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West Coast loss will send odd couple into sidings

Sir Richard Branson and Sir Brian Souter will split if they lose their bid to operate the London to Glasgow route for the next 14 years

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Double act: Sir Brian Souter and Sir Richard Branson (Chris Harris)

One is a slick showman who takes pride in his appearance; the other is spiky and combative, and cares less about sartorial elegance. Sir Richard Branson and Sir Brian Souter — the odd couple of Britain's railways — have shared their Virgin Rail joint venture since 1997.

This week their partnership could reach the end of the line when the Department for Transport reveals the winner of the contract to operate the West Coast Main Line — the London to Glasgow route — for the next 14 years.

First Group, the Aberdeen-based transport company, is seen as the favourite to snatch the marquee route from Virgin, leaving it with nothing in the rail sector. The two other bidders — Abellio of the Netherlands and France's SNCF — are thought to be out of the running.

Losing the franchise would be a blow to Branson's business empire. Virgin Rail is 51% owned by the tycoon, with 49% held by Souter's Stagecoach, the Scottish transport group he founded and still runs.

It has not always been an easy ride, but the pair have transformed the line — improving service and doubling passengers to 30m a year. They have also made a small fortune from the railway. Branson has banked about £204m in dividend payments from the venture. But it appears the Virgin supremo's cash cow is about to be grabbed by First Group, which has put in the highest bid to run the West Coast line.

The Scottish transport company is thought to be offering the government £6.5 billion to £7 billion in premium payments over the course of the 14-year deal, compared with £6 billion from Virgin. A £7 billion bid equates to an annual premium of £500m a year for the Treasury, a huge jump on the £160m net premium paid by Virgin last year.

The Department for Transport does not always go with the highest bidder. But the ministry is said to be under pressure from the Treasury to maximise earnings from rail franchising as the economy flatlines.

Fears that his rail interests are about to be shunted into the sidings have stung Branson into action. He has written to Justine Greening, transport secretary, to warn that awarding the deal to First Group could lead to a repeat of the mistakes that have dogged the East Coast Main Line.

Two previous operators of the London to Edinburgh route — GNER and National Express — have been forced to walk away from the franchise after making ambitious revenue forecasts that failed to materialise. Branson argued that First Group's bid would only work if it "drastically cut the quality of services". One source said: "It seems that First Group has put in a pretty aggressive bid on cost."

It is difficult for train operating companies to make huge cost cuts because about 70% to 80% of a franchise's overheads are fixed, mainly related to leasing rolling stock. However, First Group is said to be weighing plans to scrap some first-class carriages and ditch the buffet car to make way for more standard class seating and a trolley service.

West Coast has about 800 catering staff and union leaders fear that most could go if the group presses ahead with the radical reorganisation.

After slashing the cost of running the service, First Group would need to push up the number of passengers using the line and may also be forced to raise fares. Rival bidders hope the government could take a more cautious view and reject the highest offer. Ministers are sure to take note of First Group's weak financial position.

The FTSE 250 company has a market value of £1.2 billion but is saddled with £1.8 billion of debt. Trading has also been weak — the group shocked investors this year by warning that profits would be lower as its British bus division struggled. City analysts believe that the company's financial situation means that if it doesn't win West Coast it will need to tap investors for cash in a rights issue to pay down the debt pile.

This year's profit warning has also cast doubt on the future of Tim O'Toole, chief executive of First Group. The company is believed to have sounded out Dean Finch, chief executive of National Express, as a potential replacement for O'Toole.

Joe Thomas, analyst at HSBC, said: “I have got concerns about their balance sheet and they are dependent on rail cash to support them. There is pressure on them . . . they have got weak finances, they have got problems in America, they have got problems in the UK bus business. They have promised a lot and they have still got a lot to do.”

The City is also concerned about the make-up of the new, longer franchises, which are being phased in to replace the current seven-year contracts. It is thought the government has asked bidders to put up more collateral, in the form of a “performance bond”, plus a loan guarantee. Sources suggested First Group has been asked to put up a £300m guarantee for West Coast that would be forfeited if it walked away from the contract. Analysts at JP Morgan Cazenove said this raised concerns that First Group may be overbidding for the franchise.

Branson and Souter must now decide whether to keep Virgin Rail together to bid for the East Coast franchise, which comes up for grabs at the end of this year. If not, an amicable separation beckons for the odd couple.