

Aircoach: An Experiment in Deregulation

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The deregulation of the city centre to Dublin Airport bus route is examined in this essay. Nina Kauntze and Stephanie Forde examine how this first example of bus deregulation came about, and its success so far. They conclude that the project has been a success, improving the productivity of all public transport serving the airport, and increasing customer choice.

Introduction

Dublin Airport is one of the only hub European airports not served by a rail to city centre link, but is served by a taxi and bus service. Taxis are expensive but direct, while the buses prior to November 1999 offered a cheaper but more inconvenient alternative. Aircoach is a frequent (every fifteen minutes), luxury coach service serving fourteen Southside points via O'Connell St to the airport. Aircoach, which began operating in November 1999, is a recent example of how a private enterprise has penetrated the semi-state bus market in Ireland. Mary Leane, the Director of Aircoach said, '*CIE Union employees simply believed that deregulation would not take place*'.¹ This study looks at how Aircoach managed to break the mould.

Economic Theory: Deregulation and Contestability.

Deregulation has become important for competition in transport markets. The failure of state-run industries '*to achieve the social goals they were set up to attain*'², has proved that they are a dated solution to the problems that might occur in an open market: monopoly or excessive competition. Nationalised industries have continually lost money in terms of extensive X-inefficiencies and have proved their inability to deliver fast, frequent and efficient services to the public.

Deregulation is needed to increase competition as it encourages new firms to enter an industry that was once purely state occupied. However, deregulation in a transit industry needs careful attention. It boasts many economies, including network and density economies. It has been found that '*transit firms operate under conditions of*

¹ From an interview conducted by authors on 30/01/02.

² McAleese, D. (1997)

*excess capacity of rolling stock*³, and incumbent firms can use this as an entry deterring strategy. In this way and others, they will want the entrant to fear the risk of huge sunk costs or greatly lower the entrants expected profits. The incumbent's resources are thus often misallocated.

Contestability is required to remove these distortions. Baumol's contestable market is '*one in which entry is absolutely free and exit absolutely costless*⁴'; he also states that there should be '*no cost discrimination against entrants.*' This is combined with other vital conditions such as '*insignificant sunk costs relative to fixed costs*⁵'. If Baumol's conditions were to prevail, theory says that following deregulation there might even be just one firm operating in a particular network market who is engaged in average cost pricing, earning zero monopoly profits. Entrants that now have the freedom to enter the market would undercut any higher pricing. Hence, in contestable market theory, the threat of entry is enough to make the firm act competitively and not earn monopoly profits, despite any production properties it may hold that could enable it to do so.

In the case of the Irish Bus Industry, full deregulation has not occurred. However, further integration with Europe means a fiscal movement away from nationalised industries such as this. If a contestable market does involve "absolutely free entry", the Irish Bus Industry is not contestable as will be shown.

The industry evolved from early 1932, when the Fianna Fail government, led by de Valera, worked from a policy of economic self-sufficiency. The success of the newly state-sponsored body, the Electricity Supply Board (ESB), meant that other state-sponsored bodies were set up in many fields including air, train and bus transport. These were seen to be successful at a time of depression and when the '*private sector did not appear to be very enterprising*⁶'.

The Road Transport Act 1932 prohibited the operation of private scheduled passenger services except under licence from the Minister for Industry and Commerce. The Minister stated that the independent bus owners could exploit areas

³ Banister, Berechman and de Rus Mendoza, (1993)

⁴ Baumol W.J, (AER, 1982)

⁵ See footnote 3.

⁶ Haughton, J. (1995)

not already covered by the main companies. The policy was to restrict bus operation other than by railways, namely the Dublin United Tramways Company (DUTC). The DUTC bought out independent bus licences and the industry was soon nationalised. The results of this Act '*reduced the number of passengers carried by independent bus companies from 34.5 million to 1 million per year, as estimated by the Tribunal on Public Transport in 1939*'⁷. Past studies have shown that diseconomies of scale have existed in bus operation. CIE were not keeping prices to a minimum and on similar-distanced routes were being shown up by cheaper independent bus services. Also, some potentially profitable routes were not being fully exploited as will be illustrated in our study of the Aircoach.

The Arrival of the Aircoach

An interview with the Director of Aircoach, Mary Leane revealed the difficult process of creating a private bus route in a semi-state monopoly market. Mary Leane, prior to her endeavour to set up Aircoach, worked for Coras Iompair Eireann (CIE) for five years, where she met John O'Sullivan, the Chief Executive of Aircoach. Through the experience and knowledge of the bus industry Mary Leane saw a gap in the market that could be filled, the city centre to Dublin Airport Bus route. The following points show the market gap:

- In 1999 only expensive taxis and an indirect cheap bus route operated by Dublin Bus served the airport.
- The traffic congestion needed to be reduced (increase of 172% in the number of new private car registrations between 1995 and 2000, approximately half of which were registered in Dublin⁸).
- Increasing passenger numbers at Dublin airport - Aer Rianta has reported that there has been an increase of 5.5 million passengers since 1990 to 14.3 million passengers in 2001⁹.
- The economic boom in Ireland has increased the number of people who can afford to travel.

⁷ S. Barrett & E. Gaughran, (1981)

⁸ Source: Sunday Tribune 13/01/02.

⁹ Interview with Aer Rianta marketing representative.

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- The expansion of Ryanair has also made flights more affordable both for people leaving Ireland and for tourists coming to Ireland.

To acquire a license the company needed to have a Transport Manager with a Certificate of Personal Competence (CPC). Mary Leane attained this and then applied for the license. This procedure incurs high legal costs that can only be refunded by the state if a license has been granted; hence there is a strong financial disincentive to compete with the state monopoly. Upon application Mary Leane was told, *'the current service seems adequate and there were no grounds on which to grant licenses to anybody'*¹⁰. However, Mary Leane appealed on the grounds that there was no link from the Southside of the city to Dublin Airport served by Dublin Bus. This was brought to attention in 1981 by Dr. Sean Barrett in his suggestions for policy in this industry *'Where potential operators offered a new fare or service, this could be licensed as a measure to cater for passengers not catered for at present'*¹¹.

The final outcome was a change in government policy for a period of time. The license was given on the grounds that the fare charged was £4 and the service offered had to be of a premium standard. The company was granted its licence to operate on a Dublin Airport to city centre route in September 1999 and they began operating on the 22nd October 1999 with eight coaches and a £2m bank loan. The reason for this urgency was *'otherwise we would have been crushed by the semi state'*¹², said Mary Leane.

The Effects of the Evolution of the Aircoach.

Initially Aircoach was in direct competition with the taxis and Dublin Bus. The full effects of having a competitive market can be seen at the airport today. Two more private bus services entered the market within twelve months of operation. These served the airport but to different areas of the city, the Aerdart private bus service that links the Dart station at Howth Junction with the Airport and the Route 2411 a private bus service between Tallaght and Dublin Airport. Almost immediately the Dublin Bus also improved its service. The number of bus routes to Dublin Airport increased dramatically. In May 1999 the 747 and the 748 served the route. Now the

¹⁰ From an interview conducted by authors on 30/01/02.

¹¹ S. Barrett & E. Gaughran, (1981)

¹² See footnote 8.

route is served by the 747, 748, 16A, 746, 230, 41, 41A, 41B, 41C, 33N, 41N, 46X, and 58X covering all areas of Dublin. This shows that this potentially profitable route was not being fully exploited by Dublin Bus prior to the establishment of Aircoach. Dublin Bus has therefore put itself in competition with Aircoach on certain routes and improved its service dramatically with a frequency of buses every ten minutes. This is a classic case of incumbent reacting to entrant, as Mary Leanne said *'a little bit of competition is the best thing in the world'*¹³.

The arrival of the Aircoach was not without opposition. There were reports of blockades by taxis and eggs being thrown by bus drivers. A current problem that has been encountered by the Aircoach bus drivers is that taxi drivers are pulling up at Aircoach stops and taking passengers to the airport for the same fare. This is in fact illegal but difficult to prevent¹⁴.

Aircoach, after the loss of £600,000 in the first two years of operation, is now turning a profit. The stopping of the Malahide route in November 2001, as it was not as profitable, has been essential in cutting losses. Mary Leane believes the key points of success of the Aircoach to be *'frequency, quality, the right route, reliability, with a competitive fare'*. The Aircoach now carries on average between 1800- 2500 passengers a day. The fare of five Euro includes luggage and children go free, this is directly comparable to the high taxi fare that does not include luggage and charges for children. Hence the service differentiates from those provided by taxis and Dublin Bus. Also unlike Dublin Bus the route of the Aircoach serves hotels and many residential areas. The main market for the Aircoach is business travellers, hotel guests, and residents close to the busiest stop in Donnybrook. Hence the customers are the sort of people that the "luxury" service appeals to and also those who do not wish to pay the high airport car park charges. Aircoach has thus captured a market.

Survey of Airport to City Centre Transport Route:

We undertook a study of the effects of current deregulation of the bus industry at Dublin Airport on Friday 25th January 2002 in order to determine if any one route seemed to be suffering. We conducted a study at two separate times: 10.30 a.m. and 11 a.m. The study comprised of passenger counts on each departing bus service from

¹³ See footnote 8.

¹⁴ Source: Results from a questionnaire carried out with bus drivers, (25/01/02)

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the airport. The number of people in the taxi rank queue was also recorded. The results have been averaged and are listed below:

- Taxi rank - 29 people.
- Dublin Bus - 36 people.
- Aerdart - 6 people.
- Route 2411 - 3 people.
- Aircoach - 21.

From our observations and short interviews with the bus drivers from each company we are able to conclude that there are enough passengers on the peak days (Monday and Friday) to sustain the popular routes. This applies to the taxis, Dublin Bus and Aircoach. The services that appear to be suffering are Aerdart and Route 2411.

Through deregulation of the bus industry at Dublin Airport consumer choice is greatly increased, thus increasing their utility and making people better off, as more efficient services are provided at a competitive price. *'The commuter will truly believe in public transport only when the market provides choice, quality and reliability through competition'* said David Manley President of the Dublin Chamber of Commerce¹⁵.

Other Examples of Bus Deregulation.

U.K.

Britain completely deregulated its bus industry in urban areas in 1985. Before deregulation, the bus industry was similar to Ireland's: local monopoly state operations with standard fares and internal cross-subsidisation between routes. The reasons for deregulation were to end local monopoly control and introduce competition, especially on highly profitable routes. Cost efficiency was also paramount and as a result costs were reduced by up to 20%¹⁶. Privately run buses operate to London airports as well as rail links, an example being to Stansted

¹⁵ Manley, D. The Irish Times 24/03/00

¹⁶ Banister, Berechman and de Rus Mendoza, (1993)

Airport. A single fare on the Stansted Express train is £15 Sterling to London Liverpool Street. An alternative option is to take the bus from Oxford Street, costing £8 Sterling one-way.

New York, U.S.A.

The U.S. bus industry has adopted a policy of competitive tendering which has brought costs down by up to 20% in some cases¹⁷. This bus policy has been particularly appropriate for New York, which has always had rail link problems due to its core being situated on an island, Manhattan. A city centre hotel hopper bus that is cost and output efficient serves its hub airport, J.F. Kennedy airport.

France.

Competitive tendering also operates here with a contract period of up to seven years. This applies to routes in urban, inter-city and inter-urban areas. A result was an increase in the revenue-cost ratio hence subsidy levels have decreased. A private bus service operates from Paris Beauvais airport to an Irish pub, The James Joyce, in the City Centre. This is primarily to cater for the Ryanair customers and serves a number of hotels in the proximity.

The Future

The future of Aircoach can be summed up by Mary Leane's reaction to the introduction of the Metro, '*we will have to be innovative and differentiate the product*'¹⁸. Aircoach has applied for more licences on different routes and will soon begin operating a Dublin to Cork route. The license for this has been acquired with expected resistance from CIE. Aircoach's plans for the future are to increase ticket sales on the Internet. This will remove the responsibility from the drivers, decreasing boarding time and cutting costs, a policy adopted by their cost cutting ally Ryanair. Ryanair sell Aircoach tickets on board their inbound flights to Dublin. Ryanair have helped Aircoach avoid the negative effects of September 11th due to increasing the number of European routes and low fares. The circulation of the Euro, it is hoped, will also increase the number of European passengers due to price transparency.

¹⁷ Banister, Berechman and de Rus Mendoza, (1993)

¹⁸ From an interview conducted by authors on 30/01/02.

Conclusion

We consider that the entry deregulation of a prime Dublin City bus route has been quite successful so far. The entry of Aircoach has not taken away from the revenues, but has rather increased the productivity of Dublin Bus and has met the rising demand for city centre travel from the airport. As a result consumer choice has greatly improved. Overall we feel that the Dublin City centre to Airport Bus Route has moved towards a more contestable market and is an example of how competition has improved the service for the consumer. As Des O'Malley (TD) said, '*after the success in Dublin of Aircoach we should seek to replicate it on a lot more routes. Deregulation should spread the benefits of competition through the country*'¹⁹.

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¹⁹ O'Malley, D. (11/08/00) 'Sharing Our Success' National Conference 2000.

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