

STAGECOACH ACQUISITIONS OF EASTBOURNE BUSES/CAVENDISH ARE REFERRED TO THE COMPETITION COMMISSION

1 BACKGROUND

- 1.1 On 13 May 2009, the OFT referred Stagecoach's completed acquisitions of Eastbourne Buses Limited ("Eastbourne Buses") and Cavendish Motor Services ("Cavendish") to the Competition Commission (the "CC"). They were acquired in two separate acquisitions. Both Eastbourne Buses and Cavendish provided local bus services in Eastbourne¹. Prior to the first acquisition, of Eastbourne Buses, Stagecoach did not operate bus services in Eastbourne, but did operate two inter-urban services between Eastbourne and Hastings.

2 JURISDICTION

- 2.1 The OFT claimed jurisdiction on the basis of the share of supply test, since for each transaction, the merged entity far exceeded 25 per cent of the share of supply of bus services in Eastbourne. In fact, as a result of both acquisitions, Stagecoach became the monopoly supplier. Stagecoach questioned whether Eastbourne constituted a "substantial part of the UK", given that it had a population of approximately 95,000, derived its primary income from tourism, and the local bus market was not of economic importance, valued at around £6 million.
- 2.2 The OFT rejected these views, concluding that Eastbourne was a substantial part of the UK. It relied primarily on a previous CC decision², and the fact that the OFT decides upon the existence of a relevant merger situation on an "is or may be the case" standard.

3 MARKET DEFINITION

- 3.1 In previous bus merger decisions, rather than focus on market definition, the OFT considered the competitive effects of the merger on a flow-by-flow basis. The OFT did not do so here because as a result of the acquisitions, Stagecoach became the monopoly operator of commercial services in Eastbourne. Also, the OFT found that competition between Eastbourne Buses and Cavendish occurred on a network wide basis, and therefore assessment on a network-wide basis was the more pragmatic starting point at Phase 1. It also noted:
- (a) tendered services – there were at least five other operators in Eastbourne and so did not raise competition concerns; and
 - (b) inter-urban services – are unlikely to be a constraint on intra-urban services in Eastbourne.
- 3.2 Other forms of transport, including rail, coach, walking, cycling, taxis and private cars, did not compete with commercial local bus services in Eastbourne.

4 COMPETITIVE ASSESSMENT

The counterfactual

- 4.1 The merger needs to be assessed against the appropriate counterfactual (i.e. what would have happened absent the merger). The decision contained detailed discussions given the sequencing of the two acquisitions. Stagecoach argued that absent the acquisitions

¹ And the neighbouring town of Hailsham.

² Tesco/Co-op Slough, November 2007 where the population of Slough was 120,000.

by it, bus operations in Eastbourne would have ended up with one operator, since whoever bought Eastbourne Buses would have sought to acquire Cavendish, and failing that, Cavendish would have exited the market.

- 4.2 The OFT rejected this argument, noting that competition between Eastbourne Buses and Cavendish was "sustainable". Stagecoach's own internal documents were not helpful to them on this point. The OFT also questioned Stagecoach's reasons for acquiring Cavendish if it was genuinely inevitable that Cavendish would exit the market, and noted that there were rival bidders for Cavendish (and Eastbourne Buses). The OFT therefore decided to assess the mergers on the following basis (a) for the acquisition of Eastbourne Buses – Stagecoach owning Cavendish, and (b) for the acquisition of Cavendish – Stagecoach owning Eastbourne Buses.

Horizontal issues

- 4.3 As a result of the acquisitions, the OFT noted that Stagecoach is the monopoly provider of commercial local bus services in Eastbourne. Eastbourne Buses' and Cavendish's networks overlapped extensively pre-merger and, as a result, actual competition between Eastbourne Buses and Cavendish was lost.

Barriers to entry

- 4.4 The OFT considered that depot capacity was the principal barrier to entry. Stagecoach had argued that owning a depot was not a barrier to entry, submitting that Cavendish entered in 2006, with four buses operating a single route, by using a portakabin in a shared parking space to house its buses.
- 4.5 However, the OFT considered that small-scale entry (such as that by Cavendish) may no longer be viable since any new entrant would now be competing against Stagecoach, a well-resourced national operator, and the minimum requirements for viable, sustained entry had therefore been increased by the merger. Also, Cavendish's entry had been at a time when Eastbourne Buses was in financial difficulties and was limited in its ability to retaliate. The OFT also noted that Stagecoach had a reputation for responding aggressively to new entry and that a number of market participants had indicated that they would not be prepared to enter, or indeed expand, at all into an area where Stagecoach was the incumbent.
- 4.6 The most likely entrant was Cavendish's former parent, Renown. However, Renown told the OFT that it did not believe entry against Stagecoach was viable and in any event was prohibited by a non-compete obligation from competing with Stagecoach for two years.
- 4.7 The OFT concluded that 'it is or may be the case' that each merger has resulted or may be expected to result in a substantial lessening of competition, raising the duty to refer.

5 EXCEPTION TO THE DUTY TO REFER

De minimis

- 5.1 Stagecoach argued that the OFT should apply the 'de minimis' exception on the basis that the value of the market was significantly less than £10 million per annum.
- 5.2 In applying the test, the OFT considered the following factors:

- (a) *the size of the market(s) concerned* – based on combined turnover the OFT approximated the size of the market as just over £6 million³. The OFT noted that it had not previously applied the 'de minimis' exception in markets this large and was unlikely to do so unless other factors strongly suggested it should;
- (b) *the strength of the OFT's concern* - the merger 'may be' expected to result in the loss of all competition on direct overlap routes. The strength of the OFT's concerns was of a 'may be the case' standard;
- (c) *the magnitude of competition lost by the merger* - although Cavendish's size, measured by turnover, was small, the merger will result in a merger to monopoly on a large part of the local market. The magnitude of competition lost by the merger is expected to be reasonably significant;
- (d) *the durability of the merger's impact* - as the OFT had not identified any potential entrants it did not consider any substantial lessening of competition would be limited in duration; and
- (e) *the transaction rationale and the value of deterrence* - Stagecoach would become the monopoly operator and had contemplated the benefits of a loss of competition in internal documents. The deterrence factor was, therefore, "no less than average".

5.3 Overall, the OFT concluded that the evidence pointed towards the impact of the merger being significant, and did not consider that this was a case suitable for application of the 'de minimis' exception.

Undertakings in lieu

5.4 Stagecoach had offered two forms of undertakings in lieu of reference:

- (a) to release or waive Renown from the non-compete clause; and
- (b) to hold pricing in Eastbourne constant for a period of three years by committing not to increase prices above standard rises in East Sussex and Kent.

5.5 The OFT did not see this as a case for resolution by means of undertakings in lieu. Moreover it considered that even without the non-compete clause, Renown would be unlikely to enter the market. Also, the OFT considered that price control would be a poor substitute for price competition that could have taken place absent the merger and would be unlikely to address any of the other quality or service benefits that competition can bring.

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³ The OFT did not accept that turnover for concessionary travel should be removed.