

Motivating Question: Tokyo's Taxi Fares

This motivating question deals with the attached article from *The Economist* (March 1, 1997) on the new pricing system for Tokyo taxis. Since the Ministry of Transportation regulates taxis, you should ignore the fact that there exist several companies. Assume a constant marginal cost of ¥100 per Km and zero fixed costs. Ignore the last paragraph on future tariff discounts.

- Which type of price discrimination scheme are cabs using? What is the effect on the price per Km?
- The purpose of this question is that you analyze the welfare effect of the new pricing as compared with the previous one. In order to simplify, ignore that initial payments allow you one or two Km ride without additional charge (it does not change the answer qualitatively). Do you agree with the journalist's opinion that "this is a step in the right direction" in the sense that the new pricing scheme is welfare increasing? Explain your answer. Use a graph to illustrate your point.

Taxing times for Tokyo taxis

TOKYO

TOKYO'S taxis offer a plethora of frills: lacy white seat covers, doors that spring open automatically, white(ish) gloves on the driver's hands. But no amount of gift-wrapping can disguise the fact that prices are extortionate and service feeble. Few cabbies have a clue how to get anywhere; and, in return for telling them, passengers have to fork out ¥650 (\$5.30) just to climb in. From April 1st, as well as a map, travellers will need to carry a calculator and a pair of dividers. Believe it or not, this is a sign that things are improving.

On February 24th, four Tokyo taxi companies applied to the Ministry of Transport (which will say yes) for permission to give discounts. Another 16 are expected to join them. By April, 10% of the city's cabs will probably be charging a bargain ¥340 for the first kilometre (0.62 miles) and ¥80 for each subsequent quarter-kilometre. The current fixed fares are ¥650 for the first 2km and ¥80 for each 280 metres thereafter. Sharp-

eyed readers will have noticed that the new fare structure will be cheaper only for journeys of up to 1.75km.

Horribly complex it may be, but the fact that the ministry is prepared to allow even a little price competition is a step in the right direction. Until now, the ministry has decided how many taxis may run (there are 43,000 in Tokyo at the moment) and what they may charge. The result, as the chief taxi regulator admits, is that Japanese cabs are the dearest in the world. It costs about ¥24,000 to go from Narita, Tokyo's international airport, to the city centre some 75km away.

In return for the privilege of overcharging, Tokyo's taxi drivers have to satisfy standards that would make a London cabbie laugh. They must be over 20, hold a driving licence (gosh!) and pass an almost unflunkable geography test. Scant preparation, in short, for negotiating the capital's maze of nameless streets and houses numbered in the order in which they were built. Small wonder that from a peak of 4.3 billion in 1965, the number of passengers using Japanese taxis dwindled to 2.8 billion last year.

Hence the mandarins' keenness to breathe life into the taxi industry by deregulating it. From April 1st, companies will get automatic approval for any reductions of up to 10% off the standard fares, and 2,000-3,000 extra cabs will be allowed in Tokyo. Within five years, all restrictions on the number of taxis or their prices will be lifted. Who knows? By then some of the drivers might have learned their way around.

