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# *Economic* PERSPECTIVE

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## THE PRIVATISED SCOTTISH BUS INDUSTRY

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### 1. Introduction

Within Scotland the bus industry has played a key role in the public transport system, with substantially higher bus journeys and bus kilometres per head of population than in any other part of the UK. Specific reasons for this are difficult to identify, however low levels of car ownership and massive population relocations in the 1950s and 60s are both possible contributory factors. The importance to Scotland of transport as a whole, has been recognised in the fact that it is to be one of the areas of devolved power for the Scottish parliament.

Much has been published on individual changes to the industry over the last ten years, particularly from the Department of the Environment, Transport and the Regions (DETR), and these are relatively well documented elsewhere (see for example DoT 1997). To very briefly summarise, since 1990 in real terms prices have risen and unit costs fallen, passenger numbers substantially declined and total bus kilometres increased.

Given the importance of mobility to the economic and social welfare of communities, particularly the role of bus transport for those on low incomes (Farrington 1994), this paper uses data in the public domain to examine the effects of privatisation and deregulation on the Scottish industry within a British context. Where possible, Scottish figures are compared to the rest of Britain outside London, although some variation will exist within these areas. Nevertheless, it is the overall trends which are considered, with some of the wider ranging effects of rising prices, falling costs and increased output also identified.

### 2. Historical Perspective and Bus Privatisation

Prior to the 1980s, the bus market within Scotland was characterised by heavy state ownership in the form of the nationalised Scottish Bus Group (SBG), local authority owned companies and the Strathclyde Passenger Transport Executive. Furthermore, it was heavily regulated under the Road Traffic Act of 1930. This originally divided Britain into thirteen regional areas, which subsequently became nine with one covering the whole of Scotland, and gave substantial powers to the respective area traffic commissioners.

Consequently, bus services were essentially local monopolies, with very little competition within the industry. The four largest conurbations in Scotland had local authority owned operators, with other towns and cities under the remit of the SBG. This situation remained relatively unchanged until the passing of the Transport Acts of 1980 and 1985. The main provisions of these acts can be broadly summarised as:

- the abolition of all route licensing.
- Traffic Commissioners' control over fares and subsidies severely limited.
- reorganisation of the National Bus Company (NBC) and the Scottish Bus Group into 81 regional operators.
- local authorities required to reorganise municipal operators so that they effectively operated at arms length to the authority.

The actual privatisation of the SBG did not occur until 1990, some four years after the sale of the NBC in England and Wales. Prior to privatising, the group was reorganised on a regional basis into ten wholly owned subsidiaries. Five were sold to management employee buy outs (MEBO), and the other five to existing bus companies, with only one bought by an English based concern.

The sale process itself was not without its critics. McLeish (1992) highlighted a lack of a regulatory framework for the new companies, and argued the whole process was driven by the prevailing political dogma. Moreover, the Committee of Public Accounts (1994) notably identified a conflict of interests arising from many of the pre-privatised companies being managed by the eventual buyers, who thus

effectively had a financial vested interest in the company prior to sale.

Straddling SBG privatisation was the sale of three of the four local authority based companies. Grampian Regional Transport was one of the first sold within the UK, to a MEBO in 1989, Tayside Public Transport to its employees in 1991, and Strathclyde Buses to a MEBO in 1993. Lothian Regional Transport still remains under public ownership.

### 3. Supply of Bus Services

Consistent with extensive state ownership, the bus industry within Scotland has traditionally been heavily concentrated. In 1985 for example, the SBG carried some 46% of all passengers. Figure 1 presents the concentration ratios for the time period 1988 to 1996 for both Scotland and the UK as a whole. This shows the percentage of total revenue accounted for by the three largest companies in the bus industry.

Privatisation in Scotland was thus successful in reducing market concentration, however this was only in the very short term, essentially between 1989 and 1993. Substantial increases have followed, primarily achieved through mergers and take-overs, which have virtually resulted in a return to the 1988 position. Three companies in particular dominate the Scottish market - Firstbus, Stagecoach and Lothian Regional Transport. Importantly however, the first two are public limited companies rather than nationalised concerns as in 1988, which probably explains rising fares and increased output.

Concentration has been far less marked within the UK as a whole, due to the larger overall market size, the larger number of 'big' players with a significant market presence, and consequently higher 'barriers to take-over' in the form of the sheer cost involved of any such acquisition. Nevertheless, the UK position is beginning to follow the Scottish trend, as even the very large companies begin to merge. An early example is Firstbus's acquisition of Strathclyde Holdings in 1996, when the latter in revenue terms ranked sixth and first in the UK and Scotland respectively.

The reason commonly cited for this increased concentration, and hence increased company size, is economies of scale (e.g. TAS 1997, Potts 1995), although the impact such economies have in the bus industry, particularly at the top end, is perhaps open to debate (see Button and O'Donnell (1985) and

Jørgensen (1995)). Two other reasons may be suggested. Firstly, companies are attempting to sales maximise and hence attain a dominant market position, market behaviour entirely consistent with Baumol (1959). Within a declining or stagnant market, such as the bus industry, this is most easily achieved through merger and acquisition of other companies. Secondly, with 12 of the 15 major Scottish companies now owned by PLCs, rather than the position immediately preceding where the majority were owned by MEBOs or local authorities, the demands of the stock market for higher rates of return have led to more expansionist company policies. Simply, direct competition reduces profits, hence rather than compete directly against other operators, improved profitability is easier to achieve through take-over and merger.

With regard to operating costs, Table 1 gives the real cost per bus kilometre for the time period 1985/86 to 1995/96 (excluding depreciation). Figures are shown for Scotland, Great Britain, and Great Britain outside London and Scotland (GBOLS), although it should be recognised that some of the data published by the DETR is known to be unreliable and not sufficiently robust for detailed analysis. As noted above however, it is the overall trends which are of importance. Also shown are the number of passengers per bus kilometre, as a proxy for rates of utilisation.

As has been well documented elsewhere (see for example DoT op.cit.), real costs have fallen substantially over the time period, and consistently, through the changes from a large state owned industry, to smaller operating units, and finally to the dominance of large public limited holding companies. Furthermore, Office for National Statistics (1997) figures suggest these cost reductions have been partly as a result of real wage cuts, longer working hours and staff reductions, and hence not solely achieved through gains in total factor productivity. In general economic terms therefore, this partly represents a transfer from employees to shareholders, rather than solely improvements in efficiency.

Interestingly however, most costs efficiencies in Scotland were achieved in the early part of the period under review, whilst the industry was principally under public rather than private ownership. This suggests 'efficiency' gains were more as a result of deregulation than either company size or ownership form. Looking at operating costs over the whole period, these have been lower in Scotland, but

given an overall faster rate of decline elsewhere, relative costs have become almost uniform across Britain. This would appear to be as a result of mergers and acquisitions which have probably standardised labour costs and integrated working practices throughout.

With falling utilisation rates however, it is questionable if the increase in output from the aforementioned 'productivity' gains has actually been effectively used. More precisely, although there are in effect more buses, these have been primarily used on existing routes to serve a diminishing number of passengers, rather than on expanded networks to serve additional passengers.

#### 4. Fares

Table 2 charts movements in bus fares adjusted for inflation since 1985/86, with 1992 given as the base year. In order to provide an indication of relative price levels, the revenue per passenger for each area is also shown, as actual price data is not collated by any public body and difficult to determine accurately. As figures are quoted for local bus services, variations in fares charged to passengers due to differing average distances should be minimal, and therefore should give a reasonable indication of trends and price differentials.

Since 1985 real fare levels have risen in both Scotland and the rest of Britain, although like operating costs, the pace of this change has not been consistent across the whole country. Fares actually fell in real terms within Scotland in the run up to, and immediately after, privatisation, but since have risen at approximately the same rate as the rest of Britain. Deregulation therefore would seem to have increased competition in Scotland, hence cutting real prices, but privatisation has allowed consolidation to occur within the market and reduced the level of competition, resulting in higher fares. It could be further argued that under public ownership, lower costs were passed onto the consumer in the form of lower prices, which also helped maintain the companies' market share prior to privatisation, but once in the private sector lower costs have resulted in higher profit margins, as mergers or acquisitions have occurred.

In terms of relative fare levels, differentials in the proxy real revenue per passenger fluctuate even more widely, but follow this same rough pattern. These suggest that Scotland began with significantly higher fares than the rest of Britain, a position which was reversed by the

mid point of the period. After 1993 however, slightly higher fare increases had resulted in almost uniform average fares across Britain by the end of the period shown. Prior to privatisation therefore, it may be argued that companies priced on a regional basis, but subsequent industry consolidation and the removal of pricing regulations have resulted in a pricing policy based more on a national perspective.

#### 5. Subsidies

Public support for bus services falls under two general headings. Firstly, public transport support is paid to operators on a franchised basis to provide services deemed by the local authority to be essential. Secondly, concessionary fares are targeted to certain groups within society, and currently in the UK only includes pensioners and the disabled. Given the latter group of subsidies are dependent upon demographic factors, and hence out with the scope of this paper, analysis concentrates on the former. Table 3 therefore gives figures for public transport support, in terms of the percentage of bus kilometres which received local authority support, and the standardised values per supported bus kilometre.

Consistent with higher fares and lower costs, Scotland has seen both a lower proportion of subsidised bus kilometres and a lower subsidy per subsidised bus kilometre. Comparing with the rest of Britain (including London), as with fares and costs the differential has decreased but not by as large an amount, not surprising given such factors are determined at a local level. Nevertheless, it is notable that following deregulation in England and Wales subsidy per subsidised bus kilometre initially fell before beginning to rise in 1990/91. This pattern has not been apparent in Scotland, where the rate of subsidy has remained more or less constant since the early 1990s. The substantial cut in 1993/94 in the English and Welsh figures is primarily due to the removal of subsidy to London Transport, which followed the deregulation and subsequent privatisation of London Buses.

#### 6. Conclusions

At the beginning of the time period under review, the market in Scotland for bus services showed distinct regional characteristics, notably higher fares and lower costs per bus kilometre. Under a nationalised industry, this resulted in lower rates of subsidy. Over the last decade the position has changed

significantly, with fare levels and operating costs becoming uniform across the country, but interestingly differences still remaining in subsidy levels. What is most notable however is the pace of this change, with many differentials first increasing at the time of privatisation in England and Wales, and narrowing since privatisation in Scotland. Furthermore, the situation in Scotland has not been as might have been predicted, as all of the perceived advantages of privatisation actually occurred whilst the industry was still publicly owned. This suggests it was deregulation of the buses and not privatisation which had the larger impact. Post privatised, the industry in Scotland has seen substantial rises in real fares in line with the rest of Britain, and the rate of cost efficiencies decline i.e. a reversal of many of the gains from deregulation. This is not a basis however for proposing a return to the 'free for all' which followed deregulation, but certainly some form of re-regulation may be required, at the very least to limit the regressive effects of rising prices on certain groups within society.

Furthermore, privatisation has led to a 'de-regionalisation' of bus services in Britain, to such an extent that in many cases market differentials have been eradicated. Whether this de-regionalisation is advantageous or not is out with the scope of this short paper, however given bus services are non-transferable and regulated, albeit it lightly, and subsidised at a local level, some regional variation may be to be expected due to the higher dependency and general usage in Scotland. Some of these discrepancies may well be addressed through the new Scottish parliament, but the major danger is in the process of constitutional reform and the nature of the other devolved powers, transport policy as a whole may come low on the political agenda.

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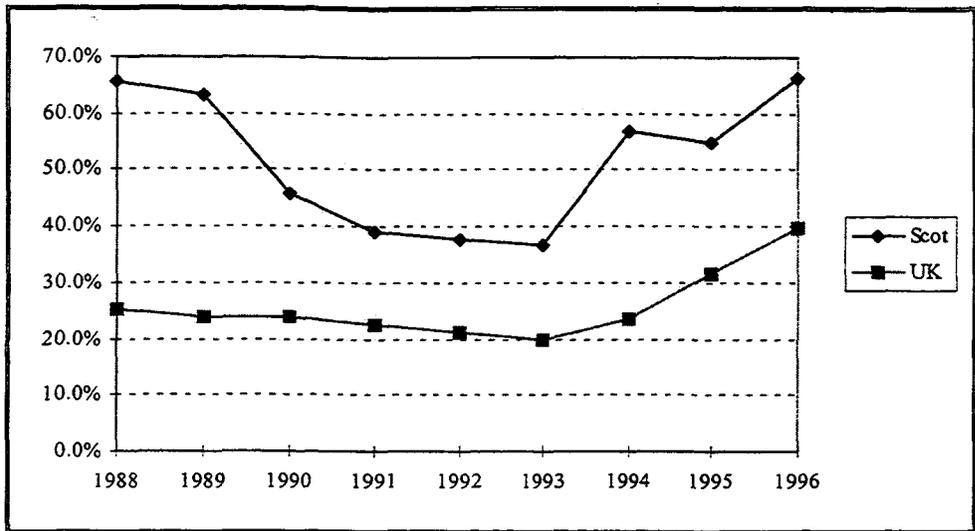
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Figure 1 - Concentration Ratio, % of Revenue Largest Three Firms, Scotland and UK



Sources: Compiled from TAS (1998), DETR (1997) and Scottish Office (1998).

Table 1: Operating Costs per Bus Kilometre, 1985/86-1995/96 (pence), Constant Prices, Passengers per Bus Kilometre, 1985/86 - 1995/96

Year	Operating Cost			Passengers per bus km		
	Scot	GB	GBOLS	Scot	GB	GBOLS
1985/86	127	150	139	2.35	2.72	2.52
1986/87	116	133	121	2.13	2.47	2.24
1987/88	103	115	103	1.97	2.26	1.98
1988/89	98	110	97	1.99	2.18	1.89
1989/90	89	104	94	1.82	2.08	1.80
1990/91	87	101	88	1.74	1.98	1.71
1991/92	79	99	89	1.61	1.87	1.62
1992/93	78	95	84	1.53	1.78	1.53
1993/94	77	90	81	1.45	1.70	1.46
1994/95	75	86	77	1.39	1.67	1.42
1995/96	75	83	76	1.42	1.67	1.40

Source: Adapted from DETR (1997)

**Table 2 - Index of Real Local Bus Fare Movements (1992=100) and Revenue per Passenger in pounds (1996 prices).**

Year	Fare movements		Revenue per passenger	
	Scot	GBOL	Scot	GBOLS
1985/86	100.6	87.6	0.52	0.45
1986/87	101.0	94.1	0.53	0.48
1987/88	100.8	95.6	0.51	0.50
1988/89	99.1	94.9	0.48	0.50
1989/90	96.5	94.6	0.48	0.51
1990/91	94.7	95.0	0.50	0.53
1991/92	97.3	98.5	0.51	0.54
1992/93	101.0	100.7	0.54	0.55
1993/94	102.7	102.6	0.55	0.58
1994/95	106.1	104.3	0.59	0.58
1995/96	106.8	105.5	0.59	0.59

Source: Adapted from DETR (1997)

**Table 3: Percentage Subsidised Services to Total Services, Subsidy per Subsidised Bus Km at Constant Prices**

Year	% Subsidised to total			Subsidy per subsidised bus km		
	Scot	GBOL	GBOLS	Scot	GB	Eng & Wales
1987/88	14.6%	16.9%	17.28%	0.67	1.39	1.51
1988/89	13.5%	16.6%	17.20%	0.64	1.29	1.39
1989/90	14.0%	16.8%	17.31%	0.43	1.03	1.12
1990/91	13.1%	15.9%	16.37%	0.32	1.12	1.24
1991/92	14.4%	16.4%	16.83%	0.43	1.24	1.37
1992/93	13.3%	16.1%	16.59%	0.46	1.22	1.33
1993/94	15.0%	16.1%	16.32%	0.43	0.80	0.86
1994/95	13.9%	15.6%	15.90%	0.43	0.78	0.84
1995/96	15.5%	16.1%	16.25%	0.41	0.73	0.79

Source: Calculated from DETR (1997)

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