

HEDGING STRATEGIES ADOPTED BY TRANSPORT OPERATORS

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BACKGROUND

Fuel hedging is defined as the advance purchase of fuel at a fixed price for future delivery. This is a common strategy adopted throughout the transport sector however, the stigma attached to hedging is not always positive.

Translink's fuel purchasing policy has recently come under criticism. Translink adopts a strategy whereby *it enters into hedge contracts by calendar quarter and has between 5 and 8 quarters ahead covered at any time.*¹

This briefing note identifies fuel purchasing policies adopted by other transport operators including those receiving public funds.

Research and Library Service has requested information from the publicly funded transport organisations considered within this note on what, if any, government rules and regulations are in place to protect the public against the risks associated with hedging with public monies. Further information on this will be forwarded to the Committee upon receipt.

CIE GROUP – IRELAND

The Irish Government is the sole owner of the CIE group which includes the subsidiary companies Dublin Bus and Bus Eireann which deliver bus services throughout Ireland. Through PSO² agreements, Dublin Bus and Bus Eireann receive funding from the Irish Government.

A recent cost and efficiency review of Dublin Bus and Bus Eireann identified the CIE policy with regards to hedging. It states that:

Possible fuel requirements are hedged 12-18 months in advance.

It further stated that,

*through a rising market this has benefited the group and kept fuel costs down. However, the most recent hedging was at a relatively high price so more recent falls in price will take some time to feed through.*³

¹ NITCH / Translink submission to the Committee for Regional Development, *Questions arising from the Committee Meeting of 26th November 2008.*

² Public Service Obligation Agreements

³ Deloitte, Cost and Efficiency Review of Dublin Bus and Bus Eireann, January 2009.
<http://www.transport.ie/upload/general/final%20report%20bus%20review%20220109.pdf>

The report, which identifies cost efficiency opportunities, makes no recommendations relating to the purchasing policy as fuel costs make up only 7% and 8% of Dublin Bus and Bus Eireann respectively.

ARRIVA

The Arriva Group is one of the largest private passenger transport providers in Europe.

The Arriva Group policy is to maintain fuel price fixes at least 12 to 15 months ahead on a rolling basis. The requirement to fix fuel prices is determined after taking into account the extent to which the businesses are protected from fuel price volatility through contract price indexation.⁴

Contract indexation is a procedure whereby a long-term contract for the provision of goods and services includes a periodic adjustment to the prices paid for the goods or services based on the increase or decrease in the level of a nominated price index. The purpose of such a contract is usually to take the inflationary risk out of the contract.⁵

In December 2008 Arriva announced that:

*Its hedging policy protected the group from material impact in 2008 and that it had 82% of its anticipated fuel requirement for 2009 fixed in price; 14% covered by indexation, and 4% remaining unfixed.*⁶

It further announced that:

*For 2010 it had so far fixed around 51% of prices and 13% were covered by indexation.*⁷

OTHER STATE OWNED TRANSPORT OPERATORS

A range of other state owned or semi state owned transport operators implement fuel hedging strategies. These include:

- State Transit – the government owned authority responsible for the operations of Sydney Buses, Australia.
- BC Transit – the provincial crown agency charged with coordinating the delivery of public transportation throughout British Columbia, Canada.
- TTC – the Toronto Transport Commission charged with planning and providing local public transport in the Toronto region.

Research and Library Service has requested additional information from these organisations on the rules and regulations relating to their fuel purchase strategies given that they are funded from public monies.

⁴ Arriva, *Investor Relations*, http://www.arriva.co.uk/arriva/en/investor_relations/regulatory_news/rnsitem?id=1173337272nRN1H5366S&t=popup

⁵ OECD, *Stats Glossary*. See: <http://stats.oecd.org/glossary/detail.asp?ID=4877>

⁶ Arriva, Pre-close trading statement.

⁷ *Ibid.*