

Completed acquisition by Go-Ahead Group plc of Arriva plc's Horsham (West Sussex) business

**ME/4248/09**

The OFT's decision on reference under section 22(1) given on 16 November 2009. Full text of the decision published on 24 November 2009.

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**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. **Go-Ahead Group plc** (Go-Ahead) is one of the UK's largest train and bus operators. It is the parent company of **Metrobus Limited** (Metrobus), a supplier of local bus services in the south of England.
2. **Arriva plc** (Arriva) is another of the UK's large bus and train operators. Arriva plc's subsidiary company, Arriva West Sussex Limited, operates local bus services in West Sussex in the south of England.

## **TRANSACTION**

3. On 3 October 2009, Metrobus acquired Arriva's bus interests in Horsham, West Sussex which was being operated by Arriva West Sussex Limited (the Acquired Business). The Acquired Business included staff, 19 buses and supplementary assets (for example, ticket machines, vehicle spares and workshop equipment). The Acquired Business had a turnover of approximately £2.5 million in the year ending 31 December 2008.

## **JURISDICTION**

4. The OFT considers that the Acquired Business constitutes an enterprise within the meaning of section 129 of the Enterprise Act 2002 (the Act). As

a result of this transaction Go-Ahead and the Acquired Business have ceased to be distinct.

5. The parties overlap in the supply of local bus services and the share of supply test in section 23 of the Act is met with respect to tendered bus services in West Sussex (where the parties estimated that together they account for around 29 per cent<sup>1</sup>).
6. The OFT therefore believes that it is or may be the case that a relevant merger situation has been created.
7. The statutory deadline in this case is 2 February 2010 and the OFT's administrative deadline is 17 November 2009.

## **MARKET DEFINITION**

8. Go-Ahead and the Acquired Business overlap in the supply of local bus services (both commercial and tendered) within Horsham and surrounding areas.

### **Product scope**

9. In previous merger investigations involving passenger transport, the OFT has tended to focus on the competitive effects of the merger rather than specifically defining the appropriate relevant market.<sup>2</sup> In practice this has meant considering the competitive constraints on different transport modes on a flow-by-flow basis and, where relevant, an analysis of network effects (if any) in order to determine whether the merger may provide an incentive to increase fares or reduce service levels. The OFT has taken the same approach in this case and therefore it has focused directly on the competitive constraints removed by the merger.<sup>3</sup>

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<sup>1</sup> Based on number of buses.

<sup>2</sup> For example, in Completed acquisition by Stagecoach Group plc of Eastbourne Buses Limited, and Cavendish Motor Services, Case Nos. ME/4030/09 and ME/4031/09, OFT decision of 13 May 2009; and Completed acquisition by Stagecoach Group plc of Preston Bus Limited, Case No. ME/4032/09, OFT decision of 28 May 2009.

<sup>3</sup> The same approach was adopted by the Competition Commission in its recent reports: A report on the completed acquisition by Stagecoach Group plc of Preston Bus Limited, 11 November 2009; and A report on the completed acquisition by Stagecoach Group plc of Eastbourne Buses Limited and Cavendish Motor Services Limited, 22 October 2009.

10. Notwithstanding this, some key aspects of market definition are discussed below in order to provide context for the OFT's analysis.

### **Commercial services versus tendered services**

11. Bus services can be operated on either a purely commercial basis or they can be subsidised in whole or in part (known as tendered services). Tendered services tend to be for school bus services or other socially necessary purposes for which no (or few) commercial service exists (hence there tends to be very little overlap between commercial and tendered services). In Horsham, some bus routes are operated on a commercial basis during peak times but are operated as tendered services during off-peak times. In the Horsham area it is the West Sussex County Council which is responsible for tendering local bus services.
12. As for whether tendered services are in the same market as commercial services, previous OFT and Competition Commission (CC) cases have examined tendered services separately from commercial services.<sup>4</sup>
13. In Horsham, tendered services are for a fixed duration (the West Sussex County Council submitted that contracts are usually for three or four years) and contain set parameters such as price and quality levels (including quality of buses, wheelchair access and the provision of real time bus expectancy information). Operators compete with each other to provide these services under contract from the West Sussex County Council.
14. Given these contractual conditions (governing service levels, frequency and fares), tendered services generally do not compete with overlapping commercial services on the basis of these parameters (suggesting that a competitive assessment should analyse each separately).<sup>5</sup>
15. Notwithstanding this, in Horsham there are limited instances where passengers do have a choice between a commercial or tendered service.<sup>6</sup> In such cases the two types of service are likely to be substitutes from the

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<sup>4</sup> For example, Stagecoach/Eastbourne/Cavendish; Stagecoach/Preston; and Anticipated acquisition by Firstgroup plc of Truronian Limited, Case No. ME/3533/08, OFT decision of 28 March 2008. For the CC, see Stagecoach/Preston and Stagecoach/Eastbourne/Cavendish.

<sup>5</sup> The CC came to a similar conclusion in Stagecoach/Eastbourne/Cavendish (paragraph 5.35).

<sup>6</sup> For example, the Metrobus 921 service and the Acquired Business 93 service.

passengers' perspective (suggesting that a competitive assessment should analyse each together on a cautious basis).

16. In this case the OFT has not found it necessary to conclude on whether commercial and tendered services are a part of the same product market definition (as it does not affect the overall assessment), so on a cautious basis, it has analysed these types of service separately as well as together where they overlap on flows.

### **Flows versus networks**

17. Flow-by-flow analysis refers to the direct head-to-head competition between the merger parties on a particular route or part of a route (known as a flow). While some passengers may use local buses in Horsham to travel along one route only – and therefore would only be concerned about their choice of bus operators along that one route or flow – other passengers may use several, interconnecting flows (a local bus network) to complete their journeys. This second group of passengers will be concerned about the choices available to get them from their starting point to their destination, which may involve considering using different route options. Therefore, for these customers, simply focussing on direct head-to-head competition of the type undertaken in flow-by-flow analysis will not necessarily address the loss of competition which they may face from a merger.
18. In this case the OFT has, in addition to undertaking a flow-by-flow analysis, considered the role of local bus networks in Horsham.<sup>7</sup>

### **Geographic scope**

19. As the overlapping activities of the merging parties are limited to the supply of bus services in West Sussex, the OFT has restricted its assessment to this area. In previous cases, the OFT<sup>8</sup> and the CC<sup>9</sup> have considered local markets in commercial bus services on the basis of competing services on

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<sup>7</sup> The CC undertook a similar approach in its recent report on Stagecoach/Eastbourne/Cavendish.

<sup>8</sup> For example, in Stagecoach/Preston; Completed acquisition by Go North East of Stanley Taxis, Case No. ME/3404/07, OFT decision of 18 March 2008; and Completed acquisition by Stagecoach Bus Holdings Limited of Cavalier Contracts Limited, Case No. ME/3703/08, OFT decision of 18 September 2008.

<sup>9</sup> For example, Stagecoach/Preston and A report on the acquisition by Arriva plc of Sovereign Bus & Coach Company Limited, January 2005.

a flow-by-flow basis, since it reflects particular origin to destination combinations from a passengers' point of view. The OFT has adopted the same approach in this case.

20. In addition, the OFT has also considered wider local bus networks in the Horsham area.

## **HORIZONTAL ISSUES**

### **Commercial services: flow-by flow analysis**

21. When analysing direct head-to-head competition between the parties in this case the OFT has adopted the approach in identifying competition concerns as set out in a paper by CC staff members<sup>10</sup> and used in previous OFT decisions<sup>11</sup>. These filters are not safe harbours, however, and the OFT is not bound to apply them in every case.<sup>12</sup>
22. Key aspects of this approach in flow-by-flow analysis are that a flow is deemed to be not of concern if it comprises less than ten per cent of the total revenue of a route or if the frequency of overlapping services is less than half as frequent as the main service (for example, if one is every 15 minutes and one is hourly).
23. In this case the parties overlap on six flows (table 1).

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<sup>10</sup> 'Review of methodologies in transport inquiries', May 2007 by Kate Collyer, Anthony Felet and Tom Kitchen ([www.competition-commission.org.uk/our\\_role/analysis/topics.htm](http://www.competition-commission.org.uk/our_role/analysis/topics.htm)).

<sup>11</sup> Most recently in Stagecoach/Eastbourne/Cavendish and Stagecoach/Preston.

<sup>12</sup> A similar, although not identical, approach was set out by the CC in Stagecoach/Eastbourne/Cavendish (appendix I) and in Stagecoach/Preston (appendix I). However, in the current case, adopting the CC's approach in these two cases would not alter the outcome of the OFT's competitive assessment.

**Table 1: Overlapping flows**

Metrobus route number	Acquired Business route number	Overlapping flow
921	93	Broadbridge Heath – Horsham bus station
23 and 24	98	Roffey – Horsham bus station
200	51 and 61	North Heath – Horsham bus station
89	63	Oakhill – Horsham bus station
23 and 86	98, 198 and 398	Southwater – Horsham bus station
24 and 200	398	Horsham bus station – Crawley bus station/ Gossops Green

Source: The parties.

24. On none of the overlapping flows do the parties overlap on a fully commercial basis. Instead, the overlaps involve a mix of commercial and tendered services. However, as stated in paragraph 16 above, the OFT has included tendered services in its analysis since they may represent a viable alternative to the commercial service from the passengers' perspective.
25. On three of the overlapping flows (Roffey/Oakhill/Southwater – Horsham bus station) competition concerns can be dismissed since the service operated by one of the parties is at least twice as frequent as the service operated by the other party.
26. In **Roffey – Horsham bus station**, the Acquired Business route 98 service is at least four times more frequent than both Metrobus services.<sup>13</sup> In **Oakhill – Horsham bus station**, the Acquired Business route 63 service (now changed to route 65) runs once per hour whereas the Metrobus service runs only four times per day.<sup>14</sup> **Southwater – Horsham bus station** sees the Acquired Business route 98 running four times more frequently than either of the Metrobus services. The other Acquired Business services on this flow, routes 198 and 398, are tendered school services and therefore do not offer any competition to the Metrobus services.
27. Of the remaining three overlapping flows, in **North Heath – Horsham bus station**, the overlapping flow accounts for less than 10 per cent of Metrobus' revenue and passengers for route 200, and therefore

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<sup>13</sup> The Metrobus route 23 is partially tendered and the Metrobus route 24 is a tendered service. Limited competition is offered by Compass Travel on this flow (via route 98).

<sup>14</sup> The Metrobus route 89 is a tendered service.

competition concerns do not arise (since the overlap is not considered significant enough for Metrobus to raise fares or lower service levels after the transfer of the Acquired Business).

28. Likewise, for **Broadbridge Heath – Horsham bus station** the overlapping flow accounts for 10.4 per cent of the Acquired Business' revenue for the 93 route, making it negligibly over the 10 per cent threshold. Moreover, the merged entity will continue to face competition on this flow from Compass Travel (routes 63, 70 and 101) and Arriva (route 63).<sup>15</sup> Therefore, given the insignificance of this flow for the Acquired Business and the competition offered by Arriva and Compass Travel, no competition concerns arise on this overlapping flow.
29. Finally, on **Horsham bus station – Crawley bus station/Gossops Green** the Acquired Business route 398 is a tendered school run only service (see above) and therefore does not offer any competition to the Metrobus service.
30. For the reasons given above, competition concerns do not arise as a result of the merger on any of overlapping flows.

#### **Commercial services: network effects**

31. Metrobus and the Acquired Business are the two leading local bus operators in the Horsham area, although Compass Travel also has a significant presence.
32. In Stagecoach/Eastbourne/Cavendish, the CC recently noted that network competition may be important if passengers value a network of routes more than just a series of individual routes.<sup>16</sup>
33. In this case the evidence indicates that competition between networks has not been important in Horsham. Go-Ahead told the OFT that, given the small size of Horsham, the majority of local bus users travel from their point of origin directly to either the Horsham bus station in the centre of town or the nearby Horsham train station (most local bus services go to

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<sup>15</sup> After the transfer of the Acquired Business Arriva will still have some presence in the area.

<sup>16</sup> Paragraph 7.15.

one or both of these destinations) on a single bus journey and that there is little cross-town travel or use of interconnections.<sup>17</sup>

34. Tickets available in the area include network type tickets: the 'Explorer' ticket which can be used on buses operated by any of several local bus operators, 'Metrorider' which can be used on any Metrobus within the relevant geographic zone and 'Metrovoyager' which can be used on any Metrobus service apart from some specified services. In addition, the usual single and weekly tickets are available.
35. The parties submitted fare data to the OFT. For Metrobus, almost [ ] per cent of fare revenue in the Horsham area comes from either single tickets (almost [ ] per cent) and return tickets (around [ ] per cent). Around [ ] per cent of tickets are 'Metrorider' or 'Metrovoyager' tickets.<sup>18</sup> The remainder are mostly point-to-point weekly tickets.
36. For the Acquired Business, over [ ] per cent of fare revenue in the Horsham area comes from either single tickets (over [ ] per cent) and return tickets (around [ ] per cent). Around [ ] per cent comes from network tickets.
37. These fare data suggest that travel across a network of buses has not been a strong source of competition between the parties.
38. In addition, the OFT notes that Compass Travel has a significant presence in the Horsham area.<sup>19</sup>
39. The OFT does not consider that the merger raises a realistic prospect of a substantial lessening of competition on a network basis in the Horsham area.

### **Tendered services**

40. Both parties supply tendered services in the Horsham area: Metrobus operates four tendered services in the area and the Acquired Business

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<sup>17</sup> In Stagecoach/Eastbourne/Cavendish the CC came to a similar finding. It said (paragraph 7.16) 'The small size of the Eastbourne area suggests that the extent of network travel is likely to be less than for larger markets.'

<sup>18</sup> Metrobus sales of 'Explorer' tickets are negligible.

<sup>19</sup> The parties estimated that Compass Travel accounts for around 40 per cent by buses operated and over 40 per cent by route miles in the Horsham area.



operates five out of 28 tendered services in all in Horsham. Therefore, the parties together account for around a third of tenders won in Horsham.

41. Bidding data supplied to the OFT by West Sussex County Council show that it attracts bids from between four and six bus operators (which the County Council submitted was a higher average than elsewhere in the county). Closer analyses of those data find that Metrobus and the Acquired Business have not been close competitors in the bids. Whenever both submitted bids there were at least three other competing bids and they were never ranked first and second in the bidding (the closest that they came was when Metrobus came second and the Acquired Business came fourth).
42. West Sussex County Council submitted that it did not believe that the merger would adversely affect competition or disadvantage passengers. As mentioned above, it receives a good response from bus operators in its tendering exercises and recently the amounts that it has had to pay to support local services has fallen.
43. The OFT does not consider that the merger gives rise to a realistic prospect of a substantial lessening of competition in tendered services in the Horsham area.

#### **Barriers to entry and expansion**

44. [Comments of a third party].
45. Stagecoach, a major bus operator in the UK, has a depot at Worthing (around 20 miles from Horsham) and a parking-only outstation at Henfield (11 miles, or 20 minutes, away).<sup>20</sup> It told the OFT that it could enter a service in Horsham within 56 days (the minimum notice period allowed according to Traffic Commissioner's rules). Stagecoach said that the factors it would look at when deciding to enter or expand in Horsham are prices, the frequency of competitor services and the quality of those

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<sup>20</sup> The OFT's market study found that bus operators generally throughout the UK use 20 minutes as a rule of thumb on the maximum distance a depot can be from a local bus market before operating in that market becomes unviable. 'Local bus services: report on the market study and proposed decision to market a market investigation reference', August 2009, OFT1112con, paragraph 3.5.

services. However, Stagecoach said that barriers to entry into Horsham are low.

46. The OFT has not found it necessary to conclude on barriers to entry in this case although it does note that for those already operating in the area, the evidence indicates that barriers to expansion are not high.

#### **Countervailing buyer power**

47. Customers for commercial services are individuals and therefore do not possess countervailing buyer power. For tendered services, the OFT has not found it necessary to conclude on whether West Sussex County Council possesses countervailing buyer power.

#### **THIRD PARTY VIEWS**

48. No third parties raised competition concerns in this case. As mentioned above, West Sussex Council is not concerned about the merger nor is the passengers' interest group, Bus Users UK. The OFT also received some comments from individual bus users in the area who were unconcerned about the merger.
49. Competitors are likewise unconcerned. One third party submitted that it was concerned about Go-Ahead (which operates some train services in West Sussex) excluding other bus operators from supplying rail replacement bus services when necessary. The OFT also received a complaint that the merger may have an effect on the second hand bus market in the local area. However, both of these concerns are about foreclosing local businesses and the OFT has not seen any evidence on the likelihood of this occurring. Neither has the OFT received evidence that such foreclosure would harm competition to the detriment of passengers in any substantial way.

#### **ASSESSMENT**

50. Metrobus and the Acquired Business overlap in the provision of local bus services in the Horsham area.

51. For the reasons explained in paragraphs 25 to 29 above, the OFT does not consider that the merger will lead to a realistic prospect of a substantial lessening of competition in direct head-to-head competition.
52. The OFT considered whether local bus networks were of importance in the Horsham area and, if so, what the merger effect on these would be. It found that local bus networks are not an important feature of local bus services in the Horsham area and therefore the merger does not lead to a realistic prospect of a substantial lessening of competition in local bus networks.
53. Finally, the OFT considered whether the merger is likely to lead to a substantial loss of competition in tendered bus services. It found that there is a healthy degree of competition (besides the merger parties) for tendered services in Horsham and that Metrobus and the Acquired Business had not been especially close competitors for tendered services in any case. [ ].
54. Consequently, the OFT does not believe that it is or may be the case that the merger has resulted or may be expected to result in a substantial lessening of competition within a market or markets in the United Kingdom.

## **DECISION**

55. This merger will therefore **not be referred** under section 22(1) of the Act.

**OFFICE OF FAIR TRADING**

**16 November 2009**