Impact of the Removal of RET Fares from Commercial Vehicles on The Western Isles, Coll and Tiree

Report for Transport Scotland

In Association With ProVersa Limited

March 2013

mvaconsultancy

Document Control

Project Title:	Impact of the Removal of RET Fares from Commercial Vehicles on The Western Isles, Coll and Tiree
MVA Project Number:	101849-12
Document Type:	Draft Final Report
Directory & File Name:	H:\Contracts\Live\101849 Impact Of Removal Of RET Fares For Cvs\Report\20130109 RET CVs Draft Final Report.Doc

Document Approval

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Distribution

Issue	Date	Distribution	Comments
1	03/12/2012	Transport Scotland	First Draft
2	08/01/2013	Transport Scotland	Second Draft
3	10/02/2013	Transport Scotland	Third Draft
4	24/02/2013	Transport Scotland	Fourth Draft
5	08/03/2013	Transport Scotland	Final Draft

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1. Prior to the introduction of the Road Equivalent Fares (RET) in October 2008, fares for commercial vehicles (CVs) were set on a route-specific basis. In October 2008 the RET pilot was introduced on routes serving the Western Isles Coll and Tiree where the fare was set around the equivalent cost of driving the same distance. This resulted in significant reductions in CV ferry fares.

2. In April 2012 RET fares for CVs were removed resulting in large annual increases in single fares, both in percentage terms (up to 50%) and absolute terms (up to £100).

3. The intention of the removal of CV RET fares was to return fares to their pre-RET level. Given, however, the scale and potential impacts of the increases, transitional arrangements were put in place to limit the increases and allow the full increase to be phased in over three years.

4. The purpose of this study is to consider the impact of the removal of RET fares in April 2012 on the economies of the Western Isles, Coll and Tiree.

Findings

5. The introduction of RET for CVs made an important contribution to the initial equity objective of supporting, sustaining and developing the economies of the Western Isles, Coll and Tiree.

6. The introduction of RET had positive impacts for local businesses, including improved competitiveness, improved business performance and supporting local economic activity.

7. The removal of RET for CVs in April 2012 has had a significant negative impact on different types of hauliers. It has:

   - had a negative effect on the volumes and margins of small hauliers, who play an important role in offering choice in the market;
   - squeezed the margin of trader-hauliers who are key to the economies of small islands like Coll, Tiree and Barra;
   - necessitated an increase in prices for network hauliers who require high volumes to ensure the sustainability of their businesses. In turn this will expose these firms to volume risk; and
   - reduced the volume and economies of scale of full-service hauliers, thus increasing the long-run market rate for haulage.

8. On each route other than Oban – Castlebay / Lochboisdale, in the six months following the removal of RET carryings declined, compared to the same six-month period in the previous year. The decline ranged from 17.5% on the Oban – Coll / Tiree and Ullapool – Stornoway routes to 7.2% on the Uig – Tarbert / Lochmaddy route.

9. Over the same period revenue increased by over £380,000.

10. In most cases, hauliers used RET to offset rate rises being driven by other operating costs, particularly the significant increase in fuel witnessed in the 12 months to September 2008.

11. The evidence demonstrates that hauliers maintained transport charges at their 2008 level throughout the RET pilot despite total costs increasing at above-inflation rates. As a result of that approach transport charges to businesses remained constant over the RET pilot period but, with general inflation also rising, transport charges to businesses declined in real terms.

12. The sudden move away from RET for CVs is seen by the island communities and a number of their representatives as highly detrimental (even with the transitional arrangements) as a number of haulage firms and island customers who are tied into medium to long-term contracts and will have to absorb the cost of these rises. This issue is compounded by the short-term cash flow risks of hauliers, who are in many cases bearing the financial exposure of their whole supply chain.

13. In many cases, the removal of RET for CVs in April 2012 had been passed on in terms of higher transport charges, with 88% of businesses who participated in the survey noting that the increase in CV fares had been passed on to their business. Also, over 68% of businesses in the survey expect this increase to be in the region of £1,000 to £5,000 per annum. These increases in ferry fares have, in a number of cases, fed through to a decline in business performance across a number of sectors.

14. The removal of RET for CVs has had a negative impact on businesses that are moving or purchasing a low volume of goods; moving low value goods; or where the company is a price taker in the market. Many firms in the islands are of this type, particularly in the primary sector, with some areas' businesses in the primary sector accounting for over 35% of total businesses. The removal of RET for CVs will make these businesses less competitive in the longer-term as rates progress back to their non-RET level.

15. All areas of the Western Isles, Coll and Tiree will be affected by the removal of RET fares for CVs. Given sectoral profile, recent socio-economic trends, and business location within the haulage market, some areas will, however, be more vulnerable than others and will experience different levels of impacts.

16. Areas with a large share of enterprises in the primary sector will likely be adversely affected most. The Western Isles, Coll and Tiree as a whole have a proportionately higher share of enterprises within the primary sector. This is the case, particularly in the Uists, Benbecula, Barra, Coll and Tiree where the figure is as high as 38%. It will leave these areas more vulnerable as they already face higher than average transport charges due to the lower number of hauliers in the area and less competition in the haulage market.

17. Many of the businesses in the Western Isles, Coll and Tiree are concerned that the lack of certainty and frequent policy changes on CV fares are having a detrimental impact on business confidence and long-term investment planning. Businesses stress the need for a clearly defined longer term fares strategy by the Scottish Government.

Related Considerations

18. While the island communities covered in the study have not witnessed high levels of unemployment by Scottish standards, the rates seen are high compared to other island areas, and the Western Isles does have a number of highly deprived areas according to the Scottish Index of Multiple Deprivation, making them very vulnerable to any downturn in activity. In addition, many of the areas concerned do not have the level of industry and capacity to absorb the downturn in activity, though, say, changes in employment resulting from the increase in ferry fares.

19. RET for CVs cost the Scottish Government around £3m per year. The total reduction in annual cost to the Scottish Government associated with removing RET is estimated to be £1.5m with the transitional scheme costing the Scottish Government around £2m in 2013. The extent to which this impacts on the Western Isles, Coll and Tiree will depend on how much these costs can be passed on to customers out with the islands concerned. The impact on the Western Isles, Coll and Tiree will also depend on how much they can actually be absorbed by businesses. For example, if businesses cannot pay the higher charges, this may lead to loss of activity and a reduction in employment, resulting in an impact which is greater than the change in fares.

20. The short six month period since the removal of RET has meant that it has not been possible to quantify all the potential impacts. Furthermore, other factors, such as the changing market structure and the general slowdown in economic activity, has meant that it has not been straightforward to isolate these effects from the removal of RET.

1 Introduction

1.1 Overview

1.1.1 This document investigates and reports on the impact of the removal of Road Equivalent Tariff (RET) ferry fares for Commercial Vehicles (CVs) using services to and from the Western Isles, Coll and Tiree.

1.2 Background to Road Equivalent Tariff for Commercial Vehicles

1.2.1 In October 2008, the Scottish Government introduced a pilot RET scheme for all fare types on ferry services between the Scottish mainland and the Western Isles, Coll and Tiree. The rationale behind the pilot was to support the island economies by removing any cost disadvantage incurred by users as a consequence of travelling by ferry between these islands and the mainland. Under the scheme, users of the ferries would pay a fare equivalent to the cost of driving the same distance by road plus a flat 'boarding fare' designed to aid cost recovery.

1.2.2 At the outset, the pilot scheme was programmed to last until March 2011 but was extended for a full year to March 2012. The pilot was accompanied by a substantial monitoring and evaluation exercise to gather information and analyse the economic and wider impacts of the new fares system. On the completion of the pilot and the monitoring and evaluation exercise, Scottish Government Ministers announced a decision to begin a phased roll-out of RET fares for all island communities with mainland ferry services. However, the phased roll out was not to include RET fares for CVs and these fares were also to be removed on those routes included in the pilot. Instead, fares for commercial vehicles on routes to and from the Western Isles, Coll and Tiree were to return to pre-RET levels, taking account of inflationary impacts since 2008.

1.2.3 To reduce the impacts of a sudden move to non-RET fare levels, transitional arrangements were put in place. Under the transitional arrangements, each year the new fare would be the mid-point between the current fare and the non-RET fare, with the Scottish Government funding the difference. Additionally, a cap was put in place so that no fare would rise by more than 50% in any one year. In April 2012 new CV fares were introduced on each of the RET routes in line with these arrangements. In April 2013 the Scottish Government limited the next increase in fares to 10% across all routes.

1.2.4 In recognition of the significant increase in CV fares to their non-RET level, Transport Scotland commissioned this study to fully investigate the impact of the new fares structure on the economies of the Western Isles, Coll and Tiree. The precise aim of the study was to work with key stakeholders and hauliers to investigate the broader socio-economic impacts of removing RET fares for CVs.

1.3 Working Group

1.3.1 A Working Group of key stakeholders was convened to explore the impact of removing RET from CVs and to support and guide this study. The group consisted of Transport Scotland; Argyll & Bute Council; Comhairle nan Eilean Siar; Highlands & Islands Enterprise, HITRANS; the Outer Hebrides Commerce Group; the Freight Transport Association; and the Road Haulage Association.

1.4 Format of this Report

1.4.1 Figure 1.1 illustrates the various elements of the study, in line with the 'Aims and Objectives' set out in the Project Brief.

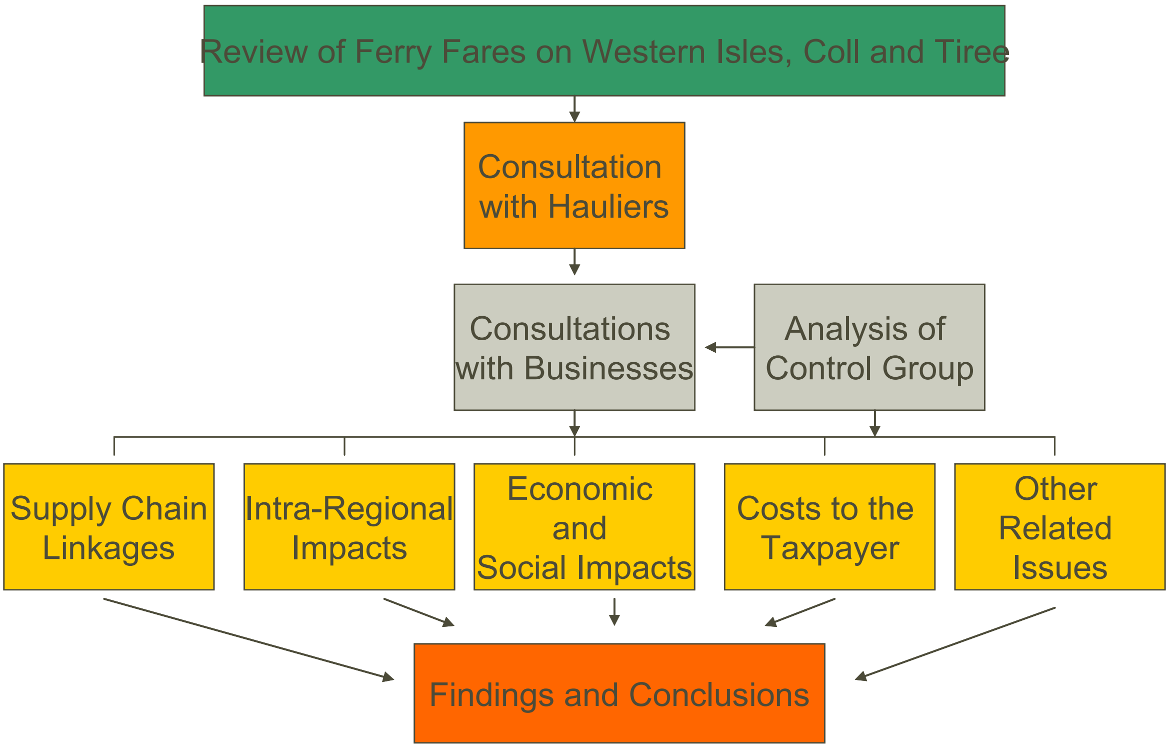

Figure 1.1 Elements of Study

1.4.2 Each task in Figure 1.1 is covered in the remaining chapters as follows:

- **Chapter 2** provides background and context by documenting fares for CV operators under different fares scenarios ie pre-RET; RET; and through the transitional arrangements back to post-RET fares;
- **Chapter 3** provides an overview of the research methodology and the approach to the evidence gathering and data collection;
- **Chapter 4** considers the impact of the removal of CV RET ferry fares on the haulage industry;
- **Chapter 5** considers the impact of the change in ferry fares on the business community;
- **Chapter 6** reviews supply-chain linkages within the islands to understand the incidence of the ferry fares increases;
- **Chapter 7** considers the geographic impact across the Western Isles, Coll and Tiree communities of the removal of RET CV fares;
- **Chapter 8** considers the wider economic and social impacts of the change in CV fares;
- **Chapter 9** illustrates the cost to the taxpayer of different fares scenarios; and
- **Chapter 10** provides emerging findings.

1.4.3 The aim of this report is to deliver clear and succinct findings for Transport Scotland and the Scottish Government and to provide an evidence base to inform future decision making. We have limited the report to around 100 pages plus an Executive Summary. However, it should be noted that there are a number of detailed working papers and consultation notes which provide further information to support the findings set out in the report.

2 Ferry Fares for CV Operators

2.1 Introduction

2.1.1 Since 2007, ferry fares for commercial vehicles have undergone a number of changes ie pre-RET levels prior to October 2008, through RET which ran from October 2008 until the end of March 2012, and during the transitional arrangements which were introduced on 1 April 2012. This chapter provides a factual record of the fare changes over this period for a range of different vehicle sizes and routes. This is helpful to provide background and context before moving on to the analysis and discussion of the impacts in later chapters.

2.2 Background

2.2.1 Commercial vehicle operators travelling on the ferry routes between the Western Isles, Coll and Tiree and the Scottish mainland have witnessed a number of different fare regimes in recent years. The Table below summarises the various fare systems that have prevailed since 2007 and that are anticipated to be in place by 2014/15. While the final row in the Table shows a move to Post-RET fares, the precise structure of future fares for commercial vehicles, and the timing, have yet to be finalised and will be informed by the findings of this study.

Table 2.1 Summary of Fare Systems 2008-2015

	2008/09	2009/10	2010/11	2011/12	2012/13	2013/14	2014/15
Pre-RET	✓						
RET	✓	✓	✓	✓			
Transitional					✓	✓	
Post-RET							✓

2.2.2 Prior to the introduction of the RET pilot, fares for commercial vehicles on routes to the Western Isles, Coll and Tiree, similar to other routes on the Clyde and Hebrides ferry network, were set on a route-specific basis. In addition, there were a small number of concessions available to hauliers depending on factors such as the number of journeys and level of turnover on a particular route.

2.2.3 The RET pilot was introduced in October 2008 and ran to the end of March 2012. During this period a single structure was applied across all routes, with the fare comprising a fixed element plus a charge per ½ metre[1] of the vehicle length.

2.2.4 Following the removal of RET fares for CVs in April 2012, the policy of the Scottish Government was to return to pre-RET fares for CVs. The proposed rates were to be based on the 2008 rate per ½ metre uplifted for inflationary increases during the period of the pilot. It was clear that the return to non-RET CV fares would involve large fare increases. Transitional arrangements were therefore introduced which were designed to cushion, in any given year, the impact of the move to non-RET levels.

[1] Under the Road Equivalent Tariff system the ½ metre rate took account of the length of the route

2.2.5 Following the early findings of this study the proposed transitional arrangements for 2013 for commercial fares were limited to a 10% increase across all routes. The final findings of this study will help inform the longer-term fares policy from 2014 onwards.

2.2.6 The key comparisons made in this chapter are to compare:

- ***the pre-RET fares (peach shaded box) with the RET fares (green shaded boxes)*** – this will establish how the introduction of RET reduced the published fares for CVs; and
- ***the RET fares (green shaded boxes) with the transitional fares (blue shaded boxes)*** – this will set out how fares have increased as a result of the removal of RET.

2.2.7 While this chapter will not analyse in detail the impact of the move to post-RET fares (as it is not currently known what these fares will be and will be influenced by the findings of this study), Chapters 6 to 9 consider the impacts of the removal of RET and Chapter 10 discusses the pros and cons of alternative fares systems which could be implemented to replace RET.

2.2.8 The routes considered under the different fares structures are those that were included in the RET pilot. These are:

- Oban – Coll / Tiree;
- Coll – Tiree;
- Oban – Castlebay / Lochboisdale;
- Uig – Tarbert;
- Uig - Lochmaddy; and
- Ullapool – Stornoway.

2.2.9 It should be noted that the CV fares for the Uig – Tarbert and Uig – Lochmaddy routes are the same. This has been the case under all fares structures and the two routes are therefore considered as a single route for the purpose of this study.

2.3 Pre-RET Fares

2.3.1 Prior to the introduction of RET, the CV fare on a particular route was the product of the length of the vehicle and the rate per half metre. The rate per half metre is broadly based on the length of each crossing, with the longer crossings typically having a higher rate per half metre, as is illustrated in the Table below where the rate per half metre is the highest on the Oban – Castlebay / Lochboisdale route which is the longest.

Table 2.2 Pre-RET Half-Metre Rates by Route

Route	Rate per ½ metre
Oban – Coll / Tiree	£10.48
Coll – Tiree	£3.99
Oban – Castlebay / Lochboisdale	£14.03
Uig – Tarbert, / Lochmaddy	£7.88
Ullapool – Stornoway	£11.16

2.3.2 Table 2.3 below presents the fares for a sample of CV lengths, namely seven metres, 12 metres and 17 metres[2]. All fares included in the Table and throughout this chapter are for a single journey and exclude VAT.

Table 2.3 Pre-RET Commercial Vehicle Fares

Route	7m	12m	17m
Oban – Coll / Tiree	£147	£252	£356
Coll – Tiree	£56	£96	£136
Oban – Castlebay / Lochboisdale	£196	£337	£477
Uig – Tarbert, / Lochmaddy	£110	£189	£268
Ullapool – Stornoway	£156	£268	£379

2.3.3 Table 2.3 shows that the highest fares were on the Oban – Castlebay / Lochboisdale route, with the lowest fares on the sailing between Coll and Tiree, reflecting the ½ metre rate per route and therefore the length of the crossing. On sailings between the mainland and the islands, the lowest fare was on the Uig – Tarbert / Lochmaddy route.

2.4 Pre-RET Discounts

2.4.1 There is an important caveat to Table 2.3 – the Table shows the published fares that commercial operators would have paid. However, a small number of discounts were available to users in the pre-RET era.

[2] A working paper is available showing the costs for all vehicle lengths. However, for brevity and the purposes of illustration only a selection of vehicle lengths are included in this report.

2.4.2 The key discount in this respect was the Traders' Rebate Scheme (TRS). The scheme offered all commercial vehicle operators a rebate based on their volume of carryings on a particular route on the Clyde and Hebrides Ferry network. The rebate was calculated on the basis of a 'Numeral', which related to annual turnover / expenditure of the haulage firm and the number of journeys undertaken on the ferry. The formula used to calculate the level of discount was:

Numeral = [(Turnover / 1000) / Rate per half metre] x no. of journeys

Where:

- Turnover = total customer (ie the haulier) fares expenditure on a specific route during the qualified period;
- Rate = published ½ metre rate for commercial vehicles on a specific route; and
- Journeys = number of journeys by operator on a specific route during qualifying period.

2.4.3 Depending on the 'numeral' calculated, an operator qualified for a discount of between 0% and 15% on a given route, for a specific twelve month period. Table 2.4 below sets out the fares assuming a 15% discount. Note that the non-discounted fare is shown in brackets, italics and red.

Table 2.4 Pre-RET Commercial Vehicle Fares with a 15% TRS Discount

Route	7m	12m	17m
Oban – Coll / Tiree	£125 *(£147)*	£214 *(£252)*	£303 *(£356)*
Coll – Tiree	£48 *(£56)*	£82 *(£96)*	£116 *(£136)*
Oban – Castlebay / Lochboisdale	£167 *(£196)*	£286 *(£337)*	£405 *(£477)*
Uig – Tarbert, / Lochmaddy	£94 *(£110)*	£161 *(£189)*	£228 *(£268)*
Ullapool – Stornoway	£133 *(£156)*	£228 *(£268)*	£322 *(£379)*

2.4.4 It can be seen from Table 2.4 that some of the TRS related discounts were quite substantial in absolute terms. For example, a 15% TRS discount made it £72 cheaper to take a 17 metre CV onto the Oban – Castlebay / Lochboisdale ferry. Indeed, even on the lowest cost crossing ie Tarbert / Lochmaddy – Uig, there was a £16 reduction on a seven metre CV and a £40 reduction on a 17 metre CV.

Who benefitted from TRS?

2.4.5 The evidence provided by the current ferry operator, CalMac, shows that, in the year prior to the introduction of RET, there were a total of 12 hauliers receiving 14 discounts across the RET pilot routes. The number of hauliers receiving discounts on routes to the mainland was:

Table 2.5 Number of TRS Operator Rebates

Route	Operator Rebates
Oban – Coll / Tiree	Two
Oban – Castlebay / Lochboisdale	One
Uig – Tarbert, / Lochmaddy	Six
Ullapool – Stornoway	Five

2.4.6 In terms of the level of discount, there were five discounts of 15% (three different operators across two routes, with two operators receiving it on both routes); two operators received 12.5%; three operators received 10%; two operators received discounts of 5%; and two operators received 2.5%.

2.4.7 The evidence provided by CalMac suggests that, on routes included in the RET pilot, twelve island hauliers received a discount, with only three firms in receipt of the maximum discount of 15%. However, while the absolute number of operators was small, their number of journeys accounted for a large proportion of total commercial vehicle journeys in any given year. It is difficult to be precise given the available data[3], but the operators receiving the discount accounted for between 40% to 50% of CV carryings on the Uig – Tarbert / Lochmaddy, Oban – Castlebay / Lochboisdale and Oban – Coll / Tiree routes in the year prior to the RET pilot being introduced. On the Ullapool – Stornoway route the figure was even higher at around 70%.

2.4.8 It can be concluded from the data that the majority of established island haulage firms had at least some form of TRS discount and were therefore not paying the full fare. The traffic that did not benefit from a TRS discount was typically either mainland based or infrequent suppliers to / from the islands.

2.5 RET Pilot

2.5.1 The aim of the RET pilot was to address evidence-based concerns that businesses on the Western Isles, Coll and Tiree were being disadvantaged by their peripheral island locations ie the main objective for the public support and intervention was on equity grounds. In theory, to remove the island-based disadvantage, the fares were set so that the cost of transporting goods by ferry was equivalent to carrying the same goods the same distance by road, taking account of factors such as fuel, insurance, depreciation, engine size and maintenance costs. In reality, the need for cost recovery necessitated the addition of a 'boarding fare' to the road equivalent fare.

2.5.2 The RET fares on the routes consisted of this boarding fare of £20 plus a rate per ½ metre per mile, the latter taking account of the length of the route. The rates per half metre on the routes in 2008 were:

[3] The information provided for total commercial vehicle trips by route includes buses, although the number of buses is likely to be a small percentage of the total.

Table 2.6 RET Rates per Half Metre 2008

Route	Rate per ½ metre
Oban – Coll / Tiree	£5.37
Coll – Tiree	£1.08
Oban – Castlebay / Lochboisdale	£8.01
Uig – Tarbert, / Lochmaddy	£2.61
Ullapool – Stornoway	£4.68

2.5.3 Using these fixed and variable rates the initial fares in the RET pilot for commercial vehicles of seven metres, 12 metres and 17 metres in length are set out in Table 2.7.

Table 2.7 RET Fares October 2008

Route	7m	12m	17m
Oban – Coll / Tiree	£95	£149	£203
Coll – Tiree	£35	£46	£57
Oban – Castlebay / Lochboisdale	£132	£212	£292
Uig – Tarbert, / Lochmaddy	£57	£83	£109
Ullapool – Stornoway	£86	£132	£179

2.5.4 Comparing the figures in Table 2.7 with those in Table 2.3 for the pre-RET fares for commercial vehicles reveals large reductions in the published fare across vehicle length and route. The Figures in Table 2.8 below show that the change in CV fares, once RET was introduced, ranged from a reduction of 33% for a 7m vehicle on the Oban – Castlebay / Lochboisdale route, to a reduction of just under 60% for a 17m vehicle on the routes between Uig and Lochmaddy and Tarbert.

Table 2.8 Changes in Pre-RET and RET fares

Route	7m	12m	17m
Oban – Coll / Tiree	-35%	-41%	-43%
Coll – Tiree	-37%	-52%	-58%
Oban – Castlebay / Lochboisdale	-33%	-37%	-39%
Uig – Tarbert, / Lochmaddy	-49%	-56%	-59%
Ullapool – Stornoway	-45%	-51%	-53%

2.5.5 While Table 2.8 shows the percentage reduction in full fares per route and vehicle length, it is clear from the information on the Traders' Rebate Scheme that many of the operators transporting goods to and from the islands were not paying the full pre-RET fare. A large proportion of the journeys being made were by operators who were receiving rebates of up to 15%, although those receiving the maximum discounts tended to be confined to the Uig – Tarbert / Lochmaddy and Ullapool – Stornoway routes. Taking account of the 15% rebate on these routes, as well as the 10% rebate offered to the main operator on the Oban – Castlebay / Lochboisdale route, the introduction of the RET pilot resulted in the changes in fares set out in Table 2.9.

Table 2.9 Changes in pre-RET and RET fares including TRS discount

Route	7m	12m	17m
Oban – Castlebay / Lochboisdale	-25%	-30%	-32%
Uig – Tarbert, / Lochmaddy	-40%	-49%	-52%
Ullapool – Stornoway	-36%	-42%	-44%

2.5.6 The Figures in Table 2.9 continue to reveal large reductions in fares on the three routes, even where the fare prior to the introduction of RET included TRS discounts. The Table shows that the fare reductions, after taking account of TRS, ranged from 25% for a 7m vehicle on the Oban – Castlebay / Lochboisdale route to 52% on the Uig – Tarbert / Lochmaddy route.

2.5.7 Under the RET pilot the fixed and variable elements of the fare increased slightly, and in the final year for RET CV fares the core fare was £21.30 and the variable element per ½ metre for each route was:

Table 2.10 RET Rates per ½ Metre 2011

Route	Rate per ½ metre
Oban – Coll / Tiree	£5.74
Coll – Tiree	£1.16
Oban – Castlebay / Lochboisdale	£8.55
Uig – Tarbert, / Lochmaddy	£2.79
Ullapool – Stornoway	£4.99

2.5.8 Applying these rates resulted in 2011 fares for CVs per route of:

Table 2.11 RET Fares 2011

Route	7m	12m	17m
Oban – Coll / Tiree	£102	£159	£216
Coll – Tiree	£38	£49	£61
Oban – Castlebay / Lochboisdale	£141	£227	£312
Uig – Tarbert, / Lochmaddy	£60	£88	£116
Ullapool – Stornoway	£91	£141	£191

Ullapool – Stornoway Freight vessel discount

2.5.9 During the early consultation with hauliers and businesses on and serving the islands, it was noted that a number of hauliers were receiving the 10% discount available to operators using the dedicated overnight freight vessel on the Stornoway – Ullapool route (ie the MV *Muirneag*). It was suggested that this discount should also be taken into account when comparing the pre-RET and RET CV fares. While it is recognised that the 10% discount was available to operators, it has not been included in the calculations. This is because the discount continued to be available at the rate of 10%, during the RET pilot. Indeed, it continues to be available to operators as part of the transitional arrangements discussed below. It has therefore had no impact on the level of reduction or increase in fares during the different periods and has been excluded from the calculations.

2.6 Post-RET Fares

2.6.1 In February 2012, the Scottish Government announced the removal of RET ferry fares for commercial vehicles, effective as of 1 April 2012. However, at the same time, it was recognised by the Scottish Government that an immediate progression to inflation-uplifted pre-RET rates would involve large sudden increases in fares. Ministers therefore introduced a three year transitional fares arrangement designed to ease the progression back to full non-RET fares. Under the transitional arrangements, each year the new fare would be the mid-point between the current fare and the non-RET fare, with the Scottish Government funding the difference. Additionally, a cap was put in place so that no fare would rise by more than 50% in any one year.

2.6.2 In addition to the transitional fares scheme, the Scottish Government redefined the threshold at which a vehicle is considered to be a commercial vehicle. Under the pre-RET arrangement and during RET itself, all vehicles over 5m in length were designated as CVs. Under the new arrangements however this threshold increased to six metres. This means that some vans which previously were charged at the commercial vehicle rate, ie those between 5m and 6m, are now charged at the car rate.

Transitional Fares Scheme

2.6.3 Under the transitional fares scheme the rates per ½ metre that were applied in April 2012 are set out in Table 2.12. The new rate ranged from £4.70 per ½ metre on the Coll – Tiree route to £16.53 on the Oban – Castlebay / Lochboisdale route.

Table 2.12 Post-RET ½ metre rates April 2012

Route	Rate per ½ metre
Oban – Coll / Tiree	£12.36
Coll – Tiree	£4.70
Oban – Castlebay / Lochboisdale	£16.53
Uig – Tarbert, / Lochmaddy	£9.30
Ullapool – Stornoway	£13.15

2.6.4 Using these ½ metre rates, the transitional fares introduced in April 2012 are set out in Table 2.13. However, on certain routes, where the percentage increase in the transitional fare compared with the current fare is greater than 50%, the fare increase is capped at 50%. The routes and vehicle lengths where this is the case are shaded pink in Table 2.13 below.

Table 2.13 CV Fares 2012 Transitional Arrangements

Route	7m	12m	17m
Oban – Coll / Tiree	£130	£222	£315
Coll – Tiree	£49	£74	£91
Oban – Castlebay / Lochboisdale	£162	£278	£393
Uig – Tarbert / Lochmaddy	£91	£132	£174
Ullapool – Stornoway	£137	£212	£286

2.6.5 Table 2.14 shows the percentage increase between the 2011 RET CV fare and the 2012 transitional fare. The pink shaded boxes show lower increases than would have taken place without the transitional arrangements ie fare increases were capped at 50%.

Table 2.14 CV Fare Increases Between 2011 (RET fare) and April 2012 (Transitional Arrangements)

Route	7m	12m	17m
Oban – Coll / Tiree	28%	40%	46%
Coll – Tiree	31%	43%	50%
Oban – Castlebay / Lochboisdale	15%	23%	26%
Uig – Tarbert, / Lochmaddy	50%	50%	50%
Ullapool – Stornoway	50%	50%	50%

2.6.6 The fares and the associated percentage increases set out in Tables 2.13 and 2.14 are for 2012 and represent the first stage of the transitional arrangements[4].

2.6.7 In December 2012 Scottish Government Ministers announced that fares across all routes would be limited to a 10% in April 2013, with future year rises to be considered in light of the findings of this study. The new fares for 2013 are set out in Table 2.15 below.

Table 2.15 CV Fares 2013 Transitional Arrangements

Route	7m	12m	17m
Oban – Coll / Tiree	£143	£244	£347
Coll – Tiree	£54	£81	£100
Oban – Castlebay / Lochboisdale	£178	£306	£432
Uig – Tarbert / Lochmaddy	£100	£145	£191
Ullapool – Stornoway	£151	£233	£315

[4] In December 2012, Scottish Government Ministers announced that CV fares for 2013 would rise by a maximum of 10% on each of the routes. The long-term strategy for CV fares will be considered following the completion of this study and consideration of the findings.

Comparison of 2007 and 2012 Fares

2.6.8 Table 2.16 below shows the fares on the routes pre RET and during the transitional arrangements in 2012. The table shows that on all routes and for all vehicle lengths the fares during the transitional arrangements in 2012 were lower than they were in 2007.

2.6.9 It should be noted however that many of the hauliers received a discount under TRS. Table 2.17 therefore presents a comparison of the pre RET fares assuming the full 15% discount on the Ullapool – Stornoway and the Uig / Tarbert / Lochmaddy routes and 10% on the other routes ie the maximum discount on all the routes in 2008. The figures in Table 2.17 present a mixed picture. A number of fares under the 2012 transitional arrangements are still lower than those in 2007 with a TRS discount, while others are higher.

2.6.10 It should also be noted however that the figures in Tables 2.16 and 2.17 are in prices of the day and take no account of inflation between 2007 and 2012. Almost all routes on the Clyde and Hebrides ferry network operated by CalMac have seen annual fare increases at least in line with inflation over this period. Table 2.18 presents the figures in 2012 prices and shows that all fares except one (7m vehicle on the Ullapool – Stornoway route), after taking account of the maximum TRS discount awarded in 2008 on each route, were lower under the 2012 transitional arrangements than they were in 2007.

2.6.11 Taking account of the 10% increase in CV fares that will be introduced in 2013 would mean that some fares would be slightly higher than they were in 2007, such as Oban – Coll / Tiree, while others would still be lower eg longer vehicles on the Uig – Tarbert / Lochmaddy and Ullapool – Stornoway routes.

Table 2.16 CV Fares Pre RET and 2012 Transitional Arrangements

	2007			2012		
Route	**7m**	**12m**	**17m**	**7m**	**12m**	**17m**
Oban – Coll / Tiree	£147	£252	£356	£143	£244	£347
Coll – Tiree	£56	£96	£136	£54	£81	£100
Oban – Castlebay / Lochboisdale	£196	£337	£477	£178	£306	£432
Uig – Tarbert / Lochmaddy	£110	£189	£268	£100	£145	£191
Ullapool – Stornoway	£156	£268	£379	£151	£233	£315

Table 2.17 CV Fares Pre RET (with 15% and 10% TRS discounts) and 2012 Transitional Arrangements

	2007			2012		
Route	**7m**	**12m**	**17m**	**7m**	**12m**	**17m**
Oban – Coll / Tiree	£132	£227	£320	£143	£244	£347
Coll – Tiree	£50	£86	£122	£54	£81	£100
Oban – Castlebay / Lochboisdale	£176	£303	£429	£178	£306	£432
Uig – Tarbert / Lochmaddy	£94	£161	£228	£100	£145	£191
Ullapool – Stornoway	£133	£228	£322	£151	£233	£315

Table 2.18 CV Fares Pre RET (with 15% and 10% TRS discounts) and 2012 Transitional Arrangements in 2012 prices

	2007			2012		
Route	**7m**	**12m**	**17m**	**7m**	**12m**	**17m**
Oban – Coll / Tiree	£145	£252	£356	£143	£244	£347
Coll – Tiree	£56	£96	£136	£54	£81	£100
Oban – Castlebay / Lochboisdale	£196	£337	£477	£178	£306	£432
Uig – Tarbert / Lochmaddy	£104	£179	£253	£100	£145	£191
Ullapool – Stornoway	£148	£253	£358	£151	£233	£315

Post-RET Discounts

2.6.12 It should be noted that vivier trailers (which move live shellfish) and lorries carrying hay and livestock only pay for the outbound leg of the journey plus any port related charges levied by the port authority on the return leg. The CV fare for the return leg is waived and paid for by the Scottish Government. The reason for waiving the fare is that these trailers are specially adapted to carry such loads and therefore have little prospect of returning with alternative cargo.

2.7 CV Carryings

2.7.1 Table 2.19 below sets out the CV carryings (lane metres) by route since 2007 covering the various fares structures. The purpose of the figures is to compare the number of CV carryings under each fares system. It should be noted however that carryings data from April 2012 are not available for the whole year. The analysis has therefore used carryings data for the six month period April to September 2012 inclusive. To provide a like-for-like comparison, data for the same six-month period has therefore been used for previous years.

Table 2.19 CV Carryings by Route April to September, 2007 to 2012

	2007	2008	2009	2010	2011	2012
Oban – Coll / Tiree	10,617	8,648	10,618	9,240	11,443	9,452
Oban – Castlebay / Lochboisdale	6,467	5,865	7,448	8,002	7,325	7,470
Uig – Tarbert, / Lochmaddy	41,558	41,354	39,237	44,367	46,072	42,776
Ullapool – Stornoway	80,068	85,300	86,791	90,886	103,545	85,318
Total	140,717	143,175	146,103	154,505	170,396	147,028

2.7.2 The figures in Table 2.19 show a similar trend in CV carryings across the four routes. While there were fluctuations during the RET pilot, carryings on all routes were higher towards the end of the pilot than at the beginning. In addition, other than the Oban – Castlebay / Lochboisdale route carryings were lower in the six months following the removal of RET than during the same six-month period the previous year. On the Ullapool – Stornoway route, for example, carryings rose over the RET pilot period by 21% and subsequently declined by a slightly smaller proportion (18%) in the six-month period directly following the removal of RET in April 2012, albeit by the same number in absolute terms. Some of this can be explained however by the drop in activity associated with the school building programme which tailed off in 2011, rather than a wholly direct consequence of RET.

2.7.3 Similarly, on the Oban – Coll / Tiree and the Uig – Tarbert / Lochmaddy routes carryings were higher towards the end of the RET pilot than at the beginning (by 32% and 11% respectively) and have seen declines in the six-month period since its removal in April 2012 (by 17% and 7% respectively). On the Oban – Castlebay / Lochboisdale route carryings increased by 25% between Apr – Sept 2008 and Apr – Sept 2011. However, carryings have continued to increase, albeit marginally, since RET was removed.

2.7.4 For all of the routes combined, the table also shows that on a year-on-year basis carryings in the Apr-Sept period increased each year between 2007 and 2011 (overall by 29,679 or 21%) and then declined in 2012 (by 23,368 or 14%).

2.7.5 It should be noted that Table 2.19 shows only one six-month period following the removal of RET. This may not necessarily be representative of the long-term picture as the behaviour of users may change over time in response to the fares increases eg contracts may be renewed over time or demand from businesses may decline if higher fares result in higher transport charges. On the other hand, there could be local factors other than RET that may have influenced the decline in 2012, such as the end of the school building programme, which will have impacted on the Ullapool-Stornoway figures, or the continued economic slowdown more generally. Further monitoring of carrying data will be required to fully understand the long-term impact.

2.8 Conclusions

2.8.1 The introduction of RET fares in October 2008 saw significant reductions in fares across the routes. This ranged from around 40% for a 7m vehicle, to over 50% for the longer vehicles on most of the routes.

2.8.2 Many of the operators were in receipt of the discount from the Traders Rebate Scheme. This meant that the fare reductions were less than announced. Nevertheless, the fare reductions were still significant.

2.8.3 The removal of RET in March 2012 resulted in significant fare increases, although these were limited to 50% in any given year.

2.8.4 Following the removal of RET, carryings between April and September 2012, compared to the same six-month period in 2011 declined on all routes other than Oban – Castlebay / Lochboisdale. Carryings fell be up to 17.5% on the Oban – Coll / Tiree and the Uig – Tarbert / Lochmaddy routes.

2.8.5 The reduction in carryings is more likely to be due to the removal of RET than the continued subdued economic activity, as the CV carryings across the rest of the Clyde and Hebrides network as a whole, and on the majority of individual routes, increased over the same period.

3 Methodological Approach to Consultation and Data Collection

3.1 Introduction

3.1.1 The key aim of the study was to analyse the impact of the removal of RET fares for commercial vehicles on the economies of the Western Isles, Coll and Tiree. To inform the analysis, a detailed consultation exercise was carried out to allow evidence and information on the impacts to be gathered. This section sets out the approach to the data collection exercise.

3.1.2 In summary, our methodological approach to the primary data collection for this study involved a combination of face-to-face haulier interviews; face-to-face business interviews; the carrying out of an online business survey; and telephone interviews with hauliers in a selected 'control group'. The findings from each of these activities, coupled with desk-based research and operator data interrogation, were used as the basis for developing this report. Summaries of each of the stages of the consultation exercise are set out below.

3.2 Haulier Interviews

3.2.1 The haulage industry is clearly an important player in this study as it is hauliers who will face the direct impact of an increase in CV ferry fares. If ferry fares were absorbed completely by hauliers then the impact on the islands would simply be the impact of the ferry fare changes on the bottom line of the businesses in the haulage sector. However, an increase in fares will, to some degree, be passed on in terms of higher transport charges to businesses. The business models and pricing behaviour of hauliers before and during the RET period and their intentions as fares return to non-RET levels are therefore key in understanding the overall impacts of removing RET for CVs.

3.2.2 To this end, a series of face-to-face interviews was undertaken with hauliers on both the islands and the mainland. A total of fifteen companies were interviewed, representing all of the main operators serving the Western Isles, Coll and Tiree.

3.2.3 The interviews with hauliers were conducted at the interviewee's premises. Each interviewee was taken through a structured questionnaire but encouraged to explore issues raised in a more discursive style. The desire to contribute was evident, and most consultees were willing to give 90 minutes upwards of their time to discuss in detail the issues from their perspective.

3.2.4 In addition to interviews with individual haulage businesses, consultations were held with the Freight Transport Association and Road Haulage Association so as to obtain a wider perspective on the view of the sector.

3.2.5 The interviews covered a number of key themes, the most important of which involved exploring hauliers' pricing behaviour as a result of RET being introduced and its subsequent removal, with a key aim to understand how higher ferry fares will impact on transport charges for businesses. The process also asked detailed questions about the business model; areas of operation; vehicles used; goods carried; frequency of ferry use etc of each haulier in the survey. Overall, the survey provided a detailed understanding of the haulage market in each of the islands taking part in the pilot, as well as the different responses to changes in ferry fares.

3.2.6 It should be noted that, in a number of cases, detailed evidence was presented by hauliers to substantiate claims made on issues such as transport charges and whether these had fallen or risen over the period of the study. However, it was emphasised by a number of hauliers that this information is commercially sensitive. It has therefore not been reproduced in this document. Nevertheless, where relevant, reference is made to the evidence presented to substantiate the claims made during the interview process and supported by general data wherever possible.

3.3 Business Interviews

3.3.1 As well as the interviews with haulage firms, a series of face-to-face interviews was carried out with businesses across the islands. The purpose of the interviews was to understand how the additional charges levied on hauliers filtered through to businesses and the wider supply chains across different sectors and geographic locations, and how higher transport charges have impacted on business performance and the wider economy. In total 37 businesses were interviewed, covering a range of industry sectors and geographic locations.

3.3.2 The interviews covered a wide range of topics, including sectors and areas of operation; business turnover and profitability; the impact on business performance from the introduction of RET and the consequences of its removal; cost pass-on from haulage firms; cost pass-on to end customers; and the rationale for current haulage arrangements.

3.3.3 It was very clear that the issues raised and views presented in the interviews with businesses correlated very closely with those provided in the haulier interviews. The same themes were put forward regularly, reinforcing the points raised and providing a consistent picture of the impacts associated with the removal of RET for CVs.

3.3.4 Similar to the haulier interviews, evidence was presented by businesses but has not been reproduced in this report due to the commercially sensitive nature of the information.

3.4 Online Business Survey

3.4.1 In order to validate the findings of the interview process, an online survey of businesses was also undertaken to canvass views of those that were not selected to take part in an interview. The aim of this survey was to assist in developing a wider evidence base to critically assess and support the findings of the business interviews. A key point is that the survey was focused more on collecting factual data than on more general opinions on the removal of RET for CVs.

3.4.2 The first section of the survey asked a series of basic questions about the respondent’s business. The survey was then split into six separate sections and the respondent was routed into the section that was most appropriate to their business, as follows:

- If the business contracts with a 3rd party haulage or delivery company to move its goods and supplies by ferry between the mainland and the islands;
- If the business uses its own commercial vehicles (ie greater than 6m in length) to move its own goods and supplies only;
- If the business uses its own commercial vehicles (ie greater than 6m in length) to move a combination of its own goods and those of others;

- If the business uses its own commercial vehicles (ie greater than six metres in length) to move goods and supplies for others only;
- If the businesses uses cars / vans (ie less than six metres in length) to move all of its goods and supplies by ferry between the mainland and the islands; or
- If the business does not directly use ferries to transport its goods/supplies because it buys/sells everything it needs from/to island-based suppliers/customers or 3rd party organisations who deal with the transport of the goods to/from the mainland.

3.4.3 The aim was to achieve 100 responses to the online survey. However, despite significant publicity, the survey only achieved responses from 49 companies. Despite this lower than anticipated response rate, the responses covered a wide range of business sectors across the islands. In addition, the issues to emerge from the survey were consistent with those from the interviews with hauliers and businesses and we are confident that the relevant issues have been captured both in a geographic and sectoral sense. In our opinion it is unlikely that a larger sample would have raised any key issues that were not picked up in the survey.

3.5 Control Group Interviews

3.5.1 A series of interviews was proposed with hauliers and businesses on islands with similar characteristics to the Western Isles, Coll and Tiree but did not take part in the RET pilot. The aim was to isolate the impact of removing RET fares for CVs by comparing the findings from the islands which had witnessed a large increase in CV fares through the removal of RET to the experience of islands with similar characteristics which had not seen large increases in CV fares over the same period. The islands chosen were Arran, Islay and Mull.

3.6 Understanding the Precise Impact of the Removal of RET for CVs

3.6.1 A key methodological issue to emerge throughout this study is the ability to isolate the impact of the removal of RET from the wide range of other factors that are impacting on the islands. For example, many businesses noted that haulage costs have gone up since April 2012 (see section 4.7) and explained that the removal of RET is a reason for this. However, they also note that it is one of a number of factors driving up costs and, when pressed, the majority of businesses could not estimate how significant the removal of RET for CVs is when compared with other factors such as fuel price increases.

3.6.2 In addition, it is important to note that the general economic slowdown is affecting the level of activity and individual business performance on the Western Isles, Coll and Tiree, in line with other island and mainland communities in Scotland[5]. While every effort has been made to isolate the impact of the removal of RET for CV fares from the impact of the wider macro-economic situation, it is difficult to be precise and one must bear in mind this limitation when interpreting the findings.

[5] Between 2007 and 2011 Scottish GDP fell by 2.8%, an average annual decline of 0.7%. This compares to long term average annual growth of 1.7% between 1979 and 2011

4 Ferry Fares and the Impact on the Haulage Industry

4.1 Introduction

4.1.1 This chapter considers the impact of the removal of RET for CVs on the haulage industry across the Western Isles, Coll and Tiree and how the changes in fares feed through to changes in pricing behaviour and transport charges for business. The focus here is on companies whose core business activity is the conveyance of goods for third parties, although the chapter does consider some companies that move their own stock as well as that of customers (eg Barratlantic).

4.1.2 The purpose of this chapter is to understand the dynamics of the haulage markets in the Western Isles, Coll and Tiree as this is key to understanding the wider context of RET fares for CVs and its subsequent removal.

4.1.3 It is important to recognise that island hauliers are not a homogenous mass – there are many different business models within the industry and RET had different impacts on each. In addition, while hauliers were generally the first recipient of the RET benefits, the impact of the policy varied across the industry. It is therefore critical to understand the make-up of the industry and the different markets served to fully appreciate the impacts of the removal of RET across the communities.

4.1.4 This chapter therefore discusses the different business models and types of haulier operations before reporting on the findings of the interviews.

4.1.5 As explained in Chapter 3, much of the information supplied by hauliers to support their claims was provided in confidence given the commercial sensitivity of many of the figures. It has therefore not been possible to present all the data in this report, but, wherever possible, more general sources and official data have been included to examine and support many of the points made.

4.2 The Interview Programme

4.2.1 The findings presented in this report are largely based on interviews with the Freight Transport Association, the Road Haulage Association and fifteen haulage firms across the islands and the Scottish mainland. Central themes covered by this chapter include:

- haulier business models;
- volume imbalances and their effect on pricing;
- overall inefficiencies in serving island markets;
- pre-RET discounts;
- passing on savings from RET CV fares;
- the impact of the removal of RET;
- haulier integration into the communities they serve;
- the vulnerable sectors;
- the alternative to RET; and
- recent market disruption.

4.3 Business Models Operating to the Islands

4.3.1 It is important to recognise that the supply of haulage services to the islands does not consist of a collection of individual companies providing a homogenous service to a common customer base. Within the overall mass of traffic there are a number of discrete business models in operation that are meeting different customer needs with tailored services. It is important to understand the different models as the introduction and subsequent removal of RET fares for CVs had a different effect on each type. Examples of a small number of the different models and the impact of RET are provided below.

Small Operators

4.3.2 Smaller operators, tend to operate two or three dedicated vehicles, typically with one or two regular and long-term customers. These companies do not have the necessary scale to win and deliver major contracts nor the depth of resource to establish either a network infrastructure or technically sophisticated services that might, for example, include onward van deliveries. However, they do differentiate their businesses by offering high levels of customer service and 'going the extra mile' compared to mass market operators. Inevitably, they tend to move much of the periodic, lower value and price sensitive commodities like agricultural products, kit houses, building materials and scrap, and often undertake subcontract work for either island or mainland principals.

4.3.3 These relatively smaller operators don't tend to carry a large business overhead beyond sustaining a living from the business and covering operating costs. While island traffic has traditionally been a core business, all of the firms spoken to have had to refocus in some way on attracting mainland-only work since RET for CVs was removed in April 2012 as business volume in some sectors declined due to higher costs (removal of RET) and less activity (general economic slowdown). This fall off in traffic reflects the markets they are primarily active in, eg construction and building materials which have witnessed relatively large declines in activity over the last few years, and the fragile nature of these sectors. These operators are more likely to be the vulnerable backbone of the sector at most risk from rising costs, predatory pricing by others, and financial exposure from cash-flow risk.

- Key points:
  - Small hauliers play an important role in offering choice and quality in the market and offer competition for the larger and more general hauliers.
  - These firms have seen a downturn in business recently, caused both by the removal of RET and the general slowdown in economic activity.

Trader-Hauliers

4.3.4 Trader-hauliers are firms that use their own commercial vehicles to move a combination of their own goods and those of others. Perhaps the most well-known example is Barratlantic, which operates a fleet of vehicles that move the company's seafood products to market but also provide general haulage services for island residents and businesses (eg importing furniture or fuel).

4.3.5 As a result of running a transport operation however, these businesses also introduce capacity into the general haulage or contract market. For example, Barratlantic, while transporting its own goods, also has the Co-operative contract to bring goods into Barra, which fits with the export of processed goods from the factory – ie it allows a two-way traffic flow.

4.3.6 Although margin is made on the sale price of the goods rather than directly on the haulage element, several of the businesses are trading commodities that are either low margin, or have volatile input costs themselves. For example, N.J. MacAskill sources and supplies hay and animal feed into the Uists and is the only registered livestock haulier on the islands. Raw material costs of the products he supplies have risen considerably as a result of global commodity price increases. The combined effect of this, and increases in the cost of transport, including the ferry fare, is that the market for his products shrinks as crofters and farmers have a substitutable option to feed livestock on silage. This lower quality feed impacts on the quality of the livestock produced, and therefore affects the prices that can be achieved at auction so it is not something the agricultural community wants to do, but in such a marginal sector, there is often little choice. Increased ferry costs of course also impact on the prices achievable at auction as mainland buyers looking to establish an appropriate auction value of the stock also have to factor in the cost of transportation back to the mainland.

4.3.7 Similarly, Iain A MacKinnon Ltd sources, supplies and delivers bulk building materials and agricultural supplies to Coll and Tiree. The selling price of these goods to islanders includes the transportation, handling and end delivery cost in most cases. Mr MacKinnon noted that it is not unusual that the cost of transportation on a per unit basis, ie per pallet, was in excess of the actual value of the goods themselves. This he believed was a dangerous situation to be in as consumption of these goods, particularly in construction, can be simple 'yes / no' decisions. If it costs twice as much to build something on the island as it does on the mainland, it is easy to see why economic activity like building simply stops. This is exactly what he has witnessed since April 2012, when the cost of basic building materials had to increase directly with the ferry fare. It was suggested that crofting activity, which underpins much of the island economy, is also exposed and Mr MacKinnon has found families ordering smaller quantities and reducing headcount as a result of increasing costs.

- Key points:
  - Trader-hauliers have witnessed lower margins on their own account products as a result of the removal of RET for CVs.
  - Trader-hauliers such as Barratlantic and MacKinnon are key to the overall functioning of the economies of small islands like Barra, Tiree and Coll.
  - A number of trader-hauliers noted that they are now carrying goods where the transportation cost per pallet actually exceeds the value of that pallet, which brings into question the long-term demand for such goods – eg building materials.

Network Hauliers

4.3.8 Some hauliers operate network services – ie an end-to-end collection and delivery service based on a relatively fixed cost infrastructure of predictable links, transhipment and end delivery or collection. The most obvious mainland comparators are couriers like DHL and FedEx.

4.3.9 These businesses require volume of throughput to maintain their 'system integrity'. Woody's Express Parcels is primarily a business focused on parcels, although has expanded more recently into large consignments up to pallet size, connecting through to a hub in Inverness. Hebrides Haulage is a pallet based groupage service offering a daily connection between Stornoway and Glasgow, connecting into wider national pallet distribution networks.

4.3.10 The service offering of both of these companies is that customers can move smaller consignment volumes at predictable or fixed cost, on a daily basis to or from the islands. The businesses offer a door-to-door service, meaning that the prices charged have to be sufficient to cover not only the primary link between hubs, but a sorting operation and a network of smaller delivery vehicles. Underpinning this, particularly in the parcel sector, is a considerable IT and administrative infrastructure designed to track consignments through the network and speed-up the handling process.

- Key points:
  - Network hauliers require high volumes to ensure the sustainability of their businesses. The removal of RET for CVs has necessitated an increase in prices which will in turn expose these firms to volume risk.
  - In the short-term, these firms are also exposed to contract risk, where their cost of carriage has unexpectedly gone up and they cannot pass this on to the customer.

Full Service Hauliers

4.3.11 As the name suggest, full service hauliers cover the whole spectrum of haulage operations. They are generally large-scale and offer both general and specialist haulage services eg refrigerated vehicles; tankers; and low loaders.

4.3.12 These businesses rely on scale to bring fleet efficiencies and both support a wide range of equipment suited to many different traffics. The capital cost of this equipment is much higher than a basic flat or curtainsided trailer. For example, one operator provided supporting evidence that the cost for a refrigerated trailer for seafood or chilled supermarket flows is £50,000-£60,000 compared to £20,000-£30,000 for a conventional curtainsided trailer. To operate in these sectors, there is usually a need to have a fleet of this equipment to be able to offer a consistent level of availability and daily capacity. This is likely to be a particular issue in the Western Isles (ie compared to the mainland) because of the logistical difficulties of moving vehicles up and down the island chain as well as to the mainland.

4.3.13 Generally, the size of these operators positions them well to attract contract customers who are looking for scale and depth of resource, such as supermarkets. Although some of this contract work is not hugely profitable, it makes a valuable contribution to getting scale economies for the rest of the business.

4.3.14 The full service operators cross over all other types of business model described previously. In addition, given the scale of goods they were transporting, they were also likely to be in receipt of TRS discounts in the pre-RET era.

4.3.15 This diversity of traffic, the scale of the business and the volume of movements allows the full service haulier to be more flexible on pricing at an individual customer or load level, either per pallet, per full load or otherwise, working within the fullest extent of the acceptable 'market rate'. This may be done for strategic reasons or to accommodate the ability of some customers to pay more than others based on their price sensitivity. Ultimately, the business as a whole has to generate an acceptable return to remain viable.

4.3.16 The effects of the introduction of RET for full service hauliers were somewhat mixed. On the one hand it helped stabilise transport charges, thus helping to maintain volumes. On the other hand, the introduction of RET and therefore lower fares, together, with the removal of volume based discounts, encouraged greater competition and changed the dynamics of the market in a very short space of time.

- Key points:
  - Full service haulage firms benefited from the introduction of RET for CVs in terms of reducing costs, thus potentially helping to protect margins and maintain numbers of customers.
  - However, RET also removed at a stroke their volume based discounts and thus their relative competitive advantage. A future fares policy that protects the scale economies of such hauliers is probably of greater significance to them than the removal of RET in itself.

4.4 Volume Imbalances and Effect on Pricing

4.4.1 A key issue affecting the freight market in the Western Isles, Coll and Tiree is the large imbalance between inbound and outbound traffic. For example, it was explained by hauliers that nine tenths of the total freight volume they carried to and from the Western Isles is inbound. During the interviews with commercial vehicle operators, rates and costs of island deliveries were discussed and it was noticeable that calculations were being based on a round trip basis. In more conventional markets, general haulage operators can usually identify a return load (known as a "backload") to enable both directions to be revenue earning. This is particularly the case where a trip is between two locations which generate a good level of freight movements. In this environment, rates tend to be calculated on a one-way basis with only a nominal amount factored in for the return leg.

4.4.2 As either end of a journey becomes more detached from the main population centres and freight hubs, the ability to find backloads reduces and the 'market rate' (ie the market price) for haulage is adjusted upwards. All of the islands in the RET group were found to be heavily biased towards imports, with a much smaller proportion of goods moving back to the mainland. The extremity of this situation increases the further away from the main Western Isles freight hub (Stornoway) a business is located due to the lack of scale in the majority of more remote areas, although there are some identifiable outbound traffics such as recyclables and landfill to the mainland.

4.4.3 Other than the small volumes of tweed and certain fish, the bulk of freight traffic to the mainland tends to be low value goods and cannot support high rates. Hauliers looking to attract return loads on the spot market talked about simply trying to cover at least a contribution to the ferry fare or fuel costs. The overall volume of freight and its directional imbalance contributes significantly to the haulage rates to the islands.

4.4.4 What this large traffic imbalance means for hauliers' customers is that they are already paying an above average haulage rate and thus their products are at an immediate competitive disadvantage to similar products in higher volume freight markets, particularly those on the mainland. A number of the businesses interviewed noted that haulage savings as a result of RET had enabled transport charges to remain below what they would otherwise have been and thus allowed them to be relatively more competitive. The removal of RET therefore means that, if increased fares are passed on through higher transport charges, the island firms could face a decline in their competitiveness, and at a time when general economic conditions and lower levels of demand are putting increased pressure on local island businesses.

4.4.5 One haulier highlighted that, while it is possible to mathematically calculate a cost to provide a basic point to point transport link, the actual rates in the market, in addition to volume and imbalance, are a function of many variables including:

- the specifics of the actual requirement in terms of goods handling or loading at depots;
- requirement for collection or onward distribution at a location other than the hauliers own hub;
- use of any special trailer equipment or additional manpower needed to load or unload the trailer; and
- demand on administration or management to ensure a satisfactory delivery.

4.4.6 A combination of these issues, in addition to direct operating costs and the ferry fare ultimately leads to the market establishing what an appropriate level of rate should be (ie a function of supply meeting demand in a commercial environment).

4.4.7 The 'market rate' determined by the factors above, is typically within a small range of acceptability. Rates in excess of the market rate will increasingly be rejected as too expensive and the customer will seek an alternative provider. Rates significantly below the market rate will be attractive but it is generally accepted that a company pricing at this level is probably quoting at a loss to attract business and the rate, ultimately, is not sustainable unless the operator has been able to match a return load to get a two way income. Very low rates may also imply service levels that are unacceptable. The same dynamics are found in both full load rates, and rates on a per pallet basis.

4.4.8 Specific factors that affect where this 'market rate' settles on Western Isles routes include:

- whether the market is being served by operators gaining advantage from the 10% freight vessel discount on the Ullapool – Stornoway overnight sailing;
- whether the route to market allows the cost advantage from moving 'drop' trailers or require the HGV unit and driver with each crossing, adding both additional vehicle length and drivers wages to the sea-leg of the journey;
- whether the operator is able to stack, or 'piggyback', empty trailers on the return leg to the mainland;
- whether the route to market has a high or low level of sailing frequency;
- whether the route to market is frequently disrupted or cancelled due to weather;
- whether there is a high volume of freight and strong competition on the route or not;
- the cost of fixed elements like the ferry fare; and
- the cost of significant variable elements such as fuel prices, wage levels, operational overheads and consumables.

4.4.9 From the above list, it is clear that islands to the south of Lewis and Harris could be exposed to these elements eg less competition and lower frequency and therefore the market rate for freight haulage is higher.

4.4.10 From the discussions with hauliers, in very broad terms, the 'market rates', at the time of the consultations, for general freight loads to the islands were:

- Lewis – Inverness
  - £1,000 - £1,250 full load / £45 - £50 per pallet
- Lewis – Central Belt / Aberdeen / Rest of Scotland
  - £1,000 - £1,250 full load
- Uists – NE Scotland
  - £1,300
- Barra – Central Belt
  - £1,250+
- Tiree / Coll – Central Belt
  - £1,350 - £1,700

4.4.11 On the basis of these figures, applying the fares set out in the previous chapter suggests that the ferry fare can account for between 15% to 35% of the cost of transporting goods to and from the islands. The precise figure will ultimately depend on a number of factors, including the size of vehicle, the load being carried, the opportunity for backload and the route used.

- Key points:
  - The large trade imbalance in the RET islands means that haulage costs are generally higher than national averages. This means that island firms have a disadvantage when competing with firms operating in areas with more balanced freight flows. RET for CVs offered a way of absorbing these impacts and an element of protection to such firms.
  - The removal of RET for CVs could make these businesses less competitive in the longer-term if haulage rates progress back to their non-RET level.
  - This issue is particularly prominent the further south one travels from Lewis and Harris due to the lack of scale of industry and activity in the southern islands.
  - The evidence suggests that the commercial vehicle ferry fare can account for between 15% to 35% of the costs of transporting goods to and from the islands.

4.5 Overall Inefficiencies in Serving Island Markets

4.5.1 During the interviews a majority of businesses raised the 'hassle factor' of operating to and from the islands and the huge levels of inefficiency and waste intrinsic in island operations. These hidden costs related to the need to work around a mainland connection that can be infrequent and / or unreliable, in terms of weather, operational related disruptions, and capacity. It was explained that the introduction of RET did not directly address these issues, but it helped to reduce the overall costs of serving the islands and thus, at the margin, helped ensure continuity of service.

4.5.2 The most significant inefficiencies are manifested on Coll, Tiree, Barra and, to a lesser extent, the Uist chain. For these relatively smaller markets, extended sailing time, low service frequency and the inability to use drop trailers was cited as a significant contributor to high freight costs.

4.5.3 Barratlantic indicated that the five hour crossing from Barra to Oban means that in a single round trip, 10 hours of labour cost is absorbed paying the driver to sit on the ferry and is unproductive. For the majority of deliveries, the driver is paid proportionally more to sit on the ferry than to drive. This structural inefficiency has to be built into the overall business cost base and margin. At RET rates the business was viable and thriving, but Barratlantic wanted to be clear that at the proposed rates, it is unlikely it would be cost competitive in its markets. As the biggest employer on Barra and an important player in the local economy, the implications of a long-term loss of competitiveness could have important implications for the local community.

4.5.4 Operators in Lewis tended to be less affected by the inefficiencies but highlighted that compared with the efficiency of mainland businesses, all island hauliers had to absorb a high level of lost productivity in waiting for ferries.

- Key point:
  - RET reduced the overall cost of haulage to and from the islands, equivalent to the reduction in ferry fares on a given route, and thus assisted hauliers in offsetting some of the inefficiencies of serving the island markets. Similarly, the increase in fares across the routes due to the removal of RET for CVs has increased costs equal to the fare increase and added further costs to those generated by the inefficiencies of serving island markets.

4.6 Pre-RET Discounts

4.6.1 All interviews included discussion on the change in CV fares between the pre-RET era and the RET pilot. All stakeholders indicated that the pre-RET published fare would have applied only to a very small number of hauliers / operators, who themselves individually would have been carrying a minor market share. In reality, as discussed in Chapter 2, most of the goods being transported would have been carried by hauliers in receipt of a discount under TRS of up to 15%. In essence, the savings from the fare reduction available under RET would have therefore been lower than the difference between the published pre-RET and RET CV ferry fares.

4.6.2 It was emphasised by hauliers in the interviews that their customers will have been aware of the TRS volume discount arrangement. Indeed, one of the largest operators noted that his customers demanded that rates charged reflected the rebate being passed through. In addition, in the case of highly sophisticated supermarket customers, a condition of contract is full 'open book' pricing and they would have been benefitting from the TRS-discounted fare. For the majority of customers therefore, including the supermarkets, it was explained that the difference between the published fare and the RET fare was not actually there to be passed on due to them already receiving lower charges due to TRS.

- Key point:
  - The existence of the TRS discount meant that in the majority of cases the published savings offered by RET were overstated. However, whilst this is the case, there remained substantial savings for all commercial vehicle operators that could be passed on to customers.

4.7 Passing on Savings from RET CV Fares

4.7.1 Establishing whether RET savings were passed through requires defining what is meant by being 'passed through'. The majority of hauliers accepted that when the RET tariff was introduced, they did not pass on the full savings to a majority of customers[6] in a recalculation of transport charges to their clients, although the larger supermarkets demanding 'open book' pricing did see their charges fall. Most hauliers indicated that in 2008 and for the preceding years, key input costs had been rising rapidly, and in most years since 2008 have continued to rise. Operators highlighted that in some years they experienced double digit annual increases in the costs of factors such as insurance, tyres and labour costs.

4.7.2 The interviews suggest that RET had been used by the majority of hauliers as a means of maintaining stable charges to the market in the face of rising costs, that is, the savings from the RET tariff were passed on in this way. A number of consultees thought that, on reflection, they should have increased charges prior to the introduction of the RET pilot to reflect the increasing input costs, and then actively reduced charges when RET was introduced to demonstrate explicitly that RET did have a positive impact on transport charges to businesses.

4.7.3 It is difficult to be precise about how much transport charges would have declined if the reduction in fares as a result of RET had been passed on in full. The previous section explained that there were a number of factors which make up the 'market rate', including the load being carried, opportunity for backload etc. Nevertheless, using the figures provided by hauliers the ferry fare generally accounts for between 15% and 35% of the cost of transporting goods. The fares data presented in Chapter 2 showed that, depending on the size of vehicle and route, ferry fares for commercial vehicles declined with the introduction of RET, approximately, by between 25% and 50%. This would suggest that total transport charges would have declined by anything between 4% (15% of 25%) or 18% (35% of 50%).

Rising input costs prior to the introduction of RET

4.7.4 In order to establish whether hauliers used RET to maintain stable charges it is useful to examine the extent to which their costs rose over the same period.

4.7.5 Total haulage costs are primarily made up of the following elements: vehicle and depreciation; road tax; insurance; driver employment costs; repair and maintenance; tyres; overhead costs; and fuel. While the figures for each of the elements changes each year, data from the UK Road Haulage Association 2008 annual survey shows the percentage of total haulage costs allocated to each category[7]. The figures are set out in Table 4.1.

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[6] The previous Halcrow report evaluating the impact of RET found that 22% of 160 companies had seen a reduction in transport charges after the introduction of RET, while the majority ie 61% responding that savings were 'never' passed on.

[7] The figures presented here represent average figures across the UK. Specific figures for hauliers on the Western Isles, Coll and Tiree are not available at this disaggregated level.

Table 4.1 Breakdown of Road Haulage Costs (UK)

Cost category	% of total
Vehicle and Depreciation	11.7
Road Tax	1.1
Insurance	4.3
Driver Employment Costs	27.2
Repairs and Maintenance	11.0
Tyres	2.9
Overhead Costs	12.0
Fuel	29.8
Total	**100**

4.7.6 The figures in Table 4.1 show that the highest cost item was fuel at marginally under 30%. This was followed by driver employment costs at just over 27%. Vehicle and depreciation, repairs and maintenance and overhead costs were the next highest cost items at around 11 – 12%.

4.7.7 It should be noted that these figures are for the UK as a whole and do not relate to the Western Isles, Coll and Tiree alone. Figures broken down for haulage companies in these islands separately are not available. The key difference between haulage companies based on islands and those for the UK more generally will be the cost of the ferry fare. Nevertheless, while there may be some differences in the precise breakdown of hauliers on the islands being considered in this study and those of hauliers in the UK as a whole, the figures in Table 4.1 provide a useful indication of the breakdown of costs for hauliers in the Western Isles, Coll and Tiree.

4.7.8 Data from the Road Haulage Association annual survey in 2008 also provides details of the changes in these cost items for UK hauliers between 30 September 2007 and 30 September 2008 ie immediately prior to RET being introduced. These cost changes are set out in Table 4.2.

Table 4.2 Road Haulage Cost changes Sept 2007 – Sept 2008 (UK)

Cost category	% change
Vehicle and Depreciation	4.9
Road Tax	0
Insurance	2.9
Driver Employment Costs	4.0
Repairs and Maintenance	4.1
Tyres	6.3
Overhead Costs	3.6
Fuel	20.1
Total	**8.9**

4.7.9 Table 4.2 shows that overall costs rose by 8.9% between September 2007 and September 2008. This compares with an increase in general inflation of 4.9%[8]. Indeed only two items ie tyres and fuel increased by more than general inflation over that period. However, the increase in fuel was over 20% and is consistent with the responses from hauliers who explained that they had been experiencing significant increases in fuel costs at the same time as RET was introduced for commercial vehicles in October 2008. It also supports the claim that transport charges would have gone up in the absence of RET due to upward pressure on running costs.

4.7.10 Using the data above would suggest that road haulage costs in general increased by around 9% in the year to September 2008, while the introduction of RET in October 2008 would have reduced the cost of transporting a load from an estimated figure of between 4% and 18%. These figures do support many of the claims made by hauliers and suggest that in October 2008, the reduction in CV ferry fares allowed hauliers to absorb the increase in haulage costs which had been increasing at a rate higher than that of general inflation.

4.7.11 The haulier survey also found that the vast majority of customers are mainland companies supplying goods into the islands. The setting of island prices is therefore generally one step removed from the haulier and in most cases there was no means of establishing if savings passed through to a supplier had been passed through to an island customer or simply absorbed by the mainland supplier or other part of the wider supply chain.

4.7.12 What was evident through the consultation was that transport charges for moving goods to and from the islands have broadly remained at a constant level since the introduction of RET in 2008. Across the market, it was indicated there had been very little, if any, rises in haulage rates between 2008 and April 2012. This was through a period where there is evidence that haulage costs, in some years, had risen significantly. Hauliers interviewed provided invoice evidence that, on like-for-like jobs, there had been no rise in rates between 2007 and April 2012. However, in April 2012, companies had increased rates following the removal of RET for commercial vehicles.

4.7.13 Evidence from the Road Haulage Association surveys shows the annual change in costs for each element. Table 4.3 below sets out the annual change in UK costs between September 2008 and September 2012 for each item of haulage costs. It also includes, for comparison purposes, the change in inflation, as measured by the Consumer Price Index, in the twelve months to September of the same year.

4.7.14 The figures in Table 4.3 reveal that, other than in the 12 months to September 2009, costs rose in each of the five years covered. Fuel costs in particular saw significant increases in 2008, 2010 and 2011. While a number of costs saw increases less than inflation, the high percentage of total costs made up of fuel meant that overall cost increases were higher than inflation when fuel costs experienced relatively large rises. These relatively large increases in fuel prices are supported by official data from the Department of Energy and Climate Change set out in Table 4.4. The figures in the table present the change in fuel prices in quarter 3 ie July to September, compared to the same period in the previous year. The figures are similar to the annual cost increases outlined in the Road Haulage Association survey results.

4.7.15 The evidence shows that between September 2008 and September 2012 hauliers' costs rose by over 16%. This covered much of the period where a number of hauliers didn't increase their rates, with the feedback from the haulier interviews suggesting the main driver for this was reduced CV fares

[8] The figure of 4.9% is taken from the Consumer Price Index, Office of National Statistics

brought about by the introduction of RET. The evidence suggests therefore that transport charges remained constant during a period when haulage costs rose by 16%. Indeed, with general inflation also rising in this period by around 12%, businesses actually saw a real terms reduction in transport charges between 2008 and 2012.

Table 4.3 Percentage Change in Individual Haulage Costs from Sept 2007 to Sept 2012

Cost category	Year				
	Year to Sept 2008	Year to Sept 2009	Year to Sept 2010	Year to Sept 2011	Year to Sept 2012
Vehicle and Depreciation	4.9	4.8	3.7	7.2	5.9
Road Tax	0.0	0.0	0.0	0.0	0.0
Insurance	2.9	9.5	2.8	6.4	6.6
Driver Employment Costs	4.0	2.2	1.5	2.1	1.5
Repairs and Maintenance	4.1	5.2	3.7	6.1	4.0
Tyres	6.3	5.7	2.8	15.4	10.1
Overhead Costs	3.6	8.1	2.0	3.4	3.8
Fuel	20.1	-9.4	10.6	14.7	1.2
Total	**8.9**	**0**	**4.9**	**7.8**	**2.9**
Change in Consumer Price Index (CPI)	**5.2**	**1.1**	**3.0**	**5.2**	**2.2**

Table 4.4 DECC Fuel Price Index Q3 to Q3

	2007 Q3 to 2008 Q3	2008 Q3 to 2009 Q3	2009 Q3 to 2010 Q3	2010 Q3 to 2011 Q3	2011 Q3 to 2012 Q3
Change in fuel price	+22.6	-11.3	+11.9	+16.5	0

- Key points:
  - The evidence from the interviews suggests that haulage firms used the cost reductions brought about by RET to offset potential rate rises being driven by increases in haulage costs, particularly fuel.
  - The evidence suggests that haulage costs increased by around 9% in 2008, while the reduction in commercial vehicle ferry fares due to RET meant that the costs of transporting goods declined by between 4% and 18%.
  - Hauliers' costs increased over the period 2008 to 2012 at a higher rate than general inflation but transport charges for many businesses remained stable.

– While the introduction of RET did not lead to a reduction in transport charges to businesses, it enabled hauliers to maintain rates at their 2008 level, meaning businesses saw a real terms reduction in their transport charges over the period of RET.

– It was also noted that the introduction of RET helped to grow volumes and create a positive environment for business investment.

4.8 The Vulnerable Sectors

4.8.1 From discussions with hauliers, it was suggested the further south in the islands one travels, the greater the issues - ie higher costs; greater inefficiencies through lower volume / demand; and fewer infrastructure benefits, like the ability to use drop trailers, all have an impact.

4.8.2 Vulnerable sectors are likely to be those at most risk and operating at low margins eg agriculture; crofting; basic building materials; shellfish; and seafood exports. Given the relatively low scale of industry on the islands, it was explained by those interviewed that income for many islanders appears to be generated by having more than one job and entrepreneurial interests. It was also explained that typically, these include a dependency on one or more of these marginal sectors.

4.8.3 It was claimed that relatively higher island prices and the generally poor macro-economic environment are leading to end customers changing buying patterns. In sectors including fuel supply, building materials, animal feed etc hauliers noted consignments of smaller quantities being ordered at one time, for example, half a pallet rather than a full pallet of materials. To hauliers with already low volumes, it was suggested this is accelerating the loss of scale efficiencies, increasing the cost of distribution, which in turn is further affecting business performance and reducing the efficiency derived by frequency of delivery.

4.8.4 Hauliers noted that for some of the most sensitive traffics, the cost of transportation is greater than the actual product cost - ie basic items can be double that charged on the mainland. It was explained that this is increasingly leading to substitution for lower quality inputs in the case of agriculture, and abandonment of discretionary activities like building.

■ Key point:

– It was claimed that the removal of RET for CVs, combined with rising costs for businesses across the board, is leading to a lower demand for haulage, hence lower volumes, lower scale economies and higher costs. This is a vicious circle which is by those interviewed creating inefficiencies and bringing into question the long-term future of local staple industries.

4.9 View on the Alternative to RET

4.9.1 A majority of hauliers accepted that, in the current climate of depressed economic activity and government budget constraints, if affordability was an issue there may be a case that RET levels were unsustainable and the tariff needed to rise. However, real concern was raised about the timing and level of increase proposed by Transport Scotland, which was considered to be of a magnitude to have significant adverse impacts on many of the sensitive sectors of the island communities (an issue consistently raised in the business interviews, see below). In addition, there were also concerns about what the alternative arrangements to RET may be.

Contracts

4.9.2 Further key concerns raised by hauliers are the risks and practical challenges that are emerging as a result of the speed of change in the fares. Each of the larger hauliers has a proportion of its customer base in a contractual relationship. These contracts are over multi-year periods with many working on rates agreed prior to the announcement of RET being removed for commercial vehicles fares.

4.9.3 It was explained that the Co-operative stores had accepted the rise, enabling contract holders to pass on the cost, but there were a number of other examples where contract customers had refused to accept increases. These customers tended to be national organisations who are themselves locked into contractual arrangements with an ultimate customer. For example, the retailer Next was found to be a company with a seven year contract with a national carrier, who in turn is in a three year contract with an island operator. Each of these contracts was fixed on agreed rates that had been determined by each party making cost assumptions in future years. Although some fluctuating costs, such as those for fuel, are usually covered with clauses like fuel duty escalators or surcharges, the unexpected and large increase in the ferry fare was not factored in. This cannot now be renegotiated until the next contract period.

4.9.4 Where costs cannot be passed on to a proportion of the customer base, it was claimed that other customers will have to make up the difference and as the 'power' of the customer in terms of size and volume diminishes the more likely it is that they will be the ones who are left facing the largest increases in transport charges.

Cash Flow

4.9.5 Several hauliers also expressed concern about the cash flow implications of the recent and proposed rises. CalMac operates strict payment terms of 30 days, but hauliers' customers rarely pay this promptly. It was explained that the standard supermarket payment terms are 90 days, and some sectors can be even longer. Agriculture, for example, is a sector identified as having a relatively poor record at paying promptly because of its own lumpy cash flow situation being tied to Common Agricultural Policy payments and seasonal livestock sales.

4.9.6 Hauliers interviewed saw the April 2012 rises as giving them particular difficulties as they believe that they will end up carrying the financial exposure of the whole supply chain. The smaller hauliers in particular find this extremely difficult, relying on overdrafts and other financial products like invoice factoring to bridge the gap. Both these means of financing contribute to increasing their overall business overhead and risk exposure, which again has to be recovered by trying to generate further margin within the business.

Discounts

4.9.7 The issue of discounts came up in almost every discussion, with strong views on their advantages and disadvantages. A view was formed that this was more of a concern, certainly in Lewis, rather than the absolute level of tariff.

4.9.8 The freight vessel discount of 10% was used by the majority of operators to and from Lewis. Those choosing to use the alternative MV *Isle of Lewis* service did so willingly because of wider business and customer service benefits, including more convenient sailing times. It was found that the ability to substitute routes across the islands was relatively small, with origins and destinations typically determining a clear route preference based on journey time and extended costs of fuel and ferry.

No operator suggested that they were using the overnight Ullapool – Stornoway sailing in preference to other routes because of the savings the freight vessel discount offered.

4.9.9 Opinions on volume related discounts were more polarised. With the exception of the two largest hauliers no operator thought that discounts related to volume carried should return. This view was even shared by some of those who had previously benefitted from TRS.

4.9.10 The overwhelming reason citied was that it distorted the market and gave some operators a fundamental operating cost advantage over others. It was believed that this prevented companies from competing for traffic on a genuine like for like basis. One operator who previously benefitted from a higher level of TRS commented that, to be a healthy market, every operator must be able to compete on his own merits and if he is not efficient or competitive enough then so be it. The view was that it should not be for CalMac, which is subsidised by the Scottish Government, to determine which operator has the cost advantage.

4.9.11 One of the main strengths and benefits of RET expressed by those against volume discounts was that it had an inherent fairness to it. Several citied the arrangements on Northern Isles routes as a good example of how the ferry tariff is applied and that it appeared to be open, simple, equal and transparent to all. A significant criticism was that the tariff and discount arrangements, formulae and mechanisms on the Clyde and Hebrides Ferry network have never been truly transparent, which has led to suspicion that 'official' levels of maximum discount were being exceeded or otherwise enhanced by other means. There was however no firm evidence presented to back up this claim.

4.9.12 Operators serving the lower volume markets to the south of the island group noted that the volume of business was so low that it was not possible to achieve higher levels of discount under the TRS formula, which was common across all routes.

4.9.13 The counter argument for volume related discounts was that, in most commercial arrangements, there is a benefit for committing volume or buying in bulk so why should the ferry be any different? It was seen as an incentive to grow the business and carry higher volumes and therefore achieve greater levels of discount. It should be noted that while the majority of those interviewed did not want to see a return to volume-based discounts, the haulier on the islands with the majority of the volume of goods being transported was a strong supporter of a volume-based discount scheme similar to TRS.

4.9.14 Overall there was an appetite for a discount mechanism that offered all island businesses some level of compensation for the disadvantage of operating on the islands and having to incur more costs travelling by ferry than driving a similar distance. It was also acknowledged however that, depending on the structure of the discount mechanism, this would raise State Aid issues.

- Key points:
  - The relatively sudden move away from the RET fare system for CVs is seen by local hauliers as detrimental (even with the transitional arrangements) as a number of haulage firms and island customers are tied into medium to long-term contracts and will have to absorb the cost of these rises.
  - This issue is said to be compounded by the cash flow risks of hauliers, who are in many cases bearing the financial exposure of their whole supply chain.
  - There is significant debate over the potential return to volume based pricing. A majority of haulage firms wish to avoid going back to volume based discounts as

RET helped to level the playing field and introduced competition, allowing all businesses to compete equally in terms of the ferry fare. The limited size of the market meant that not all hauliers had the opportunity to benefit from scale. However, the full-service operators point out that volume based discounts are a common business practice and noted that they are necessary to ensure that their high value traffics are not cherry-picked by 'low cost' firms.

- There was however common agreement amongst the commercial vehicle operators consulted that island haulage firms should benefit from some form of discount to protect against the 'white van man' cherry-picking high value cargoes and leaving hauliers with a rump of low margin products. Any mechanism would have to be designed to comply with State Aid rules.

4.10 Conclusions

4.10.1 This chapter has explored at length the issues and impacts, around removing RET for commercial vehicles on haulage firms on routes to the Western Isles, Coll and Tiree. The evidence suggests that due to the complex nature of the haulage industry and the different business models, the effects are not necessarily consistent across the sector due to the different nature of the business types / models. In addition, a combination of the short six-month period since the removal of RET, together with other influencing factors such as the changing market structure, means there are a number of other factors influencing the ongoing performance of the industry and the operational behaviour of individual businesses. Isolating these from the effects of removing RET ferry fares for commercial vehicles is not straightforward. Nevertheless, a number of important findings can be drawn from the interviews with hauliers and the evidence supplied by hauliers and from other sources.

4.10.2 A key question that this study seeks to answer is the extent to which the savings offered by RET were passed on by hauliers to island businesses. An important point about the extent of RET savings was the existence of the TRS discount in the pre-RET era. This meant that the published savings for CVs offered by RET were overstated. However, whilst this is the case, there remained substantial savings that could be passed on to customers. The evidence from the interviews suggests that haulage firms did not directly pass these savings on to all of their customers in the form of lower charges, although a number would have seen a consequential reduction in transport charges through, for example, the use of 'open book' pricing.

4.10.3 In most cases, hauliers used the cost reductions brought about by RET to offset potential rises in transport charges being driven by other operating costs, particularly the significant increase in fuel witnessed in the 12 months to September 2008, just ahead of the introduction of RET. While fare reductions, after TRS discount, of up to 50% could have resulted in lower transport charges of between 4% and 18%, general haulage costs for firms in the UK had risen by just under 9% in the year to the introduction of RET in 2008.

4.10.4 In addition, the evidence suggests that hauliers maintained transport charges at their 2008 level throughout the RET pilot in the face of total costs increasing at above-inflation rates. Therefore, the evidence does suggest that RET resulted in stable charges which would have increased in its absence. In this sense transport charges to businesses declined in real terms between 2008 and when RET was removed in 2012. It was also noted that the RET real-term cost reductions helped to grow volumes and create a positive environment for business investment.

4.10.5 One of the main policy justifications for introducing RET for CVs was the impact the cost of transporting goods by ferry was having on the relative competitiveness of businesses in the pilot area. In addition, trade imbalance in these islands means that haulage costs have typically been above national averages. Island firms therefore had a disadvantage when competing with firms operating in areas with more balanced trade flows. RET for CVs offered a degree of support to such firms and also helped mitigate other inefficiencies caused by operating on the islands, such as limited scale of industry and opportunity for transporting backloads.

4.10.6 The evidence gathered from the interviews with hauliers suggests the removal of RET ferry fares for CVs has:

- had a negative effect on the volumes and margins of some *small hauliers*, who play an important role in offering choice in the market;
- squeezed the margin of some *trader-hauliers* who are key to the economies of small islands like Coll, Tiree and Barra;
- *Network hauliers* require high volumes to ensure the sustainability of their businesses. The removal of RET for CVs has in some cases necessitated an increase in prices which will in turn expose these firms to volume risk; and
- reduced the volume and economies of scale of some *full-service hauliers*, thus potentially increasing the long-run market rate for haulage.

4.10.7 It was also explained that any additional increases in fares to non-RET levels will have further negative impacts on the industry due to limited opportunity to absorb higher costs. It is feared that higher fares will be passed on in increases in transport charges, leading to decreases in customers and volumes and further losses in efficiencies and economies of scale.

4.10.8 While there was a majority view RET was beneficial to hauliers as it led to higher volumes, it was also claimed the removal of volume-based discounts has had a negative effect on some of the larger hauliers who have a majority of the market and provide important services to a significant number of businesses. RET exposed them to competition and potential cherry picking of their more profitable markets, which could have long-term implications for the operation of the sector.

4.10.9 There was a general agreement amongst those consulted that there was a need for a discount for island hauliers to protect them from cherry picking from the white van trade. However, there was significant divergence of views on the form of this discount, with the larger full-service operators preferring volume based discounts and the smaller hauliers opposed to this and supportive of a system that is more equitable and transparent.

5 Ferry Fares and the Business Community

5.1 Introduction

5.1.1 This chapter summarises the findings from the interviews and surveys of island businesses and their views on how the removal of RET for commercial vehicles is likely to impact on their ongoing performance. It also provides a record of the discussion with the 'control group'.

5.1.2 RET for CVs was introduced specifically to support general economic activity in the islands by helping businesses and consumers. The policy recognised that both the cost of living and doing business in the islands was above the national average (even compared to other Scottish islands) and thus impacting on the long-term sustainability of these communities. It was anticipated that the RET-related savings would be passed on to businesses via lower costs and then feed through to consumers through lower prices. The extent to which RET contributed to lower business costs was a key line of questioning during the business interviews. There were also detailed discussions about the impact of the removal of RET for businesses in different sectors or geographic areas.

5.1.3 The evidence in this chapter is based on 37 interviews with business across all of the islands in the study area as well as 49 responses to the online business survey. It covers a number of key themes raised in the interviews and the responses received in the online survey, including:

- business confidence in fares policy;
- the impact of the introduction of RET;
- RET and the haulage sector;
- the impact of the removal of the CV element of RET;
- competition in the haulage market; and
- the impact of RET on competition.

5.2 Business Confidence in Fares Policy

5.2.1 A frequent issue raised during the interviews was the importance of ferry services for the ongoing success of the island economies and the role that certainty of fares played in business planning and investment. There was a common view across all islands and business sectors that, while the RET pilot had positive short-term impacts in terms of stabilising transport charges, it had also generated a degree of uncertainty for many businesses. It was explained that RET was established as a three-year pilot. As this was only a pilot, and therefore a lack of clarity around what would happen at the end of it (ie would it be removed or not?), few long-term investment decisions were made on the back of it. Consultees noted that a decision about the future of RET was not made at the end of the pilot but instead it was extended for a year. It was then announced that RET would remain but at the same time the commercial vehicle aspect of it was removed.

5.2.2 Businesses noted that ferry fares, and transport costs more generally, are often key to day-to-day operations. Indeed, the business survey found that transport costs accounted for between 10% and 25%+ of total business costs for over 50% of those surveyed. In addition, 47% of businesses noted that more than 25% of these transport costs are accounted for by the ferry fare. It was claimed that the lack of certainty and unanticipated changes in fares were damaging business confidence at a time when activity on the islands is already depressed due to the general economic downturn.

- Key point:
  - Businesses in the Western Isles, Coll and Tiree were almost universally concerned that the lack of certainty and frequent policy changes were having a detrimental impact on business confidence and long-term investment planning. Businesses stressed the need for a clearly defined longer term fares strategy that will be consistently adhered to by the Scottish Government.

5.3 The Introduction of RET

5.3.1 Business views on the benefits of the introduction of the overall RET pilot varied. For example, while further work would be required to determine this was a general and representative view, a number of businesses interviewed on Coll and Tiree felt that RET had benefited tourists more than islanders. The RET passenger fare is only around £5 cheaper than the old six-journey multi-book tickets available prior to RET, which were generally bought by locals. While there is a benefit in not having to pay the cost of six journeys up-front, the benefits have been otherwise limited. It was recognised that lower vehicle fares make the islands more accessible for tourists. However, while this has increased the number of visitors to the islands, it was claimed that many tourists take up important capacity on the ferry and, in many cases, tend to bring food with them therefore spending little locally. In contrast, most of the businesses interviewed in the Western Isles were highly positive about the benefits of RET, noting that it has increased tourism and helped to stimulate the economy at a time of economic hardship.

5.3.2 However, almost all businesses interviewed across the different islands felt that the one area where RET has been seen to be of particular value across all of the islands is for commercial vehicles, and there is concern that it is fares for this group which are being removed. Interviewees and those involved in the survey expressed surprise that the Scottish Government is prioritising personal and tourist travel over businesses, which are the main drivers of economic activity.

- Key point:
  - RET for CVs was greatly valued across all of the islands in the pilot and there was surprise amongst many businesses that this was the fare type that was being removed.

5.4 RET and the Haulage Industry Transport Charges

5.4.1 Similar to the findings from the haulier interviews, there was a general view from most businesses interviewed across all of the islands that the hauliers had used the savings from RET to compensate for a number of other costs that were rising at that time, including fuel, insurance and the cost of an operating licence and had not passed on the savings in the form of lower transport charges[9]. A number of those interviewed explained that transport charges of hauliers have been generally stable in recent years and believe this is in part a result of RET helping to maintain price levels. There appears to be minimal support from businesses for the view that hauliers used RET to subsidise their bottom line.

5.4.2 There was a wider view that haulage costs perhaps lacked some degree of transparency, resulting in some people believing that lower fares were not passed on when RET was introduced. However, similar to the views expressed by hauliers, a number of stakeholders noted that, in hindsight, hauliers should have put their rates up to reflect cost increases and then reduced these following the introduction of lower fares as part of the RET pilot.

- Key point:
  - There was a majority view amongst businesses that hauliers used RET to stabilise transport charges rather than to pass on the RET saving in full in the form of lower transport charges

5.5 Impact of Removal of RET for Commercial Vehicles

5.5.1 A number of people interviewed explained that the removal of RET for CVs had the largest impacts on businesses that have one or more of the following characteristics:

- Moving / purchasing low volumes – these organisations have very little buying power and thus have to take the price set by the hauliers and other suppliers.
  - *Examples include independent retail stores and furniture and white goods.*
- Moving a low value / low margin good – companies moving goods with either small margins and / or volatile prices experience the biggest impacts.
  - *Examples include building materials, packaging etc.*
- The company is a 'price taker' – firms which do not have the ability to influence the market price of their goods (ie they take the price set by the market) and are exposed to any cost increase.
  - *Examples include agricultural products, seafood, fuel etc.*

5.5.2 The sectors which exhibit such characteristics include small scale / independent retail; agriculture; aquaculture and fishing; construction; and low value manufacturing. There are no reliable data on the structure of the Coll and Tiree economies, however the IDBR (Interdepartmental Business Register) does provide a useful data source for the sectoral breakdown in term of employment and number of registered businesses for the Western Isles. The data are set out in Tables 5.1 and 5.2 below.

[9] A minority of businesses did believe that lower fares had been passed on in terms of reduced transport rates

Table 5.1 Registered Businesses by Sector as a Percentage of Total (Western Isles and Scotland, March 2012)

Sector	Western Isles (% of Total)	Scotland (% of Total)
Agriculture, Forestry and Fishing	23.0	10.9
Mining and Quarrying	0.4	0.2
Manufacturing	5.2	5.3
Electricity, Gas, Steam and Air Conditioning Supply	0.4	0.1
Water Supply; Waste Management and Remediation Activities	0.4	0.3
Construction	10.8	11.6
Wholesale and retail trade; Repair of motor vehicles and motorcycles	16.0	15.9
Transportation and storage	4.8	3.2
Accommodation and food service activities	8.7	8.2
Information and communication	3.0	4.9
Financial and insurance activities	0.9	1.2
Real estate activities	1.3	3.0
Professional, scientific and technical activities	8.7	16.2
Administrative and support service activities	4.8	6.3
Education	1.7	1.1
Human health and social work activities	4.8	3.9
Arts, entertainment and recreation	1.7	2.5
Other service activities	3.9	5.5

5.5.3 Table 5.1 shows a relatively high number of enterprises in agriculture, forestry and fishing industries, amounting to 23%. This is higher than any other sector in the islands and compares with a Scottish average of just under 11%.

Table 5.2 Employment by Sector as a Percentage of Total (Western Isles and Scotland, March 2012)

Sector	Western Isles (% of Total)	Scotland (% of Total)
Primary Industries	11.9	6.2
Manufacturing	6.6	10.0
Construction	12.7	6.9
Wholesale, retail and repairs	21.8	20.0
Transport and storage	6.8	4.8
Accommodation and food services	11.9	9.0
Information and communication	*	3.2
Financial and insurance services	2.6	5.0
Real estate activities	2.0	1.5
Professional, scientific and technical	5.1	7.3
Administrative and support services	3.2	8.9
Education, human health and social	9.0	11.9
Arts, entertainment and recreation	*	2.9
Other service activities	2.2	2.4

* Not available due to confidentiality reasons

5.5.4 While Table 5.1 focuses on registered business, Table 5.2 reveals employment by sector, as a proportion of the Western Isles total. The table also shows the equivalent figures for Scotland. Similarly to the figures on the number of businesses, the table shows that the Western Isles has a high dependency on the primary industries, with a much higher proportion of people employed in the primary industries (11.9%), including agriculture and fishing, compared to Scotland as a whole (6.2%). The table also shows that there is a higher percentage of employment in the construction sector compared to Scotland as a whole. Indeed, the figure of 12.7% is almost double the figure of 6.9% for Scotland.

Table 5.3 Turnover by Sector in the Western Isles (2012)

Sector	Total Turnover (£m)
Primary Industries	156
Manufacturing	48
Construction	60
Wholesale, Retail and Repairs	234
Transport and Storage	33
Accommodation and Food Service	26
Information and Communication	*
Financial and Insurance Services	NA
Real Estate Activities	10
Professional, Scientific and Personal	32
Administrative and Support Services	15
Education, Human Health and Social	19
Arts, Education and Recreation	*
Other Service Activities	7
Total	710

5.5.5 The figures in Table 5.3 on turnover also provide a good indication of the importance of the primary industries, making up 22% of the total turnover of enterprises in the area. Indeed, the sector employs the same number of people in accommodation and food services, yet the primary sector has six times the turnover.

5.5.6 While figures for 2011 will be released over the coming year, the 2001 Census provided more disaggregated data which noted that employment concentration in agriculture and fishing ranged from 5% in Lewis to 17% in Harris and Scalpay.[10] The employment concentration in these sectors in Coll was as high as 22%. The equivalent figure in Tiree was 17%, but that island also has a heavy concentration of ancillary jobs linked to this sector, such as in the food and drink industry.[11]

5.5.7 While the tables and figures above illustrate the high concentration of firms and employment in the agriculture, forestry and fishing sector, it also important to recognise that the size of the individual businesses in these sectors is relatively small. Indeed, this is a common characteristic across many of the sectors in the Western Isles. Table 5.4 below reveals the number of employees by registered businesses in the Western Isles.

[10] Scottish Ferries Review Economic Work Package – Baseline Area Analysis (High10lands and Islands Enterprise, 2009), p. 34.

[11] Ibid., p. 10.

Table 5.4 Number of firms by Employment Size Band Western Isles (2012)

Number of Employees	Number of firms
0 – 4 Employees	965
5 – 9 Employees	160
10 – 14 Employees	65
15 – 49 Employees	65
50+ Employees	10
Total	1,270[12]

5.5.8 Table 5.4 shows that of the 1,270 registered businesses in the Western Isles in March 2012, 76% of these had less than five employees. This compares with a figure of 70% for Scotland as a whole. The small size of businesses, in terms of the number of employees, is particularly evident in the primary sector. Table 5.5 below shows that of the 300 registered businesses in the primary sector, 90% of these had less than five employees. Indeed no business had more than 14 employees. The small size of firm adds to the vulnerability of this particular sector ie while they are not only operating in a sector that is characterised by high levels of competition and are generally price takers in the market, their small size also means they have limited market power in terms of being able to pass on costs to their customers.

Table 5.5 Number of firms by Employment Size Band in Primary Indstries, Western Isles (2012)

Number of Employees	Number of firms
0 – 4 Employees	270
5 – 9 Employees	15
10 – 14 Employees	10
15 – 49 Employees	0
50+ Employees	0
Total	300

5.5.9 Given the relatively high concentration of employment in the RET pilot area in businesses that display at least one of the characteristics set out in 5.5.1, it was claimed that the removal of RET for CVs and the consequent increase in business transport costs is likely to have a negative impact on the local economy. In addition, it was also claimed that, in many areas, these businesses are the key drivers of small communities which are very vulnerable and sensitive to small changes in business performance.

- Key point:
  - The removal of RET for commercial vehicles is seen to be hitting the most marginal businesses in the community the hardest. There was a general concern that this will impact on the long-term viability of many parts of the islands, particularly the most vulnerable sectors.

[12] The figures don't sum to the total as the individual categories are rounded to the nearest 5

5.6 Competition in the Haulage Market

5.6.1 While it is difficult to unpick the RET specific element of any increase in costs, this position has been made even more difficult in the Western Isles following recent changes in the haulage market. The demise of MacAskill Haulage, which was one of the 'big two' full service hauliers has distorted the overall operation of the haulage market in the Western Isles.

5.6.2 It was explained that the withdrawal of MacAskill has created fierce competition amongst the hauliers, mainly in Lewis and Harris, and the potential beginning of a 'price war'. It has also opened up opportunities for new entrants to the market in these areas, creating an increase in choice for users of haulage services. MacRitchie Highland Haulage in particular has made a concerted effort to enter the Western Isles market. The effect of this increase in competition has been to limit the impact of the removal of RET-related price rises on local businesses. Many firms noted that this is a 'honeymoon period' and expect rates to go up once the market settles down again.

5.6.3 The level of competition in the southern islands and Coll and Tiree is much more limited compared to Harris and Lewis. This is due to the generally smaller size and scale of industry and therefore the lack of viable opportunities for hauliers. These areas tend to be dominated by one or two hauliers.

5.6.4 The introduction of RET coincided with the removal of the volume-based discounts, such as TRS, which the larger hauliers benefitted from due to the greater volumes they were transporting. Together, it was claimed, these two policies had created a more level playing field. While the larger companies still had the benefits of scale to some extent, their overall advantage was reduced. The creation of a level playing field was seen as universally positive by island businesses because it had created more competition in the market.

- Key points:
  - The full effects of the removal of RET are not yet being felt in Lewis and Harris because of the current disruption in the market caused by the demise of MacAskill Haulage. There have even been instances of rates being reduced as hauliers jockey for position. However, there is a longer-term expectation that rates will increase once the market has settled.
  - The increased competition amongst hauliers driven by the level playing field created by RET is seen as universally positive amongst island business, promoting choice and competition.

5.7 Impact of RET on Competition

5.7.1 Businesses explained that the introduction of RET for commercial vehicles in 2008 had a noticeable impact on competition within the wider economy, particularly between small retailers and the large supermarkets. Given the scale of companies like the Co-operative and Tesco, they tend to adopt regional or indeed national pricing systems. Inherent within this is the absorption of all costs for each business unit within the wider company / regional grouping overheads. That is, large firms like the Co-op do not tend to consider shops as individual business units and thus their prices do not reflect the 'real' cost of doing business in a certain location ie their overheads for the whole network are split across all business units and therefore a change in ferry fares (either up or down) will be spread across a large number of units. This is in contrast to the small independent local stores who must either absorb or pass on the additional costs of doing business in an island community.

5.7.2 It was claimed on a number of occasions that RET for commercial vehicles helped keep costs down for independent stores. By reducing (or at least maintaining) the cost of a pallet with any given haulier, RET reduced (or maintained) the unit cost of individual goods sold in the shops. This was true of grocery stores to some extent but it was felt the biggest impact was on shops that sell low margin bulk goods like carpets, furniture and white goods. Stakeholders saw this as a beneficial impact in terms of both choice within the market and town centre / rural community vitality.

5.7.3 In contrast, it was explained that the initial and continued provision of RET for cars has incentivised many people to shop on the mainland. While the length of the crossing, the cost of the trip and the cost of fuel means that people are unlikely to go to the mainland to only shop, they will tie in shopping trips with visits to, for example, their family, holidays, hospital visits etc. While this is obviously rational behaviour by islanders, it is having a detrimental impact on island businesses, particularly for big ticket items like furniture or high value products like electronics where independent island stores do not have the scale to compete with national retailers.

5.7.4 Similar to most Scottish retailers, it was explained that local businesses are facing stiff competition from internet shopping. While certain mainland firms will no longer deliver to the islands (because their couriers will not go to the islands), it was suggested that the standard delivery charges offered by firms that do deliver from the mainland (eg Next, John Lewis) are very low – eg Next is £2.50 for a delivery and John Lewis deliver free of charge. Like the Co-op, these companies absorb the costs of delivery to the islands across a much larger sales base. While this is beneficial for the consumer, it was suggested it is having a serious impact on the viability of a number of small scale island businesses, particularly those that trade in 'big ticket' items.

- **Key points:**
  - Local competition brought about by RET is seen as positive for the local consumer but the increased competition between the island retailers and large mainland businesses is seen as less positive for the islands as a whole and their sustainability. Overall, however, RET for CVs was seen as an important policy in allowing small and independent island businesses to compete with large chain firms like the Co-Op and Tesco.

5.8 Survey Findings – On-line Business Survey

5.8.1 In order to validate the findings of the interview process, an online survey of businesses was also undertaken to canvass views of those that were not selected to take part in an interview. The aim of this survey was to assist in developing a wider evidence base to critically assess and support the findings of the business interviews. A key point is that the survey was focused more on collecting factual data than on more general opinions on the removal of RET for CVs. This section therefore summarises the findings from the survey[13].

[13] It was agreed at the outset of the study that a web-based survey would likely be the most effective survey mechanism in terms of maximising response rates. However, one limitation of this type of survey is that the survey organiser cannot control the sample. Therefore there is a risk of self selection and bias within the sample – ie those who have filled in the survey may be those with a specific interest in the survey outcome

Area of Operation

5.8.2 Respondents were asked on which island(s) their business operates and were permitted to tick all islands that applied. Figure 5.2 below shows the areas of activity of the businesses interviewed. It can be seen from the Figure that the responses are a reasonable reflection of the share of total population and level of business activity on the islands ie the majority of businesses are on the most populated islands of Lewis and Harris, with lower numbers of businesses on the southern islands and Coll and Tiree.

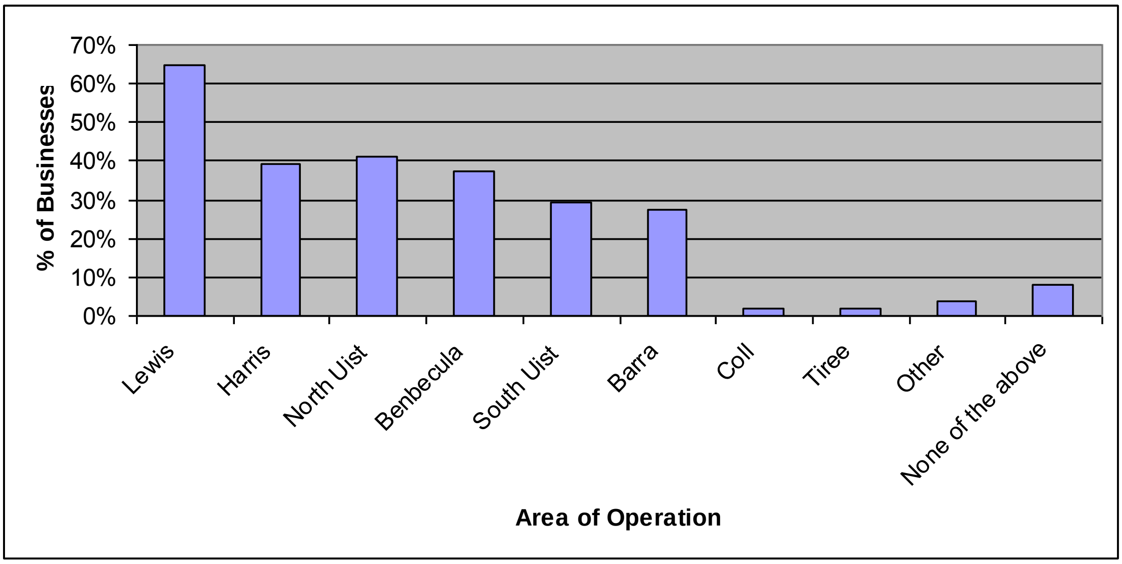

Figure 5.1 Area of Business Operation

5.8.3 Almost 65% of businesses surveyed operated in Lewis, which is perhaps unsurprising given the role of Stornoway as the economic hub of the Western Isles. Thirty nine per cent of businesses operated in Harris (many of which will also be included in the Lewis figures), while the figures across the Uists, Benbecula and Barra ranged from 28% to 41%. Only a small number of businesses surveyed operated in Coll and Tiree.

Sectoral Split

5.8.4 Figure 5.3 shows the sectoral split of businesses surveyed – note that respondents were asked to tick all of the sectors which applied, meaning the percentages in the figure do not necessarily sum to 100% due to a number of businesses operating across sectors.

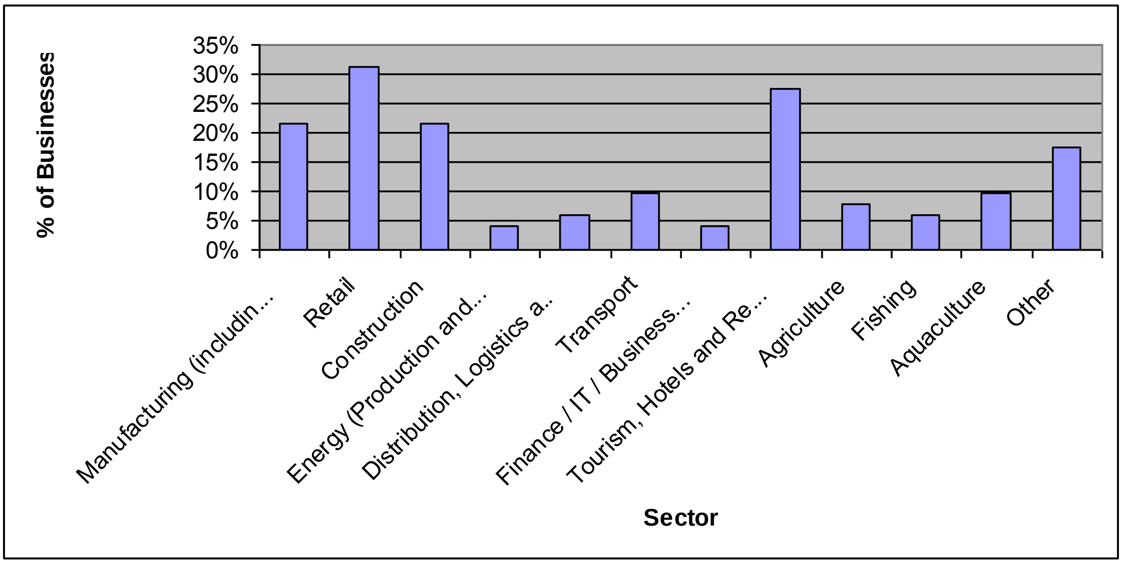

Figure 5.2 Sectoral Split

5.8.5 The sectoral split identified by respondents is broadly in keeping with the industrial structure of the study area overall. The two largest individual sectors were "Retail" and "Tourism Hotels and Restaurants", which, while being affected by the removal of RET for CV fares, will likely be major beneficiaries of the reduction in car and passenger fares under the RET pilot. These were followed by manufacturing, construction, agriculture and fishing / aquaculture. Overall, those sectors which will be impacted by the removal of RET for CVs, and will therefore be well placed to comment on the effects, are well represented in the survey.

Number of Employees

5.8.6 The majority of the businesses within the sample were relatively small in scale. Forty six per cent of businesses employed between one and three full-time staff, with only three firms in the sample employing more than 20 staff. On many occasions, these firms were supplemented by a small number of part-time and seasonal staff. Overall however, the sample reflects the small scale of businesses typical of the communities in the RET pilot area.

Average Annual Turnover

5.8.7 Figure 5.4 illustrates the average annual turnover of businesses within the sample.

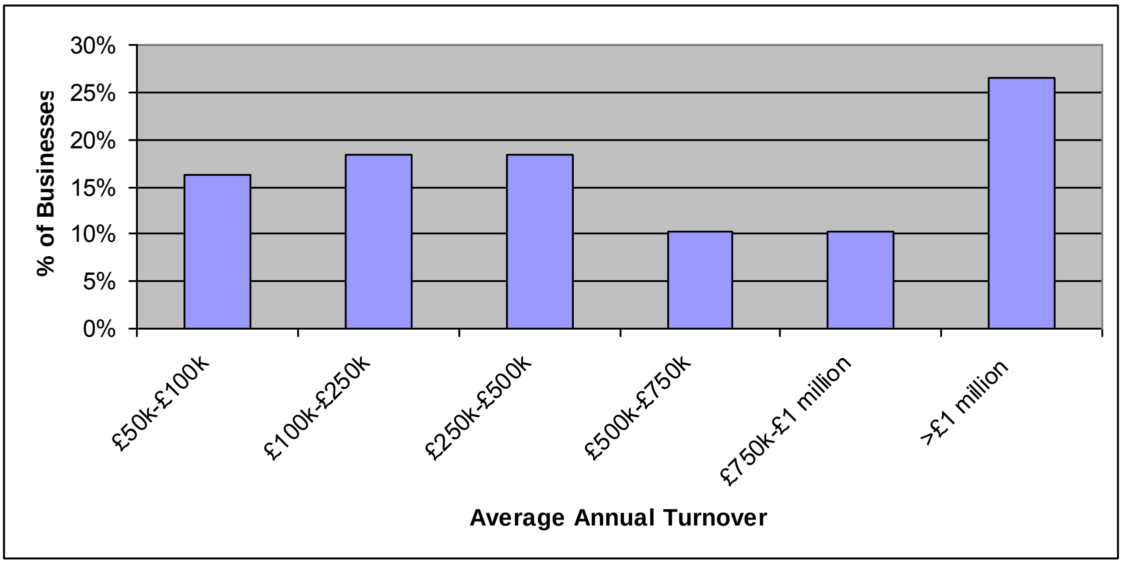

Figure 5.3 Average Annual Turnover

5.8.8 In keeping with the relatively small size of the businesses, average turnover within the sample was also relatively small. Only 27% of businesses surveyed had a turnover of greater than £1 million. Sixteen per cent of businesses within the sample turned over £100k or less on average.

Trading History

5.8.9 Despite the relatively small scale of businesses, 63% of those who responded have been trading for more than ten years, whilst a further 22% have been trading for between five and ten years. The businesses are therefore relatively well established.

Trading Performance Since 2008

5.8.10 The RET pilot was introduced in October 2008 and, therefore, an important question asked in the survey was how business profitability and turnover had changed since that year, albeit recognising that RET was not the sole factor, or indeed the most important factor, impacting on this particular metric.

5.8.11 A total of 59% of businesses noted that their turnover had increased either significantly or slightly since 2008. Similarly, 51% of business noted that their profit before tax had increased significantly or slightly since 2008. While a small number of businesses noted that their turnover and profitability had decreased, there was an overall general trend of improved business performance. These results coincide with difficult trading times more generally when economic activity has been suppressed and growth has been below its long term trend.

5.8.12 In spite of positive responses on recent performance, it was claimed by a number of businesses that fuel costs and the general reduction in activity, and therefore lower demand, are seen to be putting ever-increasing pressure on their financial performance in terms of lower revenue, turnover and profit.

Imports and Exports

5.8.13 Respondents were asked what type of goods they typically moved on and off the island. While there are too many responses to set out here, there is a clear trend of imported goods being either for the retail and hotel trade or, more prominently, as inputs for manufacturing, construction, agriculture and fishing / aquaculture. Only four (6.5%) companies who responded to this question answered that they do not import anything into the islands.

5.8.14 The majority of outbound goods are finished products heading for UK mainland or European markets. Eighteen firms (29%) noted that they do not export any goods from the islands. While not necessarily an indicator of the volume of trade, it provides a further indication that the majority of goods are imported rather than exported to and from the islands.

Transport and Ferry Costs

5.8.15 Respondents were asked what proportion of their total business costs are related to the transport of goods and supplies. The results are illustrated in Figure 5.5 below:

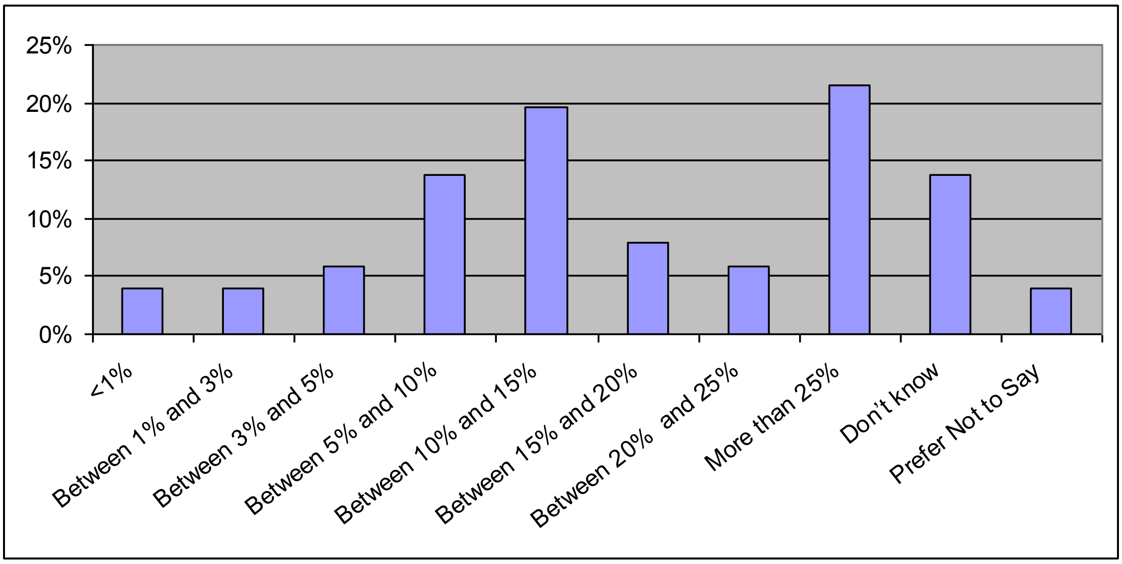

Figure 5.4 Transport Costs as a Percentage of Total Business Costs

5.8.16 The Figure shows that transport costs, as a proportion of total business costs, are mixed but relatively high in the islands. For example, 22% of respondents noted that the transport of goods accounts for over 25% of their total business costs. In addition, over 50% revealed that transport costs accounted for more than 10% of their total business costs. This compares with a figure of around 10% generally quoted for businesses across the country. In addition, transport costs of this magnitude are likely to make businesses relatively more susceptible to increases.

5.8.17 Respondents were asked what proportion of their total transport cost is accounted for by the ferry fare. The results are shown in Figure 5.5 below:

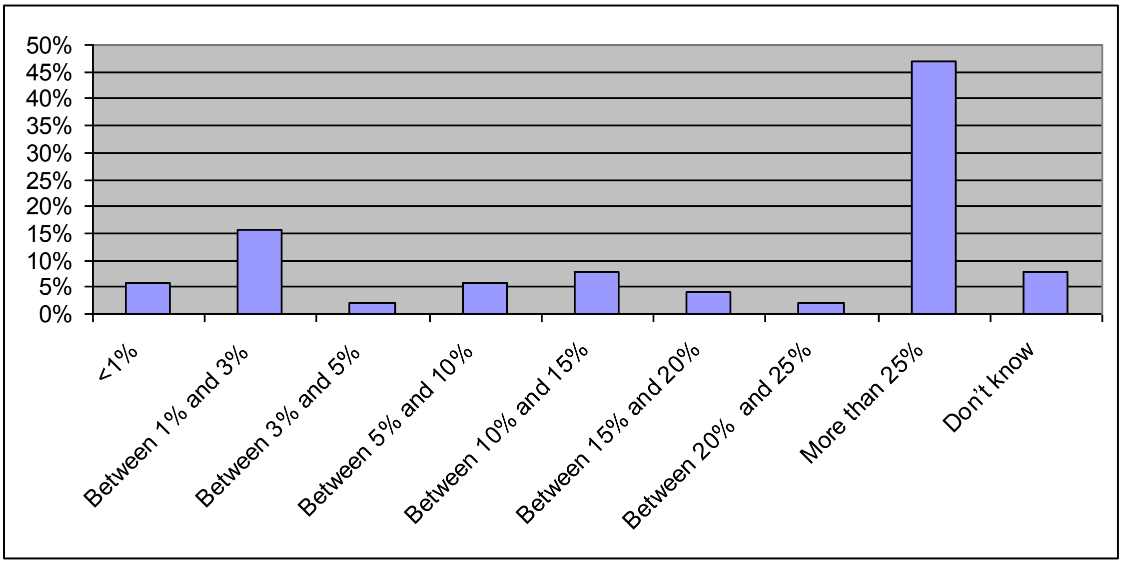

Figure 5.5 Ferry Fare as a Percentage of Total Transport Costs

5.8.18 Figure 5.5 clearly demonstrates the importance of the ferry fare to island businesses. Forty seven percent of businesses noted that the ferry fare accounts for more than 25% of their total transport costs. A business with ferry costs accounting for such a large proportion of its total transport costs is likely to be more sensitive to increases in fares if these are passed on by the haulier.

5.8.19 One important caveat here however is that, during the interviews, the majority of respondents did not have a firm grip on the precise figure for these costs. It is therefore possible that the above figures are an estimate by the businesses concerned.

5.9 Survey Findings – Routed Questions

5.9.1 Of the 49 businesses that filled in the main body of the survey, eight firms chose not to complete the routed sections. Of the 41 respondents who did complete the route questions:

- **31 businesses (78%)** contract a 3rd party haulage or delivery company to move its goods and supplies by ferry between the mainland and the islands.
- **4 businesses (10%)** use its own commercial vehicle (ie greater than 6m in length) to move own goods and supplies only.
- **1 business (3%)** uses its own commercial vehicles (ie greater than 6m in length) to move a combination of own goods and those of others.
- **1 business (3%)** uses its own commercial vehicles (ie greater than 6m in length) to move goods and supplies for others only.
- **2 businesses (5%)** use cars / vans (ie less than 6m in length) to move all its goods and supplies by ferry between the mainland and the islands.
- **1 business (3%)** does not directly use ferries to transport its goods/supplies because it buys/sells everything it needs from/to island-based suppliers/customers or 3rd party organisations which deal with the transport of the goods to/from the mainland.

5.9.2 An important point to emerge from these findings is that the majority of businesses (both from the interviews and the survey) tend to contract a 3rd party haulage or delivery company to move their goods and supplies by ferry between the mainland and the islands. This is simply because the scale of island businesses makes it inefficient for them to own their own vehicles / move their own goods. Even with the RET-related price rises, there appears to be little appetite amongst businesses, at least in the short term, for moving to their own transport. The firms that do use their own vehicles tend to be doing so either because they have specific requirements which the haulage industry can't meet.

5.9.3 Given the relatively low response rate for businesses not using a third party haulier, we do not consider the outcomes of this part of the survey here. We have instead integrated the findings from these sections into the wider analysis of the haulage sector in Chapter 4.

5.10 Businesses using a Third Party Haulage or Delivery Company

5.10.1 This section reviews the findings of the survey for those businesses using a third party contractor.

Impact of the Removal of RET for Commercial Vehicles

5.10.2 Thirty-three businesses responded to the question on whether increases in ferry fares since the removal of RET for CVs in April 2012 had been passed on to their business. Of these respondents, 88% noted that hauliers have passed on the increase in CV fares to their business. Over 68% of businesses expect this increase to be in the region of £1,000 to £5,000 per annum, while one business considers that it will cost them an additional £60,000 per annum.

Ability to Pass on Costs

5.10.3 Respondents were asked if they have passed on the increase in CV fares since April 2012 to their customers. The response here was mixed - 42% of businesses responded that they could not or would not pass on additional haulage costs to their end customers. In contrast however, 27% of businesses noted that they will pass on the full cost to their end customer; 18% said they would pass on a small proportion of the extra cost; while 12% said they would pass on a large proportion of the costs.

5.10.4 In terms of future ferry fare increases, 70% noted that they could not pass on any further increases in haulage costs to their customers. Consequently, 88% of respondents noted that they expect the future viability of their businesses to be affected by the forthcoming rise in CV fares on the ferry[14].

5.10.5 This perhaps reflects the size of the businesses that responded to the survey and the size of businesses in the Western Isles more generally. Small firms are particularly vulnerable to the removal of RET for CVs because they do not have sufficient scale to buy in bulk, set prices or negotiate effectively. They are essentially price takers and would generally expect to find the full cost of the RET related rises passed onto them, either directly from haulage firms or through the wider supply chain.

Control Group

5.10.6 To fully understand and estimate the impact of removing RET fares for commercial vehicles, a series of interviews was proposed with a 'Control Group'. From a methodological point of view, the purpose of a control group is to be able to isolate the impact of an intervention on two statistically

[14] It should be noted that this response was given when businesses anticipated the 2013 fares increase for CVs to be higher than the 10 announced by Scottish Government Ministers in December 2012.

matched groups, with one group the subject of that intervention and the other not. Strictly speaking, the intervention (in this case the removal of RET fares for CVs) should be the only difference between the two groups, meaning that any change in behaviour in the affected group is directly attributed to that intervention. The islands chosen were Arran, Islay and Mull.

5.10.7 While this approach is theoretically sound, its practical implementation proved to be somewhat more difficult. Firstly, the low response rate to the RET business questionnaire ruled out the use of a similar questionnaire with the control group – ie members of the control group had no incentive to fill in such a questionnaire so the response rate would likely have been very low and largely meaningless. In order to address this, a series of detailed telephone interviews was undertaken with the main hauliers serving Arran, Mull and Islay. These interviews considered how and why haulage rates have changed on each of these islands between 2008 and the present, and attempted to draw parallels with companies which had been involved in the RET pilot.

5.10.8 Given the complexity of the industry however and the uniqueness of some of the island economies in question, one must acknowledge that RET is not the only difference between the two groups. Therefore, while some important findings were gathered from the control group, they cannot in themselves be taken as statistically significant evidence of the impact of RET.

5.10.9 The companies who responded to the consultation included:

- Arran Haulage (Arran);
- Iain MacKinnon (Tiree based haulier who also serves Mull);
- Mundell Transport (Islay); and
- TSL Contractors (Mull).

Key Finding

5.10.10 The haulier specific comments are covered in Section 6.3. However, it is important here to focus on the key finding from the control group interviews, as it has the greatest relevance in terms of its comparison to the RET group.

5.10.11 Haulage firms in Coll, Tiree and the Western Isles noted that, while they did not pass on the RET benefits in terms of reduced rates, the fares scheme provided a cushion against other rising costs and thus forestalled a rise in transport charges. Where RET was the only difference between the two groups, one would expect transport charges haulage rates in the control group to rise in line with industry cost pressures.

5.10.12 Our interviews found that this was not the case – rates amongst the control group haulage firms have been largely static throughout the RET period. However, the interviewees noted that these stable rates are a product of greater exposure to mainland competition and a series of local factors. There was a view amongst these hauliers that they would have increased rates if they could have done so within the context of their market.

5.11 Conclusions

5.11.1 A number of clear and consistent themes emerged from the business interviews and survey. In general, the introduction of RET for CVs was seen by a large majority as a highly positive development for island businesses and its subsequent removal has had some negative impacts on many businesses and the wider economy.

5.11.2 At a strategic level, businesses in the Western Isles, Coll and Tiree were almost universally concerned that the lack of certainty and frequent fares policy changes are having adverse effects on business confidence and activity and impacting on long-term investment planning.

5.11.3 Businesses broadly supported the view that hauliers had used RET to help maintain stable prices during a period when other costs were rising rather than pass on RET in the form of lower transport charges.

5.11.4 Businesses noted that the removal of the TRS discount when RET was introduced also made the haulage market much more competitive, thus increasing the downward pressure on haulage rates. This stabilisation and occasional reduction of rates allowed island businesses to compete more readily in mainland markets; against national chain firms within the islands; and with mainland shopping trips and internet shopping.

5.11.5 The removal of RET for commercial vehicles has had a negative impact on businesses that are particularly moving or purchasing a low volume of goods; moving low value goods; or where the company is a price taker in the market. The economies of the Western Isles, Coll and Tiree are represented by a relatively higher share of businesses within industries which display at least one or more of these characteristics, including small scale / independent retail; agriculture; aquaculture and fishing; construction; and low value manufacturing. The removal of RET for CVs is therefore seen to be hitting the most marginal businesses in the community the hardest. There was a general consensus that further increases to non-RET fares for CVs will fundamentally affect the long-term viability of many businesses within the islands.

5.11.6 The removal of RET for CVs in parallel with its retention for cars also serves to worsen the competitive position of a number of independent retail business, who are competing with mainland chain stores; mainland shopping trips; and internet shopping. A number of firms explained that customers are now taking the car to the mainland or ordering high value products online with companies who have low cost or zero delivery charges.

5.11.7 Responses to the business survey reveal that transport costs as a proportion of total business costs account for more than 10% of costs in the majority of companies on the islands. In addition, for just under half of businesses the ferry fare accounts for around 25% of transport costs.

5.11.8 Discussions with a small number of hauliers in the control group revealed that transport charges did not rise in other islands during the period of the RET pilot. However, this was due to various local factors and increased competition from mainland hauliers.

6 Supply Chain Linkages

6.1 Introduction

6.1.1 An important issue raised in the brief for this study was to consider the supply-chain linkages that are particularly dependent on freight movements and trace how higher ferry fares impact on these sectors and the wider island economies. There are thousands of individual supply chain linkages and interactions in the islands involved in the RET pilot and central to understanding the incidence of increased ferry fares is to understand the dynamics of the key island markets. While it is not possible to discuss each of the individual supply chains across the islands, the chapter highlights those supply chains which are likely to be particularly affected by the removal of RET for commercial vehicle ferry fares.

6.2 The Supply Chain

6.2.1 The length of the supply chain for any particular good varies but will typically involve a number of links upstream, downstream or horizontally. Each link within this supply chain will attempt to take the input from upstream, process / convert / improve it (ie add value), and sell it to the next supplier downstream with a profit mark-up (ie a margin). The final outcome of this process is the sale of the good to an end customer, from which the retailer will recover all of the costs within the supply chain as well as an acceptable margin per unit. The key to the success of this complex chain is that the retail price of the individual product covers all of the production costs and allows each supplier within the chain to receive an acceptable margin. Where an increase in costs at any point in this chain erodes the end margin to the point where it would become unviable for one or more parts of that chain to continue supplying its input, there are two potential outcomes:

- the end retailer can negotiate the costs with suppliers or, if the market permits, increase the price of the good to restore the margin per unit; or
- immediate or gradual withdrawal from producing and selling that product.

6.2.2 In terms of the islands in the RET group, the increase in the ferry fare for CVs will impact on every good (finished or otherwise) that is imported to the islands and exported from the islands. That is, every unit moved by a CV on the ferry will have an extra cost element in it equal to its proportional share of the total additional ferry fare.

6.2.3 The key question for this study is to understand the incidence of that extra cost – ie on whom does it fall. If the additional cost rests with Western Isles businesses, for example, it can be argued to some extent that the removal of RET for CVs will have a negative impact on the islands. If, however, the additional cost falls on mainland businesses, then the removal of RET will have a limited, if any, impact on the islands. A key aspect to the analysis is the extent of the market power for individual businesses within the islands' supply chain.

Market Power

6.2.4 In general firms will tend to protect their own interests and the incidence of any cost increase will normally fall upon the weakest player in that market – ie the firm with the least market power. There are various sources of market power which typically stem from:

- barriers to entry – a firm is able to command prices in excess of marginal costs because it has created and / or can maintain barriers to entry;
- business scale – a firm has sufficient scale to command low input prices, volume based discounts and adopt differentiated pricing strategies where it chooses to do so; and
- lack of substitutes – a firm can command high prices for its goods because there is a strong demand for them and few, if any, substitutes.

6.2.5 The previous chapter explained that the Western Isles, Coll and Tiree economies are dominated by firms of small scale and are therefore unlikely to have a significant, if any, degree of market power. They are also likely to be operating in sectors where there are relatively high levels of competition and product substitutes eg agriculture. This suggests that industries will be unable to pass on any higher costs from transport charges onto their customers. This is backed up by the results from the business interviews and survey where 42% of respondents explained that they had been unable to pass on higher transport charges introduced since the withdrawal of RET fares for commercial vehicles and 88% claimed they would not be able to pass on any future cost increases.

6.2.6 This perhaps reflects the size of the businesses that responded to the survey and the size of businesses in the Western Isles more generally. Small firms are particularly vulnerable to the removal of RET for CVs because they do not have sufficient scale to buy in bulk, set prices or negotiate effectively. They are essentially price takers and would generally expect to find the full cost of the RET related rises passed onto them, either directly from haulage firms or through the wider supply chain.

6.2.7 In understanding how such market power comes into play in the Western Isles, it is prudent to split trade flows into exports and imports.

Exports

6.2.8 As explained in Chapter 5, the majority of exported goods from the Western Isles, Coll and Tiree are of relatively low value, homogenous products that in many cases are easily substitutable. Large volume exports are limited to livestock, fish and, to a lesser extent, textiles and food and drink. As these goods are, for the best part, competing in highly competitive markets and are already carrying an additional island cost-burden, there is, as a rule, limited scope for increasing the final market price.

6.2.9 The findings from the research suggest that a possible exception to this rule is perhaps the tweed industry which is experiencing strong demand and relatively high levels of sales. While the ferry fare, and therefore transport charges are, similarly to other sectors, an important element of the industry's cost base, the tweed industry may be better placed to absorb higher transport costs through reducing margins or through higher prices to customers. In addition, many tweed products are being transported all over the world, particularly the far east, and the ferry fare makes up a relatively smaller percentage of total transport and business costs.

6.2.10 Given the majority of products are low value and homogenous, the only option in the short-term is for businesses to reduce costs and hence, without efficiency improvements, the margin per unit for one or more suppliers within the chain. With regards to exports, the evidence suggests that the impact of this tends to vary as follows:

- Firms moving small volumes (eg a single pallet) will likely bear the full increased cost of that pallet from the haulier; and
- Firms moving larger volumes have more negotiating power because of the overall low volume of outbound goods and thus the haulier tends to absorb at least a portion of the additional cost. Indeed, there is likely to be some competition amongst hauliers to transport these goods which could potentially drive down transport charges.

6.2.11 In terms of the two options outlined above, the evidence from the industry profile of the island communities suggests that the vast majority of businesses are relatively small and will therefore fall within the first category. These firms are therefore more likely to be in a situation where they will have to absorb the costs as it is passed on through the supply chain, therefore having a negative effect on island businesses exporting to the mainland.

6.2.12 There are exceptions to the low volume example. For example, there are companies moving high volumes of fish from the Uists to the mainland. However, there is only one operator offering a chilled service to Glasgow ie there is no competition to transport the goods. Therefore, in the short-term at least, these companies still have limited market power when negotiating charges with the haulier ie they have to pay the haulier's going rate if they want to move their product. Moreover, in many cases these companies are unable to pass on the higher costs to their customers because of the high level of competition in the market.

Imports

6.2.13 Imports make up the vast bulk of freight traffic to the islands, with products as diverse as fuel, food, furniture, animal feed, construction materials, and raw materials for manufacturing. Given that the majority of these goods are supplied from mainland firms whose markets will typically be much wider than the islands alone, there will be little room for negotiation on price. Except where contractual agreements prevent it, mainland firms will typically pass the increase in the ferry fare straight on to the island firm or will leave the island firms to negotiate separately with the haulier. There is some scope for moving custom to other suppliers, while trade bodies for independent retailers, such as Nisa, do provide some cover for small firms. However, as a rule, the evidence gathered suggests there is limited scope for negotiating the price of inbound goods, partly because it is delivered by island hauliers.

6.2.14 The inbound haulage market does tend to involve higher volumes than the export market, but again the evidence suggests those volumes are split amongst a large customer base of relatively small firms, providing the hauliers with an element of market power. The findings from the interviews suggests that, in most instances (ie pallet traffic), the haulage firms will pass the increased ferry fare straight on to their end customer. However, the hauliers need to operate a delicate balancing act, in that they must protect their own margins but at the same time not compromise the viability of their customers, a point made by many of the hauliers on the smaller islands.

6.2.15 The only referenced exceptions to this trend are where firms moving large volumes (Tesco for example) have sufficient buying power to set the terms of the contract. In addition, it is important to revisit the point that companies like Tesco and the Co-op employ national or regional pricing models. This means that while prices in these stores may not have gone down when RET was introduced, the model also means that prices were unlikely to have gone up when RET was removed. While this may have impacted on local retailers, it would not have impacted on consumers who use these large retail supermarkets.

Importing and Exporting Firms

6.2.16 A key issue which was raised during the interviews is that a number of marginal businesses could, through the supply chain, end up paying all or a proportion of the increased ferry fares on numerous occasions for a single unit of product. A good example of this is the seafood industry, where businesses have to pay higher fares for directly imported products (eg fish feed); directly exported products (eg fish); and ancillary inputs (ie plastic and packaging). This issue is common across a number of sectors, including agriculture, manufacturing and textiles. Where the incidence of these costs all rest with the end supplier, and that supplier cannot easily pass on these costs to the end customer (seafood again being a good example), that business' margin per unit is reduced, potentially to the point where cost exceeds price and the product or business is no longer viable. While discussing specific examples is difficult due to the commercial nature of the information, examples were given in the business interviews of companies making a decision to enter a market after the introduction of RET and then withdrawing after its removal as the increase in costs due to higher fares could not be passed on and made the new venture unviable.

6.3 Impact on Sectors

Agriculture / Crofting

6.3.1 Chapter 5 explained that the primary sector is a key sector in the Western Isles accounting for 23% of registered businesses, 12% of employment and 22% of turnover. Within the sector, the area of agriculture and crofting plays a significant part. The interviews with businesses confirmed the importance of the sector. The interviews also confirmed the key role that individual farms can play in driving the local communities, such as being the main employer. It has also been explained however, that many of the firms bear those characteristics which can make them very vulnerable to increases in transport charges eg they are operating in competitive markets, transporting low value goods, and have little market power. This suggests they are price takers and have little opportunity to negotiate the level of transport charges or pass on them on in terms of higher prices.

6.3.2 The evidence gathered showed that a number of firms in this sector have seen an increase in transport charges since the removal of RET in April 2012. The evidence also suggests that firms have been unable to pass these costs on and will be unable to pass on further rises. Due the scale of the industry, as a proportion of the Western Isles, Coll and Tiree as a whole, the impacts on this sector may have important repercussions across the islands. A number of firms and geographical areas are highly dependent on the successful performance of this sector, in terms, for example, of employers / income providers and purchases of local products.

Fishing, Aquaculture and Seafood

6.3.3 The fishing, aquaculture and seafood sectors also play an important role in the local economies. It was explained during the interviews with businesses that the recent fare increases are an important issue for firms as they operate in very competitive markets and can't pass on higher transport charges. Indeed, a number of the companies have seen increased competition from a number of businesses withdrawing from the struggling European market. This is creating issues of short-term over-supply and is driving down prices at a point when costs are going up. It was claimed that further cost increases due to the removal of RET could impact on employment in the sector.

6.3.4 It was also explained by companies in this sector that the ability to pass on cost increases to customers is highly seasonal. The buoyant market between July and September provides some scope for passing on cost increases. Christmas, Easter and festival days / holidays in Spain also allow some price flexibility. However, out with these peak periods, there is little scope for passing on increases in haulage costs.

6.3.5 The companies interviewed had noticed an increase in the price of inbound goods, particularly bait. The cost of a pallet of bait increased from approximately £56 to £59 between July 2011 and August 2012. This is seen to be clearly related to the removal of RET because fuel surcharges are listed separately.

6.3.6 Most of the firms in the sector are transporting goods to the mainland on a regular weekly basis. An increase in transport charges will have a marked impact on the cost base of many of the firms. Businesses explained that this will directly impact on profitability as it is not possible to pass on the costs – many goods eg a number of fish and scallop prices have been declining in real terms for a number of years.

6.3.7 A downward spiral in the island economies could also put pressure on the supply chain for staple products. The analysis above explained the fragility of many island businesses and it can be argued that even where a business is performing well, the failure of one or more of its island based suppliers could undermine that business. From discussions with hauliers and businesses, a god example of this could be the seafood industry, which procures much of its packaging locally. Therefore, the failure of a local packaging supplier, due to higher import prices as a consequence of RET, could disrupt the supply chain and introduce a new cost of importing such products from the mainland.

Construction

6.3.8 An issue that was raised in the discussions with businesses was the importance of the construction industry, not just in its own right, but also how it supports many businesses and jobs in numerous ancillary industries. It was claimed that there has been a notable reduction in the turnover of construction firms since the removal of RET. There is some evidence that prospective builders moved purchases forward to "beat the RET deadline". However, the turnover of construction businesses overall is down and there was little evidence to suggest this would change in the near future.

6.3.9 The ferry fare, if passed on in transport charges, has an important impact on the performance of firms involved in the construction industry. A number of materials are imported from the mainland and are generally bulky goods. An increase in transport charges can therefore feed through to significant increases in construction raw materials, which then feed through to impacts on residential and commercial property building as well as other infrastructure. This can result in a downturn in activity in the construction indutry, as well as many other dependent sectors. For example, one stakeholder on Coll noted that the price of a full load will increase by £400 and it typically takes 20 loads to build an average house. The £8,000 increase in cost will either by absorbed by the contractor (depending on when the contract was signed ie before or after the price increase) or the client. This would again likely represent a net loss of wealth from the islands. This is a particularly pertinent point in the construction sector, where, in the current mortgage market, an additional £8,000 of costs could easily prevent the construction of a property going ahead. When one considers these impacts across the entire construction sector (both commercial and residential) and ancillary industries, this could have a relatively large negative impact on the overall sector performance.

Retail

6.3.10 The previous chapter set out figures showing the importance of the retail sector. While the wholesale, retail trade and repair of motor vehicles and motorcycles sector as a whole makes up 16% of registered businesses, 22% of employment and 33% of turnover, the retail sector alone makes up an important share of this.

6.3.11 It is clear that the impact on the retail sector is not uniform across geographic areas and type of goods being sold. It is also clear that the retail sector is being affected by a number of different factors at the same time eg the slowdown in economic activity, higher fuel prices, increased competition from internet shopping, lower RET fares for passengers and vehicles meaning that trips to the mainland that take in shopping are more affordable etc. The latter in particular is having an impact on the sale of 'big ticket' items.

6.3.12 It is also clear that many of the larger stores, such as the co-op and Tesco, operate a regional pricing structure where costs are absorbed within a central overhead. This means that cost increases specific to a particular area have less impact on prices in that particular area.

6.3.13 Despite the limited impact on the larger stores, the vast majority of stores in the Western Isles, Coll and Tiree are not in this category and it is clear from speaking to a number of retail businesses that the withdrawal of RET for CV fares, if passed on through higher transport charges, will have an adverse impact on this particular sector. Indeed, many of the small retailers have already seen an increase in transport charges since RET was removed for CV ferry fares. Many of these shops are operating at very small margins which cannot absorb higher charges, and the higher costs will therefore have to be passed on to customers in terms of higher prices. These higher prices will ultimately feed through to lower demand (as people stop purchasing certain goods or switch to the larger supermarkets) and / or reduced levels of disposable incomes in the local communities as people's outlays increase.

6.3.14 A key point of note here is the disproportionate impact of the fare increases on the unit price of large / bulk goods. The majority of pallets tend to contain tens or indeed hundreds of units on a single pallet, meaning that an increase in the pallet price tends to have a very small impact on the unit cost of each item.

6.3.15 In contrast, however, retailers of large and often low margin goods will feel a disproportionate impact of the RET related price increases. Furniture is a good example of this but there are many other examples including fish feed, fertiliser etc, where the end purchaser will bear the full cost of the increase. This will have direct impacts on these sectors as well as knock-on impacts up and down the supply-chain. For example, the increased cost of agricultural materials will increase the cost for farmers of rearing livestock. With little flexibility on price, this will reduce the farmer's margin per animal which in turn is a net financial loss to the local community in which the business is located.

6.3.16 There is evidence from Comhairle nan Eilean Siar that the number of houses being built or seeking planning consent has declined significantly in recent months. It is difficult to isolate the impact due to RET. This situation is common to housing markets and construction activity across Scotland, and it may be too early to attribute to the removal of RET in April 2012, but the evidence from the business interviews and online survey suggests that the increase in fares for commercial vehicles will further dampen construction activity in the islands.

6.4 Conclusions

6.4.1 Many of the businesses across the islands involved in the RET pilot are transporting low volume, low value, and in many cases, homogenous products in very competitive markets. Indeed, even those businesses exporting a number of high volume goods are still operating in very competitive industries. This can make the opportunity to pass on higher costs, in terms of transport charges, to their customers very difficult. This was very much borne out by the responses to the business surveys.

6.4.2 The economies of the Western Isles, Coll and Tiree are dominated by businesses with these types of characteristics eg agriculture / crofting, fishing / aquaculture, retail and construction. The evidence has shown the dominance of firms in the primary sector on the Western Isles economy, in terms of number of businesses, turnover and employment. In addition, the vast majority of these businesses are small, typically with less than five employees. Consequently, they are unable to pass on higher transport charges to their customers. The evidence from the business surveys confirms this, with the vast majority explaining that costs cannot be passed on. This means they will have to absorb these within their current margins or reduce their operations.

6.4.3 In many cases, firms are being affected more than once, through importing inputs and exporting finished goods. A number of the companies in this situation are of relatively small scale and therefore have limited power and therefore opportunity to pass on to their customers through the supply chain.

7 Geographic Impacts

7.1 Introduction

7.1.1 The purpose of this chapter is to report on the geographic impact of the removal of RET for CVs. The initial findings from the research suggest that, due to the types of businesses and their characteristics, the removal of RET for commercial vehicles has had, or will have, a negative impact across all of the islands in the RET pilot group. However, the evidence collected through the consultation process suggests that these impacts will be greater in some islands than others. This section explores this issue in more detail and sets out which areas could witness the greatest impacts and why.

7.1.2 It is important to note here that the economies of the islands included within the RET pilot, and the focus of this study, are, similarly to all areas of the country, being affected by the general slowdown in activity caused by the current economic climate. As explained in earlier chapters, it is difficult to isolate precisely these impacts from the removal of RET for CV ferry fares. This also applies to the geographical incidence, where local impacts may be as much due to remoteness or the limited scale of industry as they are to higher CV fares. Nevertheless, the evidence from the interviews and surveys suggest that the removal of RET may exacerbate the effects.

7.1.3 It should also be noted that, given the limited data, it is not possible to quantify precisely the impacts of removing RET in each of the geographies / island communities. However, wherever possible, evidence from the surveys and official sources are used to assess the fragility / vulnerability of the different areas.

7.2 Socio-economic Context of the Western Isles

7.2.1 This section provides a brief outline of the recent socio-economic context of the islands, taking account of issues such as the recent trend in population, the level of unemployment (as measured through the percentage of Job Seeker's Allowance claimants), gross weekly pay and the number of businesses. In addition, because it is felt that any increase in transport charges may have a disproportionate impact on businesses in the primary sector, the importance of this sector, in terms of the number of firms, is also considered.

Population

7.2.2 Table 7.1 below shows that between 1981 and 2011 the total resident population of the Western Isles declined from 31,500 (actual) to 26,100 (estimated), a fall of over 17%. There was a relatively steep decline between 1981 and 2001, with the total population falling by just under 16%. While the population has continued to fall after 2001, it has been less rapid and appears to have almost stabilised in the last few years.

Table 7.1 Western Isles Population 1981 to 2001

Year	1981	1991	2001	2006	2007	2008	2009	2010	2011
Population	31,500	29,300	26,500	26,400	26,300	26,200	26,200	26,200	26,100

Job Seekers Allowance Claimants

7.2.3 The level of unemployment in the Western Isles, as measured by those claiming Job Seeker's Allowance (JSA), is set out in Table 7.2. The table shows that the percentage of the workforce claiming JSA declined in 2007 and 2008 before rising to a peak in 2009. Since 2009 it has been relatively stable at around 3.2 to 3.3 per cent. Nevertheless, the most recent figures are higher than that experienced between 2006 and 2008.

7.2.4 In comparison with Scotland, the JSA figure for the Western Isles was above the national figure in 2006 and 2007. However, since 2008, the figure for the Western Isles has consistently been below that of Scotland.

Table 7.2 JSA as % of Workforce 2006 to 2012

Year	2006	2007	2008	2009	2010	2011	2012
WI JSA Claimants	3.1	2.7	2.2	3.5	3.3	3.2	3.2
Scotland JSA Claimants	2.7	2.3	2.4	3.8	4.0	4.1	4.1

Gross Weekly Pay

7.2.5 Table 7.3 below sets out a time series of gross weekly pay for the Western Isles and Scotland between 2002 and 2012. The table shows that gross weekly pay peaked in the Western Isles in 2009 at £493.1 before falling to £438.3 in 2012, a decline of 11% (in nominal terms) in three years.

7.2.6 The table also shows that while gross weekly earnings in the Western Isles were above the Scottish average in 2002 by 3.7%, earnings in Scotland as a whole have increased steadily in each year to £498.3 and are now 13.7% higher than those for the Western Isles.

Table 7.3 Gross Weekly Pay 2003 to 2012 (£)

Year	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012
Western Isles	383.0	355.4	361.5	380.1	402.1	416.5	463.7	493.1	460.0	436.1	438.3
Scotland	369.3	381.8	390.6	409.8	427.9	440.9	462.9	471.2	486.6	487.2	498.3

7.2.7 Chapter 5 discussed the vulnerability of businesses in the agriculture and fishing sector to changes in commercial vehicle fares if these were passed on in higher transport charges. This was because these types of firms in the Western Isles tend to be operating in competitive markets, are price takers, they are transporting low volumes of goods of relatively low value, and have little market power and therefore ability to pass on higher charges to their customers. Chapter 5 also set out details of the importance of the primary sector to the Western Isles economy, in terms of turnover, employment and number of registered businesses. While these figures are not repeated here, it was shown that the Western Isles has an above average percentage of enterprises operating in the agriculture, forestry and fishing sector, with a figure of 23%. This compares with a figure of 11% for Scotland as a whole. It was also shown that the vast majority of businesses in the primary sector are small with less than five employees.

Scottish Index of Multiple Deprivation

7.2.8 In looking at those areas most vulnerable to changes in fares feeding through to an impact on economic activity, it is also useful to consider the current levels of deprivation across the islands. The Scottish Government's Scottish Index of Multiple Deprivation (SIMD) ranks deprivation by area using a combination of indicators, including income, employment, health, education, skills and training, housing, geographic access and crime. The results for the Western Isles Coll and Tiree are set out in Figure 7.1, where the figures represent the ranking of most deprived ie one would be the most deprived area in Scotland and 6,505 the least deprived area.

7.2.9 Figure 7.1 shows that many parts of the Western Isles are considered to be within the most deprived in Scotland. The most deprived areas are located in Lewis, Harris and South Uist. However, the figure also shows that even the least deprived areas of the Western Isles, Coll and Tiree are still in the 50% most deprived areas of Scotland.

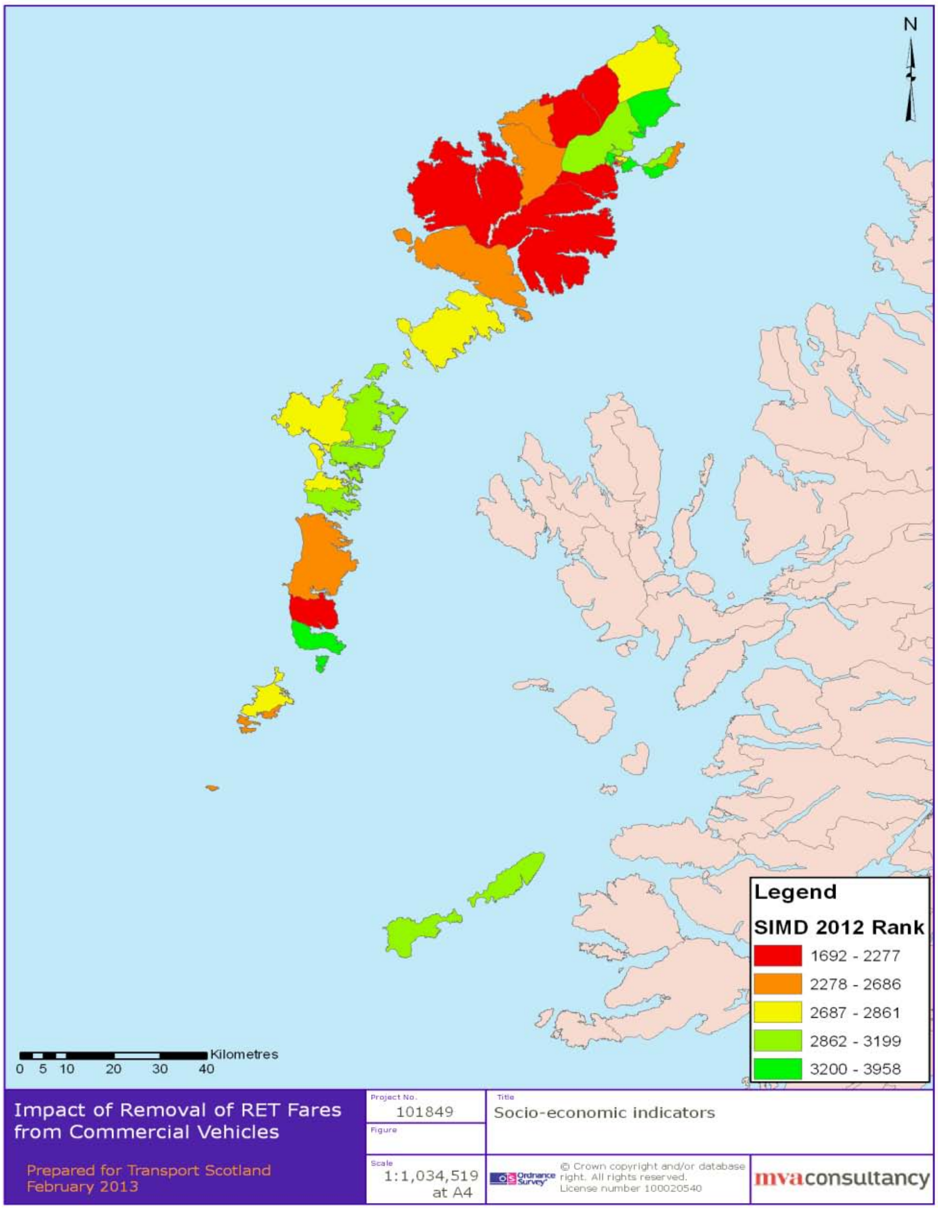

Figure 7.1 Deprivation in Western Isles, Coll and Tiree

Summary

7.2.10 This section has provided a brief socio-economic context of the Western Isles. It has shown that it has experienced a significant decline in population over the past 30 years. It has also witnessed a relative decline in gross weekly earnings compared to Scotland as a whole, particularly in the last three years. While unemployment, measured in terms of those claiming JSA, is below that of Scotland as a whole, the figure in recent years has increased. Finally, it is clear from earlier chapters that the Western Isles economy is highly dependent on those businesses in the primary sector, in terms of number of businesses, employment and turnover. It is also clear from the business survey and interviews that these companies are the most vulnerable to increases in ferry fares if they are passed on in terms of higher transport charges.

7.3 Socio economic data by island group

Lewis / Harris

Population[15]

Table 7.4 Population of Lewis and Harris (1971 to 2001)

Year	1971	1981	1991	2001	change 1971 - 2001
Lewis	20,326	20,720	20,159	18,489	-9%
Harris and Scalpay	2,879	2,489	2,222	1,984	-31%

7.3.1 Between 1971 and 2001, the island of Lewis saw its population decline by 9%. Indeed, between 1991 and 2001 alone it experienced a fall of 8.3%. Over the same 1971 to 2001 period, Harris (including Scalpay) saw a decline in its population of over 30%, from 2,879 to 1,984.

7.3.2 The latest population estimates reveal that while there may have been a slight increase in the total population of Lewis and Harris up to 2007, the 2011 figure is still very similar to that for 2001. Overall, therefore, it is clear that the area of Lewis and Harris has seen a long-term decline in population which could have an adverse impact on the sustainability of the community if it is to continue.

JSA Claimants

7.3.3 Table 7.5 below shows that the percentage of JSA claimants in Lewis and Harris peaked in 2009 at 4.0%. It then declined in 2010 and 2011 before rising again in 2012 to 3.8%. The table also shows that after 2007 the figure in Lewis and Harris has been above that for the Western Isles as a whole.

[15] In analysing the trends in population, Census data showing actual population levels has been used for comparisons between 1971 and 2001. For more recent comparisons ie post 2001, mid-year estimates are used.

Table 7.5 JSA as % of Workforce 2006 to 2012, Lewis and Harris

Year	2006	2007	2008	2009	2010	2011	2012
Lewis / Harris JSA Claimants	3.0	2.5	2.4	4.0	3.5	3.4	3.8
WI JSA Claimants	3.1	2.7	2.2	3.5	3.3	3.2	3.2

7.3.4 In terms of the trend in the number of businesses, Table 7.6 shows that, there have been ongoing fluctuations in the total number of businesses[16] in Lewis and Harris. While it experienced a decline of almost 5.5% between 2008 and 2011, it also witnessed an increase of 3.5% between 2011 and 2012. The figure in 2012 is 2.2% lower than in 2008.

Table 7.6 Total Number of Businesses in Lewis and Harris

Year	2008	2009	2010	2011	2012
Total number of businesses	920	920	900	870	900
Annual Change		0%	-2.2%	-3.3%	3.4%

7.3.5 The latest data shows that the number of businesses in the primary sector in Lewis and Harris has witnessed an ongoing decline in recent years. Table 7.7 below shows that the figure has fallen from 150 in 2008 to 125 in 2012, a decline of 17%. The Table also shows that there has been a steady year-on-year decline with the number of businesses in the sector falling in each of the four years up to 2012.

7.3.6 The latest figures also contrast with the number of business as a whole. For example, while the number of total businesses in Lewis and Harris increased in 2012, the number of businesses in the primary sector continued to decline. Given the importance of this sector across the islands, and the adverse impact that an increase in transport charges could have on businesses in the sector, the withdrawal of RET fares for CVs could have an important impact on the local economy.

Table 7.7 Businesses in Lewis and Harris in the Primary Sector

Year	2008	2009	2010	2011	2012
Number of Businesses	150	140	135	130	125
Annual Change		-7%	-4%	-4%	-4%

7.3.7 While the Western Isles as a whole has 23% of its registered businesses in the primary sector, in recent years the proportion of businesses in this sector in Lewis and Harris has been lower, at just over 15%. The figures for 2008 to 2012 are set out in Table 7.8 below.

Table 7.8 Percentage of Total Businesses in Lewis and Harris in the Primary Sector

Year	2008	2009	2010	2011	2012
Number of Businesses	16%	15%	15%	15%	14%

[16] It should be noted that the total number of businesses, and the number of businesses in the primary sector, outlined throughout this chapter are rounded to the nearest 5. While this can make it difficult to be precise about the year on year changes when dealing with relatively small numbers, it still provides a useful indication of the size and importance of the sector across the islands.

7.3.8 While all areas of the Western Isles, Coll and Tiree will be affected by the increase in ferry fares due to the nature of industry across the islands eg high concentration of primary industries, Lewis, in theory, is likely to be the island afforded the greatest protection by its sectoral mix. Areas with industries less likely to be affected directly by an increase in CV fares will be more able to support overall activity and help absorb the impacts. An example of a sector which is likely to be less directly affected by the introduction of RET is the services sector and public administration. Businesses within these sectors are much more concentrated in Lewis, and in Stornoway in particular, compared to other areas of the Western Isles.

Haulage Market Impacts

7.3.9 Lewis and Harris also support a relatively large scale haulage industry, with a higher number and concentration of operators, including large multi-purpose firms like D R MacLeod and MacRitchie's Highland Distribution. The size of this haulage market and scale of industry creates competition and economies of scale and helps keep haulage costs down. The level of competition between hauliers also makes it relatively harder to simply pass on any RET related price rises. For example, evidence from the interviews suggests that the entry of MacRitchie's into the island haulage market has assisted in keeping rates down. While this will have an impact on haulier margins, it also provides some protection for businesses in the area more generally.

MV Muirneag

7.3.10 Businesses in Lewis and Harris are protected, to some extent, against the price rises by the presence of the MV *Muirneag*. Users of the overnight freight sailing offered by the MV *Muirneag* benefit from a 10% discount on the fare charged for using the MV *Isle of Lewis*, while the ability to drop trailers reduces both vehicle length charges and the need to send a driver with the vehicle. This is a significant overall cost reduction for using the Stornoway – Ullapool route and one which is not available to the other islands in the RET group.

The Uists, Benbecula and Barra

7.3.11 This section sets out socio-economic data for the Uists, Benbecula and Barra. Where possible the data has been disaggregated. However, it has not been possible to do this for all indicators and, in some cases, the data is presented at different island levels.

Population

7.3.12 Between 1971 and 2001 the total population of the Uists and Benbecula declined by 13%. Between 1981 and 2001 alone the figure was 21%. The figures are set out in Table 7.9 below. The latest mid-year estimates suggest that the rate of decline has dropped. Nevertheless, there is clear evidence of a continued gradual decline in population levels in the area with the figure for 2011 showing a decline of 5% on the 2001 figure.

Table 7.9 Population of Uists and Benbecula (1971 to 2001)

Year	1971	1981	1991	2001	change 1971 - 2001
Uists and Benbecula17	5,598	6,122	5,903	4,857	-13%

[17] The figures for Usits and Benbecula include Eriskay

7.3.13 Table 7.10 below shows that between 1971 and 2001 the population of Barra increased from 1,088 to 1,172, an increase of 8%. The table also shows however that the population increased by 21% between 1971 and 1991, before falling by 11% in the ten years to 2001. Since 2001, the mid-year estimates reveal that the population level has remained fairly stable with small fluctuations over the period and the 2011 level is almost equivalent to what it was 10 years earlier.

Table 7.10 Population of Barra (1971 to 2001)

Year	1971	1981	1991	2001	change 1971 - 2001
Barra	1,088	1,371	1,316	1,172	+8%

JSA Claimants

7.3.14 Table 7.11 below shows that the percentage of JSA claimants in North Uist and Benbecula has declined between 2006 and 2012, from 4.5 to 3.2. In contrast, the figures also show that the percentage of JSA claimants for South Uist and Barra increased between 2006 and 2012, from 2.7% to 2.9%. The figure has increased significantly from the low of 2007 when it was 2.0%.

7.3.15 Table 7.11 also shows that while the percentage of jobs seekers in North Uist and Benbecula has been equivalent to or higher than the figure for the Western Isles as a whole, the figure for South Uist and Barra has consistently been below the figure for the Western Isles. In terms of this unemployment indicator it is clear that the area of South Uist and Barra has performed better than North Uist and Benbecula.

Table 7.11 JSA as % of Workforce 2006 to 2012, Uists, Benbecula and Barra

Year	2006	2007	2008	2009	2010	2011	2012
North Uist and Benbecula	4.5	3.6	3.7	3.9	3.3	3.7	3.2
South Uist and Barra	2.7	2.1	2.0	2.9	3.0	2.8	2.9
WI JSA Claimants	3.1	2.7	2.2	3.5	3.3	3.2	3.2

7.3.16 Table 7.12 below shows the total number of businesses registered in North Uist and Benbecula. The figures show that over the period 2008 to 2012 the total fell from 115 to 110, a decline of 4.3%. However, the most recent figure does show an improvement in 2012, where the figure of 110 was an increase of 4.8% on the number in 2011.

Table 7.12 Total Number of Businesses in North Uist and Benbecula 2008 to 2012

Year	2008	2009	2010	2011	2012
Total number of businesses	115	110	110	105	110
Annual Change		-4.3%	0	-4.5%	4.8%

7.3.17 Table 7.13 shows the number of businesses in North Uist and Benbecula in the primary sector. The figures show that between 2008 and 2012 the number fell by 12.5%. This included large declines in 2009 and 2011, but also included a rise of 16.7% in 2012. It is noticeable that the increases and declines recorded in the primary sector match the change in numbers in the total number of businesses in the area.

Table 7.13 Businesses in North Uist and Benbecula in the Primary Sector

Year	2008	2009	2010	2011	2012
Number of Businesses	40	35	35	30	35
Annual Change		-12.5%	0	-14.3%	16.7%

7.3.18 Taking the two tables together, it is clear that there is a significant dependence on the primary sector. Table 7.14 below shows the share of total businesses in North Uist and Benbecula that are located in the primary sector. While the numbers show small annual fluctuations over the period, it is very clear that North Uist and Benbecula has a very high dependence on businesses categorised within the primary sector, with around a third of the total in each year.

Table 7.14 Percentage of Total Businesses in North Uist and Benbecula in the Primary Sector

Year	2008	2009	2010	2011	2012
Number of Businesses	35%	32%	32%	29%	32%

7.3.19 Table 7.15 shows the total number of businesses registered in South Uist and Barra. The figure shows that over the period 2008 to 2012 the number increased from 205 to 210, a rise of 2.4%. Indeed, in 2012 the figure of 210 was an increase of 5% on the figure in 2011.

Table 7.15 Total Number of Businesses in South Uist and Barra 2008 to 2012

Year	2008	2009	2010	2011	2012
Total number of businesses	205	205	210	200	210
Annual Change		0%	2.4%	-4.8%	5.0%

7.3.20 Table 7.16 shows the number of businesses in South Uist and Barra in the primary sector. The table reveals that the direction of the annual fluctuations in the number of businesses in the primary sector mirrored that for businesses as a whole, although the magnitude of the percentage change was much greater in the primary sector. The figures show that over the 2008 to 2012 period the number increased by 14%. The table also shows that the figure increased by 14% alone in 2012.

Table 7.16 Businesses in South Uist and Barra in the Primary Sector

Year	2008	2009	2010	2011	2012
Number of Businesses	70	70	75	70	80
Annual decline		0%	7%	-7%	14%

7.3.21 Taking the number of businesses in the previous two tables reveals that, even more than North Uist and Benbecula, the combined areas of South Uist and Barra also have a high dependency on the primary sector. Table 7.17 below shows that the number of businesses in South Uist and Barra in the primary sector, as a proportion of all businesses in the area, was 34% in 2008, rising to 38% in 2012.

Table 7.17 Percentage of Total Businesses in South Uist and Barra in the Primary Sector

Year	2008	2009	2010	2011	2012
Number of Businesses	34%	34%	36%	35%	38%

Haulage Market

7.3.22 While the haulage market in Lewis and Harris can benefit a number of companies in that area, it can have the opposite effect in some of the southern islands such as North Uist and Benbecula. The concentration of the haulage industry in Lewis means that the majority of goods are 'hubbed' through Stornoway. While goods being transported to Barra arrive direct in Castlebay from Oban, many of the goods to the other islands come via Stornoway and businesses are therefore already paying for the cost of moving traffic inter-island and, due to the nature and characteristics of businesses located in these areas, will likely have a greater proportion of the RET related cost increases passed on to them.

7.3.23 In terms of Barra, it was explained in Chapter 4 that there was problems due to the area having a relatively small market, in terms of number of businesses, an extended sailing time, low service frequency and the inability to use drop trailers, this created inefficiencies in the haulage sector and leads to higher than average costs. It has been explained, for example, that Barratlantic drivers are paid proportionally more to sit on the ferry than to drive and this structural inefficiency has to be built into the overall business cost base and margin.

7.3.24 There is evidence from the business surveys to suggest that rates have already increased since RET for CVs was removed, and the responses from the business interviews suggest that the remote communities will find it more difficult to deal with the impacts of these rises. A number of stakeholders explained that this is a direct result of the small traffic volumes moving to and from these islands. The lack of scale for many hauliers means that costs are already high and thus the pass on of increases related to the withdrawal of RET has been, and indeed will be, significant for many of the low margin, price competitive businesses in these areas.

Coll / Tiree

Population

7.3.25 Table 7.18 sets out the long-term trend in the populations of Coll and Tiree. While the population of Coll increased by 14% (144 to 164) between 1971 and 2001, it declined by 5% in the 10 years to 2001. In Tiree, the population declined by 12% (875 to 774) between 1971 and 2001 but remained fairly stable in the decade to 2001.

7.3.26 The most recent mid-year estimates suggest that while the combined population of the two islands has fluctuated in the years following 2001 up to 2011, the estimated figure for 2011 is 1,050, an increase of 12% over the figure for 2001.

Table 7.18 Population of Coll and Tiree (1971 to 2001)

Year	1971	1981	1991	2001	change 1971 - 2001
Coll	144	131	172	164	+14%
Tiree	875	760	768	770	-12%

JSA Claimants

7.3.27 Table 7.19 shows that the percentage of JSA claimants in Coll and Tiree has been steadily increasing since 2007, from 2.4% to 5.6%. This compares with a more gradual rise in Argyll & Bute as a whole. The figures in Coll and Tiree are also higher than the island areas in the Western Isles discussed above.

Table 7.19 JSA as % of Workforce 2006 to 2012, Coll and Tiree

Year	2006	2007	2008	2009	2010	2011	2012
JSA Claimants Coll and Tiree	2.7	2.4	2.5	4.6	5.1	5.1	5.6
Argyll & Bute JSA Claimants	2.5	2.2	2.1	3.0	3.2	3.4	3.4

7.3.28 Table 7.20 shows that between 2008 and 2012 the total number of businesses in Coll and Tiree increased by 20, or 29%. The majority of the increase occurred in 2010 alone where the number of businesses increased by 15, or over 21%.

Table 7.20 Total Number of Businesses in Coll and Tiree

Year	2008	2009	2010	2011	2012
Total number of businesses	70	70	85	90	90
Annual Change		0%	21.4%	5.9%	0%

7.3.29 The latest data shows that the number of Coll and Tiree businesses in the primary sector has remained fairly steady over the 2008 to 2012 period. The figure, as shown in Table 7.21, increased from 15 in 2008 to 20 in 2012, a rise of 33%. It was noticeable however that all of the increase in the number of businesses occurred in 2010. This trend in activity is similar to that for the number of businesses as a whole.

Table 7.21 Businesses in Coll and Tiree in the Primary Sector

Year	2008	2009	2010	2011	2012
Number of Businesses	15	15	20	20	20
Annual Change		0%	33.3%	0%	0%

Table 7.22 Percentage of Total Businesses in Coll and Tiree in the Primary Sector

Year	2008	2009	2010	2011	2012
Number of Businesses	21%	21%	24%	22%	22%

7.3.30 Table 7.22 shows that the islands of Coll and Tiree also have a relatively large share of total businesses operating in the primary sector, with each of the last five years showing a figure above 20%.

7.3.31 The islands of Coll / Tiree saw the fare for a 17m vehicle rise by £99, the highest absolute increase across the RET pilot routes. Although this was the highest absolute increase, the percentage increase of 46% was lower than Ullapool – Stornoway or Uig – Tarbert / Lochmaddy. During the business interviews there was much concern expressed about this increase being passed on to businesses and the impact this would have on the islands. On Coll for example, islanders were highly vociferous about the impact of the removal of RET for CV fares on the cost of living. The majority of food deliveries to Coll is brought in on vans under the commercial vehicle threshold and there has not been a particularly notable difference in the cost of food since April. However, there has been a marked increase in the price of fuel, heating oil and coal, all of which are essential products on the island and brought in on commercial vehicles.

7.3.32 It was explained that loivestock movements work somewhat differently in Tiree compared to many other Scottish islands. The island has a reputation for producing good quality livestock which is sold at five annual auctions run by the Stirling based firm, United Auctions. The auctions are held in August (mainly for lambs); September (sheep); October / November (biggest cattle sale); February (2^{nd} biggest cattle auction) and May (cattle).

7.3.33 While Tiree livestock fetch a good price at the auction, there is anecdotal evidence to suggest that the small price premium is now being lost because the buyers face increased expense in getting the livestock to the mainland. It was suggested that the premium for Tiree cattle is now almost insufficient to cover the costs and there were concerns about the long-term future of the industry if the mainland-island differential continues to rise.

7.3.34 Farmers, for example, import hay at least once a year; concentrated feed 2-3 times per year; and other smaller items like fencing, herbicide and bale wrap. All of these goods are brought to Tiree on articulated lorries and an increase in price as a result of higher fares would have a significant adverse impact on the businesses. Some farmers purchased large volumes of goods in advance in anticipation of higher transport charges. While this insulated them against the price rises to some extent, many are worried about the impending price rises for their next purchases. Those interviewed expect that the increase in the ferry fare will be passed on in full to their businesses.

7.3.35 It was claimed that fuel in Coll is the second most expensive in Europe even though it is sold from a not for profit community filling station. Given that fuel is a highly price inelastic good, the extra cost incurred as a result of the RET decision is simply passed straight to the end customer (ie the islander). The cost of this is estimated at 1.5p-2p a litre.

7.3.36 The costs for coal and heating oil are also passed straight on to the customer. The owner of the village shop on Coll explained that the price of a bag of coal has risen from around £9 to £9.75 since April, an increase of over 8%.

7.3.37 It was also claimed that there were particular issues for Coll and Tiree because these islands only have one low frequency route. For example, during the winter timetable, Coll and Tiree only have sailings on a Tuesday, Thursday, Saturday and Sunday. With such a timetable, it was suggested that these islands (Coll in particular) are already high cost locations to serve because they necessitate tying up a lorry and driver on either the mainland or island for an extended period, with a subsequent loss of earnings. The removal of RET for CVs is an additional cost that could make the economics of serving these islands increasingly marginal, with the risks to fuel supplies perhaps being the most significant threat.

7.3.38 There was also concern that the increase in transport charges could feed through to an adverse environmental impact. For example, as Coll is a small island, there are relatively limited means of disposing of waste, a particular issue given that the agriculture industry can generate high quantities of waste products. The chair of the local recycling group has been working closely with farmers to recycle items such as bale wrap. The group has helped raise money to bring in a lorry from Solway Recycling, which removes bale wrap and other waste products and takes it to Carlisle to be recycled. The recycling lorry tends to come across twice per year but the removal of RET will make this an increasingly expensive process to maintain as Solway Recycling pass any additional costs on in full.

7.3.39 If farmers and the recycling group cannot or do not meet this higher cost, the bale wrap and other products will have to be burned. There is also a greater likelihood of such products ending in the waters surrounding Coll. Plastic-based products are highly dangerous for marine life, which often mistake them for food.

7.3.40 The Chair of the local recycling group also coordinates the 'car takeback' scheme whereby MacKinnon of Tiree move scrap cars to a scrapyard in Glasgow for recycling. The economic viability of this scheme is under question following the removal of RET for CVs.

7.4 General Regional Impacts

7.4.1 It was explained in Chapter 4 that many firms outside Lewis and Harris are paying excessive haulage costs due to a higher market rate. A number of factors impact on the market rate, including the level of competition in the haulage sector, the 10% discount on the Ullapool – Stornoway overnight service, the ability to drop trailers, the frequency of ferry services, the scale of goods being transported. The southern islands already face higher market rates due to the absence of these factors. If higher ferry fares feed through to higher transport charges it will be the southern islands that will be most adversely affected.

7.4.2 The findings from the business survey and the business interviews showed that across all geographic areas businesses expected the increases in ferry fares to be passed on in terms of higher transport charges. In most cases this was also confirmed by the interviews with the hauliers. In addition, there was no regional disparity about whether businesses would pass on higher transport charges to their customers. Across all island groups, it was generally felt that businesses would not be able to pass on any increases and would have to be absorbed within the overall company costs, having a detrimental impact on performance.

7.5 Conclusions

7.5.1 Using the evidence gathered it is likely that all areas of the Western Isles, Coll and Tiree will be affected by the removal of RET fares for commercial vehicles. However, given the profile of industry across the islands, the different indicators of recent socio-economic trends, and the location of businesses within the haulage market, it means that some areas are more vulnerable than others and will experience different levels of impacts.

7.5.2 Areas with a large share of enterprises in the primary sector will, due to the nature of these businesses, be adversely affected most. The Western Isles, Coll and Tiree as a whole have a proportionately higher share of enterprises within the primary sector. However, this is particularly the case in the southern islands, Coll and Tiree where the share of total businesses in the primary sector can be as high as 35%, leaving these areas more vulnerable. These areas already face higher than average transport charges due to the lower number of hauliers in the area and less competition in the market.

7.5.3 While the island communities covered in the study have not witnessed high levels of unemployment by Scottish standards, the rates seen are high compared to other island areas, and the Western Isles does have a number of highly deprived areas according to the Scottish Index of Multiple Deprivation, making them very vulnerable to any downturn in activity.

7.5.4 In addition, many of the areas concerned do not have the level of industry and capacity to absorb the downturn in activity, through say, changes in employment. While the area of Lewis and Harris may have the sectoral mix to absorb some of the impacts. Nevertheless, this area still has a relatively high dependence on those sectors likely to be most affected by an increase in transport charges brought about by the removal of RET CV fares.

8 Wider Economic and Social Impacts

8.1 Introduction

8.1.1 This chapter considers the wider economic and social impacts caused by the removal of RET fares for commercial vehicles. It is clear that the removal of RET in itself is not the sole cause of the difficult economic situation facing the islands over the period covered. Other factors such as the wider economic slowdown, which is impacting on all areas of Scotland, and the continued relatively high levels and rises in the price of fuel are also having a detrimental impact on business performance and economic activity more generally. It is difficult to completely separate these effects. However, the evidence from the interviews with hauliers and businesses, supplemented by the online business survey, suggests that the removal of RET has had some detrimental impacts on a number of businesses, the wider economy and the sustainability of the islands and their communities. Using the evidence gathered, this chapter explores the issues directly related to RET and provides an assessment of the impacts associated with this. It should be noted however that given the short time that has elapsed since RET has elapsed it is difficult to precisely quantify the wider economic and social impacts and the assessment therefore provides a qualitative assessment of the impacts.

8.2 Cost of RET

8.2.1 Before discussing the issues in detail, it is worth providing some context of the cost of removing RET for CVs to estimate how much extra the communities of the Western Isles, Coll and Tiree will have to absorb if the full impact of the increase in fares is paid for by local businesses.

8.2.2 In terms of spending, the cost to the Scottish Government of funding RET for CVs in the Western Isles, Coll and Tiree totalled £3.5m in 2011/12. Following the removal of RET, the cost of the transitional scheme for CVs is estimated to be £2.5m from 2012-13. The 10% increase in CV fares in 2013-14 is estimated to cost the Scottish Government £2m in 2013-14. These figures suggest that if the total additional reduction in funding was passed on to businesses in the Western Isles, Coll and Tiree, the leakage from the local economy would sum to £1.5m per annum.

8.2.3 While some of this could be passed on to customers in the supply chain, which could be located outside of the islands, the evidence from the interviews and survey discussed in the previous chapter did suggest that most of the increase in costs would have to be absorbed by local businesses. The total costs to local businesses will therefore be in the region of £1.5m. However, this depends on whether businesses can actually pay the higher transport charges. If it means that businesses cannot absorb them, which leads to loss of business and a reduction in employment, then it is possible that the impact on the local economies could be greater than the change in fares.

8.3 Vitality of the Islands

8.3.1 Earlier chapters reporting on the findings of the survey and interviews revealed there were significant concerns raised about the long-term economic prospects of the Western Isles, Coll and Tiree. While there was a general acceptance that there is a cost premium for undertaking business in the islands, a number of stakeholders noted that the cost differential between mainland and island life is now becoming so large that the ability to remain competitive and survive on the islands is becoming much more difficult for local businesses. It was acknowledged that this is simply market forces operating but numerous stakeholders emphasised that the Scottish Government has an explicit commitment to sustaining and developing Scotland's economy and this should include the island communities.

8.3.2 A number of stakeholders referred to the economic situation on the UK mainland, where the majority of businesses are experiencing poorer than average financial performance because of the general lower level of activity and growth within the economy. They noted that this problem is worse in the islands because the population and economy is small and the market, and therefore opportunities, much more limited. This makes it difficult to substitute lower export demand from the Scottish mainland and beyond to domestic demand / consumption when conditions worsen.

8.3.3 It was claimed that the small economies of the islands are highly dependent on domestic businesses for growth and survival, but are at the same time highly exposed to external competition. There was a strong feeling that as the initial and successive impacts of removing RET fares for CVs begin to be felt, both in direct terms for businesses and indirect terms for consumers, there will be a significantly adverse impact on the economic performance, and therefore sustainability, of the islands.

8.3.4 It is worth considering this issue both in terms of direct impacts on island business and indirect impacts on island life as a whole.

Impacts on Business Competitiveness

8.3.5 The evidence from the interviews and surveys suggest that, similar to the economy as a whole, there has been a squeeze on independent island domiciled businesses across a range of sectors. The additional removal of RET fares for CVs, it was claimed, was making it increasingly difficult for local businesses to compete with mainland and chain competitors, whilst there is insufficient 'domestic' demand to sustain these businesses in the long-term.

8.3.6 As explained in previous chapters, 33 businesses responded to the question on whether increases in ferry fares since the removal of RET for CVs in April 2012 has been passed on to their business. Of these respondents, 88% noted that hauliers have passed on the increase in CV fares to their business, while 97% of businesses explained that they expect that future price increases will be passed on to their company. Over 68% of businesses expect this increase to be in the region of £1,000 to £5,000 per annum. Given that 76% of the total registered businesses in the Western Isles at March 2012 were small, in terms of employing four staff or less, these are not insignificant sums and would have an important impact on their costs, competitiveness and ongoing performance.

8.3.7 Previous chapters have discussed the importance of the primary industries to the economies of the Western Isles, Coll and Tiree. The sector includes 23% of the total number of registered businesses in the islands (and in some areas over 35%) and accounts for 22% of total business turnover. However, many of the businesses in this sector are vulnerable to the increase in transport charges due to the nature of the market they are operating in and their limited ability to pass on costs through the supply chain.

8.3.8 In addition, it was claimed the independent retail sector in the islands is struggling to compete with both large retail chains and shopping trips to the mainland made possible by the introduction of lower RET fares for cars. RET for CVs played an important role in assisting the competitiveness of these businesses by lowering transport costs, particularly for big ticket items like furniture and electronics. Similarly to the primary sector, the retail sector is key to the ongoing performance of the islands. Wholesale, retail and repairs accounted for 185 enterprises in the islands at March 2012. This was only second to the primary industries and made up 16% of the total. The sector also accounted for employment of 1,410 people, which was the highest sector and 22% of the total. In terms of turnover, again this sector was highest, summing to £234m or 33% of the total.

8.3.9 While RET for commercial vehicles was not in itself a panacea for these problems, it was strongly felt it helped island firms compete both in the domestic and mainland markets by either reducing or maintaining transport charges to businesses. It played an important role in either increasing margins or cushioning firms against the increased costs of raw materials, fuel etc.

8.3.10 The direct impacts of this long-term loss of competitiveness due to the removal of RET, if it results in higher transport charges, are clear. The most notable immediate economic impacts will be:

- a reduction in profitability; followed by; and
- reduced salaries and employment and therefore local disposable income.

8.3.11 In the longer term this will feed through to:

- business closures or off-island relocation, with consequent losses in employment; and
- reduction in headcount, as firms attempt to adapt to new market realities.

8.3.12 Given the importance of transport charges for the competitiveness of key industries in the islands, such as primary and retail sectors, the impact of higher charges could have an important bearing on the short, medium and long-term performance of the economy.

Impacts on Communities

8.3.13 In addition to the direct impacts associated with the removal of RET for CVs, there are likely to be indirect / multiplier impacts as these filter through the local communities. This is a particular issue in the Western Isles, Coll and Tiree as the communities are relatively small and there is a high dependence on local expenditure and activity for their ongoing performance and sustainability. Therefore, the loss of even a small number of jobs could have more significant knock-on impacts across a number of vulnerable sectors which, from the evidence gathered in the interviews and surveys are very much operating at the margin, such as agriculture and crofting, both of which are important industries across the islands.

8.3.14 The long ferry crossing between the RET islands and the Scottish mainland has also historically made Lewis in particular relatively self-sufficient, with an above average number of, for example, furniture and carpet shops for a town the size of Stornoway. However, the increasingly open Lewis economy has had a large impact on these firms, many of whom have closed, reduced headcount and reduced the number of apprentices. Once again, this is just an example of a market 'working' but the negative impacts on the islands could be disproportionate to towns on the mainland.

8.4 Impact on Economic Development

8.4.1 The findings from the business interviews and surveys, together with the evidence from further research and analysis suggests that any increase in charges could have a number of impacts on the development of the island economies.

8.4.2 Firstly, the increase in costs and subsequent reduction in margin and profitability will have an immediate impact on those sectors most affected, such as the primary sector. This will also feed through to a loss of competitiveness, ability to invest and grow and lower employment opportunities. Given the importance of these sectors as key economic drivers of the local communities, the impact could be significant.

8.4.3 The increase in costs, and therefore relative competitiveness with mainland rivals, will also lessen the opportunity for new businesses to start, whether that is through domestic or inward investment to the islands. A number of businesses interviewed explained that higher costs, due to higher transport charges, could mean a halt in investment and expansion plans. While a number of firms had invested heavily to expand their business during the 2008 to 2012 period when transport charges had remained fairly stable, it was explained that the result of higher transport charges could lead to a reversal of these actions. Indeed, some businesses explained that their company had withdrawn from a particular market as a direct consequence of the higher costs ie the business had now become unviable.

8.4.4 There may also be impacts on the level of capital investment, such as housing. A number of stakeholders felt that this will hold the economies of the islands back in the long term. For example, there is a shortage of affordable housing on Coll and Tiree which is restraining population retention and growth, and is also impacting on the young and most marginal families. A number of people interviewed claimed the removal of RET for CVs puts between £8,000 and £20,000 on the cost of the average house – this increase in cost, coupled with difficulties in getting a mortgage or bank loan, is constraining the construction sector on the islands.

8.4.5 Storas Uibhist, a local community landowner, echoed this point. It explained that there is a shortage of high quality housing in Benbecula and South Uist and that the most attractive option is a self-build. Kits are typically purchased from Scott's on the mainland. Storas releases ten plots for new developments each year and there are typically six new houses built. However, this number is expected to decline with the removal of RET for commercial vehicles. Storas note that, on average, it costs 40% more to build a house on South Uist than on the mainland and that 10% of the total costs are related to moving goods by ferry. Therefore, any increase in ferry fares could impact heavily on the cost of building a new house. The incidence of this impact is likely to fall on young families and first time homebuyers and there were fears expressed that they may leave the island as a result of the cost of a home (or the difficulty getting a mortgage for an 'over-priced' house).

8.4.6 While the above example relates to housing, it can equally apply to the construction sector more generally, with impacts on private sector commercial developments as well as the public sector building investment. The importance of the construction sector in terms of its supply chain was discussed in Chapter 6.

8.4.7 The continued uncertainty is also seen to be of considerable detriment to the local economy. The RET pilot lasted for the better part of four years and this, combined with the loss of the commercial vehicle element, has prevented longer-term investment decisions being taken. There is also concern that constant political involvement (and in particular, party politicking) in the ferry industry is highly detrimental for island businesses as it impacts on forward planning and business confidence.

8.4.8 Overall the impacts on economic development could have implications for the Scottish Government's long-term sustainability objectives for the islands. For example, earlier chapters have explained that, while the most recent population estimates may show figures stabilising in recent years, the long-term trend has clearly shown a significant decline. The lack of development opportunities will impact on population retention if employment opportunities decline.

8.4.9 It was also shown in Chapter 7 that the Western Isles, Coll and Tiree already suffer from relatively high levels of deprivation. If the removal of RET for CVs and the subsequent increase in charges feed through to lower levels of business investment and employment, reduced salaries and number of business start-ups, this will have a negative impact on the levels of deprivation across the islands.

8.5 Lower Quality Products

8.5.1 It was explained in the business interviews that many livestock farmers have seen increasing costs, such as animal feed, in recent years in line with global commodity prices. In response to this a number of farmers have moved to substitutable options, such as silage rather than hay. This lower quality feed then impacts on the quality of the livestock produced. This then impacts on the price of the livestock at auction, which again impacts on the quality of feed that they can afford.

8.5.2 This downward spiral is impacting on the performance of these businesses and it was claimed that higher fares, if fed through to higher transport charges, will have further impacts, both in terms of higher costs for animal feed and higher costs for transporting livestock to auction.

8.6 Competitiveness

8.6.1 Chapter 4 discussed in detail the impact of the traffic imbalance on transport charges and how these affect the competitiveness of island based firms through higher transport charges. It was claimed in the interviews with businesses that the impact of RET on lower haulage costs had allowed them to increase their competitiveness relative to mainland firms. The savings had also allowed them to invest in their business. If higher ferry fares lead to higher transport costs it means that island firms could see a reversal of these impacts. It was also claimed that the loss in competitiveness in particular could have a significant impact on their business performance. This is at a time when general economic conditions are putting pressure on their operations.

8.7 Hauliers as Key Contributors to Supporting Local Communities

8.7.1 It was clear from the interviews that many hauliers felt a moral responsibility for supporting communities. In many cases hauliers are key employers in the local areas. They also play an important part in supporting economic activity. Those interviewed felt a duty to keep freight services affordable and to ensure local businesses remained competitive and survived. However, higher ferry fares would be difficult to absorb and would need to be passed on. This could have a negative impact on the local communities and on the viability of businesses. Businesses would have to deal with this by reducing employment or lowering labour and other costs. This would lead to lower income and consumption in the local area, possibly resulting in a downward spiral of activity.

8.8 Impacts on "Prices in the Shops"

8.8.1 Estimating how the removal of RET on "prices in the shops" is not straightforward. One of the justifications for the policy was that it would help reduce the price of day-to-day goods purchased by both islanders and tourists in the shops. This was monitored as part of the wider RET evaluation exercise, principally through trying to ascertain via survey data whether residents felt prices in the shops had indeed gone down as a result of RET.

8.8.2 However, this link between a reduction in fares / transport charges and the price of a good is too simplistic, a point made by many stakeholders during the interview process. The main criticism was the price of any individual item in the shops (eg bread, milk, canned goods etc) is heavily influenced by a wide number of factors. For example, the price of a bottle of milk will depend on, amongst other items, the market rate of milk at that time (ie supply and demand in the dairy market which could be influenced by many volatile factors – eg good weather could lead to increased demand for milk to produce ice cream); the cost of the carton (ie raw materials, manufacturing; transport etc); the cost of transport (ie wages; fuel; ferry fares; insurance etc); and the pricing strategy of the retailer. Given the complexity of pricing for this one relatively simple product, it is difficult to estimate how RET affects the price of this one commodity.

8.8.3 This leads on to the key term of the unit price of a good. The majority of deliveries to retail outlets on the islands are by the pallet, with the average pallet costing anywhere between £40-£60 on average. However, within each pallet is a large number of units. For example, a pallet of baked beans or garden peas will typically have 864 cans on it. If we assume a pallet costs £50, the unit price of each can on that pallet is 5.78 pence – ie the transport cost of a can of baked beans is 5.78 pence per can. If we then assume that RET reduced the price of a pallet to £44, the unit price of a can of baked beans would be 5.09 pence per can. Therefore, even if RET reduced the cost of a pallet by £6 (from £50 to £44), the unit cost of a can of beans would only be reduced by 0.69 of a penny. Given that the majority of goods bought in the shops in the Western Isles are of a similar nature (ie each pallet has a large quantity on a fixed price pallet), it is difficult to see how someone could make well informed judgements on "prices in the shops". If anything, the loss of RET for CVs could be a means of hiding increased retailer margin – ie if the above example is reversed, a retailer may only experience a 0.69 of a penny increase in the cost of a can of baked beans but could add one penny to the price, taking a mark-up of 0.31 of a penny per can.

8.8.4 Notable price impacts are only likely to be seen on larger goods (eg washing up powder) where the smaller number of units means a larger increase in the unit price. Very large items, such as furniture and white goods are where an obvious price difference will be seen and this was borne out speaking to businesses in these sectors. In general, the impact of RET on "prices in the shops" is very difficult to determine and will only become apparent after a period of time. However, from discussions during the interviews it is likely to impact on the price of larger goods before it a noticeable impact on smaller goods.

8.9 Impacts on Households

8.9.1 It was claimed that the cost of living in the islands, particularly in the less populated islands, is increasing at a historically high rate. This is principally being driven by the sharp rise in fuel costs. However, it is expected that increased fares for commercial vehicles will eventually lead to increased prices in the shops, although the extent to which this is true will depend on the extent to which higher fares are passed on through higher transport charges, which will differ across the islands. As explained in the previous section, this will also depend on the type of goods being sold.

8.9.2 In addition, it was claimed the removal of RET has removed many of the positive competition impacts that were helping to keep prices down and expand consumer choice.

8.10 Impact on Vulnerable Communities

8.10.1 The previous chapter explained that the rates of unemployment in the Western Isles, Coll and Tiree have been relatively low compared to the Scottish average, and very much lower than most Scottish mainland authorities. However, the evidence shows that they have historically been higher than other island area such as Shetland and Orkney. Recent claimant count rates at January 2013 are set out below in Table 8.1 below.

Table 8.1 Claimant Count Rates (January 2013)

Area	Claimant Count rate
Eilean Siar	2.9
Orkney Islands	1.4
Shetland Islands	1.5
Highland	2.9
Argyll & Bute	3.3
Scotland	3.9

8.10.2 Moreover, while JSA claimant rates have been low, it is clear that the removal of RET for CVs will impact most heavily on certain sectors, particularly the primary industries. The previous chapter explained that the Western Isles, Coll and Tiree have a high dependence on businesses in this sector. This can make those area very vulnerable to the changes in fares.

8.11 Future Uncertainty

8.11.1 While higher fares and transport charges will have a negative impact on business performance, the decision itself to increase fares may also have a negative impact. It was made clear during the business interviews that the constant change in ferry fares policy for the islands is having adverse effects on business confidence and activity. The decision to remove RET ferry fares for CVs will create further uncertainty and could lead to more investment decisions being postponed.

8.12 Impact of redefining a CV from 5m to 6m

8.12.1 As part of the measures to mitigate the effects of the removal of RET ferry fares for commercial vehicles, vans of more than five but less than six metres now qualify as a non-commercial vehicle. This section considers the impacts of this change.

8.12.2 The new fares for a vehicle less than 6 metres are substantially less than the equivalent fare if they had been designated as a commercial vehicle. The fares for a non-commercial vehicle, compared to the fare for a six metre vehicle are set out in Table 8.2 below. The Table shows the fare under RET and the new fare for a vehicle of 5.5 metres. The Table shows that a vehicle of this length would now pay much less on a single trip. For example, on the Oban – Castlebay / Lochboisdale route the fare would fall from £115.40 under RET to £57 under the transitional arrangements, a reduction of £58.40 or just over 50%. For a return trip this would sum to £116.80.

Table 8.2 RET and Transitional Arrangement Fares for a 5.5 metre Van

	Oban – Coll Tiree	Oban – Castlebay / Lochboisdale	Uig – Tarbert / Lochmaddy	Ullapool - Stornoway
Fare for 6m CV	£84.40	£115.40	£59.10	£72.00
Fare for non-commercial vehicle	£47	£57	£26	£42.50

8.12.3 The findings from the haulier interviews suggested that this policy change has had only a very limited impact in the islands to date. As the policy was only introduced in April 2012, there has been very little opportunity to change fleet configurations. In addition, vans do not offer the economies of scale of larger vehicles and there was little suggestion from stakeholders that redefining their fleet configuration was an immediate priority going forward. Nevertheless, it was explained that the issue will continue to be monitored over the medium term to determine whether the situation changes.

8.12.4 The geographic characteristics of the RET islands, coupled with the low frequency ferry service and long crossings has also limited the "white van invasion" from the mainland. There are only limited opportunities for mainland vans to pick off valuable traffics as a vehicle coming over from the mainland would be facing a full day round trip or, in the case of Coll and Tiree, at least one overnight stay on the islands. It is, in effect, uneconomical. While this may not necessarily be the case on islands that are located closer to the mainland and have higher ferry frequencies, eg Arran, Bute, Mull etc, it was not an attractive opportunity on services to the Western Isles, Coll and Tiree.

8.12.5 One aim of the study was to consider whether change in definition will encourage businesses to provide their own haulage arrangements at the expense of existing freight operators. There was very little evidence from the business interviews to suggest that island firms saw the redefinition of commercial vehicle length as an incentive to switch from using contracted haulage services to their own vans. The main reason for this was that it added another costly fixed overhead to the business - ie vehicles and servicing, fuel, driver costs; insurance etc. The majority of firms were moving small volumes and noted that contracted haulage arrangements remained far more cost effective. The only firm we consulted who noted that they had moved to using their own vehicles was Kallin Shellfish. However, this was due to the demise of MacAskill and the lack of an alternative direct chilled service to Glasgow rather than any RET related impact.

8.13 Conclusions

8.13.1 This chapter has discussed the wider economic and social impacts of removing ferry fares for commercial vehicles. The total reduction in costs to the Scottish Government associated with removing RET is estimated to be £1.5m. The extent of how this impacts on the Western Isles, Coll and Tiree will depend on how much these costs can be passed on to customers out with the islands concerned. The impact on the Western Isles, Coll and Tiree will also depend on how much they can actually be absorbed by businesses. For example, if businesses cannot pay the higher charges, this may lead to loss of activity and a reduction in employment, resulting in an impact which is greater than the change in fares.

8.13.2 In addition, the Chapter has discussed how higher transport charges will impact on business competitiveness if they can’t be passed on to customers. They may also impact on the sustainability of communities and populations if higher fares result in reductions in profitability, employment, investment and growth. They could also result in a reversal of investment decisions and removal of competition as companies withdraw from the market. Ultimately, this will have implications for the long-term sustainability of the local communities, and the wider Western Isles, Coll and Tiree economies specifically.

8.13.3 Finally, many parts of the Western Isles are characterised by relatively high levels of deprivation. If higher fares and transport charges lead to a reduction in income and employment, as suggested in the business interviews, the outcome could be a worsening of this position and deprivation ranking.

9 Costs to the Taxpayer

9.1 Introduction

9.1.1 This chapter provides an assessment of the impact on the cost to the taxpayer of the removal of RET fares for commercial vehicles in April 2012. Specifically, in line with the brief the analysis considers the costs to the taxpayer of subsidising fares for commercial vehicles to the islands within the study areas.

9.1.2 In terms of spending, the cost to the Scottish Government of RET for CVs in the Western Isles, Coll and Tiree was £3.5m in 2011/12. Following the removal of RET, the cost of the transitional scheme for CVs was £2.5m in 2012-13. The 10% increase in CV fares in 2013-14 (announced in December 2012) will cost the Scottish Government £2m in 2013-14.

9.1.3 The 'cost to the taxpayer' is defined here as the change in revenue as a direct consequence of an increase in fares for CVs via the transitional arrangements introduced in 2012 ie the change in revenue will directly impact on the level of subsidy provided to the operator and therefore the cost to the taxpayer. The analysis does not include the cost to the UK taxpayer as a whole as paid by all Scottish and UK government departments through, for example, changes in corporation tax, income tax, national insurance payments, welfare benefits etc.

9.2 Data

9.2.1 To date there is six months of carrying and revenue data since the removal of RET fares for CVs was introduced ie April to September 2012. This has been used as the starting point to show how revenue has changed, compared to the equivalent six-month period in the previous year. This has then been grossed up to provide an estimate of the annual change in revenue using the 2011 six month and twelve month revenue figures.

9.2.2 It should be noted that there are limitations with this approach: using six months of data will not necessarily provide a precise estimate for the whole financial year 2012/13 and beyond as users (businesses and hauliers) may not change their behaviour immediately in the face of higher fares eg businesses may be in contracts where transport charges may remain in place during the first six months and change in the second half of the year, or demand for final products may change over time as increases in ferry fares feed through to changes in prices of final goods, thus reducing demand for hauliers / commercial vehicles in the second six-month period.

9.2.3 It should also be noted that the removal of RET was not the only change occurring over the period. The economic downturn may have affected carryings more generally and local projects, such as the completion of the school building programme in 2011, may also have had an impact.

9.3 Impact of changes in fares

9.3.1 Table 9.1 below shows the percentage change in fare across the 4 routes[18] as documented in Chapter 2.

[18] The table doesn't include the inter-island Coll – Tiree route as the figures are small and unlikely to make a significant difference to the overall revenue figure, and therefore subsidy / cost to taxpayer

Table 9.1 Change in Fares from 1 April 2012

Route	% change in fare April 2012
Oban – Castlebay / Lochboisdale	23%[19]
Oban – Coll / Tiree	40%
Uig – Tarbert / Lochmaddy	50%
Ullapool - Stornoway	50%

9.3.2 From the survey responses and interviews with hauliers and businesses, it is clear the removal of RET fares for CVs has impacted on the number of carryings and level of revenue generated. Table 9.2 below shows the number of CV lane metres carried and CV revenue generated by individual route, and total pilot area, for April to September 2011 and April to September 2012. The Table also shows, the absolute and percentage changes between the two six-month time periods.

Table 9.2 Carryings and Revenue by Route Apr-Sept 2011/12 and Apr-Sept 2012/13

	Apr–Sept 2011/12		Apr–Sept 2012/13		Apr–Sept 2011/12 – Apr–Sept 2012/13		Apr–Sept 2011/12 – Apr–Sept 2012/13	
	Actual Carryings (m)	Actual Revenue (£)	Actual Carryings (m)	Actual Revenue (£)	change in carryings	change in revenue (£)	% change in carryings	% change in revenue
Oban – Coll / Tiree	11,452	169,295	9,452	181,505	(2,000)	12,210	(17.5%)	7.2%
Oban – Castlebay / Lochboisdale	7,343	119,922	7,470	136,802	127	16,880	1.7%	14.1%
Uig – Tarbert / Lochmaddy	46,077	336,014	42,776	442,742	(3,301)	106,728	(7.2%)	31.8%
Ullapool – Stornoway	103,550	1,117,935	85,318	1,365,039	(18,232)	247,104	(17.6%)	22.1%
Total	**168,422**	**1,743,166**	**145,016**	**2,126,088**	**(23,406)**	**382,922**	**(13.9%)**	**22.0%**

9.3.3 Table 9.2 shows that in the six month period following the removal of RET fares for CVs on the Oban – Coll / Tiree, lane metres carried declined by 2,000 (17.5%), compared to the same six-month period in 2011/12. The change in fares combined with the change in carryings resulted in an increase in CV revenue of £12,200 (7.2%) for the six months.

9.3.4 On the Uig – Tarbert / Lochmaddy route, fares increased by 50% and lane metre carryings for CVs declined by 3,300 (7.2%). This resulted in an increase in revenue of just under £107,000 (32%).

[19] Fares on the Oban – Castlebay / Lochboisdale and Oban – Coll / Tiree increased by different percentages depending on the length of the vehicle. Figures shown are for 12m

9.3.5 On the Ullapool – Stornoway route, CV fares also increased by 50%. This was followed by a reduction in lane metre carryings of 18,232 (17.6%) and an increase in CV revenue of just over £247,100 (22.1%) over the six-month period between April and September 2012.

9.3.6 The slight anomaly occurred on the Oban – Castlebay / Lochboisdale route where fares increased by around 23%. Following this fare increase, carryings rose slightly by 127 (1.7%). However, despite an increase in carryings, the increase in revenue ie 14.1% (£16,880) was less than the increase in fares. The explanation for this anomaly is due to the concession for seafood lorries travelling empty ie while more lane metres or vehicles were being transported on the route, the introduction of the fares concession for the return trip from the mainland meant that the increase in revenue generated was less than the fare increase. It should be recognised that seafood lorries make up a significant proportion of CVs on this route.

9.3.7 Taking all of the routes together shows that following the fare increases, carryings declined by just over 23,400 (13.9%)[20] and revenue rose by £382,922 (22.0%) over the six-month period.

9.3.8 The total annual CV revenue for 20I1/12 across the four routes was £3,287,300. If we assume that the increase in revenue of 22.0% remains constant over the 12 month period then the absolute increase in revenue between 2011/12 and 2012/13 would amount to £657,460. If it is also assumed that this feeds directly through to a pound for pound reduction in subsidy, then the saving to the taxpayer from the removal of CV ferry fares would amount to £657,460.

9.3.9 The extent to how much this figure directly translates into a reduction in activity of this size across the islands will, as has been discussed elsewhere, depend on how much the increase in fares is passed on in higher transport charges and, subsequently, how much this can be passed on to customers outside of the islands. The evidence from the interviews suggests that most of the hauliers will pass on the increase in ferry fares to businesses. However, 42% of businesses surveyed explained that they could or would not pass on additional haulage costs to their end customers, while 27% of businesses said they would pass on the full cost to their end customer. While it is difficult to arrive at a precise figure on how much of the increase in fares will be passed on to final customers in the islands and elsewhere, the evidence from the interviews suggests the majority of end customers are located in the islands, and therefore the final impacts on activity will be felt there.

9.3.10 There are a number of assumptions here that may impact on the actual figure of £657,460. Firstly, for example, it is assumed that the percentage change in carryings and revenue remains constant between the first and second six-month period. It could be that carryings decline further as demand for transported goods falls (either imports or exports), leading to a decline in the estimated revenue. In this case the increase in revenue (between 2011/12 and 2012/13) will also fall, leading to a lower saving to the taxpayer.

9.3.11 Secondly, the estimate assumes that carryings and revenue would not have changed between 2011/12 and 2012/13 if RET had not been removed. It may be the case that carryings and revenue would have increased in the absence of the removal of RET, therefore reducing the estimated savings to the taxpayer. It is noticeable that CV carryings across the CalMac network as a whole, excluding the RET pilot routes, increased by 8% between Apr – Sept 2011 and Apr – Sept 2012. If this trend had been reflected on sailings to and from the Western Isles, Coll and Tiree if RET fares

[20] As Chapter 2 explained, all of this decline may not necessarily be a direct consequence of the removal of RET fares for CVs. Other local factors and the general economic slowdown may also have been influencing factors.

for CVs had not been removed, then revenue on these routes would have increased, meaning that the estimated saving to the taxpayer would be lower.

9.3.12 In addition to the cost to the Scottish Government of CV fares on Western Isles, Coll and Tiree, the Scottish Government has also absorbed additional costs of fare arrangements for livestock and shellfish lorries as well as for 5 to 6m commercial vehicles. With regard to the latter, in discussions with CalMac, together with anecdotal evidence from hauliers and businesses suggest that in the first six months since the removal of RET for CVs there has not been a noticeable increase in the number of vehicles of this length on these routes. However, it was also recognised that it may take a longer period of time for behaviour of hauliers to change, particularly when it comes to changing / replacing the size of vehicles in their fleet.

9.4 Conclusions

9.4.1 From the evidence gathered, together with the official data from the operator, the total CV lane metres carried in the first six months since the removal of RET declined by just under 14%, compared to the same six-month period in the previous year, across all routes. This compares with a 22% increase in revenue over the same period. The largest percentage decline in carryings were witnessed on the Oban – Coll / Tiree and the Ullapool – Stornoway routes, which saw CV lane metres fall by 17.5% and 17.6% respectively. Carryings on the Oban – Castlebay / Lochboisdale route actually increased, by a small rate of 1.7%. The largest increase in revenue was on the Uig – Tarbert / Lochmaddy route, which saw CV revenue increase by just under 32%.

9.4.2 The total change in revenue over the six-month period amounted to 22.0%. This equates to £382,922. If a similar percentage increase in revenue is witnessed over the 12 months since the removal of RET then this will equate to £657,460. This will be the savings to the taxpayer as a direct consequence of removing RET for CVs. This analysis does not take account of other tax and revenue impacts to other UK government departments, such as the change in income and corporation tax and national insurance contributions falling on from changes in transport charges feeding through to changes in business performance.

9.4.3 If the increase in revenue of £657,460 translates directly into a reduction in activity, then the evidence suggests that the majority of this impact will be felt in the islands.

10 Emerging Findings

10.1 Introduction

10.1.1 This chapter sets out the key research findings, which have been discussed in previous chapters, identifying the impacts of the removal of RET for commercial vehicles on services to and from the Western Isles, Coll and Tiree. This is followed by a review of actions that could be taken to mitigate these impacts as well as an overview of the key issues that should be considered in any future CV fares policy.

10.2 Research Findings

10.2.1 The economies of the Western Isles, Coll and Tiree, similar to many areas of the country, are suffering from the general economic slowdown which is impacting on activity and individual business performance. The poor macro-economic situation coincided with the removal of RET ferry fares for commercial vehicles in April 2012. The combination of both events happening together has made it difficult to isolate the impacts of the removal of RET fares for CVs. Despite this however, based on the evidence and views gathered it is concluded that the removal of RET has had a detrimental impact on the local economies of the Western Isles, Coll and Tiree.

10.2.2 This study has considered the impact of the removal of RET for CV fares in great detail, gathering views and evidence through interviews, surveys and desk-based research. The key finding is that the introduction of RET ferry fares for CVs in October 2008 had made an important contribution to the initial equity objective of supporting, sustaining and developing the economies of the Western Isles, Coll and Tiree. Our evidence suggests that while reduced ferry fares did not lead to a reduction in transport charges, the cost savings offered by RET were, in the main, used by hauliers to stabilise transport charges between 2008 and 2012 (ie it is likely that in the absence of RET transport charges to businesses would have gone up).

10.2.3 The real-terms reduction in transport charges between 2008 and 2012 provided a number of benefits to local businesses. In many cases it enabled them to improve their competitiveness with mainland firms. It also allowed a number of companies to increase investment in their business, thereby improving performance and helping to support economic activity on the islands.

10.2.4 The evidence and views gathered during the consultation exercise suggests that when RET fares for CVs was removed in April 2012, haulage rates either increased immediately or are forecast to rise when existing contracts come to an end. Over 80% of businesses reported that hauliers had passed on the increases in ferry fares, which are expected to feed through to a decline in business performance across a number of sectors. For example, interviews and business survey findings suggest that the removal of RET has already led to withdrawal from markets by some firms, as well as a small reduction in headcount by others. It is also anticipated that future significant increases in fares will be passed on by hauliers and have further negative impacts as companies will find it difficult to pass these on to end customers.

10.2.5 The removal of RET has had a number of negative impacts for some businesses. For example, it has led to a fall in business confidence due to the uncertainty caused by the ongoing change in fares policy. The increase in transport costs has impacted on the competitiveness of island firms during a period of difficult economic conditions. It has increased transport costs for firms which have a relatively high proportion of these costs as a percentage of total business costs. It has impacted on the performance of a number of companies which are dependent on the ferry for imports (raw materials) and exports (finished goods). Perhaps of most significance, the removal of RET for CVs is impacting on the staple industries of the islands (eg agriculture, crofting, aquaculture, construction and manufacturing), characterised by small firms operating at the margin. It is also having a disproportionate effect on the smallest communities, both in terms of a direct loss of income and the subsequent multiplier impacts.

10.2.6 While RET for CVs in itself will not determine the economic future of the islands, its removal may combine with numerous other current economic pressures (eg energy costs, declining real income, wider economic situation etc) to impact on the sustainability of island firms and local industries. The potential social impacts on the islands in terms of population retention, and long-term viability could also be important.

10.3 Impact Mitigation – The Components of a Future Fares Policy

10.3.1 This section sets out the issues that should be considered in designing a future fares policy for commercial vehicles that meets the needs of island businesses and ensures the Scottish Government secures value for money, while at the same time contributes to its equity objective and supports sustainable economic growth for the island communities. It considers five potential fare options which could be applied together or separately. It is important to note that any fares scheme must comply with European State Aid legislation, which would mandate that all haulage firms have a right to free and equal access to the island markets ie the Scottish Government cannot discriminate in favour of island firms. It is also important to recognise that any fares system must be considered in light of current budget constraints and affordability issues, while also offering value for money for the taxpayer more generally.

10.3.2 We do not recommend any specific option for future policy as this is an issue that will need to be discussed further with Ministers and the local communities in question. Instead we set out the advantages and disadvantages with each fare option for consideration.

Full Non-RET Fares

10.3.3 The evidence presented in this report on the impact of the removal of RET to date suggests that any return to the full non-RET fares after the transitional scheme would have a negative impact on local businesses and the wider economy of the islands more generally. The interviews and survey data suggest that the removal of RET is already impacting on the performance of some businesses. While it is very early to understand the full future impact of the fares increase, the initial figures provided by companies suggests: costs for a number of companies have increased, profits have fallen, employment levels in some cases have fallen, albeit marginally and, a small number of firms have withdrawn from activities developed following the introduction of RET.

10.3.4 As explained above, it is also clear from the evidence gathered that the removal of RET ferry fares for CVs would impact harder on some areas than others. Those likely to be most affected will be staple employment sectors and the smaller islands / remote areas with relatively lower levels of industry and activity.

10.3.5 The full non-RET fares would offer an immediate reduction in the Scottish Government subsidy level. However, while not a task of this study, it is possible that the wider cost of maintaining the island economies in the longer-term would rise and that this cost would outweigh the savings in subsidy.

Return to RET or 'RET Lite'

10.3.6 There was strong support among the island communities for a return to an RET-based fare system for commercial vehicles. First and foremost, RET was seen as an important mechanism for reducing the competitive disadvantage suffered by island businesses through reducing the cost of sales and providing a cushion against other rising costs that the islands are particularly exposed to – fuel costs for example. A number of businesses provided evidence that the reduction in ferry fares brought about by this policy allowed for an increased level of investment in the business as well as an occasional diversification of activities.

10.3.7 The policy was also seen to support the competitiveness of businesses operating within the islands. For example, independent retailers were able to use the discount to compete with; chain stores using regional pricing; shopping trips to the mainland; and internet shopping. Many island businesses are suffering because of their lack of scale, something which RET, to some extent, helped to insulate them.

10.3.8 RET was also seen as a much fairer system that treated all operators equally, thus generating greater competition and more choice for businesses. This helped to encourage efficiency within the market. It was also seen as a much more transparent system, while many of those interviewed were also in favour of a distance-based system.

10.3.9 In the short-term, a return to the previous RET system for CVs will increase the level of subsidy required and may raise affordability issues. However, as explained in Chapter 4, a majority of hauliers accepted that in the current economic climate of low activity and budget constraints there could be a case for increasing the rate per mile to make it more affordable. This variation of RET ie RET Lite would maintain the benefits of RET in terms of being fair, transparent and distance-based, but would be based on a rate per mile above the current rate. The rate would be influenced by a combination of affordability and road equivalent cost, rather than being primarily determined by the latter.

Volume-Based Discounts

10.3.10 It is also important for the Scottish Government and other stakeholders to draw a clear distinction between discounts designed to support the economy of the islands and discounts designed to reward haulage firms for volume. RET was introduced specifically to support the economies of the islands and there was an expectation that hauliers would pass on this benefit through the supply chain – indeed the perception that this was not happening was one of the justifications for withdrawing RET for CVs. On the other hand, volume based discounts like TRS were designed to reward hauliers that achieved the largest volumes – this is a common commercial practice across all industries and it would be unrealistic to expect any haulier to pass on their discount unless it was contractually mandated or in their interests to do so. One must therefore recognise that a return to volume based discounts alone will assist the largest hauliers but would have a neutral impact at best for other hauliers and most island businesses. It is essential that stakeholders have clarity on this issue: RET and TRS are two very different types of discount and thus are not mutually exclusive – they can be applied together or alone.

10.3.11 The issue of volume-based discounts (particularly TRS) was a highly emotive issue during the consultation, with strong advocates for and against such discounts. Many stakeholders saw the argument in terms of "RET or TRS" – however, as explained above, the issue of volume based discounts for hauliers is wholly independent of the debate on the need for RET.

10.3.12 The key rationale for re-introducing a volume-based discount is that it is a common business practice to offer reduced prices for buying in bulk – indeed, it is a practice that many of the businesses with whom we consulted are involved. A volume-based discount provides an incentive to grow the business and realise economies of scale. The key question that must be answered with regards to such discounts is the extent to which they are passed through the supply chain, generate additional business and contribute to the improved economic performance of the island economies.

10.3.13 It was clear from the interviews that the vast majority of operators were strongly against volume-based discounts as they believed they distort the market in favour of the largest firms. However, it was also clear from the large hauliers who have the majority of the market share in the islands by a significant margin that they were keen supporters of volume-based discounts and brought a number of operational benefits eg cross subsidy, which could be passed on to businesses.

Multi-Journey Tickets

10.3.14 Another potential fares scheme that could replace RET is the introduction of multi-journey tickets for commercial vehicles. This could provide one journey free for a given amount paid for by the haulier and therefore reduce the average fare paid for a given size of vehicle. The benefit of such a scheme is that, while it is non-discriminatory in State Aid terms, it is likely that the island hauliers would benefit the most as they use the ferry the most.

10.3.15 While this scheme could be attractive, it is not clear that it would be any less costly than RET or offer any other benefits over that fare system. In addition, there would be intrinsic volume based discounts with this scheme as the large hauliers purchasing the largest number of journeys will also receive the greatest number of 'free' journeys.

Targeted Island Specific Fare Schemes

10.3.16 An alternative approach to setting fares would be to move towards a series of island specific fares that take account of local considerations. This study has focused only on the impact of removing RET for CVs and thus cannot comment specifically on potential fare strategies for individual islands. However, a good example of the type of issue that could be investigated in more detail is in Coll, where consultees noted that RET for cars and passengers has brought few benefits because it offers negligible savings on the old six-journey books and the lack of tourist accommodation on the island has limited additional income from this sector. There may therefore be an option where RET for cars is withdrawn and RET for CVs is reinstated in its place.

10.3.17 It should be noted that this is not an actual proposal but an example of the types of issues that could be considered in more detailed follow-up studies. However, similarly to the Ferries Plan 2013–2022 which has suggested ferry services targeted at the needs of islanders (eg exports, tourism, commuting and personal), this would involve designing fares structures compatible with the needs and requirements of island communities.

10.3.18 The disadvantage of this system is that it could be very cumbersome, difficult to manage effectively and not straightforward. Indeed, the cost associated with designing and administrating it could outweigh any potential benefits from more effective targeting of fares to local needs.

Drop Trailers

10.3.19 While not necessarily part of fares policy, the issue of dropped trailers was raised during interviews with businesses and hauliers on a number of occasions. The inability to drop trailers on the majority of routes to and from the Western Isles, Coll and Tiree can impact on efficiencies of hauliers and, ultimately, the competitiveness of businesses. If the latter is an objective of fares policy it is a factor that could be considered as it could reduce transport costs for businesses on the islands.

Appraisal of Fares Options

10.3.20 Before finally deciding on a fares system for the islands it is recommended that an objective-led appraisal is carried out in line with the Scottish Government's appraisal guidelines to ensure a value-for-money solution is arrived at. Transport Scotland and the island authorities must be clear about what objectives a fares system should be aiming to achieve before finally deciding on what is the preferred option to achieve these objectives. Individual options should be appraised against the agreed objectives, as well as the Scottish Government's other criteria, including value for money, to ensure the most effective fares system is chosen. Without appraising the various options in detail it will not be possible to understand which fares system is likely to most effectively deliver the needs of the Scottish Government and the local communities.

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