OFFICE OF FAIR TRADING

Anticipated acquisition by Survitec Group Ltd of the SOLAS Division of Zodiac Marine & Pool SASU

ME/5017/11

The OFT's decision on reference given on 17 August 2011. Full text of decision published 19 October 2011.

Please note that the square brackets indicate figures or text which have been deleted or replaced in ranges at the request of the parties or third parties for reasons of commercial confidentiality.

PARTIES

1. **Survitec Group Limited ('Survitec')** supplies marine and aviation safety products,[1] defence related products and contractor logistics support. Survitec is ultimately owned by Warburg Pincus & Co, a US based global private equity firm. Survitec manufactures marine safety products including liferafts and marine evacuation systems (MES) for use in commercial shipping. Survitec is also active in the distribution and servicing of marine safety equipment through its wholly owned subsidiary, Seaweather Holdings Ltd ('Seaweather'). Survitec supplies liferafts and MES under the RFD, Beaufort, DSB, and RFD Toyo brand names.

2. **Zodiac Marine & Pool SASU ('Zodiac')** is a French société par actions simplifiée active worldwide in three main business areas of swimming pool care, the marine sector and the environmental sector. Zodiac is controlled by Carlyle Europe Partners II, L.P. and Carlyle Europe Partners III, L.P., investment funds sponsored by The Carlyle Group, a global alternative asset manager.

[1] The term 'marine safety products' denotes a wide range of safety and survival products for use at sea and includes marine liferafts, marine evacuation systems, rescue boats, life boats, life jackets, immersion suits, pyrotechnics and fire safety products.

3. The target business is the SOLAS business of Zodiac's marine division comprising Zodiac Solas ('ZSO'), a French société par actions simplifiée and DBC Marine Safety Systems Ltd ('DBC'), a Canadian company (together, **'the Target Business'**). ZSO is primarily active in the design and manufacture of marine liferafts and MES under the Zodiac and Bombard brands at its facility in France. DBC is active in the design and limited scale manufacture of DBC branded marine liferafts and marine evacuation chutes (which are used in MES) at its facility in Canada. In the year to 30 September 2010, the Target Business' worldwide turnover was £[ ] million, of which £[ ] million was generated in the UK.

TRANSACTION

4. On 11 April 2011, Survitec entered into a Share Purchase Agreement to acquire the Target Business from Zodiac for a consideration of [ ] million euros.

5. The administrative deadline (extended) for the OFT to make a decision on this case is 17 August 2011.

JURISDICTION

6. As a result of the transaction, Survitec and the Target Business will cease to be distinct. The parties have a combined share of supply of [30-40] per cent by revenue in marine liferafts sold in the UK (with an increment of [10-20] per cent). Therefore the share of supply test in section 23(3) of the Act is met. As a result, the OFT believes that it is or may be the case that arrangements are in progress or in contemplation which, if carried into effect, will result in the creation of a relevant merger situation.

RATIONALE FOR MERGER

7. The parties submit that the rationale for the transaction is to expand the Survitec product range, particularly in relation to MES. The parties also consider that the transaction will extend Survitec's geographic footprint and will generate economies of scale in terms of the purchasing of materials and servicing of marine safety products on a global basis.

MARKET DEFINITION

Background

8. The parties overlap in the supply of marine safety products specifically liferafts and MES for use on commercial shipping (including cruise ships, ferries, container ships and fishing vessels).

9. The marine safety products sector comprises the supply, distribution and servicing of marine safety products.

Supply and distribution

10. Producers of marine safety products may be vertically integrated and supply their products direct to end-users and/or to third party distributors.

11. Distributors in the UK (whether independent or owned by a manufacturer) will typically stock a broad range of marine safety products (that is, liferafts, rescue boats, life jackets, immersion suits, pyrotechnics and other safety products) in order to supply both commercial and leisure users. As such, distributors will typically:

    a. produce some of the marine safety products which they sell (that is, either in-house or via outsourced or white-label arrangements)[2] and

    b. enter into, often multiple, cross-distribution arrangements with producers of other marine safety products.

12. In addition to purchasing marine safety products outright, end-consumers also have the choice of renting the equipment from a supplier/distributor such that they can trade-in their old equipment in part-exchange for new products (buy back and hire). Alternatively, customers may enter into straightforward hire arrangements where no buy back is provided.[3]

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[2] Commercial liferafts are, in some cases, produced by the distributor of the liferaft, for example, Viking and Survitec. Survitec outsources the production of its commercial liferafts to a third party Chinese manufacturer.

[3] The parties note that the only marine safety equipment which can be hired is commercial and leisure liferafts, lifejackets and immersion suits.

Regulation and servicing

13. The testing and approval process will depend on the regulatory regime to which the marine safety products are subject. Marine safety products used on commercial vessels in open seas will generally be subject to the testing and approval requirements set out in the International Convention for the Safety of Life at Sea ('SOLAS') and related codes and guidance issued by the International Maritime Organisation ('IMO') which have been implemented in the EEA by means of the Marine Equipment Directive (MED).[4,5]

14. The IMO has set out the requirements for servicing of certain marine safety products, particularly those commercial products which are subject to SOLAS requirements. Most categories of SOLAS approved liferafts require servicing on an annual basis. Where the IMO guidelines apply, marine safety products including commercial liferafts and MES can only be serviced by persons authorised to do so by the manufacturer of the particular product. In such cases, the site will be inspected by the manufacturer and Maritime & Coastguard Agency (MCA) in the UK.[6] The manufacturer must provide access to the product handbook and individuals who will be responsible for the servicing may be required to attend a one to two week training course.

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[4] Council Directive 96/98/EC of 20 December 1996 on Marine Equipment, as amended. The MED has been implemented in the UK through the Merchant Shipping (Marine Equipment) Regulations 1999 (SI 1999/1957).

[5] Only those commercial vessels which meet certain size and type requirements are required to carry SOLAS liferafts. Commercial vessels which do not meet these size and type requirements are not required to carry SOLAS liferafts and are free to use 'leisure' liferafts. In addition, marine safety products which are used by commercial vessels in coastal or inland waters or on leisure or other non-commercial vessels do not require SOLAS approval.

[6] The site will be inspected by a Notified Body which in the UK is appointed by the Maritime & Coastguard Agency. In the UK, the list of Notified Bodies, according to MarED, is Lloyd's Register, British Standards Institute, QinetiQ and ABS Europe Ltd.

Product scope

15. The OFT's approach is to first consider if narrow candidate product markets can be widened through substitution on the demand-side, and then, if appropriate, to consider if substitution on the supply-side allows several products, which are not demand-side substitutes, to be aggregated into one wider market.[7]

The supply, distribution and servicing of commercial liferafts

Supply[8] of commercial liferafts

16. The parties submit that the appropriate market is the supply of marine safety products.[9,10]

17. As noted above, marine safety equipment covers a diverse group of complementary products rather than substitute products with varying regulatory requirements. The OFT's investigation did not find evidence to support the parties' view that the appropriate product scope was the supply of all marine safety products. For example, the parties submitted that for newly built ships, each marine safety product will typically be tendered for separately. Similarly, distributors enter into multiple cross-distribution arrangements with suppliers of different products rather than source as a bundle. Therefore, the OFT has found no reason to aggregate the products into a single product scope on the demand-side, given the complementary nature of the products, and focused on liferafts on the demand-side as opposed to other marine safety products.

18. Marine liferafts are used on either commercial or leisure vessels but tend to differ in size[11] and the authorisation process they require. Typically, commercial liferafts are required to comply with SOLAS requirements but this is not the case for leisure liferafts. As a result, the OFT considers that there will be little demand side substitution between leisure and commercial liferafts. In answer to this, the parties provided information relating to

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[7] See Merger Asessment Guidelines, Joint publication of the Competition Commission and the OFT, September 2010, paragraph 5.26

[8] 'Supply' refers to the upstream supply by a manufacturer of commercial liferafts.

[9] The Target Business does not undertake any manufacturing in the UK.

[10] The parties provided separate shares of supply of leisure liferafts, commercial liferafts and MES.

fishing vessels. The parties estimated that around 90 per cent of the fishing vessels in the UK are not required to carry SOLAS liferafts and are therefore free to choose between SOLAS and leisure liferafts.[12] Although the number of fishing vessels that is required to have a SOLAS liferaft may be small, the OFT considers that for these vessels, there is no substitute product that can be used and hence the OFT is not persuaded to consider widening the product scope to include leisure liferafts. The OFT therefore considers it appropriate to focus on commercial liferafts from the demand-side.

19. For the sake of completeness, the OFT also considered the extent of demand side substitution between commercial liferafts and MES but considered this to be limited. MES are commonly used on commercial vessels, such as cruise ships, ferries and passenger vessels, where a large number of passengers may need to be evacuated quickly in an emergency. The size of the system will depend on the size and shape of the vessel (vessels with a higher freeboard[13] will require a longer evacuation chute or slide), as well as the number of passengers and crew on board. Although many of the materials and component parts are the same as those used in the production of marine liferafts, MES are typically designed and fitted to the ship and, as such, require a degree of bespoke design.

20. From a demand-side perspective, the OFT therefore considers that commercial liferafts are not substitutable with other marine safety products.

21. The OFT considers that markets are defined primarily on the basis of demand-side substitution. The OFT can, however, consider the scope for supply-side substitution and may aggregate several narrow relevant markets into one broader one on the basis of supply-side substitution when:

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[11] Commercial liferafts will range in size from four-150 person rafts, whereas leisure rafts will typically be designed for four to 10 persons

[12] In 2010, the UK had 6,477 registered fishing vessels of which around 700 vessels are over 15 metres in length and required to carry a SOLAS liferaft. Under the Code of Practice for the Safety of Small Fishing Vessels 2007, liferafts installed on board fishing vessels under 15 metres need not be SOLAS approved.

[13] The 'freeboard' is the distance between the waterline and the main deck or weather deck of a ship or between the level of the water and the upper edge of the side of a small boat.

a. production assets can be used by firms to supply a range of different products that are not demand-side substitutes, and the firms have the ability and incentive to quickly (generally within a year) shift capacity between these different products depending on demand for each, and

b. the same firms compete to supply these different products and the conditions of competition between the firms are the same for each product.[14]

22. The parties note that all the major manufacturers of commercial liferafts also produce leisure rafts as the manufacturing process is broadly the same for both types of rafts. In particular, the parties submit that producers are able to switch production between different marine safety products in response to an increase in price of five to 10 per cent within a relatively short period of time for the following reasons:

    a. regulatory requirements and standards apply to a broad range of marine safety products

    b. most products in the sector use common materials (sourced from third parties) and production techniques

    c. the use of outsourced manufacturing is well-established and new arrangements can be put in place relatively quickly.

23. The parties submitted that it would cost an existing manufacturer of leisure liferafts less than £[300,000-500,000] and take approximately 12 months to establish itself as a manufacturer of commercial liferafts. The parties provided information on an Italian based firm, Arimar, by way of example and argued that the requirement for a servicing network is not a barrier to supply side substitution as all the major manufacturers of leisure liferafts already have such a network. The parties also identified Zodiac that entered the market in the 1990s as an example of how a manufacturer of leisure liferafts can enter the commercial liferaft market easily.

24. The OFT has considered whether the product scope could be widened to include other marine safety products, most obviously leisure liferafts, but

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[14] See Merger Assessment Guidelines, Joint publication of the Competition Commission and the OFT, September 2010, paragraph 5.2.17.

notes that Zodiac is selling its commercial liferaft business, but is retaining its leisure liferaft business. Further, that the regulatory requirements do differ between marine safety products. For example, the OFT understands that there is a legal responsibility placed on the manufacturer under the SOLAS regime to authorise and audit service stations which is not required for leisure life rafts.

25. The OFT notes that Arimar, the example provided by the parties, first started producing SOLAS liferafts in 2005 but did not begin exporting until more recently. The OFT also notes that it currently has less than half the number of service stations that Zodiac has worldwide and has only approved one service station in the UK to undertake its servicing. This would indicate that it takes time to expand a service station network and is unlikely to be achieved to a sufficient magnitude in 12 months. The importance of a global network to a supplier of commercial liferafts was noted by several third parties. The OFT therefore considers that it is more appropriate to consider Arimar under the competitive assessment in terms of new entry rather than expanding the product scope to include both leisure and commercial liferafts.

26. Similarly, the OFT notes that Zodiac established its reputation as a manufacturer of commercial liferafts over a number of years (and required an expansion in its servicing network) rather than within a 12-month period which is typically considered necessary in order to expand the product scope to take account of supply-side substitution.

27. On the basis of this evidence, the OFT considers that the conditions of competition between firms are likely to differ for commercial liferafts compared to other marine safety products, such as leisure liferafts and is not convinced by the parties' arguments on supply-side substitution.

28. The OFT has not, therefore, received sufficient evidence to support the view that leisure liferafts (or other marine safety products) and commercial liferafts are part of the same market, and therefore, considers the appropriate frame of reference on which to examine the transaction as the supply of commercial liferafts.

Distribution[15] and servicing of commercial liferafts [16]

29. The parties submit that the market is the distribution and servicing of marine safety products.

30. The OFT does not consider that there is evidence to indicate that there is sufficient demand-side substitution in the distribution and servicing of marine safety products to consider broadening the product scope for the distribution and servicing of commercial liferafts. The reasons for this are the same as those set out under the 'supply of commercial liferafts' (see paragraphs 17 to 20)

31. The OFT has also considered the scope for supply-side substitution, as set out under paragraph 21 above.

32. The parties note that from a supply-side perspective, the vast majority of distributors and service stations supply and service a range of marine safety products, competing on the basis of the range of marine safety products that they supply and service akin to a 'one stop shop'. The parties also note that the bulk of distributors and service stations distribute and service a range of marine safety products (both leisure and commercial) or could diversify their distribution and servicing within a matter of weeks.[17]

33. The OFT notes the parties' views that distributors and service stations seek to offer a 'one stop shop'; however there is a legal requirement placed on the manufacturers of SOLAS liferafts to authorise and audit their service stations. The OFT considers that this reduces the extent to which the distribution and servicing of commercial liferafts should be seen as comparable, from a supply side perspective, with other marine safety products.

34. The OFT has not, therefore, received sufficient evidence to support the view that distribution and servicing of leisure liferafts (or other marine safety products) and commercial liferafts are part of the same market, and therefore, considers the appropriate frame of reference on which to

[15] 'Distribution' refers to the downstream supply of commercial liferafts to end customers
[16] The Target Business has no sales to the end customer in the UK and does not own any distribution or servicing facilities in the UK.
[17] The parties estimate that it would take less than two weeks to train two service station employees, and an incremental cost of £[1,500-3,000] for an existing leisure liferaft service station to have the full capability to service commercial liferafts.

examine the transaction as the distribution and servicing of commercial liferafts.

Distribution and servicing of commercial liferafts as a bundle

35. The parties also submitted that from a demand-side perspective, servicing is increasingly procured as a bundle with commercial liferafts either as part of a fixed–term contract which includes ongoing service provision within the upfront purchase price or hiring the product with the cost of subsequent servicing included in the hire price. This reflects the fact that the servicing cost of a raft is relatively high compared with the initial purchase cost. As the customer must have its SOLAS approved liferafts serviced in order to comply with marine safety regulations, one of the key factors which determine the brand of equipment that customers choose is the total cost of the product during its life. The parties provided information that showed that the hiring of commercial liferafts, at £[ ] million, now accounts for about a third of total market revenues from distribution and servicing in the UK.

36. Further evidence provided by the parties indicates that there is an increasing trend towards hiring and fixed price servicing agreements (this is discussed further under unilateral effects). Specifically, bidding data provided by the parties indicated that the majority of competitive opportunities in the market relate to hire. This linkage between distribution and servicing was supported by a distributor who confirmed that it was unlikely to stock commercial liferafts if it was unable to also service the liferaft.

37. As a result, although there are some independent non-authorised distributors,[18] the OFT considers that customers tend to consider the whole life cost when purchasing a commercial liferaft and therefore distribution and servicing costs are considered as a bundle rather than separately.

[18] Independent non-authorised distributors include PFC Marine, OTEAC, Ross Survival (annex 1 of the parties' response to the OFT's Issues letter)

The supply, distribution and servicing of MES

Supply[19] of MES

38. The parties submit that the appropriate market is the supply of marine safety products.[20,21]

39. The demand side arguments put forward in relation to the supply of commercial liferafts apply equally to the supply of MES. The OFT has found no reason to aggregate the products into a single product scope on the demand-side, given the complementary nature of the products, and focused on MES on the demand-side as opposed to other marine safety products. In addition, as explained at paragraph 19 above, the OFT considered the extent of demand side substitution between commercial liferafts and MES but considered this to be limited.

40. On the supply side, the OFT considered that, due to the bespoke nature of MES, it was unlikely that firms would have the ability and incentive to shift capacity from the production of other marine safety products to MES. In addition, the OFT considers that the conditions of competition between firms is likely to differ for MES compared with other marine safety products, including commercial liferafts.

41. The OFT therefore considers the appropriate frame of reference on which to examine the transaction as the supply of MES.

Distribution[22] and servicing of MES

42. The parties submit that the market is the distribution and servicing of marine safety products. The Target business has exclusive supply arrangements with two distributors and does not supply MES direct to end customers in the UK. However, the OFT considers that the Target business is an exception and notes that MES is often distributed direct by manufacturers to end customers rather than via distributors (as is typically the case for commercial liferafts in the UK). The OFT therefore considers

[19] 'Supply' refers to the upstream supply by a manufacturer of MES.
[20] The Target Business does not undertake any manufacturing in the UK.
[21] The parties provided separate shares of supply of leisure liferafts, commercial liferafts and MES.
[22] 'Distribution' refers to the downstream supply of MES to end customers.

that it is appropriate to only consider servicing of MES at the downstream level.

43. Similar to the OFT's views in relation to commercial liferafts, the OFT does not consider that there is evidence to indicate that there is sufficient demand-side substitution in the servicing of marine safety products to consider broadening the product scope for the servicing of MES.

44. On the supply side, the OFT notes that MES is more often supplied by the manufacturer than via a distributor due to the bespoke nature of the product. While servicing of MES can be undertaken either by the manufacturer or an independent service station, the OFT considers that due to the bespoke nature of the product, the servicing of MES may require a greater degree of expertise than for other marine safety products. On this basis, the OFT considers that there is limited supply side substitution for MES.

45. The OFT therefore considers the appropriate frame of reference on which to examine the transaction as the servicing of MES.

Conclusion on product scope

46. For the purposes of the competitive assessment, the OFT considers the appropriate frames of reference to be:

    a. the supply of commercial liferafts
    b. the supply of MES
    c. the distribution and servicing of commercial liferafts
    d. the servicing of MES.

47. However, as no competition concerns arise as a result of the transaction, it has not been necessary to conclude on the precise product scope.

Geographic scope

Supply of commercial liferafts and supply of MES

48. The parties submit that the geographic scope for each of commercial liferafts and MES should be at least EEA wide as the regulatory requirements apply EEA-wide and suppliers operate worldwide.

49. The OFT considered whether it was appropriate to adopt a narrower frame of reference, that is the UK, to reflect the fact that there will be some customers that travel in international waters but who are based in the UK. For example, a ferry company that purchases a commercial liferaft or MES direct from a supplier. However, the OFT considers that UK-based customers who purchase commercial liferafts or MES direct from a supplier will be relatively small in number.

50. The OFT therefore considers that a national frame of reference may be unduly cautious, particularly in light of the fact that the SOLAS regulatory requirements relate to international shipping and are applied on an EEA-wide basis. Further, suppliers of commercial liferafts and MES appear to operate worldwide and, in the case of commercial liferafts, it is not unusual for distributors to be supplied by imports as suppliers are based outside of the UK. This is the case in relation to both commercial liferafts and MES for Zodiac which does not have any manufacturing base in the UK. On this basis, the OFT considered that it is appropriate to expand the frame of reference beyond the UK.

51. The OFT has therefore considered the transaction with respect to the supply of commercial liferafts and the supply of MES on an EEA basis but has also had regard to national issues in terms of considering the closeness of competition between the parties.

Distribution and servicing of commercial liferafts and servicing of MES

52. The customers in relation to distribution and servicing are end customers, as opposed to being distributors (who are the customers at the supply level). It is therefore possible that the geographic market may be smaller at this downstream level of the supply chain.

53. There is no prescribed port at which a shipowner is required to obtain servicing of its commercial liferafts. As such, vessels may service their rafts at any location and most commercial vessels which are subject to the SOLAS requirements will have a wide choice of service stations both in the UK and other countries. However, suppliers of MES commented that, not having an option to service MES in the UK would impact on ship owners, both financially and logistically.

54. The parties submit that the market is at least national in scope as service stations typically transport liferafts all over the country for servicing and provided examples in support of this.[23] Further, the parties submit that the increasing trend towards the hiring/swap-out of liferafts means that the relevant geographic scope has broadened as a customer no longer needs to wait for the servicing to be completed before recommencing their journey. The distributor then transports the liferaft to any of its service stations in the UK to carry out the servicing.

55. MES tend to be transported further distances than other types of marine safety products for servicing as transport costs (as a portion of the total cost of servicing of MES) are proportionately lower than for other types of marine safety products and the time available for such servicing also tends to be longer.

56. Nevertheless, the OFT considers that there is likely to be a proportion of customers who will seek a distributor/service station at the port where they are based and therefore a local analysis may also be appropriate.

57. The OFT has therefore considered the transaction with respect to the distribution and servicing of commercial liferafts and servicing of MES on a national basis, but has also had regard to any local issues.

Conclusion on product and geographic scope

58. For the purposes of its competitive assessment, the OFT therefore considers the appropriate frames of reference to be:

a. the supply of commercial liferafts in the EEA
b. the supply of MES in the EEA
c. the distribution and servicing of commercial liferafts in the UK and
d. the servicing of MES in the UK.

59. However, as no competition concerns arise as a result of the transaction, it has not been necessary to conclude on the precise product and geographic scope.

[23] Ocean Safety's service station in Glasgow was closed following a fire in early 2011 and liferafts have been serviced at the Plymouth and Southampton sites.

COUNTERFACTUAL

60. The OFT notes that Survitec is simultaneously seeking to acquire the shares of a number of companies and various assets comprising the marine division of Cosalt plc (Cosalt). Cosalt is a distributor and service agent of Survitec products in the UK.

61. As set out in the OFT's guidance,[24] 'the Authorities may be required to consider a merger at a time when there is the prospect of another merger in the same market (a parallel transaction). For the OFT, the question is, as always, whether the transaction under review creates the realistic prospect of a substantial lessening of competition (SLC), and it is likely to consider whether the statutory test would be met whether or not the parallel transaction proceeds (unless the parallel transaction can clearly be ruled out as too speculative).'

62. In this case, the OFT considers that the relevant question is whether, given the proposed acquisition by Survitec of Cosalt, the addition of the Target Business itself creates a realistic prospect of an SLC.

HORIZONTAL ISSUES

UNILATERAL EFFECTS

63. The OFT has first considered unilateral effects for MES in terms of supply and separately for servicing, and secondly for commercial liferafts separately for supply, and distribution and servicing.

A. MES

Servicing of MES

64. The Target Business is not active in the servicing of MES in the UK and therefore no unilateral effects issues arise in this area. The following sections relate to the supply of MES.

[24] See Merger Assessment Guidelines, Joint publication of the Competition Commission and the OFT, September 2010, paragraph 4.3.25 and 4.3.26

Supply of MES[25]

Shares of supply

65. The parties estimate that post-merger they will have a combined share of supply of [35-45] per cent (with an increment of [zero to five] per cent) in the supply of MES in the EEA, based on value. The parties also provided figures for UK and estimated that post-merger, they will have a combined share of supply of [35-45] per cent (with an increment of [zero to five] per cent) in the supply of MES, based on value.[26] However, the OFT received market data from a third party that raised doubts over the reliability of the parties' estimates regarding the supply of MES in the UK. The third party provided figures for its own supply of MES which were significantly higher than those estimates provided by the parties. Using the third party's own supply figures, the OFT estimates that the total market value for the supply of MES in the UK in 2010 to be £[ ] million. Based on this figure, the parties would have a combined share of supply of less than [10-20] per cent.

66. Taking account of the third party's estimates, the transaction does not raise concerns over unilateral effects. However, the OFT notes that these estimates of shares of supply are based on tenders and there are relatively few in a single year (particularly in the UK) such that shares of supply can vary significantly year on year. The OFT has therefore gone on to consider the closeness of competition between the merging parties and constraints from existing competitors.

Closeness of competition

67. The parties submit that they are not each other's closest competitors in the supply of MES. Survitec has a limited range of MES products. In particular, Survitec:

    a. has a product, know as Marin-Ark which is mainly used by cruise ships carrying more than 2,500 passengers and ferries carrying more than 1,000 passengers, but

[25] The Target Business does not supply MES directly to customers in the UK, instead selling via UK distributors.
[26] The parties provided revised estimates for the supply of MES in the UK which included revenues for spares, certificates and training related to MES. Using these figures, the parties had

b. does not have a product range which is competitive in relation to smaller cruise ships or ferries. The Target Business does however have a range of products suited to this type of customer.

68. This view was largely supported by third parties who also considered that the parties' products complemented each other for MES.

69. The parties also provided bid data for the EEA that indicated that the merging parties are not the closest competitors in the supply of MES. Survitec participated in 19 bid processes for large MES (Marin-Ark systems) in the EU in the last three years; Viking bid in all cases whereas the Target Business was only present in five cases and was not successful in any bid. Similarly, of the 94 MES projects identified by the Target Business in the EU in the last three years, it participated in 85 per cent of cases. Survitec was present in only 25 per cent of cases whereas Viking was present in more than 80 per cent of cases. LSA was identified as a bidder in less than [ ] per cent of cases, although the parties noted that the data may underestimate LSA's participation in the bids.

70. On the evidence available, the OFT does not consider that the merging parties are closest competitors in the supply of MES in the EEA or UK.

Constraints from existing competitors

71. Supply of MES in the UK is small compared to the EEA as a whole and reflects the limited shipbuilding undertaken in the UK. The parties submit that the merged entity will continue to face vigorous competition from Viking and LSA, in the EEA and UK.[27]

72. The OFT considers that post-merger the merged entity will continue to face strong competition from Viking and also LSA in the supply of MES both in the EEA and the UK. The OFT also notes that there are a number of smaller companies which supply MES to customers in the EEA, namely Brude and Fujikura.

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a combined share of supply, based on value, of [30-40] per cent (with an increment of [10-20] per cent) in the supply of MES in the UK in 2010.

[27] The OFT has considered the impact of the Cosalt merger on [ ] – see paragraphs 75 to 82 of the Anticipated Acquisition by Survitec of Cosalt. The OFT believes that [ ] will continue to provide a competitive constraint on the merged entity going forward.

Ease of switching

73. End customers for MES are shipyards (in the case of new build vessels), cruise lines, ferry companies and operators of passenger vessels. In the UK, the main customers are ferry companies and operators of smaller passenger vessels. Due to the bespoke nature of fitting MES,[28] it is expected that switching (other than for a refit) is rare once the contract has been awarded.

Barriers to entry and expansion

74. The OFT has not needed to examine the barriers to entry into the supply of MES given its view that competition concerns do not arise.

Conclusion on unilateral effects in supply of MES

75. On the basis of the information received, the OFT considers that the increment caused by the merger at EEA level is limited. In the UK, information received indicates that the parties' share of supply may be particularly small. Further, due to the different types of MES systems the merging parties supply, the OFT does not consider Zodiac to be Survitec's closest competitor. This is supported by the bidding data provided by the parties that indicates that Viking is considered to be Survitec's closest competitor. The OFT considers that the parties, post merger, will be sufficiently constrained by Viking and LSA to prevent a substantial lessening of competition in the supply of MES. As a result, the OFT considers that the evidence available to it does not point to a realistic prospect of an SLC in the supply of MES in the EEA (or UK).

B. Commercial liferafts

Distribution and servicing of commercial liferafts

76. The Target Business is not active in the distribution and servicing of commercial liferafts in the UK and therefore no unilateral effects issues arise in this area. The following sections relate to the supply of commercial liferafts.

[28] For example, elements of the system may need to be designed to allow the MES to be stored and launched in the space available on board a particular vessel.

Supply of commercial liferafts

Shares of supply

77. The parties estimate that post-merger they will have a combined share of supply of [35-45] per cent (with an increment of [five-10] per cent) in the supply of commercial liferafts in the EEA, based on value. The parties also provided figures for UK and estimated that post-merger, they will have a combined share of supply of [50-60] per cent (with an increment of [20-30] per cent) in the supply of commercial liferafts, based on value.

78. Third parties broadly confirmed these figures with regard to commercial liferafts, although one third party commented that there is a lack of reliable data with which to estimate UK shares of supply.

79. Viking will remain the merged parties' strongest competitor post merger; it currently has an estimated share of supply of commercial liferafts of [25-35] per cent in the EEA and of [30-40] per cent in the UK, based on value. There are also a number of manufacturers based in the Far East, namely, Youlong (Seasafe) and CSM, who are active in the EEA market and have higher or equivalent market shares to Zodiac at around [five-15] per cent, based on value. At present, these Asian-based manufacturers have lower shares of supply in the UK than they do in the EEA.

80. The parties' share of supply figures for commercial liferafts are sufficiently high to give the OFT prima facie cause for concern over potential unilateral effects such as to warrant further examination.

Closeness of competition

81. Where products are differentiated, for example by branding or quality, unilateral effects are more likely where the merging firms' products compete closely. This includes situations where the parties are often amongst the leading candidates for the award of supply contracts.

82. The parties supply a number of branded liferafts[29] but the parties clarified that there is little differentiation between the different brands. Nevertheless they argue that their closest competitor is Viking in the EEA and UK. Both

[29] Survitec's main brand in the UK is RFD; other brands include DSB, Beaufort, Toyo, Eurovinil. Zodiac's brands include Zodiac Solas and DBC.

Viking and Survitec outsource the manufacture of their liferafts to Far Eastern manufacturers and are seeking to expand their in-house distribution and servicing networks. In addition, over the past year, both Survitec (RFD) and Viking have introduced leasing programs with ship owners.

83. Third parties consider the parties' products to be close substitutes. For example, during the investigation, the OFT was told that larger customers will have different brands of liferafts on their ships including Survitec and Zodiac rather than only using a single brand. This was confirmed by the parties who provided further examples of large customers who multi-source commercial liferafts from a number of manufacturers including Wilhelmsen and Youlong (Seasafe) as well as Survitec, Zodiac and Viking. As such, the parties submit that as all brands can be found on the same vessel and are for the same purpose, all are equally close substitutes such that Zodiac is no closer a substitute to Survitec than Youlong.

84. The parties also provided bidding data (which is discussed further below) that indicates that distributors who sell and service the brands produced by Asian manufacturers are providing a stronger competitive constraint on Survitec than distributors who sell the Zodiac brand.

85. Although the evidence in this respect is mixed, the OFT considers that there is some evidence that Survitec and the Target Business are not each other's closest competitors in the EEA or UK.

Constraints from existing competitors

86. Third parties raised concerns that the merger will further strengthen Survitec's already strong position in the market. The merger will result in the parties supplying over [35-45] per cent of commercial liferafts in the EEA.

87. The parties, however, argue that the merged entity will continue to face vigorous competition from Viking, CSM, Youlong (Seasafe), Wilhelmsen[30] and other suppliers. Viking, which is active across the board of sale, hire and servicing of liferafts is particularly active in offering the option of hire and fixed price servicing.

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[30] Wilhelmsen sells commercial liferafts under the 'Unitor' brand.

88. The parties provided bidding data for 2009-2011 to show the extent of inter-brand switching by end-customers at the downstream distribution level of the market. The parties note that due to the limited shipbuilding undertaken in the UK, customers typically purchase commercial liferafts from distributors and service stations and therefore consider that the bidding data at the distribution level may provide an indication of competition between brands at the supply level.

89. The OFT considers that there are limitations on the extent to which this data can provide useful inferences about the competitive constraints between brands at the supply level. The OFT notes that:

    a. the data has not been independently collected and therefore may contain certain biases and

    b. the data has been collated by a limited number of service stations and therefore does not provide an industry wide review.

90. Whilst the OFT does not consider that the data can be relied upon to provide an accurate assessment of the totality of the competitive constraints at the supply level, it may provide some indication of the strength of the Asian brands at least in the UK market.

91. The bid data suggests that distributors of both Viking and Zodiac are active and strong competitors against Survitec, competing in approximately a third of tenders and wining a significant number of them. However, Viking's distributors are winning over 50 per cent of the tenders it participates in while Zodiac's distributors are only winning 30 per cent. Despite a number of customers choosing to remain with the Viking brand, there is evidence of strong price competition determining the outcome of these tenders. For example, in 47 per cent of the tenders Viking has won on price.

92. Further, the bid data indicates that the distributors of CSM and Youlong (Seasafe) are becoming increasingly active in the UK market as they seek to build share of supply in the UK from a stronger European base. In contrast, the number of bids where Zodiac commercial liferafts have competed with those of Survitec has remained relatively static.

93. The parties submit that CSM, Youlong (Seasafe), Fujikura and Samgong compete aggressively on price. The bid data show that distributors[31] of these brands have bid against those of Survitec in over a third of cases (as many as Zodiac) and have been successful in the majority of the cases they participated in. Whilst many of these contracts may be relatively small in value, the OFT considers that the increasing competitive constraint placed on Survitec by these brands may reflect changes in the dynamics of competition in the sector as these manufacturers become successful in building their shares of supply in the UK. Further, the parties provided evidence to indicate that some of these competing manufacturers are seeking to expand their servicing network in the UK and Europe.[32] The presence of these brands has been particularly evident in relation to hire contracts (and is discussed further under 'ease of switching' below).

Ease of switching

94. Third parties contacted during the investigation indicated that once a brand of commercial liferaft is fitted on a new vessel by the ship builder, it is unusual to switch to an alternative brand during the lifetime of the vessel due to the associated costs, for example, the cost of changing the retaining cradle. However, the parties provided examples to show that cradles do not necessarily need to be replaced or if they are, their cost is relatively small and therefore does not represent a barrier to switching. The parties also clarified that there is a move to a more standardised cradle which removes the need for changing it in the majority of cases.

95. The parties submit that it is relatively easy to switch commercial liferaft brands as they are manufactured in the same size and formats and provided evidence of this. Between 2009 and 2011, the parties' bidding data indicated that over [ ] of contracts with their distributors involved the customer switching the brand of commercial liferaft as well as service station.

96. The parties submit that the option of hiring liferafts has further reduced the barriers to switching and that this option now accounts for over [ ] of the revenues from the distribution of commercial liferafts. The parties argue

[31] The Distributors identified were Blue Anchor (CSM), Norwest Marine (Seasafe), Denholm Fishselling (CSM), Liferafts International (Fujikura).
[32] See www.areamoura.com/html/estaciones_ingles.htm

that the presence of 'buy back and hire' schemes mean that customers are not 'locked in' to the manufacturer authorised service stations for their servicing needs. The parties provided specific examples to demonstrate that customers will swap out liferafts from ownership to hire in year one due to the pricing benefits (that is, lower, more predictable costs) and flexibility provided by hire arrangements.[33]

97. The parties submitted that their bid data indicates that [35-45] per cent of contracts (in terms of volume) involved the customer switching away from ownership to hire. Furthermore, the parties submitted that the vast majority of customers enter into the hire agreement with the service station for a one year period.[34] The OFT notes that service agreements direct with manufacturers may be for longer periods, for example, Viking's Shipowner Agreement is for a five-year period. However, the parties provided additional evidence[35] to show that there is strong competition between Viking and Survitec to win customers prior to the end of the contract period.

98. The OFT therefore considers that hiring offers customers an alternative option to purchasing a commercial liferaft and appears to have a strong impact on the existing dynamics in the supply market as customers switch their brands of liferafts.

Some third party concerns

99. Some third parties expressed doubts that the Asian manufacturers will be able to effectively compete with the merged entity and Viking post-merger because these smaller competitors do not have an existing relationship that large European manufacturers have with ship builders and shipowners. However, the OFT notes that Europe now accounts for less than 15 per cent of new build vessels, which contrasts with Asian shipyards which now account for approximately 85 per cent of new build vessels worldwide.[36] Whilst, there may be some regional bias in favour of European built ships being serviced in Europe, the OFT does not consider that the existing relationships with ship builders or owners will act as a barrier to

[33] [ ] both decided to switch to hire even though the liferafts were less than one year old.
[34] Some [ ] per cent of Cosalt's hire fleet is subject to annual agreements and in the case of Seaweather, [ ] per cent of its fleet is subject to annual agreements.
[35] See parties' response to the OFT's Issues letter, paragraph 8.2 and footnote 60.

expansion by Asian manufacturers in the supply of commercial liferafts in the EEA.

100. The OFT also considered whether low cost competitors operate a different business model, with their focus on the supply of smaller capacity rafts of six to 25 persons or have limited after sales service. However, the OFT was told that these smaller size liferafts account for [ ] per cent of the parties' sales in the UK. The OFT notes that Survitec and Viking have a degree of vertical integration, and considered whether this gives them a significant advantage in competing for contracts that involve long term servicing of commercial liferafts. However, the OFT notes that Zodiac does not operate an integrated servicing network and this does not appear to have prevented Zodiac from increasing its share of supply in the EEA or UK.

101. As such, post-merger, customers will be faced with a choice of manufacturers for the supply of commercial liferafts in the EEA and UK. The OFT therefore considers that, to the extent that it has sought to characterize the market in terms of the nature of active and significant suppliers, the merger represents, at worst, a reduction from 'five to four' in suppliers of commercial liferafts. Based on the evidence available, the OFT considers that the merged entity will be constrained from raising prices post merger by competition from distributors of Far Eastern brands of commercial liferafts as well as from Viking.

Barriers to entry and expansion[37]

102. Third parties have argued that it is very difficult in terms of cost and time to begin supplying commercial liferafts in the UK. One third party commented that the cost of development and testing would run into millions of pounds; another third party estimated £3 million. In addition, third parties indicated that a manufacturer would have to set up a worldwide distribution and service network and that it may be difficult to

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[36] The parties submit that commercial liferaft manufacturers such as CSM, Youlong, Samgong, CRV and others have excellent relations with the Asian shipyards.

[37] When assessing barriers to entry and expansion, the OFT will consider whether entry and expansion is (i) timely, (ii) likely, and (iii) sufficient. In terms of timeliness, the guidance suggests that the OFT will look for entry to occur within two years (See Merger Assessment Guidelines, Joint publication of the Competition Commission and the OFT, September 2010, paragraph 5.8.3).

find an independent distributor with sufficient capacity which is not exclusive to Survitec or Viking.

103. The parties do not accept that the cost of entry into the UK would be millions of pounds. The parties estimate that it would cost an existing manufacturer of leisure liferafts less than £[300,000-500,000] and take approximately 12 months to establish itself as a manufacturer of commercial liferafts. This takes account of the redesign process, sourcing of materials, third party testing and approvals process and marketing. The parties submit that a leisure liferaft manufacturer would expect to see returns on its investment within 18 months to two years.

104. The parties point to the entry by low cost Asian manufacturers[38] in to the UK and EEA as evidence of an absence of significant barriers to entry. Whilst these suppliers have low shares of supply in the UK, they have a comparable share of supply to Zodiac in Europe. The parties provided evidence in support of their view that low cost Asian manufacturers are increasing their servicing network worldwide, including Europe. The parties also identified a new European-based entrant, Arimar, that has expanded from the supply of leisure liferafts into commercial liferafts.

105. The parties also note that Wilhelmsen, which supplies commercial liferafts under its 'Unitor' brand, has a white-label arrangement with Survitec and directly with an Asian manufacturer. This white-label arrangement would be another possible means by which potential new entrants may seek to enter the market and would minimise any entry costs as a new entrant would not need to have to establish its own manufacturing facility prior to production.

106. Evidence on barriers to entry is mixed with the need to establish an international servicing network appearing to be the most significant barrier. As a result, producers of leisure liferafts, who already have some form of servicing network, may be best placed to expand into the supply of commercial liferafts as both Zodiac and, more recently, Arimar appear to have done. However, given that the OFT has no concerns that a substantial lessening of competition will arise as a result of the merger, it has not been necessary to conclude on barriers to entry.

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[38] The parties identify a Chinese manufacturer, CRV, as the most recent entrant into the UK market following the authorisation of Premium Liferaft Services as a service station.

Conclusion on unilateral effects in supply of commercial liferafts

107. On the basis of the evidence available, the OFT considers that the parties post merger will be sufficiently constrained to prevent a substantial lessening of competition in the supply of commercial liferafts. Viking is considered to be Survitec's closest competitor. Also, based on share of supply data provided by the parties at EEA level, Youlong and CSM have greater and closer shares of supply to Survitec than Zodiac; suggesting that Zodiac may not be considered to be a closer competitor of Survitec than CSM or Youlong (Seasafe) at the EEA level. Whilst this is not currently reflected in the share of supply figures at the UK level, bidding data provided by the parties indicates that, at the distribution level, brands produced by manufacturers based in the Far East are providing an increasing competitive constraint on the merging parties and this is expected to continue post-merger. Specifically, the increasing demand by customers for hiring or fixed price servicing contracts of relatively short periods should facilitate an increase in switching between brands.

108. As a result, the OFT considers that the evidence available to it does not point to a realistic prospect of a SLC in the supply of commercial liferafts in the EEA (or UK).

CO-ORDINATED EFFECTS

A. MES

109. During the investigation, the OFT did not receive any evidence suggesting that there is existing co-ordination between suppliers in the supply of MES. However, taking account of the proposed acquisition by Survitec of Cosalt, the OFT has considered whether the merger could make it more likely that co-ordination between suppliers of MES will take place going forward.

110. The OFT considers that three conditions must be satisfied for co-ordination to be possible.[39] First, firms need to be able to reach and maintain the terms of co-ordination. Secondly, co-ordination needs to be internally sustainable. And thirdly, co-ordination needs to be externally sustainable.

[39] See Merger Assessment Guidelines, Joint publication of the Competition Commission and the OFT, September 2010, paragraph 5.5.9.

111. It is difficult to make inferences regarding symmetry between suppliers in terms of shares of supply due to the difficulties in obtaining robust estimates. However, the OFT notes the lack of symmetry regarding the degree of vertical integration between the main suppliers of MES and hence it is unclear whether all suppliers will have the ability to reach and maintain the terms of co-ordination.

112. Co-ordination will only be sustainable where the additional profit from co-ordination is sufficiently high, and there is an effective mechanism to punish deviation. The OFT notes that switching is limited and hence there is not the repeated interaction (particularly if servicing costs are included in the initial contract price) that may facilitate monitoring or provide the ability to punish one party in the event of deviation from an agreed strategy.

113. Lastly, in respect of external stability, the OFT considers that co-ordination would be unsustainable in the face of countervailing buyer power (which is discussed below). The OFT also notes that no concerns have been expressed by third parties about the impact of the merger in terms of the possibility of co-ordinated effects in the supply of MES.

114. On the evidence available, the OFT does not consider that this merger will create the conditions for co-ordinated behaviour.

B. Commercial liferafts

115. During the investigation, the OFT did not receive any evidence suggesting that there is existing co-ordination between suppliers in the supply of commercial liferafts. However, taking account of the proposed acquisition by Survitec of Cosalt, the OFT has considered whether the merger could make it more likely that co-ordination between suppliers of commercial liferafts will take place going forward.

116. The OFT has considered the three conditions that must be satisfied for co-ordination to be possible (as set out in paragraph 110) in turn.

117. In terms of the ability to reach and monitor a co-ordinated outcome is concerned, the OFT observes that the merger will not result in increased symmetry in terms of the share of supply between Survitec and Viking. In fact, the merger will result in a differentiation in terms of shares of supply (as the merged entity that currently has similar shares of supply to Viking

at both EEA and UK level would become larger in size). Both firms operate a partially vertically integrated business model, although the number of owned service stations may vary between countries. The OFT notes that Survitec will become vertically integrated to a greater extent as a result of the acquisition of Cosalt within the EEA and UK.

118. The OFT notes that the product ranges offered by Viking and the merged entity are considered to be similar in the supply to ship builders/owners and there is a degree of price transparency due to the publication of price lists and feedback from customers to allow competitors to monitor each other's behaviour. However, the parties submitted that while price lists are provided to distributors, Survitec and Viking have no distributors in common and moreover, discounts to such price lists are not published. Due to a mix of evidence, it is unclear whether suppliers will have the ability to reach and maintain the terms of co-ordination.

119. Co-ordination will be sustainable only where the additional profit from co-ordination is sufficiently high, and there is an effective mechanism to punish deviation. The OFT notes that the only likely monitoring mechanism appears to be in the form of bidding for a number of contracts, albeit of varying sizes, over time, rather than a single 'winner takes all' contract very occasionally. This repeated interaction may provide an ability for one party to punish the other in the event of deviation from an agreed strategy.

120. However, in respect of external stability, it is doubtful whether Survitec/Zodiac and Viking would be able collectively to exercise a degree of market power. Rivals based in Asia appear to be challenging the established European suppliers by competing aggressively on price, and the option of hiring is further reducing the barriers to customers switching brands of commercial liferafts. The OFT also considers that there is a degree of countervailing buyer power (which is discussed further below) that would also affect the stability of any co-ordination.

121. Finally, the OFT notes that no concerns have been expressed by third parties about the impact of the merger in terms of the possibility of co-ordinated effects in the supply of commercial liferafts. On the evidence available, the OFT does not consider that this merger would create the conditions for co-ordinated behaviour.

NON-HORIZONTAL ISSUES – VERTICAL ISSUES

122. The OFT has considered whether vertical concerns could arise in respect of the merger. Vertical concerns are potentially relevant in terms of commercial liferafts (where both parties are present upstream in terms of supply, but Survitec is also present downstream through Seaweather and will have additional presence as a result of its acquisition of Cosalt). The merger does not raise any vertical concerns in relation to MES, however, given that the OFT has found that competition concerns do not arise in relation to the supply of MES as a result of the merger and the Target Business did not distribute or service MES of other MES suppliers prior to the merger. The analysis below therefore focuses in relation to vertical concerns arising in relation to commercial liferafts.

123. The SOLAS regime requires the manufacturer of SOLAS liferafts to authorise and audit its service stations. During the investigation, some concerns were raised that third parties may be foreclosed by the merged entity by removing authorisations to service its commercial liferafts. The OFT therefore considered if the parties have the potential to foreclose competing distribution and service companies. Specifically, the theory of harm considered by the OFT would be that the merger allows the parties to remove approval to service its liferafts from third parties so that they will no longer be able to compete in the provision of these services with the parties' distributors,[40] which would reduce choice for customers and would allow the parties to be able to profitably raise prices.

124. The parties submitted that there is a potential vertical relationship between the parties on the basis that the Target Business produces commercial liferafts and Survitec distributes and services commercial liferafts along with its other marine safety products (through its Seaweather operations). However, Survitec considers that there is no risk of foreclosure as a result of the transaction and states that [ ]. Nevertheless, Survitec goes on to consider the effect of integrating the distribution and servicing functions in house. The parties argue that the effect on the Target Business' existing distributors – and the downstream distribution and servicing activity – will be limited. This is explored further below.

[40] Manufacturers of SOLAS liferafts may establish their own service stations or authorise independent third parties.

125. In assessing the likelihood of such a foreclosure strategy resulting from the merger, the OFT considers in turn the ability of the parties to foreclose rivals at the distribution and servicing level, for example by raising prices or refusing to supply them; the incentive to engage in such a strategy; and the effect on competition in the foreclosed market of such action.[41]

Ability to foreclose

126. As explained above, commercial liferafts can be serviced only by persons authorised to do so by the manufacturer of the particular product. During the investigation, the OFT has become aware of manufacturers withdrawing their approval of independent third parties to service their liferafts. [ ] ,[42] [ ]. However, the OFT's concerns remain as third parties have indicated that when Survitec has previously acquired brands of commercial liferafts, authorisations for servicing these brands have been withdrawn.

127. The parties submitted[43] that the merged entity's ability to foreclose is limited as the customer relationships and agreements are between the service station and the end customer and notes that currently the Target Business has no direct sales in the UK.

128. The OFT is of the view that the parties have the ability to prevent third parties from competing in the servicing of their own commercial liferafts through withdrawal of the relevant SOLAS authorisation. To some extent, this could be considered as being equivalent to the ability to foreclose (in so far as service stations, and in practice therefore distributors, are unable to operate without the required authorisation).

129. However, the OFT notes the existence of a number of alternative commercial liferaft suppliers to whom third party distributors could potentially turn for authorisation in the event that their license were withdrawn by the merging parties: see paragraph 93 above. To this extent, although the parties may have the ability to foreclose distributors and service stations from operating in relation to the Survitec and Zodiac brands, this would not stop them from operating in relation to the

[41] See Merger Assessment Guidelines, Joint publication of the Competition Commission and the OFT, September 2010, section 5.6
[42] See Project Alpha Commercial Due Diligence report 9 March 2011, page 128.
[43] See the parties' supplementary submission on commercial liferafts of 18 July 2011.

distribution and servicing of commercial liferafts given the existence of alternative supply brands to who they could feasibly turn.

Incentive to foreclose

130. The parties submitted that the merged entity would not have the incentive to foreclose service stations which currently service Survitec or the Target Business' liferafts because it would result in a significant loss of liferaft sales and related service revenues as a result of:

a. a service station's ability to substitute the parties' products with other manufacturers' products
b. the availability of liferaft hire, and
c. the negative impact on the parties' brands.

131. The OFT notes the parties' arguments. However, the extent to which the parties may have an incentive to foreclose is largely determined by the trade off between those profits lost in the sales to distributors as a result of withdrawing approval and the profits gained from offering servicing in-house won as a result of foreclosing rivals.[44]

132. [ ][45] [ ].[46] Further, the OFT understands that Survitec is seeking to offer a 'one stop shop' for the supply, distribution and servicing of marine safety products and therefore, it is argued, has an incentive to restrict supply of Survitec products to third party distributors.

133. Evidence provided by the parties on switching indicates that a service station would be able to substitute the parties' products with those of another manufacturer. As evidenced by the discussion on unilateral effects (see above), there would be a number of remaining manufacturers, whose products distributors could stock. Further, as noted earlier, some of these manufacturers are currently seeking to expand their servicing network.

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[44] It could be argued that the parties' incentives to foreclose specific service stations may be stronger where the parties would be present themselves. As a result, even if the parties did not have an incentive to foreclose nationally, they may have an incentive to do so locally. The OFT observes that the parties will, as a result of the acquisition of Cosalt, have 12 service stations in the UK which should provide sufficient capacity to bring all servicing of Survitec and Zodiac branded commercial liferafts in-house.
[45] Annex 14 Zodiac Solas Business Strategy July 2010. Page 8.
[46] In 2010, Survitec's margin for the supply of commercial liferafts to distributors was [ ] per cent and [ ] per cent for servicing.

134. Whilst the OFT considers that the loss of any sales to the parties would be spread over a certain period of time as distributors take time to market their new brand of commercial liferaft, the evidence provided by the parties on switching suggests that the loss of sales is feasible. As a result, it is unclear to what extent the parties have an incentive to foreclose distributors if these distributors can turn to alternative manufacturers in order to retain sales.

Effect of foreclosure

135. In addition to considering the ability and incentive to foreclose, the OFT has considered the effect of a foreclosure strategy on the downstream commercial liferaft distribution and servicing market. The OFT considered the effects of such a foreclosure strategy downstream both on inter-brand competition for the distribution of commercial liferafts and intra-brand competition for servicing of Zodiac branded commercial liferafts.

136. The parties submit that foreclosure of rivals downstream (in terms of the withdrawal of their ability to service Survitec and Zodiac branded liferafts) would not result in anti-competitive effects as the service stations will continue to offer the commercial liferafts of other manufacturers and to compete through the offer of buy-back and hire schemes. In this respect, the OFT notes that Ocean Safety, which is a major distributor of leisure liferafts, ceased distributing Survitec's DSB leisure liferaft and replaced it with a Chinese-manufactured leisure liferaft which it sells under its 'Ocean' brand.

137. The OFT considers that at the supply level, there will be a number of competing suppliers of commercial liferafts, the products of which a distributor will be able to stock. As a result, any foreclosure at the distribution level is not expected to lead to a substantial lessening in competition as customers will continue to have a choice of commercial liferafts.

138. To the extent that the OFT were to consider intra-brand competition for servicing (that is, for those customers that have already acquired a Survitec or Zodiac commercial liferaft for which they require servicing), the OFT considers, as discussed above under unilateral effects, the parties' ability to increase prices will be constrained by the availability of hire options and fixed price contracts which will enable switching to an alternative brand of

commercial liferaft. Accordingly, as customers appear to take into consideration the cost of service when they decide to purchase a commercial liferaft, Survitec would have little incentive to increase its distribution and servicing prices.

139. Further, the OFT considers that the barriers to entry into distribution and servicing are low; the parties estimate that it would take less than two weeks to train two service station employees, and an incremental cost of £[1,500-3,000] for an existing leisure liferaft service station to have the full capability to service commercial liferafts. It is therefore expected that, post-merger, customers will have an expanding choice of service stations offering a number of competing brands.

140. On the basis of the evidence available, the OFT does not consider that the merger creates a realistic prospect of a SLC in relation to foreclosure of competing third party distributors and service stations of commercial liferafts.

BUYER POWER

141. The parties submit that manufacturers of MES often supply end customers directly. Customers include shipyards (in the case of new build vessels), cruise lines, ferry companies and operators of passenger vessels. In the UK, the main customers are ferry companies and operators of smaller passenger vessels. The OFT considers that these customers will have a degree of countervailing buyer power in relation to the purchase of MES and this was indicated in the responses from some third parties.

142. In relation to commercial liferafts, the parties submit that their direct customers for commercial liferafts are distributors or, in some cases, shipyards or operators of commercial passenger vessels and, as such, are relatively sophisticated and able to compare prices between different manufacturers and where appropriate, engage in a tender process. However, the responses from third parties were mixed. One third party indicated that they considered that they did have buyer power but this was not typical across all customers. Further, there is no evidence to suggest that any purchasing power on the part of larger customers would also benefit smaller customers.

143. In response, the parties provided examples that customers can and do use procurement processes to increase their buyer power, for example, in 2008, [ ]. The parties also provided evidence of smaller customers entering into joint purchasing agreements in order to gain negotiating strength. The parties consider that with the increasing trend towards hire and fixed price servicing, individual customer's negotiating strength will improve as customers will more easily be able to compare prices and switch demand between service stations and hence the manufacturer.

144. The OFT therefore believes that there may be a degree of countervailing buyer power enjoyed by customers in these markets, albeit that its strength will vary amongst customers.

THIRD PARTY VIEWS

145. The OFT received comments from customers (end customers and distributors) and competitors of the parties. Third party views have been discussed in other parts of the decision where appropriate.

146. A number of end customers raised concerns regarding the merger, specifically noting that there are a limited number of manufacturers of commercial liferafts. This reflects doubts expressed by some customers as to whether the Asian-based manufacturers can compete effectively with the merged entity post-merger. These concerns have been addressed under unilateral effects. On an EEA basis, the Asian-based manufacturers have an equivalent share of supply to that of Zodiac and whilst this may not yet be replicated at the national level, there is sufficient evidence to indicate that the Asian-based manufacturers are a more competitive constraint than their share of supply would suggest and this is expected to grow with the increased demand from customers for hiring options.

147. Concerns were also expressed regarding the potential reduction in the choice of service stations post merger for commercial liferafts. However, the OFT considers that customers do consider the whole life cost when purchasing a commercial liferaft and this is reflected in the increasing trend of customers favouring the hiring or fixed cost servicing options. The OFT considers barriers to entry into servicing are relatively low and it is expected post-merger that customers will continue to have a choice of service stations offering a number of different brands of commercial liferafts.

148. Distributors expressed concerns about increased concentration in the supply of commercial liferafts leading to the closure of service stations, specifically those currently authorised to service Zodiac commercial liferafts. However, as explained under unilateral effects, the OFT considers that there is sufficient choice of branded commercial liferafts and therefore distributors will be able to stock and service an alternative brand of liferaft replacing the competitive constraint lost by this merger.

149. Comments received from competitors were mixed with some expressing concern that the merger will limit customer choice. However, others considered that whilst the merger would result in the loss of a strong, independent brand of Zodiac, it was noted that competition from Chinese manufacturers is forcing European manufacturers to reduce prices. The shift by customers in favour of hiring rather than purchasing commercial liferafts was also noted.

150. Overall, third party views were mixed. However, as discussed above, on a European basis, other manufacturers have been identified at the supply level and are expected to provide a strong competitive constraint on the merged entity post merger which will also be apparent at the distribution level.

ASSESSMENT

151. The parties overlap in the supply of marine safety products. Given the overlaps between the parties, the OFT's investigation focused on the supply of commercial liferafts and MES in the EEA and the UK.

152. In relation to the supply of MES, the parties estimate that they will have a combined share of supply, based on value, of [35-45] per cent (with an increment of [zero to five] per cent) in the EEA. In the UK, they estimate their combined share, based on value, will be [35-45] per cent (with an increment of [zero to five] per cent). However, the OFT notes that estimates based on third party information would give the parties a combined share of supply in the UK of less than [10-20] per cent.

153. In relation to MES, the OFT does not consider the parties to be the closest competitors as the parties' products are not strong substitutes. Survitec

does not have a product range specific to smaller cruise ships or ferries. In contrast, the Target Business does have a range of products suited to this type of customer. This was confirmed by third parties. The OFT considers that the constraint represented by existing suppliers, notably Viking and LSA, will be sufficient for the merger not to raise unilateral competition concerns in relation to the supply of MES in the EEA or UK.

154. In relation to the supply of commercial liferafts, the parties will have an estimated combined share of supply of [35-45] per cent (with an increment of [five-10] per cent) in the EEA, based on value. However, in the UK the parties' estimated combined share of supply of commercial liferafts is higher at [50-60] per cent (with an increment of [20-30] per cent), based on value. On the basis of the share of supply data, Viking is (and will remain post-merger) the parties' most significant competitor.

155. In addition to Viking, it is expected that the parties will continue to face a competitive constraint from Asian-based manufacturers. It is notable that at a European level, Youlong (Seasafe) and CSM have higher or equivalent shares of supply to those of the Target Business at [five-10]-[10-20] per cent. The parties provided UK bidding data which indicated that those distributors of Asian-based manufacturers are competing strongly and successfully with Survitec's distributors. The OFT considers that, as switching costs are relatively low, Asian-based manufacturers will continue to expand their share of supply in the UK and EEA. In addition, the increasing trend by customers in favour of hiring is expected to further reduce barriers to switching.

156. As a result, the OFT does not consider that the merger raises unilateral competition concerns in relation to the supply of commercial liferafts in the EEA or UK.

157. The OFT considered the potential for co-ordination between suppliers of each of MES and commercial liferafts post-merger. However, for the reasons given above, the OFT did not consider that the merger would increase the prospects for co-ordination in the future. In particular, the OFT found that rival Asian manufacturers compete aggressively on price and would have the capacity to disrupt any co-ordination.

158. During the investigation, some concerns were raised by third parties that distributors and service stations of commercial liferafts may be foreclosed

by the merged entity by removing authorisations to service its commercial liferafts. The OFT therefore considered whether the parties have the potential to foreclose competing distribution and service companies. The OFT noted that, even if the parties were to remove the Survitec or Zodiac authorisation to service their brands of commercial liferafts, competing distributors and service stations would have a number of alternative, credible suppliers of commercial liferafts to whom to turn. In addition, there would remain a strong competitive constraint from Viking. In this respect, evidence on switching by customers between brands would suggest that any attempt by the parties to increase prices for servicing would be defeated by customers switching to alternative brands and/or choosing to hire their commercial liferafts. The OFT therefore does not consider that the merger creates a realistic prospect of a SLC in relation to foreclosure of competing third party distributors and service stations of commercial liferafts.

159. Consequently, the OFT does not believe that it is or may be the case that the merger may be expected to result in a substantial lessening of competition within a market or markets in the United Kingdom.

DECISION

160. This merger will therefore not be referred to the Competition Commission under section 33(1) of the Act.

ENDNOTES

1. With reference to footnote 5, the parties clarified that commercial vessels will require a commercial marine liferaft depending on size and type of vessel rather than location in inland or coastal waters. This clarification has no impact on the OFT's conclusions in this case.

2. With reference to paragraph 82, Viking clarified that it has not out-sourced the manufacture of its liferafts to Far Eastern manufacturers but has opened a factory in Thailand that it manages and operates on the same basis as its facilities in Europe. This clarification does not impact on the OFT's conclusions in this case.

3. With reference to paragraph 136, Ocean Safety clarified that it continues to sell Survitec's DSB leisure liferaft, albeit in very small quantities. Further, Ocean Safety clarified that it designed its own leisure liferaft range which it manufactures at Southampton in the UK. This clarification does not impact on the OFT's conclusions in this case.