2025 following the conclusion of the three-year Government Spending Review announced in October 2021. It is anticipated that similar constraints will apply to 2025–26.

3.18 Oversight of the flexibility of grant payments within Scotland continues to fall within the remit of Transport Scotland and the Scottish Government's budgetary process for CP7. Transport Scotland confirmed that the budgetary flexibilities available in CP6 will broadly continue for CP7.

3.19 Further details on the budget flexibility rules for CP7 are explained in our PR23 financial framework document.

Regulatory asset base, net debt and gearing

3.20 Network Rail's regulatory asset base (RAB) increased by £2.3 billion to £89.8 billion in the year April 2024 to March 2025. The increase was due to indexation plus renewals added to the RAB offset by the amortisation of existing assets and a £16 million deduction for property sales.

3.21 Network Rail no longer issues debt to fund its capital expenditure. However, it continues to hold legacy debt (£60.2 billion), including financial instruments issued to investors before the company's reclassification to the public sector. It incurred £2.5 billion of financing costs in the year, including £1.3 billion of financing costs on index-linked debt. Network Rail's current gearing (net debt relative to RAB) is at 67%.

- ← Previous 2. Network Rail's financial performance and efficiency
- → Next 4. Network Rail Scotland's financial performance and efficiency