Completed acquisition by Stagecoach Bus Holdings Limited of Cavalier Contracts Limited

ME/3703/08

The OFT's decision on reference under section 22(2)(a) given on 18 September 2008. Full text of decision published 26 September 2008.

PARTIES

1. **Stagecoach Bus Holdings Limited** (Stagecoach) is part of the Stagecoach Group, an international public transportation group with operations in the UK, USA and Canada. Stagecoach Group's UK bus division operates 7,000 vehicles across a number of regional operating companies in more than 100 towns and cities in the UK. The two Stagecoach operating companies relevant to this merger are Viscount Bus and Coach Company Limited and Cambus Limited.

2. **Cavalier Contracts Limited** (Cavalier) is a local bus company operating bus services and contracts throughout Cambridgeshire and southern Lincolnshire. It operated 78 vehicles primarily from its operating bases at Long Sutton, March and Huntingdon. The turnover associated with those parts of Cavalier's business acquired by Stagecoach was £5 million in its last financial year. Since completion of the acquisition, Cavalier was renamed Stagecoach in the Fens Limited.

TRANSACTION

3. The acquisition of the full share capital of Cavalier by Stagecoach completed on 31 March 2008.

4. The OFT's statutory deadline for deciding whether to refer the merger to the Competition Commission (CC), extended under sections 25(1) and 25(2) of the Enterprise Act 2002 (the Act), is 18 September 2008.

JURISDICTION

5. As a result of this transaction Stagecoach and Cavalier have ceased to be distinct. The parties overlap in the supply of bus services in Cambridgeshire, where their combined share of supply is above 25 per cent and therefore the share of supply test in section 23 of the Act is met. The OFT therefore believes that it is or may be the case that a relevant merger situation has been created.

RELEVANT MARKET

Product scope

6. Both parties are active in the supply of bus services, which can be segmented between commercial and tendered services. It is usual for operators of commercial services to provide tendered services and, to a lesser extent, for operators of tendered services to provide commercial services. However, in past cases the OFT has taken the view that these two types of services have different characteristics and are not substitutes from a market definition standpoint.[1] Tendered services are subsidised by the local authority in order to provide transport services where it would otherwise be unprofitable for private companies to do so. Bus operators bid for tendered contracts, which are re-tendered every few years, and the local authority will, usually, specify the routes, the timing (or frequency) of services and the fares to be charged on those routes. Competition in tendered services occurs at the bidding stage rather than in operating the service. The evidence before the OFT does not suggest that it would be appropriate to depart from this distinction in the present case.

Geographic scope

7. When making a journey, passengers travel from a particular origin to a particular destination and therefore other origin/destination combinations

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[1] OFT C*ompleted acquisition by Arriva plc of Premier Buses Limited*, 1 June 2006.

are not likely to be substitutable from a demand-side perspective. The OFT and the CC have previously considered local markets in transport cases on the basis of the substitutability of competing services on point-to-point flows.[2] In this case, the OFT also considered it appropriate to consider the impact of the merger on potential competition (or supply-side substitution) across the wider area in which the merging parties' business activities overlap, that is, Cambridgeshire and the Peterborough area. In addition, given that both parties were expected to operate on the Cambridge Guided Busway (the Busway) which starts functioning next year, future competition in the provision of services on the Busway itself was also considered as a separate overlap.

8. The OFT has focused its assessment on the impact of the merger on commercial bus services for two key reasons. First, there are currently a large number of alternative providers of tendered services in the areas of overlap, while in commercial services the number of alternatives is more limited. Second, the local councils in the area affected by the merger, who are the direct customers of contracted services, were unconcerned about the merger, and confirmed that there are a number of alternative providers of tendered bus services in the area. Therefore, the OFT considers that, if the merger does not raise competition concerns in the commercial services segment, it is unlikely that concerns would be found in relation to the tendered services segment. As the analysis below demonstrates, the OFT does not believe there is a realistic prospect that the merger will lead to a substantial lessening of competition in commercial services (apart from in relation to the Cambridgeshire Guided Busway, which will be considered separately). For this reason, the OFT does not consider that it is necessary to define the appropriate frame of reference against which to assess the impact of the merger on tendered services.

Conclusion

9. Therefore, the appropriate frame of reference for this merger is the supply of commercial bus services on each flow in which the parties overlap, the

[2] Competition Commission, *A report on the proposed acquisition by FirstGroup plc of the Scottish Passenger Rail franchise currently operated by ScotRail Railways Limited* June 2004, OFT *Anticipated acquisition by FirstGroup plc of the Greater Western Franchise* 30 September 2005. A flow is a bus journey between specific start and end points, which may be all or part of a longer bus route.

entire Cambridge Guided Busway, as well as the wider area comprising Cambridgeshire and Peterborough.

HORIZONTAL ISSUES

COMMERCIAL OVERLAPPING FLOWS

10. The parties overlap in the provision of tendered services in Cambridgeshire and Lincolnshire, and commercial and supported services in Cambridgeshire. As discussed above, this decision focuses on the commercial services.

Whittlesey to Peterborough

Pre-merger conditions

11. The Stagecoach and Cavalier services overlapped on the flow between Peterborough City Centre and Whittlesey. The parties operated on the same frequency (three buses per hour) for most of the time in which this service is available.[3]

Significance of overlap

12. The OFT considered whether the overlapping flow is too small vis-à-vis the overall routes in terms of revenue and/or passenger numbers to make it worthwhile for the parties to adjust fares and/or reconfigure routes post-merger. However, the OFT concluded that the overlap occurs for a relatively high proportion (above 40 per cent) of revenue and passengers on both routes, and that therefore it is unreasonable to discount the incentive that the parties may face in changing fares and service levels post-merger.

[3] Note that the service frequency has been slightly decreased post-merger. As discussed below, the relevant local councils (Cambridgeshire Council and Peterborough City) were satisfied that the new service timetable is more appropriate given that it provides a regular headway between buses.

Alternative bus operators

13. A third operator, Judds's Travel (Judd's), also operates on this flow. On the one hand, both single and return tickets are cheaper on Judd's services than on the merging parties'. On the other hand, Judd's buses are less frequent than Stagecoach's and Cavalier's (only one per hour versus around six per hour for the merged entity), and the OFT was also told that they are significantly older than the parties' fleet (25 years versus four to seven years old).

Alternative mode of transport

14. 25 per cent of passengers travelling on this flow travel on the whole length of the flow, that is, from Peterborough to Whittlesey (or vice-versa). For these customers, the OFT has considered whether travelling by rail is an alternative to bus. There are ten daytime services in each direction on this flow, run by three train operators.

15. On the one hand, the trip by train is much quicker than by bus (eight to nine minutes by train compared to 20 to 37 minutes by bus). On the other hand, train single fares are almost twice the cost of an equivalent Cavalier single ticket cost. Return train ticket prices are more comparable, but still around a third more expensive than equivalent bus tickets.

Third parties' views and entry

16. Cambridgeshire County Council and Peterborough City Council were satisfied that, despite the reduction in frequency on this flow post-merger (see footnote 3 above), the revised frequency is appropriate for the local area and the new timetable provides a regular headway, whereas the previous combination of services did not.

17. Judd's reported several occurrences of entry and exit on this flow. Judd's itself entered 18 months ago. It said that it would consider operating more services if Stagecoach reduces its frequency, but also thought that at the moment many buses operate near-empty which means that overall frequency is likely to decline.

18. Two other companies stated that they would consider entering the route if service frequencies were reduced. One of them is not currently a bus

operator, while the other can be considered a viable likely entrant who identified an existing secure outstation six miles from the route which could be utilised as a base for entering. The OFT has also found two bus depots with enough spare capacity to service this flow within around ten miles from the flow.

Conclusion

19. On the basis of the information available, the OFT does not consider that the merger raises competition concerns on this flow. The parties operated similar frequencies pre-merger. Post-merger, although there are public transport alternatives for travelling on the flows and therefore some constraint on Stagecoach, the alternative transport means cannot be considered as alternatives to Stagecoach for all passengers on the flow. However, given the recent history of entry on this flow, the fact that Judd's submitted that it would consider expanding its services in case Stagecoach further decreases frequency, and the fact that two third parties (at least one of which is a credible entrant) would consider entering this flow in the case of service decreases and/or price increases, the OFT considers that the merger does not raise competition concerns on this particular flow.

Girton to Cambridge

20. The parties overlap on the 4km flow between Girton and Cambridge city centre.[4]

Pre-merger conditions

21. Pre-merger, Stagecoach operated seven buses per hour along the overlapping flow while Cavalier operated less than half this frequency with three buses an hour.

[4] Although both parties also operate a service between Girton and St Ives, because of the significantly different routes and journey times, this is not considered to be an overlap. This is supported by data provided by the parties indicating that less than one per cent of Stagecoach passengers travel the full journey from Cambridge to St Ives, as opposed to 16 per cent in the much shorter Cavalier services, which is intended to be a direct commuter service between St Ives and Cambridge.

Significance of overlap

22. The overlapping flow is of very small significance to Cavalier's services (less than three per cent in revenue terms), although more significant to Stagecoach's overall route (12 per cent in revenue terms).

Alternative bus operators

23. Post merger, the parties will face competition from Whippet Coaches (Whippet). However, Whippet runs an irregular timetable that is less frequent than the parties' services - approximately two buses an hour in the times in which the parties overlap.

Third parties' views and entry

24. Cambridgeshire Council expressed no concerns regarding this route.

25. There are four local depots which appear to offer a suitable base from which to operate on this flow. One local operator commented that it 'would not dare' to enter against Stagecoach given its aggressive behaviour on routes in the Cambridge area. Whippet submitted that its local depot is amenable to expansion and that if the parties were to reduce frequencies or increase prices then it would be able to fill any voids in the scheduled regular bus service provided that demand existed.

Conclusion

26. Pre-merger Stagecoach operated a service that was more frequent than both Cavalier and Whippet. Post-merger, Whippet will continue operating on this flow (albeit much less frequently than Stagecoach), and it said that it would be willing to expand its services in case service levels decrease. Therefore, the OFT does not consider that the merger raises competition concerns on this particular flow.

Peterborough to Chatteris

Supported services

27. Services between Chatteris and March benefit from central government funding (the 'Kickstart' scheme) in the form of a lump sum subsidy which

was awarded in return for improvements in services in the local area. Funding was obtained in an effort to raise patronage on bus services and is due to expire in 2009, after which the routes will revert to regular commercial routes. As part of the Kickstart funding arrangements, the Cambridgeshire County Council negotiated a combined timetable with a pre-defined spread of services. However, the level of fares is set independently by each operator.

28. Stagecoach argued that, because this service is supported by the Council, it is more akin to a tendered service, and that the fare structure has to be competitive to attract patronage. Although it is clear that the merging parties cannot alter the frequency and timing of services on this flow while the funding scheme is in place, this fact in itself is not sufficient to exclude the possibility of anti-competitive effects resulting from the merger on this flow. First, there can be competition on price and quality of services between the parties, which, as discussed below, the only two bus operators on this flow. Second, the Kickstart funding is due to cease next year, and the parties will then have the full ability to change timetables and frequencies.

Concessionary travel

29. Stagecoach submits that because a high proportion of journeys on this flow (roughly 50 per cent of all passengers travelling on this flow with both merging parties) are made by customers using concessionary travel cards, a significant proportion of passengers would not be affected by any price increase implemented by Stagecoach post-merger. However, the OFT notes that those passengers would still be affected by any service decrease permitted by the loss of competition between Stagecoach and Cavalier for the fare-paying passengers. In addition, Stagecoach might still have the incentive to increase fares for the other 50 per cent of passengers who do not benefit from concessionary travel.

Pre-merger conditions

30. Stagecoach's X8/X9 service and Cavalier's 337 services overlap between Chatteris and Peterborough.[5] Pre-merger, Cavalier operated five vehicles on the 337 route during peak service.

31. The parties' services overlap in the morning and early afternoon, when the X8/X9 and 337 services are run by each operator at two-hourly intervals. As a consequence, the overlapping services have the same frequencies during the time of the day in which they overlap. Stagecoach asserts that the one-hour time gap between the services means that, in reality, these services do not compete with one another. The OFT agrees that this might be true for time sensitive passengers. However, given that the services are not very frequent, it is possible that some passengers are time insensitive and have the opportunity to plan their journeys with some flexibility. For these passengers, the parties' services are substitutable. However, Stagecoach argues that a significant proportion of 'time insensitive' passengers are likely to be concessionary passengers in relation to whom Stagecoach would not have the incentive to increase prices post-merger. Stagecoach also suggests that, because Cavalier operates only three or four (depending on the direction) of the 12 or 13 (idem) daily services on this flow, the merging parties should not be considered effective competitors. However, as seen above, Cavalier's services do not cover the whole of the day but, for the period they do run, those services are interspersed (evenly) between those of Stagecoach.

32. There are no alternative bus services to the merging parties' services on this flow.

33. Five per cent per cent of (fare-paying) passengers travelling on this flow travel from March to Peterborough (or vice-versa). For these customers, it might be the case that travelling by rail is an alternative to bus. The rail frequency is similar to bus, and the rail service is considerably quicker than the bus (18 to 23 minutes versus a little less than one hour). While

[5] The services overlap on a seven mile flow between the towns of Chatteris and March. North of March, the services soon take different routes to Peterborough. Although journeys to Peterborough were not originally identified as overlapping by the parties, the journey times between March and Peterborough are similar and therefore the OFT considered that the Cavalier service is an alternative to the Stagecoach service on journeys to Peterborough.

single fares are more expensive via train, rail return fares compare favourably to bus day tickets. Therefore, for the passengers travelling from March to Peterborough or vice-versa, rail provides a viable alternative. However, this alternative is only available to a fraction of the passengers travelling on this flow.

Relative importance of the flow

34. In past transport cases where there have been a high number of overlapping flows, filters have been applied to allow the OFT and CC to focus their analysis on those flows most likely to give rise to competition concerns. The 'ten per cent filter' is based on the relative importance of the flow compared to the overall route, and excludes from the initial analysis flows in which the sum of all overlapping flows on a single route account for less than ten per cent of the route's passengers and revenue. The rationale behind this filter is that the incentives for parties to adjust fares or services on flows that constitute only a small proportion of a route's revenue is low and that, if no competition concerns are identified on the relatively larger flows (in relation to the route), it is unlikely that the merger will result in competition concerns on these smaller flows. If competition concerns are identified on the relatively larger flows it may be necessary to conduct a more detailed competitive assessment across all flows.[6]

35. On the overlapping flow identified by the parties (between Chatteris and March) the overlap accounts for 21 per cent of the relevant Stagecoach revenues, eight per cent of the Cavalier revenues, and 13 per cent of total combined revenue for the X8/X9 and 337 services. If the whole flow between Peterborough and March is considered, these figures will be higher. If both parties' services are bundled together, the combined revenues on the flow will be above the 'ten per cent filter'. However, the OFT considers that the overlapping flow is still a small proportion of the overall route, and that Stagecoach's incentives to change fares and service levels post-merger as a result of its stronger position in this particular flow is reduced. This is true in particular in view of the small annual revenue associated with this flow ([less than £50,000] for the merging parties combined).

[6] See the *Review of methodologies in transport enquiries* report (the *CC methodology report*), paragraph 25.

Third parties and entry

36. Cambridge County Council viewed the merger as effecting a positive change and does not expect the merger to impact on the service level for these services.

37. When assessing the impact of a merger on a flow-by-flow basis, it is appropriate to identify specific potential entrants on each relevant flow and to determine whether they have any intention to enter the flow and whether they have the ability to enter (such as available capacity in nearby depots) on a scale that replicates the increment caused by the merger.

38. In this case, sufficient depot capacity exists near this flow to replace to level of service frequency operated by Cavalier (which was lost by the merger). One local bus operator and one local coach operator told the OFT that they would be interested in expanding onto this flow in the event of a fare rise and/or frequency reduction. Also, three further operators said that they could feasibly enter the route between March-Chatteris on a tendered/funded basis.

Conclusion

39. Based on the evidence available to it, the OFT does not consider that the merger will raise competition concerns in relation to this flow. This is a very small flow, both in absolute terms and in comparison with the overall route. The scope for Stagecoach benefiting from the loss of Cavalier as an independent constraint is further diminished by the high percentage of concessionary travel on this flow and by the fact that a part of the flow required public funding to increase patronage. There is capacity available in local depots, and a number of third parties manifested interest in entering this flow either on a commercial or tendered basis.

POTENTIAL COMPETITION / SUPPLY-SIDE SUBSTITUTION

40. The OFT also considered whether the merger may result in the loss of a significant competitive constraint on the activities of either or both of Stagecoach and Cavalier in Cambridgeshire and Peterborough more widely than on the overlap flows. In this section the OFT considers the scope for

the merger to raise competition concerns in relation to **potential** for head-to-head competition that in itself acts as a significant competitive constraint, as opposed to **actual** head-to-head competition that was assessed in the flow-by-flow analysis above. Although this potential for head-to-head competition might be viewed as supply-side substitution in some circumstances (that is, if a wider market definition is adopted), the OFT considers it more appropriate in this case to refer to it as 'potential competition' for clarity.

41. A loss of potential competition could arise through the removal of actual entry that would, or could, absent the merger, increase competition above pre-merger levels (actual potential competition) and/or the removal of the constraint on the incumbent imposed by the mere threat of entry (perceived potential competition). Unlike the constraint from actual entry, which by definition has not arisen under pre-merger conditions, a constraint from perceived potential entry that gives incentive to the incumbent to respond to this threat does exist in the pre-merger environment. Both theories of potential competition may apply in an individual case: in other words, a merger could in principle eliminate both the existing constraint posed by the threat of entry (perceived potential entry) and the potential for increased actual competition post-entry (actual potential entry). In this case, because there is no reason to consider that each party would not be aware of the actual prospects for entry by the other, evidence relating to the loss or otherwise of actual potential competition applies also to perceived potential competition.[7]

42. Stagecoach argues that Cavalier does not provide a significant competitive constraint on Stagecoach's activities (and vice versa), in particular because there have not been any episodes of entry by either of the merging parties into each other's routes in the recent years. Stagecoach could identify only two situations in the last five years in which Stagecoach or Cavalier entered a route in which there was already an existing operator present. In one case, this was in response to exit by another operator and in the other the entry involved Kickstart funding. Stagecoach said that another scenario in which it would enter a route in competition with another operator is if there were unfulfilled passenger

[7] See further OFT *Completed acquisition by Air France finance S.A.S / City Jet Ltd of VLM Airlines N.V.* 9 May 2008 for a fuller discussion of potential competition and the evidentiary standards applicable to it.

demand due to a new housing development, for example, but it would not normally consider entry in competition with an incumbent operator as viable outside these three opportunity 'windows'.

43. The OFT does not consider that the fact that there have not been episodes of entry by the merging parties in competition with each other to be conclusive of the lack of potential competition between them. In particular, in some industries (bus services likely to be among them) potential competition materialises only sporadically, when 'bursts' of actual competition occur. However, this does not mean that the removal of 'latent' potential competition is necessarily insufficient to create competition concerns. Nonetheless, the absence of previous entry by each party into the other's routes is clearly of some probative value and, in any event, in this particular case, the body of evidence available to the OFT does not indicate that the merger will cause the loss of significant potential competition.

44. First, the OFT has seen no specific evidence of potential competition materialising or being likely to materialise in the foreseeable future in this instance from either party.

45. Second, to the extent that Cavalier poses a constraint in terms of potential competition on Stagecoach, the OFT considers that Whippet will continued to provide a constraint of similar magnitude post-merger. In Arriva / Sovereign[8] the OFT concluded that one of the reasons why the merger raised potential competition concerns was that Sovereign was the closest competitor to Arriva in the affected local area. In that case, Sovereign covered more towns and had a less concentrated network compared to its rivals and had twice the number of depots compared to its nearest rival. In this case, according to share data provided by third parties, Cavalier and Whippet have similar shares in the area of between five and ten per cent each (in comparison to Stagecoach with between 70 and 80 per cent). In this case, given Whippet's share of supply in the overlapping area, the fact that it competes with Stagecoach on a number of routes, the fact that it has some spare capacity in its depots, and the fact that it said it would be willing to enter some of the overlapping flows if service levels decreased post-merger, the OFT believes that Whippet

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[8] OFT *Anticipated acquisition by Arriva plc of the assets of the Hertfordshire bus operations of Sovereign Bus and Coach Company Limited* 3 August 2004.

provides a constraint of similar magnitude to that posed by Cavalier. In other words, the OFT does not believe that Cavalier is uniquely placed to challenge Stagecoach, nor that it is its closest competitor.

46. Equally, the evidence before the OFT does not lead it to believe that Stagecoach provided a significant constraint in terms of potential competition on Cavalier. In addition to the lack of specific evidence on the history of entry (actual or threatened) discussed above, Cavalier's focus on rural, and to some extent tendered, routes differed from Stagecoach's business model, which tends to target the more profitable urban commercial routes. In that sense, Cavalier's former shareholders told the OFT that Whippet was a closer competitor to it than Stagecoach was.

47. The CC in the Arriva / Sovereign report[9] also considered whether the acquisition would give rise to a significant loss of competition by eliminating possible acquisition opportunities for entry by operators from outside the overlapping area or expansion by existing operators in the overlapping area. This is particularly relevant in view of Stagecoach's submission that it is more concerned about the prospect of entry by one of the large national operators (which is unlikely to take place on a single flow, but rather as a wider entry) than of expansion by a small local operator.

48. In this case, the OFT considers that Cavalier is not a unique 'stepping stone' into Cambridgeshire. It believes that Whippet is as attractive for an entrant as Cavalier, for the same reasons discussed in the paragraphs above.

49. Finally, the OFT notes that no competition concerns in relation to potential competition have been articulated by third parties.

CAMBRIDGESHIRE BUSWAY

Background

50. The Cambridgeshire County Council (the Council) is currently constructing the world's longest guided busway at a cost of over £100 million, due to

[9] Competition Commission, *A report on the acquisition by Arriva plc of Sovereign Bus and Coach Company Ltd* January 2005, paragraph 5.58.

open in spring 2009. The Busway is a 'track' on which specially adapted buses can run and are not required to steer along its length.

51. The Busway runs alongside the A14, which suffers significant congestion. The Council's intention is, by offering quick and comfortable journeys, to attract passengers to the Busway that would have otherwise used private means of transport.

52. The Council predicts that in the first year of opening nearly 11,500 trips per day will be made on the Busway. This number is expected to increase to more than 20,000 journeys per day by 2019.[10] However, the OFT was told that a considerable proportion of these journeys would be made by people travelling from and to the new town of Northstowe, the construction of which has been delayed.

53. The Council published notices in 2005 and 2006 inviting expressions of interest from bus operators wishing to provide services on the Busway. Five bus operators originally manifested interest. However, only three operators subsequently signed inception agreements with the Council: Stagecoach, Cavalier and Whippet (together, the Busway Operators).

54. Under the inception agreements signed at the end of 2006, the Busway Operators committed to providing a minimum number of services on the Busway for five years in return for, in essence, exclusive access to the Busway during that period. In addition, the Council will charge the Busway Operators an access charge in return for allowing access to the Busway. Provided minimum services levels are maintained by the Busway Operators, during the exclusivity period, no other bus operator may operate on the Busway without the Council first offering the Busway Operators the opportunity to provide the new service.

55. The combined minimum service levels currently contracted with the three Bus Operators do not cover the overall minimum service levels for the Busway as a whole established by the Council. The OFT was told by the Council that under the individual inception agreements the Council could enter into further inception agreements with additional bus operators until

[10] www.cambridgeshire.gov.uk/NR/rdonlyres/EF2D4AF0-A488-404F-BC4B F3E4E83A33AC/0/GuidedBuswayfactsFINALJul08.pdf

the overall minimum service level is reached. However, it would be open for the Bus Operators to argue that the Council has been acting to date as if it deemed the hitherto contracted services with the three Bus Operators to be sufficient. This would mean the Bus Operators could therefore stop the Council from entering into further inception agreements with other operators. In addition to this point, the Council does not believe that any other operators would in fact be interested in entering into a new inception agreement given the lack of interest shown in the past.

56. A number of aspects of the Busway operations that are relevant for the competitive assessment of this merger have not yet been defined. The Council envisages that certain important specifications, such as timing and headway between services and the pricing policy, will be contained in the Quality Bus Partnership Scheme and in the Ticket Schemes, which have not yet been formalised by the Council. As a consequence, the OFT's assessment and conclusion that a realistic prospect of a substantial lessening of competition arises from the merger in relation to the Busway is based on the expected configuration of the Busway as currently planned.

Relevant market

57. According to the service levels currently contracted by both merging parties with the Council, the merging parties would overlap on the Busway in services between either Longstanton and Cambridge city centre or St Ives to Cambridge city centre.[11] Nonetheless, the OFT considers that the appropriate relevant market in relation to the Busway is the whole Busway itself. The merging parties and Whippet are the only operators who have signed inception agreements, and therefore, given the exclusivity provisions applicable, they are the most likely operators in the parts of the Busway that have not yet been contracted. In addition, this overlap is significant in the context of the Busway as a whole. In any event, given the exclusivity provisions, the OFT does not consider that the assessment of the merger differs according to whether it focuses on the particular overlapping flow or on the Busway as a whole.

[11] This depends on the result of the discussions with the Council to extend Stagecoach's operations to commence from St Ives.

Assessment

58. The theory of harm to be tested is that, after the merger, Stagecoach may have the ability and incentive to increase fares and/or reduce service levels on this flow (or on the Busway as a whole) due to the loss of an independent constraint (Cavalier).

Counterfactual – operators on the Busway

59. In this case, because not only the Busway is not yet in operation, but also a number of important parameters of competition are still being decided by the Council in consultation with the Busway Operators, the counterfactual to the merger is not the pre-merger situation (as is generally the case for most merger inquiries), but the likely conditions of competition on the Busway absent the merger. Normally, the assessment of the counterfactual is largely a question of fact whereas the assessment of the effects of the merger is a more predictive exercise. In this case, establishing the initial counterfactual also involves a certain degree of prediction (in that it involves considering which parties would operate on the Busway absent the merger), and in this scenario the OFT considers that – given the factual uncertainties – it is appropriate to consider alternative counterfactuals to the extent that there is evidence that they are plausible.[12]

60. Stagecoach argues that Cavalier had not undertaken adequate financial planning or made provisions for the investment in new buses to operate on the Busway. The only supporting documentary evidence provided by the parties in this respect is a copy of Cavalier's 2005/2006 accounts which the parties argued indicate that Cavalier was struggling financially and could have faced difficulties in obtaining financing for the new, specially-adapted buses required to operate on the Busway. However, given the fact that Cavalier had signed the inception agreement, the OFT considers this evidence falls short of being unequivocal evidence that Cavalier could not have operated on the Busway. Stagecoach also argues

[12] For the OFT's general approach to the counterfactual in OFT merger investigations, see OFT *Anticipated acquisition by Tesco Stores Limited of five former Kwik Save stores (Handforth, Coventry, Liverpool, Barrow-In-Furness and Nelson)* 11 December 2007.

that the fact that Cavalier [REDACTED], is 'strongly indicative' that Cavalier had no intention of operating on the Busway.

61. Cavalier's former owners told the OFT that the Busway would have added value to their business and that it was wholly realistic to consider that they would have gone on to operate on the Busway absent the merger, although they did acknowledge that it was 'quite a gamble to take'. Although Cavalier had signed an inception agreement with the Council to operate on the Busway, Cavalier's former owners did not believe it would have incurred financial penalties (as strictly provided under the inception agreement) if it had not fulfilled its obligations under the agreement, although it would have 'soured relations' with the Council had they left the Busway project. The Council itself believed that Cavalier would have stayed in the project absent the acquisition.

62. The evidence before the OFT is not unequivocal as to whether Cavalier would have operated on the Busway absent the merger. In addition, even if it is accepted that Cavalier's former shareholders were not interested in running the business themselves, it does not necessarily follow that there would not be a less anti-competitive realistic alternative to the merger, that is, a scenario in which Cavalier is acquired by a third party who would then operate on the Busway as an independent competitor to Stagecoach and Whippet.

63. In summary, the OFT considers it appropriate to take a cautious approach to the counterfactual in the particular factual circumstances of this case given that the reference test is not one on the balance of probabilities but rather one of realistic prospect.[13] In this case, on the basis of the evidence available to it, the OFT regards it as entirely plausible that Cavalier would have stayed as an independent operator on the Busway. It has therefore considered the effects of the merger on the basis that Cavalier would have operated on the Busway.[14]

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[13] The OFT's approach to the counterfactual in this case (to examine the impact of the merger on the basis that Cavalier would have operated on the Busway absent the merger) aligns with its general starting position in other cases (which is to assume that suppliers active in the market at the time of the merger would, absent compelling evidence to the contrary) have continued to operate had the merger not gone ahead.

[14] The alternative counterfactual – that Cavalier would not have operated on the Busway – would mean the merger raises no competition concerns as regards the Busway project.

64. During the course of the OFT's investigation, Whippet raised the possibility that it may also leave the Busway as a result of the merger (which would therefore be a merger effect, rather than a counterfactual issue, but which is dealt with here for ease of explanation). It submitted that it will be much more difficult for it to compete against the merged entity on its own rather than competing against Stagecoach, particularly given the possibility of some form of co-operation with Cavalier.[15] Whippet has not provided any internal documents to support its claim, and the OFT believes that its contractual situation before the Council is similar to that of Cavalier, as discussed above. In addition, the OFT notes that Whippet does compete with Stagecoach on a number of bus routes in Cambridgeshire, and it is not clear why it would be more difficult to compete on the Busway than on the road. Furthermore, it is probable that Whippet would try to sell its Busway operations to a third party operator rather than simply exit from it – in such case, anti-competitive effects are unlikely to arise.[16] The Council believes that Whippet will stay on the Busway.

65. On the basis of the evidence available, and in conjunction with the factual evidence the OFT has examined when considering the correct counterfactual to be applied to whether Cavalier would have operated on the Busway, the OFT does not believe that, post-merger, Whippet (or a successor to Whippet in terms of the Busway) will exit the Busway such that it should not be considered as an independent constraint on the Busway.

66. On the basis of the above, the OFT has considered the effect of the merger to be to reduce (in particular for the overlap stretch) the number of competitors on the Busway from three to two. The OFT has considered whether this reduction creates the realistic prospect of a substantial lessening of competition given the conditions of competition on the Busway.

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[15] This suggestion was not explained in detail by Whippet.

[16] Assuming that Whippet would not be acquired by Stagecoach which, in light of the discussion below, would risk raising its own antitrust concerns.

Competition on the Busway

67. As discussed above, the precise timetable for the services has not yet been defined. On the stretch of the Busway on which the parties overlap (Longstanton or St Ives to Cambridge), the contracted minimum service levels are three services an hour for Stagecoach, two services an hour for Whippet, and two services an hour in off-peak times and four services an hour at peak times for Cavalier.[17]

68. Therefore, Stagecoach and Cavalier would operate very similar frequencies on the Busway. The only other operator in the Busway, Whippet, will operate a slightly lower frequency than either of the merging parties on the overlapping flows. Once Stagecoach's and Cavalier's services are combined, Whippet will operate less than half of the frequency of the merged entity.

Pricing

69. The OFT was told that there will basically be three types of tickets in the Busway: (i) single-operator single tickets, (ii) multi-operator single tickets (which can be sold in the format of a carnet), and (iii) single-operator network tickets (such as Stagecoach's Megarider).

70. According to the latest draft of the Ticketing Scheme for the Busway received by the OFT, there will be a committee responsible for setting and reviewing the level of fares for the multi-operator tickets. In this committee, votes will be allocated pro rata to service levels on the Busway – that is the bus operator with the greatest number of services will have the highest number of votes, in addition, the Council will have the same number of votes as the Busway Operator with the highest number of votes. As a consequence, post-merger, the Council will have the same number of votes as the merged entity, and Whippet will have fewer votes. Decisions will be taken by a majority resolution except in cases in which the Council may exercise its veto to protect the interests of passengers of the Busway.

[17] The OFT understands that Cavalier had raised with the Council the possibility of running three services per hour throughout the day and it is not clear therefore what its service levels would have been absent the merger. In any event, this does not materially affect the substantive analysis.

71. Stagecoach put forward two main arguments to support the argument that the merged entity will not have the ability to increase fares post-merger.[18] First, the Council will have a veto over any increase of multi-operator fares (one of the three fares referred to above) which it considers to operate against the public interest. On this basis, Stagecoach contends the multi-operator ticket is effectively 'regulated'. Second, the multi-operator ticket will effectively operate as a cap on the price of the single-operator tickets.

The role of the Council

72. The OFT considers that the assessment of the competitive impact of the merger on the Busway must take into account of the factors influencing the Council's decision-making in relation to the Busway.

73. The Council has invested a significant amount of resources in setting up the Busway, and it aims to attract as many passengers as possible to it. The Busway is one of a number of initiatives to increase use of public transport in Cambridgeshire, such as the introduction of 'park-and-ride' schemes and the implementation of congestion charging in Cambridge city. The Council's policy objectives relating to the Busway scheme may therefore be considered to be an incentive for the Council to prevent price increases post-merger.

74. In addition to these incentives, the Council also has, to some extent, the ability to prevent price increases post-merger. As discussed above, the Council may veto fare rises against the 'public interest' in addition to its voting rights at the scheme committee.

75. However, the OFT does not consider that the role of the Council in itself is sufficient to prevent a price increase post-merger.

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[18] Given that the Busway is not yet in operation, it is not entirely precise to refer to 'price increases' as a potential anti-competitive effect arising from the merger. The relevant question is, rather, whether fares in the Busway (or on any network tickets that can also be used in the Busway) post-merger might be initially set at a higher level than it would have otherwise been the case, as well as whether the initial fares will be subject to higher potential increases than would have otherwise been the case. However, this shorthand is used for convenience in this decision.

76. First, it is not clear what the Council would consider to be a fare rise 'against the public interest'. For example, a price increase below five per cent as a result of the merger is a non-negligible effect from a competition perspective, but might be insufficient to trigger a reaction from the Council in terms of exercising its voting and veto powers. In addition, it is not necessarily true that a price increase following the merger would drive the number of passengers down to any noticeable extent from the perspective of the Council such that it would necessarily veto the price increase. The OFT considers, therefore, that there is scope for price increases post-merger, albeit that the level of these is likely to be limited by the Council.

77. Second, while the Council might have some power over the multi-operator fares, it cannot control any anti-competitive effects arising from the merger on single-operator tickets, as will be discussed below.

78. Third, given the substantial resource commitment that the Busway represents to the Council, and given that Stagecoach will be by far the largest Busway Operator post-merger (it will run six out of eight services per hour), there will inevitably be a symbiotic relationship between the Council and Stagecoach. Stagecoach submits that having good relations with the Council is essential for its business in the Busway, but the OFT also considers that the (at least short-term) success of the Busway also depends on Stagecoach not dropping out. While the OFT is confident that the Council would wish to protect the interests of Busway passengers against any attempt by Stagecoach to impose excessive price increases, as discussed above, there remains the possibility of a gap between anti-competitive effects and price increases at a level that would trigger the Council's reaction.

79. Passengers' sensitivity to price increases discussed above is also relevant for the argument made by Stagecoach that, because the Council's intention is to attract to the Busway passengers who normally use cars on the congested A14, cars will remain an alternative mode of transport that Busway users could revert back to if prices went up. Stagecoach cites an external report[19] which states that the demand for Busway services 'is likely to fall if there is an increase in either fares or journey times'. Whereas this statement means that the demand for the Busway is not

[19] WS Atkins Transport Assessment, paragraph 6.21.

inelastic (as one would expect), it does not elucidate **how** elastic it is. Given that a significant proportion of passengers on the Busway will have switched from cars to the Busway, it is not unreasonable to assume that they will not be particularly price-elastic given that public and private transport are typically not very close substitutes for each other.[20] Such price insensitivity, to the extent it exists, would be particularly true in relation to the initial fares (as opposed to future increases to the initial fares) due to the lack of good benchmarks for passengers to establish whether tickets are 'too expensive' and to the distinct advantages (especially faster and more comfortable journeys) associated with travelling on the Busway.

Multi-operator and single-operator tickets

80. Stagecoach submits that the majority of tickets sold on the Busway will be multi-operator tickets and that this would lessen the importance of price competition between operators. The OFT accepts that the availability of multi-operator tickets is part of the vision for the Busway. The Council intends the Busway to be a 'turn up and go' service in which passengers will take the first bus arriving at the stop.

Single-operator tickets

81. Although it is true that multi-operator tickets will effectively impose a cap on single-operator single tickets, and some constraint on single-operator network tickets, it is not necessarily the case that passengers will prefer to purchase a multi-operator ticket on the Busway rather than a (slightly cheaper) single ticket or a version of an individual operator's network ticket (for example, Stagecoach's Megarider ticket). Each Busway Operator will be allowed to introduce single-operator tickets, for which (in contrast to the multi-operator ticket) they will have total freedom to set prices and fare structure.

82. Pre-merger, a multi-operator ticket would have been comparatively more attractive than it will be post-merger, given that the chance of the first bus to arrive at the stop being a Stagecoach bus was (absent the merger) only three out of eight (38 per cent) (see paragraph 66 above). Post-merger, six out of eight buses (75 per cent) on the Busway will be

[20] See the *CC methodology report*, para 14.

Stagecoach's. It seems much more likely that in the post-merger scenario customers will be relatively more willing to buy Stagecoach's exclusive tickets (given the increased proportion of buses on the Busway that will be Stagecoach) instead of the multi-operator given the incentive of either (i) a cheaper single ticket or (ii) a network ticket that, albeit more expensive, allows access to Stagecoach's wider bus network.

83. This is particularly true in view of the extensive Stagecoach bus network in Cambridgeshire (see discussion on paragraphs 40 to 48). Stagecoach said that it would not alter the prices of its successful Megarider ticket to benefit from a (hypothetical, in their view) lessening of competition in a small part of their network, that is, the Busway. However, Stagecoach could, for example, launch a new version of its Megarider ticket (that is, a 'Busway Megarider'), that allows access to its regular network **and** to the Busway at a premium price.[21] The OFT notes that the availability of network tickets can be generally considered to be an efficiency associated with bus networks. However, this is not to say that there cannot be anti-competitive effects in relation to those tickets. In this case, whereas pre-merger the price of such a 'Busway Megarider' would be to a certain extent constrained by the attractive multi-operator ticket (given the more even distribution of services across operators discussed above), the OFT considers it plausible that, post-merger, Stagecoach will be able to price the hypothetical Busway Megarider at a higher level due to the loss of that constraint.

84. There is also scope, albeit potentially somewhat limited, for increasing the price of single-trip single-operator tickets. To the OFT's knowledge, the price differential between the multi-operator tickets and the single-operator tickets has not yet been set, although the Council has said that it envisages that there will only be a small premium for the multi-operator ticket over the operator-specific prices. As such, it is possible that, given the presence of two rather than three competitors on the Busway, conditions of competition will be relaxed and the merged entity will have an incentive to price its single-operator tickets closer to the cap effectively created by the multi-operator tickets.

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[21] Indeed, Stagecoach already offers two types of 'Megarider' tickets in Cambridgeshire. The £10 Megarider is valid for seven days unlimited travel using both Park & Ride and other Stagecoach Citi routes. The £20 Megarider Plus is valid for seven days unlimited travel on Stagecoach and Citi buses throughout Cambridgeshire.

Multi-operator tickets

85. In addition to the concerns set out above, contrary to Stagecoach's submissions, it may also be the case that the post-merger price for the multi-operator ticket will be higher than it would have been absent the merger. First, it appears plausible that, pre-merger, Cavalier and Whippet would have the incentive to vote to price the multi-operator ticket at a lower level to make it more attractive in comparison with Stagecoach's Megarider. Second, given the symbiotic relation between Stagecoach and the Council in relation to the Busway, which is strengthened by the merger, the Council might find it more difficult to oppose the setting of the multi-operator tickets at a higher level than it would have been able to do without the merger if it perceives that, in doing so, it would, for example, put the realisation or timetable of the Busway in jeopardy.

Services

86. A number of the arguments made above in relation to fare raises also apply equally to service levels. Although the Busway Operators have signed up to minimum service levels, the merger could cause the merged entity (and possibly also Whippet) to provide lower service levels (as opposed to price increases) than would have been the case absent the merger, if one assumes that the optimum number of services absent the merger is above the minimum service levels.

Barriers to entry

87. The evidence before the OFT suggests that barriers to entry into the Busway would be higher than into regular bus operations, in particular in view of the five-year exclusivity for the existing Bus Operators discussed above. In addition, because specially adapted, high-specification vehicles are required to operate on the Busway[22], a decision the Busway to enter involves significantly more financial commitment than the normal decision by a bus operator to switch between 'regular' routes.

[22] Stagecoach submits that the price differential between a regular new bus and a bus that will meet the specifications to operate on the Busway is £30,000.

88. The OFT has not received any evidence that the prospect of future entry into the Busway is sufficiently timely, likely and sufficient in scope such that it would prevent any attempt by the merged entity to increase prices or decrease service levels in the Busway. In particular, only five bus operators originally expressed interest in operating on the Busway, and only three subsequently signed inception agreements.

89. The OFT accepts that displays of interest when the Council first invited operators to get involved on the project tender may not necessarily be a wholly accurate proxy for likely levels of interest in entering once the Busway is up and running, when entry will be less risky than committing to a project almost three years before it is implemented and when the necessary infra-structure had not yet been built (as it was the case when the Busway Operators signed the inception agreements). However, it would be too speculative for the OFT to conclude that, even when the Busway is operative, there would be likely to be other new entrants, in any event, any such new entrants would not necessarily meet the timely, likely and sufficient criteria and have not in fact been identified by the OFT in the course of its investigation.

View of the Council

90. The OFT has been in close contact with the Busway team within the Council throughout this investigation. In the Council's view, despite a reduction in the number of Busway Operators, the merger will not have any practical impact. The Council will seek a regular headway on services and thinks that ensuring that just a small premium for multi-operator tickets would be in customers' best interests, which, in conjunction with its veto powers, would prevent larger price increases. In addition, the Council pointed out that operators will be subject to the Quality Bus Partnership Scheme and that potential entrants can exploit unfulfilled demand. The OFT has considered each of these points, and its analysis of them, in the reasoning set out above.

Conclusion on Busway

91. The OFT considers that, overall, the reduction in the number of future independent operators on the Busway from three to two, given conditions of competition, creates a realistic prospect of a substantial lessening of competition. On balance, the OFT considers that it is more than fanciful

that the merger will allow Stagecoach to increase prices or decrease service levels on the Busway in comparison to what the conditions would have been absent the merger. The OFT believes that the Council plays an important role in ensuring that multi-operator tickets on the Busway are not priced excessively, but as discussed above, its incentives and powers are not sufficient to rule out anti-competitive effects arising from the merger.

92. The OFT considers it important to make two precisions in relation to this finding. First, as discussed above, there is a limit to the scope for price increases due to the fare structure as presently envisaged and the role played by the Council. Second, a substantial lessening of competition would only occur in the event that the correct counterfactual is that Cavalier would have stayed in the Busway. Taking the evidence on this second point in the round, the OFT considers that the prospect of Cavalier staying in the Busway are sufficiently great that, overall, the merger can be said to create the realistic prospect of a substantial lessening of competition.

EXCEPTIONS TO THE DUTY TO REFER

Introduction

93. The OFT's duty to refer under section 22(1) is subject to the application of certain discretionary exceptions, including the markets of insufficient importance, or de minimis, exception under section 22(2)(a) and the undertakings in lieu exception under section 73(2) of the Act. Stagecoach argued that the OFT should apply the de minimis exception to the duty to refer[23] on the basis that the annual size of the Busway 'market' was below £10 million.

Undertakings in lieu of reference and de minimis

94. As stated in the Dunfermline/BRN case,[24] and as explained further in the BOC/Ineos case,[25] the OFT believes that it would be proportionate to refer

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[23] See OFT 516 b, November 2007.

[24] OFT *Completed acquisition by Dunfermline Press Limited of the Berkshire Regional Newspapers business from Trinity Mirror plc* 4 February 2008.

[25] OFT *Anticipated acquisition by BOC Limited of the packaged chlorine business and assets carried on by Ineos Chlor Limited* 29 May 2008.

a problematic merger (that is, not to apply the de minimis exception) where the OFT considers that it is 'in principle' clearly open to the party or parties to offer a clear-cut undertaking in lieu of reference – but they choose not to do so - because the recurring benefits of avoiding consumer harm by means of undertakings in lieu in a given, and all future like cases, outweighs the one-off costs of a reference.

95. In this case, it was not clear to the OFT, based on its objective evaluation of the transaction, that this case was a clear candidate for undertakings in lieu. It does not seem to be easy to distinguish the assets required to operate on the Busway from the assets employed in the wider Cavalier business, in particular given the commonality of depots and the link, for example in ticketing, between the Busway and the wider Stagecoach regional network. Therefore, the OFT does not consider that there is a clear cut divestiture package and accepts that it would not be appropriate, at this stage of the analysis, to rule out an evaluation of the de minimis exception in this case given that it would not appear to be open to the parties to offer a clear-cut – that is, effective and proportionate – undertaking in lieu.

Application of the markets of insufficient importance exception to this case

96. The pivotal issue for the OFT in applying its de minimis exception is determining whether the impact of the merger is likely to be particularly significant (such that the de minimis exception should not be applied) or more limited (when the OFT may apply the de minimis exception). The factors that the OFT considers in making this determination were set out in detail in the BOC/Ineos case and were applied again recently (in favour of exercise of the discretion) in FMC/ISP[26] and (against the exercise of the discretion) in Nufarm/AH Marks.[27] Those factors are:

- market size
- strength of the OFT's concern
- magnitude of competition lost by the merger
- durability of the merger's impact, and
- transaction rationale and the value of deterrence.

[26] OFT *Anticipated acquisition by FMC Corporation of the alginates business of ISP Holdings (U.K.) Limited* 30 July 2008.

[27] OFT *Completed acquisition by Nufarm Limited of AH Marks Holdings Limited* 29 August 2008.

97. The OFT considered each of the factors above in determining whether to exercise its discretion in this case.

98. Market size – The OFT has found that there is a realistic prospect of a substantial lessening of competition in the Busway. There are a number of variables affecting the estimation of the revenues on the Busway, but the OFT considers that a reasonable assumption is that on the first few years the total annual size of the market (that is, the revenues associated with the Busway as a whole[28]) will be in the region of £3 million. The total size of the affected market is in the lower to mid-range of the OFT's £0 – £10 million band, meaning that whilst the de minimis exception is potentially applicable, the size of the market is nevertheless non-negligible.

99. Strength of the OFT's concerns – The OFT's belief that the transaction may be expected to result in a substantial lessening of competition in the Busway is not particularly strong, that is, it is above fanciful and in the 'may be the case' standard, but materially below a 50 per cent likelihood. As a result, the relatively low strength of the OFT's belief that harm will result from the merger, although not in itself conclusive, points towards the exercise of the de minimis exception in this case.

100. Magnitude of competition lost by the merger – The merger causes a reduction in the number of operators on the Busway from three to two. However, as discussed at length above, the OFT considers that any price increases resulting from the merger may not be that significant. The main reasons for this are the limited ability of Stagecoach to cause an increase on multi-operator tickets, the constraint on Stagecoach's own tickets posed by multi-operator tickets, and the role played by the Council on limiting and vetoing price increases. As a result, any price increases resulting from the merger would not be expected to be particularly significant, pointing strongly in favour of the exercise of the de minimis discretion.

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[28] The OFT normally takes into account only the overlapping flows where an SLC can arise when calculating the size of the market in transport cases. However, given that the merging parties and Whippet are the only operators who have signed inception agreements, as well as that they are the most likely operators in the parts of the Busway that have not yet been contracted, the OFT considers it should, on a conservative approach, consider the predicted revenues for the entire Busway.

101. Durability of the merger's impact – The Busway Operators have a five-year exclusivity on the Busway, and therefore any anti-competitive effects caused by the merger would be expected to last for at least that period. However, the Council may bring in new operators in case the existing Bus Operators do not fulfil the overall minimum service levels. In that sense, there is limited scope for the merged entity to profitably refuse to extend its services post-merger (as this could precipitate the entry of a new operator or expansion by Whippet). The limited (but non-negligible) scope for price effects has been discussed above.

102. Transaction rationale and the value of deterrence – The Busway is a singular project in the UK, and the rules applying to it (in particular the Council's role in setting price and service levels and the exclusivity clause) are different from the conditions of competition affecting regular bus operations. In that sense, not applying the de minimis exception to this case should not have the effect of deterring similar transactions that have an anti-competitive impact from being contemplated or pursued due to the peculiarity of the Busway. On the other hand, internal documents from Stagecoach indicate that an important rationale for the potential acquisition of Whippet's Busway business (which the OFT understands was being contemplated as an alternative to the acquisition of Cavalier) was to avoid its takeover from one of major bus groups. The OFT considers it reasonable to consider that the same rationale applies to the acquisition of Cavalier, in particular given that Stagecoach was primarily interested in the Busway operations. In sum, taking into account the unique nature of the Busway project, and the implications for deterrence considerations, but given also that the transaction might be motivated materially by the acquisition of market power on the Busway, the OFT considers it appropriate not to consider deterrence a particular aggravating factor in this decision for the purposes of its de minimis assessment.

103. Overall, although the factors are relatively finely balanced in this case, the OFT considers that the evidence points towards the impact of the merger being relatively limited. In particular, the size of the market is well below the £10 million threshold, there is only a relatively low probability of anti-competitive effects arising from the merger, and these, if they occur, will be of limited scope for the reasons discussed above. The OFT therefore has decided to exercise its discretion not to refer this transaction to the Competition Commission.

THIRD PARTY VIEWS

104. The OFT has conducted an extensive consultation with third parties in the investigation of this merger. Specific third party comments were dealt with throughout the text of the decision.

105. Most third parties were unconcerned about the merger. In particular, the three local councils contacted by the OFT (Cambridge County, Peterborough City and Lincolnshire County) not only were unconcerned but also thought the merger would have a positive impact on their communities.

ASSESSMENT

106. The parties overlap in the supply of commercial bus services on three commercial flows, on the Cambridge Guided Busway. They are both present in the wider area of Cambridgeshire and Peterborough.

107. On the three overlapping commercial flows, the OFT considered that the merger does not create competition concerns, in particular in view of the threat of expansion and/or entry by other bus operators.

108. On the wider area comprising Cambridgeshire and Peterborough, the OFT considered whether Cavalier exerted a significant competitive constraint on Stagecoach, or vice-versa, even when not currently competing on a flow-by-flow basis, as a potential competitor. However, the OFT could not find any evidence that Cavalier should be regarded as a potential competitor on Stagecoach (or vice-versa) such that its removal generated competition concerns. The OFT also considered that, even if such a constraint exists, Cavalier is not in a unique position: Whippet remains as an independent competitor post-merger, is in a similar position towards Stagecoach as Cavalier was pre-merger.

109. The OFT considers that the removal of Cavalier as an independent competitor on the Busway creates the realistic prospect of a substantial lessening of competition, as it is it is more than fanciful that the merger will allow Stagecoach to increase prices or decrease service levels on the Busway in comparison to what the conditions would have been absent the merger. Despite the important role played by the Council in seeking to

ensure that prices on the Busway are not excessive, the OFT considers that it may be the case that its incentives and powers are not sufficient to dismiss the possibility of anti-competitive effects arising from the merger.

110. Consequently, the OFT believes that it 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.

111. However, the OFT has decided to exercise its discretion not to refer this merger to the CC on the basis that the market concerned is of insufficient importance to justify a reference. Overall, although the factors are relatively finely balanced in this case, the OFT considers that the evidence points towards the impact of the merger being relatively small. In particular, the size of the market is well below the £10 million threshold, there is only a relatively low probability of anti-competitive effects arising from the merger, and these, if they occur, will be of limited scope for the reasons discussed above.

DECISION

112. This merger will therefore not be referred to the Competition Commission pursuant to section 22(2)(a) of the Act.