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"Bus Deregulation: Lessons from the U.K."

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Bus Deregulation: Lessons from the U.K.

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I. UK Policy Changes

1. The 1985 Transport Act deregulated local (stage) services in the UK outside London, provided for the privatisation of National Bus Company, the formation of Municipal bus operations into arms length subsidiaries, and revised methods of paying subsidy to bus operators. No constraint on the entry or quantity of bus service provided was henceforth to be imposed, subject only to registration of services and notification of their withdrawal. The National Bus Company, separated into 52 mainly geographical units was progressively to be sold off, many to managerial buyouts by former NBC staff. Subsidy was to be paid for specified services, subject to open competitive tender, in a context where competition on routes was quite free.

2. These simultaneous and sweeping changes make it very hazardous to try to answer the question - what does the record show, so far, about the impact of deregulation, the most exportable of the changes, and one which presumably most interests this conference. Moreover, we have to consider the 'dogs that did not bark in the night'. The Act did not say so, of course, but Government policy at the time was not only to change subsidy payment methods, but also to save on subsidy, which had grown alarmingly over the previous decade. From the point of view of saving public money and preserving bus output, deregulation was seen as a key move, because it would, it was hoped, both discipline wage rates and encourage productivity bargains. Also, from the point of view of predicting the outcome of policy changes, what was logically needed was an analysis of entry conditions remaining after the

licencing constraint was removed. Only one such potential "dog" had been identified at the time, the possible anti-competitive potential of bus station ownership, (due to the experience with Victoria Bus Station after the 1981 deregulation of long distance coaches). This was dealt with in the Act, but there was no attempt to define a policy for whatever impediments to entry there might be once what was assumed to be the binding constraint, the licencing system on local stage service, was removed. Some of us responsible for providing the policy guidance at the time knew this well, but the point was too subtle and difficult to answer in time to affect the policy process. I shall return to this point later.

3. However, the Government did set up a quite elaborate evaluation system for deregulation, the centre-pieces of which were to learn about the services offered, and to track their changes, by using the new licencing records, and to set in train a series of local studies of bus services. The result has been that the Bus and Coach statistics (December 1988) now tell us much more about local stage bus services than they did; and we have the benefit of several reports of what has been happening, both in metropolitan and non-metropolitan areas. In March 1989, the Monopolies and Mergers Commission reported on its analysis of a merger between two former NBC companies, Badgerline Holdings and Midland West Holdings. The merger was referred because though it was by no means the only move after 1986 to undo the divestiture of the NBC by recombining former subsidiaries, it put together two geographically contiguous successors. This report adds its quantum to information about developments.

II The Impact of deregulation?

4. I begin by presenting what seem to be the key findings in the Bus and Coach data. It is mainly notable for dividing its findings into different

areas of GB, which allows some comparisons directed at the likely impacts of the policies. A proper statistical design based on contrasting experience in different areas would proceed as follows. We first nominate the principal policy elements, which in this case are deregulation, subsidy and privatisation. We would try to distinguish areas of contrast on these; namely of

deregulation/no deregulation;

those where subsidy changed much and where it changed little;

those which experienced privatisation or did not.

From these contrasts we would get $2 \times 2 \times 2 = 8$ possible combinations. We would then divide our observations among these combinations, both to distinguish the impact of the separate elements and, more elaborately, their interactions.

5. Unfortunately for such logic, certain combinations in the 8 refuse to emerge in practice. For example, London was not deregulated, which provides the required contrast on that dimension with the rest of the UK. We would then hope to hold the other two changes, privatisation and subsidy, constant. But London was not privatised (London Regional Transport was obliged however, progressively to adopt tendering systems for all services). And the statistics bearing on local stage services draw a veil over London's subsidy position. So, despite the difficulties, what comparisons can we usefully make?

6. The most useful comparisons are possible between operations in English Shire Counties (ES) and English Metropolitan counties (EM). ES represented 41% of all local bus service kilometers in Great Britain 85/86, and 47% outside London. EC covered 28% and 32% respectively. Limited comparisons are possible also with Scotland, for which the comparative figures are 14% and 16%. We can take 1985/86 as the best available representation of the "before the Act" situation, and the latest representation two years later, 1987/88.

(Whether 2 years is a period long enough to measure the impacts of the Act is question to which I return later; this is all we have so far, largely because the effort to record relevant variables was itself coterminous with the Act).

7. In terms of the Act's chief policy variables each of these areas may be characterised as follows:

. Deregulation:

all were subject to deregulation.

. Subsidy:

they varied in the commencing (1985/86) incidence of subsidy.

ES had an average subsidy per vehicle km of about 19p; EM 61p; and Scotland 30p.¹ Operating costs per vehicle km excluding depreciation and net of

fuel duty rebate are not recorded for these areas, but they are for other aggregates which may be taken as fairly representative. I take the

respective representatives as 'Other English Operators' for ES ;

'Metropolitan PTC's' for EM; and 'Scottish Welsh Operators' for Scottish.² So

for 1985/6, we may nominate for ES £0.9 per km; EM £1.3 per km, and

Scotland £0.9 per km. The approximate degrees of relative subsidy was ES 21%; EM 47%; and 33%, on a vehicle km basis.

1. The computation and sources are shown below

2. From Table 4.1 Bus and Coach Statistics 1987/8, (Provisional) DOT, December 1988, hereafter quoted as 'B&CS'.

. Privatisation:

On privatisation they also differ. ES contained most of the NBC company territory, so was subject to full privatisation plus divestiture. EM covers much of the major conurbations outside London, and so was the scene of most restructuring of municipally owned companies to become subsidiaries of local authorities. In Scotland, no privatisation occurred. The Scottish Bus group, left intact, operated 59% of stage vehicle km in Scotland in 1985/86 (Tables 1.3 and 1.1 B&CS).

8. These areas' common experience of deregulation was tempered by different starting points and collateral changes. As between ES and EM, there was a very differing level of initial subsidy for policy to attack. On the other hand, ES was the scene of most privatisation; the EM organisational change here was meant at the time to facilitate change in subsidy methods, and as a possible precursor only to privatisation later. So here we have the two policy measures affecting each differently. A comparison between EM and Scotland focuses more on the privatisation issue, though Scotland had markedly higher level of initial subsidy.

9. From B and CS we can build up the following picture of passenger experience and impact on operator finances over the 2 years. Table 1 presents changes in numbers of journeys made; a quality variable, namely, the quantity of service offered in vehicle km; and average fares. Unfortunately, the monitoring effort did not include systematic sampling for passenger mileage, so we have to make, here and elsewhere, the rather shaky assumption of no change in average passenger trip length if we wish to interpret journeys as a measure of output demanded.

Table 1

Passenger experience over 1985/6 to 1987/8 % charges

	ES	EM	Scotland
Journeys ⁽¹⁾	-3.0	-16.2	-3.3
Quality of Service ⁽²⁾ (v kms supplied)	+17.8	+7.5	+15.4
Real Fares ⁽³⁾	+1.4	+28.5	-2.9

10. Alongside these changes were important shifts in operators' finances. These elements are involved - the change in fare box, money collected via direct charging;
changes in costs;
and changes in subsidy received.

B&CS allows estimates to be made as follows:- passenger journeys (T2.1) are multiplied by the real fares index (T3.1). For costs, vehicle km (T1.1) are multiplied by relevant costs per km (T4.1), using the proxies mentioned earlier. Subsidy comprises 4 elements for ES and Scotland: Public Transport support (T5.2); Concessionary Fares (T5.3); Fuel duty rebate (T5.1) and Rural bus grant are estimated by the proportion of UKms operated in GB outside London, the basis for T5.1.

(1) Calculated for T2.1 - B&CS

(2) Calculated for T1.1 - B&CS

(3) Calculated for T3.1 - B&CS, using the RPI deflator presented

11. Table 2 presents these changes, together with changes in costs per vehicle km(T4.1) and the calculated incidence of subsidy per passenger journey. We do not have figures of total revenue. So the weight of the fare box compared to subsidy cannot be calculated. But certain combinations of the signs of the changes permit the net change in finances to be indicated.

- Table 2 about here -

12. Comparisons between these three areas must be primarily concerned with what is added to deregulation by changes in the other variables, subsidy and privatisation. Easily the most conspicuous changes have been in subsidy. Here EM, the English Metropolitan counties, stand out, with a 25.5% fall in subsidy over the two years. This is the more remarkable when we consider that the fuel duty rebate is affected by operators own actions - if output (VKM) is raised more duty accrues.* Government policy here was merely to let

* But not for specialist work, eg, school contracts.

TABLE 2: Changes in Operating Costs and Finances 1985/6 to 1987/8

	ES		%Change		EM		%Change		Scotland		%Change	
	85/6	87/8	85/6	87/8	85/6	87/8	85/6	87/8	85/6	87/8	85/6	87/8
% Fare Box	-2.5				+7.7				-2.9			
<u>Subsidy</u>	£m real				£m real				£m real			
Public Transport Support	94	67			218	117			29	22		
Concessionary Fares	69	68			115	124			40	43		
Fuel Duty Rebate	57	58			39	36			19	19		
Rural Bus Grant	-	11			-	-			-	4		
Totals	220	204			372	277			88	88		
<u>Total Costs</u>			-7.3				-25.5				+0	
<u>Subsidy per vehicle-mile</u>	.259	.204	-8.4		.647	.448	-19.4		.309	.267	+2.6	
<u>Subsidy per vehicle passenger journey</u>	.139	.134	-21.2		.179	.160	-30.7		.309	.267	-13.4	
<u>Representative costs per vehicle mile</u>	0.9	0.7	-3.8		1.3	0.9	-10.7		.131	.136	+3.5	
			-22.2				-30.8		0.9	0.8	-11.1	
<u>Ratio % of total subsidy to total vehicle costs</u>	28.8	29.1			49.8	49.8			34.3	33.4		

the fuel rebate's value to decline with inflation. Government's most important direct action was to cut public transport support. Local authorities could and to some extent did offset this by increasing Concessionary fare support.

13. A plausible scenario for EM sector is that the authorities' companies raised fares sharply, in response to a drastic cut in subsidy, but were much helped by deregulation, whose effect on costs was drastic. Deregulation, it seems, represented a credible threat to rents enjoyed by labour under regulation. The appropriate adjustments were quickly achieved. That the bargaining position of local authority bus operators versus organised labour shifted sharply in the former's favour is well brought out by Table 7.3 of B and CS, reprinted as Annex 1. Here the shift in the types of staff employed over the two years is tracked amongst different types of operators. Arguably, most formidable strongholds of union power was in maintenance and in the urban areas. Yet in two years the Metropolitan PTC's shed 41% of their maintenance staff, easily the highest among all the operator categories. (National Bus followed with 23%.) Presumably maintenance was contracted out instead. The shift in platform staff, by contrast, though generally downwards, had more to do with achieving required output change. In Scotland, where subsidy was hardly changed, the reduction in overall costs per vehicle mile was much less but, again, it did not experience privatisation.

14. As Table 2 shows, costs per vehicle mile fell over 20% in ES. But this sector was also that most affected by shifts in the operator's vehicle size. Table 6.3 of B and CS makes it possible to infer that the seats supplied in smaller (less than 35 seat) vehicles, including so called 'mini buses', may

have shifted from about 2% to over 10% during the 2 years.* No other type of operator was affected nearly so greatly. The obvious marker for the effect of deregulation would be London Buses Ltd where no credible threat of deregulation yet existed. LBL's cost per vkm fell by about 12%. But there, contracting for individual services was proceeding quite rapidly over the same period. The figures include the services operated under these contracts. That there has been a major effect of deregulation on costs is widely conceded and is certainly supported by these comparisons; but its precise magnitude is doubtful.

15. Subsidy change also clearly affects the 'passenger experience' quoted in Table 1. One could not expect EM, losing subsidy heavily, to expand service quality as much as did Scotland or ES, and so it happens. Yet all did increase service. Scotland's very small change in subsidy, when seen against the others' experience, permits the generalisation that quality of service was probably strongly positively affected by deregulation. Net of subsidy effects, fares were probably not much changed, and neither were journeys. On a Scotland - ES comparison the principal additional effect of privatisation, was probably also to reinforce the drive for cost reduction.

+ Attributing 14 seats to the up to 16 seat category, 25 seats to the 17-35; 10 seats to the 36 plus category and 70 to double deckers

16. The principal warning arising from the data is that one ignores the impact of the change in subsidy on activity levels at one's peril. But as Table 2's figures on the ratio of subsidy to vehicle costs per km shows, the UK stage bus industry remains a heavily subsidised one. Those of us who were helping to formulate the Government's policy in 1984 stressed that it would be most unwise drastically to reduce subsidy whilst carrying out the other major reforms, including the reshaping of subsidy itself. From the figures just quoted, it seems that an almost miraculous feat of minimising subsidy change with respect to realised output has occurred! Yet the fact of high remaining subsidy has a part to play in explaining the degree to which new competition has appeared since 1986. A principal expectation of deregulation was that considerable entry would occur. Before exploring this, probably the widest held belief about deregulation, let us examine the principles involved.

III. Expectations about competition

17. Entry, or the threat of it, is the mechanism by which all firms are constrained to produce socially optimal outputs of the quality and at the price demanded at costs reflecting opportunity costs of resources put in, and no more. This roughly describes the normal neoclassical approach to policy recommendations, implicitly or explicitly arguing from a set of conditions in which there are no obstacles to entry. In buses, the minimum size of an operating unit may set some ineluctable barrier, and might in circumstances of low demand - e.g. after peak hours, create an unassailable natural monopoly element via the threat of sunk costs. But this would not, it was normally thought, constitute much of a barrier. However, this useful insight has to be greatly supplemented when it comes to predicting the effect of deregulation; and this was certainly true of UK in 1985.

18. It was known, or at least expected, that regulation itself was, after 50 years of influence, the leading constraint to entry. The industry had adapted to it, and to the subsequent movements in rising then falling demand, growing subsidy etc which affected all existing and potential players. That perception was probably correct; but it was insufficient to argue the likely effect of deregulation by debating the question of economies scale, and whether the incumbents could, independently of entry conditions, use their often large size to deter entry. Yet these were preoccupations both of most of the government side and of the academic critics. As I remarked earlier, what was not done was systematically to consider how and why entry would occur after deregulation. This involved both a different reference point for analysis and a good deal of hard empirical work. Stephen Glaister and I tried to inculcate the former; the latter was impossible in the time available. Unfortunately, the analytical needs are still not being met in the monitoring outputs so far, or indeed their specification, so far as I can tell.

19. Whether entry will occur will depend on whether an entrant can foresee a profit. The removal of the ^{primary} \wedge constraint (in this case quantity control) gives the potential; but this merely sets up the problem. An entrant must be able to overcome disclosed barriers, if they exist; but also will be more likely to enter if he has some unique deterrent of his own, be it only first mover advantages. Further to move away from simple neoclassical assumptions, entry is more likely, ^{the greater} \wedge ^{is} the difference \wedge in perceptions and prospective performance of entrants and incumbents. Entry in general is in fact largely explainable by differences in views of the realities of existing demand, costs, etc. Innovation - in organisation as well as developing new market niches, contracting labour etc., - is an important basis for entry because it simultaneously erects a potential shelter from further challenge. So to

predict entry is an exercise in the simulation of profitable opportunities.

20. If one takes this view of entry, it follows that predicting interactions between incumbents and entrants, potential or actual, also becomes complex. Entry conditions cannot be assumed, as in most neo-classical accounts; they have to be established. Clearly, if incumbents anticipate, and are capable of emulating, all entrant moves, no entry will occur, so long as they shift to the entry - deterrent quality and prices. But their capacity to do this is one of the questions to be addressed. So is the relative profitability of repelling entry to restore the status quo, or adapting to it, or merging with entrants when established, etc. In general, incumbents are most unlikely, if pursuing profit themselves, simply to sacrifice to profit in attempted predation against newcomers merely to restore the status quo. What compensates for the loss of profit in the meantime? The most likely answer is -it will be worthwhile only if the action itself leads to a shift in the condition facing entrants, that is, some new barrier can be erected. In the 1985 UK context, incumbents stage services, even after the NBC divestiture, were quite large (there was an idea that 200-300 buses were an 'optimal' scale for bus operation). How the initial market position of incumbents would be used was unclear, because no sound basis for prediction had been established. Moreover, the incumbents themselves had no ready-made analysis. They would have to learn from experience following deregulation.

21. In practice, to predict entry, one does one's best to imagine the lurking barriers, to reason by analogy from other, freer industries, and understand how those placed upstream and downstream of the activity under scrutiny could themselves profit by organising entry, not necessarily by themselves. As seen earlier, the Act's framers did spot the importance of one potential barrier, bus stations, largely because of experience with

Victoria Station after the 1981 deregulation of long distance buses, and acted to circumvent this. But access to bus stations is of much less importance in running local stage service, and little else was actively anticipated. Two years of experience of deregulation suggests possible disclosed barriers to entry.

IV. Impediments to entry?

22. It is generally agreed that actual entry into established incumbents' service areas has been very patchy so far. TRRL's study of deregulations' first year reports that '400 more private operators are running local bus services.'^{*} The total number of private operators in GB is about 5000. From a very low base, private operators' stage service provision outside London nearly doubled between 1985/86 and 1987/88 (B and CC, Table 1.4). Much of this new work was probably from successful bids for contracted subsidised services. Private operators supplied 29% of these services outside London in 1987/8 (B and CC, Table 1.4). The entrants have contributed substantially to what most observers would judge to be active competition for the new-style specifically subsidised services, contracted by local authorities.

* Bus deregulation in Great Britain: A review of the first year. R J Balcomb, J M Hopkins and K E Penet, TRRL Research Report 161, p 23.

23. However, there are few signs that changing to this new form of subsidy has provided important profit-making opportunities for new styles of operation. I had some hopes in 1986 that the new-style of individual route tendering, oriented explicitly to social purposes, would be the basis for a new kind of specialist enterprise, organising bidding in several geographical areas simultaneously, rather in the style already found in subsidised catering work. Part of the attraction of this postulated new enterprise would be skill in defining bases and rationalisations for specific subsidies, a much underdeveloped expertise. Unfortunately for this hope, the scale of this form of subsidy has fallen substantially. As Table 2 shows, in ES and EM and Scotland, Public Transport Support declined in real terms from £341m to £206m over the two years. This is hardly conducive to innovatory effort! As I shall argue later, there were other inhibitions to any form of organisation such as I envisaged, which would require great flexibility in hiring factors of production.

24. Private and other operators have probably regarded the subsidised work as a fringe activity. A very wide dispersion of bids has been observed, and as Stephen Glaister's and my paper on London bidding shows has been a repeated pattern over a considerable period. Bidding is opportunistic, dictated essentially by the state of a company's work in other areas at the time of bidding, which will mostly be non-stage work. The search for profit then produces bids ranging from those reflecting attempts to fund new vehicles and men to those filling up spare capacity.

25. Organisational innovation is much dampened by the survival of barriers to entry from pre 1986 days. Specifically, vertical disintegration of bus ownership and operation appears to be very difficult because of rules on operators' licences, which are of course still required to offer a service.

Some of these do not seriously inhibit entry and are desirable on other grounds, for example, the requirement to be of 'good repute'. But to get a standard licence, to quote, 'You or your transport manager must satisfy the requirement of professional competence', meaning either a grandfather right, or by examination by various competent professional bodies.* 'Financial fitness' and adequate maintenance arrangements have also to be shown. The significance of these barriers to vertical integration in particular was shown in a recent case concerning the question of whether a licence holder could franchise drivers without the qualifications to run buses on his behalf. That is, could drivers holding only PSV licences, entitling them simply to drive buses, be hired as self-employed persons? The answer was 'no'. This reinforced the need for drivers to be wage earners and blocked off what for many might be an attractive way to get independence, with attendant risks, returns (and tax advantages).

26. The consequences of this for entry are clearly adverse, and go further than imposing a cost of entry for any driver-employee who wishes to compete independently. (Until deregulation, the almost universal norm was for bus companies to own, not lease vehicles, as part of a fully integrated operation through to the drivers.) Franchising, or more widely, the divorce of ownership of vehicles from their use by individual drivers, is an important support for the growth of the bus-leasing business, at present slow. In the London taxi trade, where leasing is common and there are no bounds on disintegrated forms of production, drivers can and do surmount substantial personal entry costs, to create very elastic labour supply. (In the London case, the principal requirement is for 'the knowledge' of London routes.) We

* PSV Operator Licencing, HMSO Nov 1986, para 8 and appendix 5.

can perhaps expect disintegrated forms of production in the stage carriage buses eventually to emerge even after the set-back just described. But we cannot be certain that there are not other inhibitions to such organisational innovation, yet to be disclosed.

27. In the 'commercial' operations (defined as those not specifically tendered) which comprise over 80% of stage carriage work, substantial incumbents have not, so far, apparently had to yield much market share. As explained earlier, an immediate effect of deregulation was to loosen the labour market. This was probably a differential bonus to the larger incumbents, especially those in urban areas, because the rents enjoyed before deregulation were higher there. Their position was strengthened relative to potential competitors, whose initial labour rents were probably lower. Again, NBC successor companies in particular anticipated innovatory moves by investing heavily in minibuses before deregulation and then running them during the change-over. It is possible to interpret events so far in a way which would be in line with ideas about contestable markets namely, that incumbents have been constrained to act as if in competition. But are incumbents sustained in other ways? Two leading candidates to consider are the impact of subsidy and its operation; and access to locations for operating.

V. Subsidy and entry

28. We have seen that largely as a result of falling unit costs, subsidy in total is as important to finances now as it was before deregulation and has switched towards concessionary fares. Methods of giving concessional fares vary, and have different consequences for calculations about entry. Concessionary fares are an important element of receipts in 'commercial' routes (ie, those not directly subsidised and subject to tender). An entrant

who wishes to establish a competing service of whatever size, must be able to anticipate cash flow from this source. What risk does he face?

29. Local authorities are formally forbidden to operate schemes which favour the incumbents. Whatever scheme is devised must be open to all comers. (Most were focussed on 'elderly persons', the blind, and those with limited mobility at the time of deregulation.*) From the present view-point the important distinction is between those schemes which generate trips through putting the cost at the marginal trip, albeit within stated times etc at zero; and those which do not. The principal form of the latter is the token, entitling a fixed recompense to an operator getting one from a customer. Apart from the transaction costs he faces to do so (and incumbents cannot escape these either) tokens pose no special problem for the entrant in terms of predicting quantity of travel. Token schemes are far more frequent than we realised in 1985. But they are mostly found outside the big conurbations, where the bulk of subsidies for concessionary fares are spent. The conurbations also have a disproportionate share of large incumbents, often municipal operators.

30. The principal problem for a would be entrant is judging what his revenue will be. In considering 'commercial' operations the potential entrant, particularly in urban areas, has a very difficult task in computing what his take (the contribution from subsidy) will be. He will be recompensed when he carries, say, an old age pensioner on a half fare pass, but how many times can he hope to pick up pensioners, and with what certainty? What is known about

* (Compare Table 1 Concessionary Fare Schemes in Great Britain: D M O'Reilly, TRRL Report 165, 1988.)

trip-makers' reponse to half price, or even more, free pass travel is of little comfort. The TRRL report on Bus Trip Generating fares concessionary fare schemes in six towns makes the uncertainty very clear.* Further, there is the problem of the subsidy authority's cost of validating claims. These must be backed up by enforcement procedures, involving some form of spot checking. This is disproportionately costly, the smaller the entrant, and it would not be surprising if the subsidy authority operates the system in practice so as to discourage the small operator.

28. Now, an entrant's most simple way of judging demand is by practical trials. This was always the most effective form of market research. But it is severely discouraged where there is a substantial quantity of concessionary fare travel. Moreover, an experiment, if he attempts it, must also be defined and carried out for six weeks before he can withdraw. In order to reduce the uncertainty of pay-outs from subsidy, the scale of entry must be raised. (If it was large enough, presumably the entrant's expectation of pay-out would be the same as the incumbents'.) So, in present conditions a substantial barrier to entry arises.

29. In metropolitan areas with alternative public transport modes, eg, some form of rail operation, the potential entrant's difficulty in assessing pay out is compounded by the operation of cross-mode passes. Buses represent an important short trip complement in such cases. The problem of getting proper recompense from these here is important for London Buses, even though LBL is in the same ownership as London Underground; the method of computing the cash due to LBL from trips made by such pass holders has been very contentious.

* TRRL report no 127, P B Goodison, J M Hopkins and R P McKenzie.

30. All forms of fare passes, whether offering free trips at the point of use or not, offer user convenience. Were a specialist form of agent to arise dealing in such passes, a would be entrant's difficulty in overcoming incumbents' advantages would be eased. (An incumbent, has for example always the right to refuse to recognise another company's pass, and would always do so unless adequately compensated.) So far as I am aware, there has been little sign of agency activity of this sort. It is hardly surprising, since would be agents too must judge the chances of entrants' establishing worthwhile business. Thus the problems generated by subsidy are compounded.

31. There have nevertheless been some well-publicised attempts at larger scale entry, some with as equally well publicised failures. Greater Manchester's response, as an incumbent, to a large scale minibus incursion in south Manchester was to respond with matching services. One obvious option, of serving north Manchester instead and thus attempting a geographical division, ceding market share in the South but getting at least first mover advantages in the North, was rejected. After persisting for over a year, with substantial losses both sides, the entrant withdrew. The MMC report on the Badgerline Holidays (BL) take over of Midland Red West reports BL's losses from entry into Salisbury and Poole, geographically fairly distant from its established home around Bristol. BL lost £560,000 in 1987, most of an overall reported loss on a turnover of £15.4million of £577,000. BL lost a further £402,000 in 1988 before the services were discontinued. MMC also reports that very few attempts at entry occurred in Midland West's ('City Line') territory, the centre of Avon, including Bristol itself. The six recorded registrations of new services have been 'works' services operating only in the early morning and early evening. By contrast; in Badgerline's territory outside Bristol, BL 'faced competition on all or part of 52 of its services, from 21 private operators.'¹

VI. Property constraints

32. These experiences strongly suggest that entry into urban core areas is differentially impeded. Unfortunately, the MMC did not investigate this question, and so does not throw any light on the possible importance of the factors I have suggested. But their report does by implication add another probable constraint: the ownership of bus depots. City Line owns 4 bus depots for maintenance and storage of vehicles, three of these under licence from Bristol City Council. BL owned one such site in Central Bristol. A major reason for merging - indeed easily the most substantial tangible cash benefit - was realising the value of this and other sites. 'Ways of realising this potential are being investigated and may include the merger of BL Bristol and City Line engineering work shops on to a single site'. The property covered stood at over £3m in the balance sheet².

1. Page 9, MMC Report.

2. Page 18, MMC report. We are not told what the market valuation was or if different from the book value.

33. Many incumbents in central urban areas have inherited sites such as these, whose scarcity value in bus operations is sustained by town planning rules. Conversion of a rival suitable premises for operations by existing uses probably at best involves a protracted planning negotiation. Incumbents owning these service sites have the option of profiting from their sale, but then have to substitute premises, if they also wish to continue in bus operations. If they can find a suitable partner with well placed excess capacity, they can both sell and continue bus operations without incurring the costs of search, conversion of a new location etc. (This seems to have been a basis for the BL and Cityline merger. BL had the freehold, City Line licenced depts from which bus operations could be sustained by BL.)

34. Town planning restrictions, impeding the operation of the property markets, thus take their role in bus operation, as in many other service-oriented industries. It may well itself account for much of the patchy emergence of urban competition so far; entry has been dependent on the location of usable premises. But their significance hinges on the scale and organisation of bus operations. Minibuses in particular could well be operated in this respect like London taxis, where the old style large firm, with its large depot, has long since disappeared. Owner operators of minibuses, for example, could easily overcome property scarcity even in London. As I have argued, however, there are other barriers which keep the scale of effective entry high, and hinder the organisational innovations which would encourage small scale ownership.

VII. Conclusions

35. If we together put the suspected entry constraints which have been revealed by the withdrawal of the primary constraint, the pre 1986

restrictions, we have the hypothesis that entry has been both quantitatively greater and more likely to have been sustained, the less densely populated the area of operation. The relative incidence of subsidy, its constitution, its administration, and the impact of locations for operations all go in the same direction. Also, negatively, the inhibition on organisational innovation, which is basically more favourable where labour supplies are plentiful, has yet to be realised. One would like to see this hypothesis properly tested; unless and until this is done, entry constraints remain speculative.

35. However, I think the UK experience as just interpreted does offer some warnings to those who launch on a policy of deregulation. Do not expect much competition to arise unless the underlying constraints are also tackled, though you can expect more productive labour contracts. Also, do not expect successful entry for a considerable period after reform. Much learning about the new possibilities has to go on by incumbents and entrants alike. Collateral changes have to take place in supplying activity, eg, the growth of a bus leasing market in the UK case. Above all, subsidy policy needs careful definition. Reducing total subsidy will have the unsurprising effect of dampening down total activity and therefore entrepreneurial interest. But its constitution is more important. Socially oriented subsidy in the form of bidding for specific contracts is mildly conducive to competition. Subsidy in the form of concessionary fares plays into the hands of incumbents.

36. A final warning is in order. If substantial competition is to occur, management culture has to change, towards more stringent profit-seeking orientation. I doubt whether the UK has gone far yet towards this, perhaps especially in the big conurbations. Privatisation is a key move in affecting managerial attitudes to profit. Divorce of ownership of bus operations from local authority control is perhaps the most significant of the unfinished

business left by the Acct of 1985. Local authorities are being encouraged to go in for voluntary privatisation, of course, and some are responding, as in West Yorkshire. Ironically, the Secretary of State for Transport, in using his powers of consent to that management buyout, has felt obliged to match the size of nearby incumbents, - a last reminder that the underlying props to incumbent scale have yet to be seriously challenged.

By type of employment and operator

Thousand

		Platform staff	Maintenance staff	Other staff	All staff
London Buses Ltd	1985/86	17.9	3.7	4.2	25.7
	1986/87	16.1	3.5	3.8	23.4
	1987/88 (p)	13.4	3.2	3.1	19.8
Metropolitan PTCs	1985/86	19.2	10.3	6.5	36.0
	1986/87	17.1	8.0	5.4	30.4
	1987/88 (p)	16.0	6.1	4.4	26.5
Municipal PTCs	1985/86	9.6	3.9	2.6	16.1
	1986/87	9.0	3.3	2.3	14.7
	1987/88 (p)	9.4	3.2	2.2	14.7
Scottish Bus Group	1985/86	5.6	2.1	1.5	9.2
	1986/87	5.8	2.0	1.6	9.4
	1987/88 (p)	5.6	1.9	1.5	8.9
National Bus Co (and ex-NBC)	1985/86	28.0	10.3	8.8	47.0
	1986/87	29.0	9.4	8.5	46.9
	1987/88 (p)	28.5	7.9	7.2	43.5
Other private companies	1985/86	25.1	6.9	8.1	40.1
	1986/87	26.7	6.8	8.2	41.7
	1987/88 (p)	30.4	7.5	7.5	45.4
All operators	1985/86	105.4	37.3	31.6	174.3
	1986/87	103.7	32.9	29.9	166.5
	1987/88 (p)	103.3	29.7	25.8	158.8

(1) For 1985/86 and 1986/87, figures shown are annual averages; for 1987/88, they relate to the year end.

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(1) Revenue support, prior to deregulation on 26 October 1986. The figures for 1985/86 and earlier years are not entirely consistent with those for 1986/87 and are thought to affect the broad trends shown.

Source: administrative returns by local authorities and PTAs.

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