

SUSTAINABLE TRANSPORT – BACK TO BASICS

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ABSTRACT

This paper discusses the fundamental requirements for transport to be economically sustainable and argues that the solution to many transport problems is to go 'back to basics'. The single most important requirement for economically sustainable transport is wealth and its cause - economic growth. Wealth is essential to provide transport infrastructure (roads, railways, airports and harbours). The fundamental determinant for wealth creation and economic growth is economic freedom of which the main components are the size of government, a sound legal and regulatory environment, sound money, freedom to trade internationally and minimal regulation. For the transport sector this means that decision making should be guided by the price mechanism, the application of the 'user-pays' principle, an efficient profitable private sector, competition wherever possible and privatisation of transport enterprises to increase efficiency. These principles are then discussed for various aspects of transport including roads, public transport, road freight, railways, harbours and the airline industry, which is analysed in some detail,. It is concluded that economic freedom to generate wealth and economic growth is the single most important requirement for economically sustainable transport.

1. INTRODUCTION

This paper discusses the fundamental requirements for transport to be economically sustainable and argues that the solution to many transport problems is to go 'back to basics'. Sustainable in this paper refers to 'economically' sustainable and not environmentally sustainable.

The single most important requirement for economically sustainable transport is wealth and its cause - economic growth. Wealth is essential to provide transport infrastructure (roads, railways, airports and harbours). The fundamental determinant for wealth creation and economic growth is economic freedom. *'Economic Freedom of the World'* (Gwartney 2008) analyses over 140 countries and shows that the more economic freedom a country has, the greater is its economic growth and hence its wealth. The main components of economic freedom are:

- The size of government (i.e. low government expenditure, low tax rates, few government enterprises)
- A sound legal and regulatory environment (i.e. judicial independence, protection of property rights, legal enforcement of contracts)
- Sound money
- Freedom to trade internationally (i.e. low trade barriers)
- Minimal regulation of business and labour

Translating the above components to the transport sector would mean the following:

- decision making should be guided by the price mechanism

- application of the 'user-pays' principle where the users pay for the transport that they use directly or indirectly
- an efficient profitable private sector
- competition wherever possible (such as the deregulation of the road freight industry in the 80s) to increase efficiency
- privatisation of transport enterprises (roads, public transport, SAA, harbours) to increase efficiency and where this is difficult to achieve, the government should only pay for but not construct, operate or maintain the infrastructure

In addition it is necessary to go 'back to basics' in much of what is done in the transport industry. Examples include:

- As roads are a scarce resource, users should be charged for their use
- In public transport, first world solutions such as Gautrain are introduced while ignoring basics such as the provision of bus/taxi shelters
- In the airline industry unfair competition should be eliminated by privatising SAA

Similar views are discussed in 'Gridlock' (O'Toole) where the author discusses how to fix America's transportation system by focusing on free market improvements. The author presents a wide range of innovative ideas and policy recommendations for creating an effective transportation system. At the center of O'Toole's solutions are three core principles: those who use transportation facilities should pay for them; negative effects should be dealt with in a cost-efficient manner; and new technologies that will increase mobility at a low cost must be embraced.

It is clear from the above that the fundamental requirements for economically sustainable transport do not exist for many of the transport modes in SA.

Before discussing the application of the above principles to the various modes of transport, it is necessary to briefly mention that the price mechanism is what governs supply and demand in a free economy where as demand increases, prices increase and this attracts more producers and vice versa. This is sometimes referred as the 'feedback mechanism' and is described in more detail in Transport Policy (Markman, 1984). The supply of offices is a good example. A shortage of office space leads to an increase in rentals and attracts more developers to provide office space. And, just as importantly, a surplus of office space leads to a decrease in rentals and discourages developers from building offices.

Space does not allow a detailed analysis of all aspects of transport. Thus roads, public transport, road freight, railways and harbours are discussed briefly, followed by a more detailed analysis of the airline industry, by way of a case study.

2. ROADS

To achieve a higher level of sustainability of the road infrastructure, the price mechanism, the 'user-pays' principle and privatisation should be introduced wherever possible.

Ideally, the price mechanism (as for say offices) should determine both the total amount of expenditure on the entire road network as well as the expenditure on each road within the road network. Thus sufficient revenue should be collected from all sources of all road users to pay for the entire road network. All of this revenue (tolls, fuel tax, licenses, road engineering contributions, etc) should then be paid into a dedicated road fund. In this way the cost of using roads would tend to determine the amount of roads provided and road

users as a group pay would for the road network. One way of directing expenditure to specific roads, would be to allocate expenditure on roads in proportion to their usage and to introduce higher prices where demand is greater than supply i.e. where there is congestion. Thus area wide pricing should be introduced in congested urban areas as has been done in Singapore, London and a few other places. (This has to be applied with caution especially when defining the area where pricing is introduced as those areas that have congestion pricing may be at competitive disadvantage over other areas.) An example of dedicated expenditure is toll road fees where about 85% are dedicated to road maintenance. Electronic collection of tolls, when introduced in Gauteng will make it easier to apply the 'user pay' principle.

Privatisation should be introduced into certain aspects of roads. The construction of virtually all roads is already privatised. The operation and maintenance of all national and provincial roads that are tolled can and should be privatised so that they are operated efficiently and the maintenance of all other roads should be privatised.

3. PUBLIC TRANSPORT

To achieve a higher level of economic sustainability of public transport, the price mechanism should be introduced. This requires that public transport be deregulated and privatised to increase competition and make public transport more efficient.

Subsidies in various forms are widely used in public transport but interfere with the price mechanism and hence are not a good idea. As long as public transport is subsidised, it should be 'mode' neutral. One way of doing this is to direct the subsidies by way of transport vouchers at the passenger so that each passenger and not the authorities choose which public transport to use. This would enhance competition within the public transport sector.

Whilst many bus companies are already privately owned, some are owned by municipalities. These should be privatised to become as efficient as the private companies. This would result in savings for local authorities. Should they wish to provide services on unprofitable routes, these routes could be put out to tender.

3.1 Public transport infrastructure

Every transport policy document discusses the importance of public transport. And yet very little is done to provide passengers with shelters at bus stops. Even in Sandton, one of the wealthiest areas in SA, there are some bus stops with no shelters. Passengers stand in the rain waiting for a bus. The situation is even worse in areas where the poor live. We seem to go from third world to first world (Gautrain and BRT) without anything in between. Getting back to basics requires that more emphasis be placed on making existing public transport (bus and taxi) more attractive by providing better shelters and stopping places. In addition, special bus and taxi lanes should be provided. Taxis are cursed when they 'create' their own lanes but often this is in places where a taxi lane could be provided at a fairly nominal cost. And yet billions are spent on BRT bus lanes.

3.2 Unfair competition

BRT systems which are subsidised and have dedicated lanes, compete unfairly with taxis. It is too early to know what the level of subsidisation will be but it is likely that it will be substantial. Taxis on the other hand have to make a profit to survive. Furthermore, the dedicated BRT bus lanes mean that buses will be able to travel faster than the taxis – again putting the

taxis at a disadvantage. Ralph Jones spokesman of the United Taxi Associations Forum is well aware of this. He said 'this is taking us out of work. It is saying to us we don't have to exist because people will obviously run to those buses because they are subsidised and use dedicated lanes.' (Star 17.2.10)

3.3 Taxis

Much of what is wrong with the taxi industry is as a result of unfair competition and inadequate enforcement. Taxis were unsubsidised until the Taxi Recapitalisation Programme (TRP) was introduced which was a mistake as it is unsustainable and the taxi industry will become dependent on subsidies rather than focusing on running their taxis efficiently. Furthermore, the 'TRP will restrict entry into the taxi industry by imposing costly upgrades' (Boudreaux, K). To achieve a viable sustainable taxi industry will require eliminating unfair competition, providing special taxi lanes and taxi stops with shelters and enforcing the rules of the road. Furthermore, much can be learned from similar successful forms of transport known as paratransit that occur mainly in developing countries and are privately owned small vehicles and are profitable (Roth, G and Shephard, A).

4. ROAD FREIGHT

The freight industry is an excellent example of applying the correct policy to achieve economic sustainability. The industry, which was deregulated in the 1980s, is a highly competitive, efficient and profitable private sector industry where decision making by all parties is guided by the price mechanism and the users pay the full cost of transporting their freight. Before deregulation there were many absurd inefficiencies. One example was the 'empty leg' which was created because a license was required to transport freight. Very often this was given for only one direction and so the vehicle returned empty.

5. RAILWAYS

To increase its economic sustainability and efficiency, the railways should be deregulated and privatised. Decision making would then be guided by the price mechanism, there would be competition and the users would pay for the use of rail transport

Deregulation of the railways would allow anyone in the private sector to start a railway line. If this results in a few private railways it will be a sign that there is a latent demand. Just as heavy vehicles use toll roads, the private sector should also be allowed to run its own trucks on the state owned railways. It is likely that many of the mines would do this as they find the existing rail service inefficient. This is done in Australia and has already been introduced in SA where Rovos Rail, a private operation, uses the railways.

Privatisation could be undertaken in stages. Transnet has already taken steps to sell off some of its non-core operations. As a first step, Transnet should sell off its rolling stock and only operate the infrastructure. The actual operation and maintenance of the railways could be privatised as is done for the toll roads. Finally the infrastructure should be sold off. This could be done in sections. For example, some mines would only be interested in those lines on which they operate. Gautrain is an example of total privatisation and there are many examples of successful private railways throughout the world.

There would be major advantages of privatising the railways. The greater efficiency of the privatised railways would attract freight from the road network. This would reduce the

congestion on the roads as well as save road maintenance costs as there would be less damage to the roads from heavy vehicles.

6. HARBOURS

All the harbours should be privatised as was done in the UK (O'Malley). Each harbour should be sold off separately so that there is competition between harbours. This would improve the efficiency at the harbours.

7. AIRLINE INDUSTRY

The airline industry is already deregulated resulting in a dramatic increase in competition. To achieve economic sustainability and increase efficiency would require privatising SAA, the Airports Company and Air Traffic Control. Decisions would then be guided by the price mechanism, there would be competition and passengers would pay for air travel.

Privatisation will create a more stable environment and encourage more airlines to enter the market. The management of a privatised SAA and the private airlines will be able to focus on running their airlines rather than be concerned with **political** issues. The Government will become the referee and not be an operator and regulator at the same time. There are numerous lessons from throughout the world towards privatising of state owned airlines. Unfair competition will be eliminated as SAA, unlike the private sector, is allowed to make losses.

The policy should also allow more competition from international airlines. This would benefit all passengers, the tourism industry and increase employment in the tourism industry. It will be argued that, just as passengers have benefited from deregulation of domestic air transport, so will international passengers benefit from more competition from international airlines.

7.1 Background

The South African airline industry underwent probably the biggest change in its 80-year existence with the deregulation of the domestic airline industry in the early 90s. At that stage SAA had more than 95% of the domestic airline market. It is now estimated that this has fallen to about 50% as it has lost market share to airlines such as Comair.

Passengers have benefited enormously from the increase in competition arising out of deregulation. Air fares have reduced dramatically, frequencies have improved and passengers have greater choice. More passengers than ever before are now flying, many of whom could not afford to do so before the industry was deregulated.

SAA's operating figures do not reflect a healthy airline. It is estimated that over the past 20 years, SAA has cost the taxpayer billions of rands in subsidies. This is in stark contrast to Comair, which has made a profit every year since 1946 when it commenced operating in. SAA is clearly not sustainable although it has done better recently. In 2006 Transnet realised that SAA was a liability and sold SAA to the Department of Public Enterprises. The government should now sell SAA to save taxpayers billions of rands and get rid of a massive liability.

The advantages and disadvantages of privatising SAA are discussed below.

7.2 Advantages of Privatising SAA

There are numerous advantages of privatising SAA. Some of these are as follows:

- 7.2.1 *Taxpayers will not have to subsidise SAA.* Privatising SAA will not only save taxpayers from the cost of subsidising SAA's losses, estimated to be R20 billion over the past 20 years but general taxes could be reduced because of increased tax revenue from a privatised SAA.
- 7.2.2 *The poor will no longer subsidise the rich.* Subsidisation of SAA means that taxpayers are subsidising SAA passengers who are amongst the wealthier section of society and hence the 'rich' are being subsidised by the 'poor'. Surely the Government should not operate an airline serving the 'rich' at massive losses when private operators can do so efficiently and profitably?
- 7.2.3 *Unfair competition from SAA will be eliminated.* At present, state-owned SAA competes unfairly with the private airline industry as, unlike private airlines, SAA can and does make losses with the certain knowledge that Government will bail it out. This can only be described as 'unfair competition' as the private sector does not have this luxury. When the private sector makes losses it goes out of business. With privatisation unfair competition by SAA will be eliminated.
- 7.2.4 *Depoliticisation.* Privatisation of SAA will mean that the new management will be able to focus on running the airline rather than be concerned with political issues.
- 7.2.5 *Misallocation of resources.* Losses are a signal from the market that something is wrong – that the business should cease to operate as it is either inefficient or does not provide what the consumer wants. However Government ignores these market signals by not allowing SAA to go out of business. Thus SAA continues to operate unprofitably or inefficiently or provide services for which there would be no demand but for the subsidisation. SAA also keeps the existing airlines from further expansion or new airlines from entering the market and providing passengers with what they want. This results in a misallocation of resources. With privatisation misallocation of resources in the airline industry will be eliminated.
- 7.2.6 *Privatisation will encourage more airlines to enter the market.* Rather than privatise, SAA has moved in the 'opposite' direction by starting Mango, a low fare airline which competes directly with the low cost airlines initiated by the private sector. There is much debate about whether Mango is profitable or not. It is unlikely that the taxpayers will ever know if SAA subsidises Mango. Thus privatisation will create a more stable environment that will encourage more airlines to enter the market, as the private airline sector will 'only' have to deal with the market and not unfair competition from SAA.
- 7.2.7 *Government will not have a conflict of interests.* At present the government is both player and referee - particularly for international services where it is an operator and also responsible for allocating routes. In the past this has often meant that the demand for new routes by other airlines has been refused because SAA objects. Clearly the travelling public is at a disadvantage and the tourist industry is concerned that this has a negative impact on tourism. With privatisation of SAA, the Government will become the referee only.

- 7.2.8 *A positive impact on tourism.* Privatising SAA will benefit the tourist industry as there will, in all likelihood, be more airlines flying into SA making it easier and cheaper for tourists to visit SA. The increase in tourism will create more jobs in the tourism industry. It is estimated that about 1 job is created by 7 to 8 tourists.
- 7.2.9 *Consumers will benefit from improved service.* Evidence throughout the world is that, following privatisation, passengers benefit from improved service and lower airfares largely as a result of increased efficiency.
- 7.2.10 *Job creation.* Privatisation of SAA will result in job losses as state-owned enterprises (SOEs) are less efficient and employ more people than private enterprises per unit of production. However, whilst some SAA employees will lose their jobs and this must be fairly dealt with when SAA is privatised, there will be other jobs created in both the new and existing airlines as well as the tourist industry.
- 7.2.11 *The only way to 'save' SAA.* Experience since domestic airline deregulation about eighteen years ago has shown that SAA cannot survive without perpetual wealth-consuming subsidies. It has already lost 50% of market share which is effectively the same as if it had been 50% privatised. The privatised SAA would survive and prosper like other privatised airlines (discussed below). It is in the interest of SAA's management and staff to be privatised.

7.3 Disadvantages of Privatising SAA

- 7.3.1 *Strategic argument.* It is sometimes argued that SAA needs to be retained as a SOE for 'strategic' purposes. However the exact strategic reason is seldom stated. Certainly there should be a 'compelling reason' to divert billions of rands from health, housing, education and policing to SAA.

The Government may decide that certain 'strategic' routes would not be served by the private sector that should be served. Such routes could be put out to tender. This would be far cheaper and the Government would know the exact cost of the 'strategic' route.

If the Government does not want to allow **foreign ownership** of SAA, there are mechanisms that can be introduced to ensure that the airline is retained in South African hands. One such mechanism that was introduced when BA was privatised is to have a 'golden' share. This allowed the British government to veto the sale of the airline to foreigners. This 'golden' share has since been removed.

- 7.3.2 *The need for a flag carrier.* Most countries have or used to have state-owned airlines. America is one of the few exceptions. One of the reasons often cited is the need to have a flag carrier. Any country can have a flag carrier more economically by entering into a contract with a private airline to operate as the country's flag carrier. Thus privatisation would not have to mean the demise of the flag carrier.
- 7.3.3 *Job losses.* If SAA were to be privatised any job losses would have to be addressed as part of the privatisation process. Aer Lingus, discussed below, provides an example of what can be done. It is understood that many jobs have already been lost in SAA, as the employee-passenger ratio has fallen. However deregulation has already contributed substantially to market growth, so that there are more

employers and more jobs in the airline sector. In addition, as discussed above, the privatisation of SAA will result in additional jobs being created in the tourist industry and by the new airlines. It is likely that the privatisation of SAA will result in jobs being created.

7.4 Methods of Privatising SAA

There are a number of different ways to privatise SAA.

7.4.1 *Commercialise SAA and set a programme.* It is essential that SAA remain a commercial entity and not be 'lost' in the Department of Public Enterprises. Successful airline privatisations have usually followed the establishment of a company with the government being the sole shareholder. This provides prospective purchasers with the necessary financial history of the organisation. A date should be set by which time privatisation should take place.

7.4.2 *Sell portion or the entire airline (as a going concern).* Unfortunately selling the entire airline is not often implemented, as there is reluctance on the part of governments to part with 100% of SOEs. The reluctance to sell 100% of SOEs can sometimes be addressed by the 'golden share' discussed above in section 7.3.1. Selling portion of the airline has a possible advantage in that should the semi-privatised SAA do well, the Government will benefit from an increase in the value of the airline when it sells off the remainder.

7.4.3 *Sell the domestic and international portions separately.* A possible benefit is that, because the domestic and international markets are different, there would be more interested parties bidding for each portion, which may result in a higher price.

7.4.4 *Give or sell some or all of the shares to employees or blacks.* Sono has argued that the fairest way of redistributing wealth is to transfer state owned assets to the previously disadvantaged. (Sono 1999) There is a curious national mindset which regards BEE as the transfer of assets from whites to blacks, yet by far the fastest, cheapest, most substantial and nationally most beneficial way to empower blacks is by redistributing the vast amount of assets such as SAA accumulated by and inherited from the apartheid regime. The Telkom privatisation is a case in point where a percentage of the shareholding was allocated to poor black empowerment investors.

Instead of using SAA for BEE purposes, nearly half of it has already been 'privatised' without blacks getting any shares or the government getting a single cent. On the contrary, billions of Rands have been diverted needlessly from taxpayers and the poor for decades.

7.4.5 *Privatisation-by-default.* Whilst the government hasn't 'officially' privatised SAA, nearly 50% of SAA's domestic arm has been 'privatised' since deregulation 18 years ago. With deregulation came competition and SAA lost nearly 50% of its market share to the private sector.

7.4.6 *Restructuring.* SAA is presently being restructured. It is important to realise that restructuring is **not** a form of privatisation. The answer is not restructuring but privatisation. The lessons have been learnt all over the world that only privatisation eliminates ongoing losses. It is not necessary to lose more billions.

7.5 Lessons from International Airline Privatisation.

Since British Airways (BA) was privatised in 1987 for \$1,37 billion numerous other countries have also privatised their airlines. BA started making changes a few years before it was privatised to get its house in order and, as a result, became a profitable organisation. Since privatisation, BA has become 'the world's favourite airline', carrying more international passengers than any other airline – 26.6 million in 1996.

The privatisation of the Austrian airline began in the late 1980's when about a quarter of its shares were sold and the Netherlands also reduced its share in KLM.

Nearly a decade after it first announced its intention to privatise Aer Lingus, the Irish Government sold off the majority of Aer Lingus through an Initial Public Offering in 2007. As part of the deal, the government earmarked approximately 10,8m euros (R107m) for an employee trust, which benefits more than 6 000 current and former employees.

New Zealand airlines have been privatised and the airline industry has been deregulated. The results are typical of what happens wherever privatisation and deregulation occurs. The door-to-door level of service has improved; the range of fares available to passengers has increased, with a variety of discounted fares; the frequency of services to most centres has increased; and the airport facilities have been improved.

The loss making Kenya Airways was partially privatised in 1997 when the Kenya Government sold 26% to KLM and 14% to other foreign investors. The airline is now growing and profitable. In 2006 it made a \$126m (R900m).

The lessons from international airline privatisation are that the private sector turns loss making state-owned airlines into profitable ones, the service improves and the fares are reduced. Thus passengers are far better served by privately owned airlines.

7.6 Future Airline Policy

For many years SAA has tried unsuccessfully to reduce costs to become profitable. If taxpayers are to be saved from further funding of SAA and if SAA is to meet future challenges then the airline industry must be free to respond to market forces and the privatisation of SAA must take place as quickly as possible.

In 2000 the African Economic Union met at Yamoussoukro to implement an open skies policy. Not much has happened since then. Having introduced a domestic 'open skies' policy in 1992, SA should lead the way in Africa and internationally. As a start we could enter into an 'open skies' agreement with the EU who want to have such an agreement with the USA. This would allow more competition from international airlines and would benefit all passengers, the tourism industry and increase employment in the tourism industry. The recent International Air Transport Association survey showed that Africa was the region with the second-highest passenger growth rate. To meet the increase in demand, airlines must be free to be able to start new services without any barriers placed in their way. Just as domestic passengers have benefited from the deregulation of domestic air transport, so will international passengers benefit from more competition from international airlines.

The airline industry in SA was started by private sector about 80 years ago. It is time to return it to the private sector.

8 CONCLUSIONS

This paper has argued that the solution to many transport problems is to go 'back to basics' with wealth and economic growth being the single most important requirement for economically sustainable transport. Going back to basics for the transport sector includes decision making being guided by the price mechanism such as charging for the use of roads, the elimination of subsidies, the application of the 'user-pays' principle, an efficient profitable private sector, competition wherever possible and privatisation of transport enterprises.

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