# Anticipated acquisition by Carillion plc of Alfred McAlpine plc

ME/3457/07

The OFT's decision on reference under section 33(1) given on 8 February 2008.
Full text of decision published on 19 February 2008.

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

## PARTIES

1. **Carillion plc** (Carillion) is a provider of construction and various building-related maintenance and facilities management (FM) services. It is active in a wide range of areas within the UK including the construction and FM of commercial and defence buildings, hospitals, and road and rail infrastructure. It also provides a fleet car hire and management service. For the year ending 31 December 2006 Carillion's UK turnover was approximately £2.8 billion.

2. **Alfred McAlpine plc** (McAlpine) is a provider of construction, FM and civil engineering services. McAlpine's construction and FM activities include commercial buildings, rail and road infrastructure, water and other utilities, and government-owned buildings. McAlpine also provides maintenance and renewal services to the utilities sector and a number of IT services. Moreover, McAlpine provides fleet car hire and management services in the UK and supplies slate for aggregates, roofing and architectural products. For the year ending 31 December 2006, McAlpine's turnover in the UK was over £1 billion.

## TRANSACTION

3. On 10 December 2007 Carillion and McAlpine announced that they had reached agreement on the terms of a recommended proposal whereby Carillion would acquire the entire share capital of McAlpine. McAlpine's shareholders voted in favour of this arrangement on 21 January 2008. The total consideration for the acquisition will be around £570 million.

4. Carillion notified the Office of Fair Trading (OFT) of this merger on 21 December 2007 and the OFT's administrative target date to announce a decision is 20 February 2008.

## JURISDICTION

5. The EC Merger Regulation (Regulation 139/04; ECMR) does not apply because each party achieves more than two-thirds of its EC-wide turnover in the UK, thus meeting the two-thirds rule in Article 1(3) ECMR.

6. As a result of this transaction Carillion and McAlpine will cease to be distinct. The UK turnover of McAlpine exceeds £70 million, so the turnover test in section 23(1)(b) of the Enterprise Act 2002 (the Act) is satisfied.

7. The OFT therefore believes that it is or may be the case that arrangements are in progress or in contemplation which, if carried into effect, will result in the creation of a relevant merger situation.

## MARKET DEFINITION

8. The parties overlap in the supply of construction, FM and fleet car hire and management services. Each of these areas is discussed below.

### Construction

Product scope

9. Previous OFT decisions have explored the possibility that the construction sector involves a number of markets from some combination of the private housing, public housing, non-housing new building, infrastructure[1] and

[1] 'Infrastructure' covers construction work for roads, railways, airports, utilities (electricity, gas and water) and telecommunications.

repair, maintenance and improvement (RMI) segments.[2] Distinguishing / segmenting by industry sector (for example, education, health, defence, office and retail) and by contract size (since construction companies are able to take on different levels of financial risk associated with contracts) has also been discussed in previous cases. However, in none of these decisions has the OFT had to conclude on the precise scope of the product market.

10. In this case, the parties submitted that firms who are active in one type of construction activity (for example, public housing building) of the UK construction sector can and do switch to the provision of other construction services (for example, non-housing building) since the key skills required are the same. Further, the parties submitted that all of the major construction suppliers operate across a number of different industry sectors.

11. Several third parties contacted by the OFT in this investigation corroborated the parties' argument, confirming that switching from one segment to another (for example, from non-housing new builds to private or public housing) is easy and can be achieved within one year.[3] One third party told the OFT that moving into infrastructure work is more difficult since it might take several years to establish a meaningful business in this area.

12. By size of contract, the parties submitted that most of their main competitors are capable of bidding for contracts of all sizes (raising the possibility that even if segmenting by contract size were sensible, a chain of substitution may link them to form a single market). Third party responses to the OFT corroborated this which indicates that it is not appropriate to segment by contract size.

13. The OFT has not found it necessary to conclude on the product market in this case since the outcome of the competition assessment is the same

[2] For example, see: OFT decision of 12 October 2007, Completed acquisition by Balfour Beatty plc of Cowlin Group Limited; OFT decision of 17 May 2007, Anticipated acquisition by Taylor Woodrow plc of George Wimpey plc; OFT decision of 13 April 2007, Anticipated acquisition by Barratt Developments plc of Wilson Bowden plc; OFT decision of 1 September 2006, Anticipated acquisition by Balfour Beatty plc of Birse Group plc; and OFT decision of 24 January 2006, Anticipated acquisition by Carillion plc of Mowlem plc.

[3] The third parties contacted by the OFT were all large construction companies involved in multiple construction segments.

regardless of which approach is employed. However, for the purposes of this competition assessment, the OFT has examined the case on the basis of construction services as a whole, and by the various sector segmentations and industry sectors listed in paragraph 9 above.

Geographic scope

14. The parties submitted that the relevant geographic market for construction services is national. Third parties tended to agree. Most competitors contacted by the OFT said that the geographic focus of their construction activities is national although two said that sometimes it is difficult to work in unfamiliar geographic areas because of insufficient knowledge of local customers, suppliers or subcontractors.

15. Almost all construction customers reported that there are no geographic constraints and that they consider construction firms from the whole of the UK.

16. The OFT has not found it necessary to conclude on the geographic market in this case since the outcome of the competition assessment is the same regardless of which approach is employed. For the purpose of the competition assessment, however, the OFT has conducted its analysis on a national and a regional basis.

**Facilities management**

Product scope

17. FM services cover a broad range of activities from cleaning services, security services, building upkeep to the operation of technical installations.

18. The parties submitted that FM services should not be segmented into smaller product markets. They said that operations can be subcontracted and key skills required are generally the same for many segments and industry sectors (making switching between them easy). Third parties contacted by the OFT agreed.

19. In this case the OFT has not found it necessary to conclude on whether all FM services should be assessed together or segmented into industry sector

since such delineation does not affect the outcome of the competition assessment.

Geographic scope

20. The parties submitted that the relevant geographic market for FM services is national. No third party suggested or provided evidence that the market is narrower than national. Indeed, several customers said that local proximity to the supplier of FM services was not a key factor in their choice.

21. On the basis of the evidence received, and consistent with a previous OFT decision, the OFT has examined the effects of the merger on FM services on a national basis.[4]

**Fleet car hire and management**

Product scope

22. Fleet car hire and management (FCH) involves leasing cars to customers, sourcing those cars, repairing and maintaining them, and breakdown and accident management.

23. In a previous case, Lex/HSBC, the OFT considered the possibility that the supply of FCH services to commercial customers was distinct from the supply to private hire customers because of differing distribution channels.[5] In that case the OFT also considered whether FCH should be segmented into types of services (for example, funding, maintenance and servicing of leased cars) but decided to examine the merger on the basis of the total bundle of FCH services. The parties submitted that the OFT should assess this case on the same basis as it did in Lex/HSBC.

24. In this case no third parties contacted by the OFT considered that FCH services should be segmented.

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[4] This is consistent with the approach the OFT adopted in Carillion / Mowlem.

[5] OFT decision of 25 October 2005, Anticipated acquisition by Lex Vehicle Leasing Limited of the fleet car hire business of HSBC Bank plc.

25. On the basis of the evidence received, and consistent with its Lex/HSBC decision, the OFT has examined this merger on the basis of all FCH services.

Geographic market

26. The parties submitted that the relevant geographic market for FCH services is national. No third party disagreed. Some competitors told the OFT that they are able to provide services on a nationwide basis and are not constrained to a particular geographic location.

27. Therefore the OFT has examined the effects of the merger on FCH services on a national basis.[6]

## HORIZONTAL ISSUES

### Construction

Unilateral effects

National level

28. According to the latest *Construction Statistics* published by the Department for Business, Enterprise and Regulatory Reform (BERR) in August 2007, the total output of construction activities (including RMI) in Great Britain in 2006 amounted to around £114 billion.[7]

29. Regardless of how market shares are calculated, the parties' national share of construction services is low. For example, their combined share of total construction work by value is less than [0-5] per cent. By new contracts won (an indication of current performance) in the UK during 2006 (latest available data) the parties' combined share of supply is [0-5] per cent (by contract value). Across the various segments of construction activity (such as public housing, private housing, infrastructure; see paragraph 9 for more detail), the parties' combined share is also low (less than 10 per cent) for

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[6] This is consistent with the OFT's approach in Lex / HSBC.

[7] Construction Statistics Annual 2007, Table 2.1, p. 31 (available at: www.berr.gov.uk/files/file42061.pdf). These data do not include Northern Ireland. However, the parties' share of construction activity in Northern Ireland is less than [0-5] per cent across all segments.

all segments. Their highest combined share on this basis is in the infrastructure segment where they have a combined share of [5-10] per cent (by value of contracts). Furthermore, by industry sector (for example, education or health) the parties' combined share is equally low – less than 10 per cent across all sectors.

30. According to the parties Carillion will become the second largest construction company in the UK (measured by new orders), behind Balfour Beatty plc, and will be of a similar size to Skanska UK plc, Kier Group plc and Bovis Lend Lease Limited. Customers told the OFT that these construction firms will continue to offer effective competition to Carillion after the merger as will other firms such as Sir Robert McAlpine[8], Laing O'Rourke, AMEC, Morgan Sindall and Edmund Nuttall.

31. The parties are involved in a number of joint ventures with some of these competitors, including Balfour Beatty, AMEC, and Sir Robert McAlpine.[9] However, all but one of these joint ventures are for the purposes of a set number (usually one off) projects and hence will not affect the parties' incentives when bidding for future contracts. The one on-going joint venture (with Europool BV) is Eurailscout, a rail infrastructure inspection company. The increment arising from the merger for rail infrastructure work is very small (below [0-5] per cent) indicating that the loss of competition arising from the merger is negligible.[10] No third party raised concerns about the impact of the merger on rail infrastructure work.

32. The parties submitted information on construction bids that they had participated in over the past three years (2005 to 2007 inclusive). They categorised the instances in which they both bid for the same contract into 'new general construction' and 'infrastructure' contracts. In relation to the public and private housing segments, there were no instances where the parties competed for the same housing contract.

33. Within the 'new general construction' (that is, non-housing new building) segment (which is worth around £35 billion a year) the parties only competed against each other on [0-10] occasions. For [0-5] of these

[8] McAlpine and Sir Robert McAlpine are separate companies without any corporate connection between them.

[9] The parties submitted that, combined, they are involved in almost 60 joint ventures.

contracts one of the parties won and in two (of these [0-5]) the parties were winner and runner up.[11] The fact that the parties bid against each other on a such a small number of occasions supports the proposition that the parties are not close competitors in bidding for 'new general construction' contracts.

34. Within the 'infrastructure' segment (worth around £6.5 billion) the parties competed against each other on [40-50] occasions. On one contract the customer has not yet selected a winner (since there is a legal challenge with respect to the planning approval) and in two others the parties could not confidently recall whether either of them was the runner up (although the parties submitted that neither won those two contracts). However, it makes no difference to the outcome of this merger assessment if the bidding information is analysed on the basis of [40-50] bids. In no instance that the parties could identify was one party the runner up to the other in winning the contract (although in [5-15] instances in which one of the parties was awarded the contract the parties could not identify who the runner up was). Notwithstanding that the parties bid for the same contract on a relatively significant number of occasions, the bidding data – in particular the fact that the parties' were not the first and second choices in any contract – supports the proposition that the parties are not particularly close competitors in bidding for 'infrastructure' contracts.[12]

35. In light of the above bidding data and the fact that the parties' combined share of new construction contracts is less than 10 per cent (overall and for all segments), the OFT considers that competition concerns do not arise in relation to construction services at a national level.

36. This view is confirmed if the parties' competitive strength is viewed in terms of contract size. Both parties receive the bulk of their construction revenues from contracts worth at least £20 million (Carillion receives about [55-65] per cent of its construction revenues from contracts worth over £50 million). Nevertheless, both parties bid for and win contracts of all value sizes. The information before the OFT does not show that after the merger Carillion will hold a significant share of contracts of values above or

[10] The parties submitted that in 2006 Carillion's turnover in rail infrastructure work was around £[-]m while McAlpine's was around £[-]m. Total rail infrastructure work in the UK was worth around £3.2 billion.

[11] Two tenders are still outstanding.

below £20 million (for contracts worth less than £20 million the parties' combined share is less than [0-5] per cent, and for those worth over £20 million the parties' combined share is less then 10 per cent).

Regional level

37. When the parties' activities are analysed at the regional level, with the exception of infrastructure work, the parties do not together account for more than 15 per cent of any type of construction activity (for example, private housing or non-housing new work). As regards infrastructure work, the parties together account for around [25-35] per cent (increment [5-15] per cent) in the North East and around [15-25] per cent (increment [0-10] per cent) in the East Midlands.

38. The OFT has been unable to obtain any reliable estimates for the shares of infrastructure work accounted for by rivals in the North East and East Midlands. However, bidding information (referred to in paragraph 34 above) indicates that the parties competed against each other for an infrastructure contract located solely in the North East on only one occasion over the past three years. On [5-15] occasions[13] the parties competed against each other for a contract located in the East Midlands. Of these occasions the parties have not been able to identify any contract for which one was the runner up to the other. Accordingly, these bidding data – in particular, the fact that the parties competed against each other only once for a North East contract, and were not the first and second choices for any East Midlands contracts – supports the proposition that the parties are not particularly close competitors for infrastructure work in the North East or East Midlands.

Barriers to entry and expansion

39. The parties submitted that barriers to entry into construction services are low. They pointed to BERR estimates which show that there were around 186,000 construction firms in the UK in 2006 and around 1,300 of these employed more than 80 people (and over 50 employed more than 1,200

[12] To put this in perspective, Carillion submitted that it bids for around [>500] construction contracts per year and McAlpine bids for around [>200] construction contracts per year.

[13] From the information submitted, it was unclear whether the location of one bid was the East Midlands or West Midlands.

people). This, in the view of the parties, suggests that the construction market is highly fragmented and characterised by ease of entry and exit.

40. As discussed in paragraph 11 above, third parties told the OFT that switching between segments of construction activities is, in the main, easy. One third party said that entry barriers are low because much of the work on a project is subcontracted, there is a well developed plant hire market (and therefore owning your own plant is not a barrier), there are limited economies of scale to be realised (mostly because building materials are purchased locally to keep down transport costs) and staff are generally mobile.

41. Two third parties submitted that knowledge and relationships at the local / regional level are important (paragraph 14 above) which may form a barrier to entry to some extent.

42. In this case the OFT has not found it necessary to conclude on the strength of barriers to entry in construction services since it does not affect the outcome of its competition assessment.

Countervailing buyer power

43. One customer told the OFT that it did consider that it had some buyer power which would countervail any price increases since it faced sufficient choice of suppliers. Others did not say that they possessed countervailing buyer power although acknowledged that there is sufficient competition between suppliers for their contracts.

44. In this case the OFT has not found it necessary to conclude on the strength of countervailing buyer power since it does not affect the outcome of its competition assessment.

Coordinated effects

45. The OFT has considered whether the merger creates or strengthens the opportunity for rivals to engage in coordinated behaviour, whether tacit or explicit, within the construction industry such as raising prices, reducing quality or curtailing output.

46. Last year the OFT announced that it was investigating bid rigging activities in England (especially in the East Midlands, Yorkshire and Humberside).[14] However, in this merger investigation the OFT has not received any evidence from any third party to suggest that this merger will strengthen any coordinated behaviour within the industry. Moreover, there is no evidence presently available to support a theory that the merger raises the likelihood of coordinated behaviour within the industry.

47. In reaching this conclusion the OFT has taken into account that, on the evidence before it, (i) the merger does not create a structural forum for contact between potential members of a collusive oligopoly that did not previously exist; (ii) there is no evidence before the OFT that McAlpine currently acts as a maverick[15]; (iii) for construction as a whole, as well as for individual construction segments (such as non-housing building and housing building), the merger does not appreciably increase symmetry between rivals since the increment in share is small on a national and (albeit to a slightly lesser degree) regional level, thereby reducing the incentive to coordinate; and (iv) the number of firms in the sector after the merger will remain relatively high which means that the merger does not substantially increase concentration and, to this extent, makes adverse effects based on collusion flowing from this particular merger less likely.

48. Accordingly, the OFT does not consider that there is a realistic prospect of the merger resulting in tacit or explicit coordination in the supply of construction services in the UK. The fact that the OFT concludes there is insufficient evidentiary basis for a merger effect in the relevant market(s) carries no inference in relation to the question of whether past infringements based on explicit collusion have been or will be established.

**Facilities management**

49. Estimates of the value of the FM services market vary greatly – from around £14 billion to £65 billion.[16] Depending on which estimate is used, after the merger Carillion will account for either a little less than 10 per cent or around [0-5] per cent of FM services in the UK.

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[14] OFT press release 22 March 2007.

[15] In the sense of acting as a binding constraint on coordination due to incentives contrary to those of other major firms in the market.

[16] Using market research reports from AMA Research, i-FM and MBD (Market and Business Development).

50. Bidding information submitted by the parties indicated that they competed for the same contract in only [0-15] instances in the three years 2005 to 2007 (inclusive).[17] Of these [0-15], there were [0-10] instances in which the parties knew who had been the runner up and in none of these occasions was one of the parties runner up to the other. This indicates that the parties have not been particularly close competitors in the provision of FM services.

51. Customers contacted by the OFT named a number of suppliers as credible rivals to the merging parties including, among others, Dalkia, Johnson Controls, Sodexho, ISS UK and Mitie Group.

52. By industry sector, Carillion will not account for a high share of supply in any sector post merger (its highest share will be around [10-20] per cent in the corporate sector), and a number of significant suppliers will remain.

Barriers to entry and expansion

53. Barriers to entry in FM services are low according to the parties. They submitted that customers can and do switch between suppliers, even on larger jobs.

54. Third parties agreed that barriers to entry are low. They said that switching between sectors and services is easy and timely. The OFT has been told by competitors of recent entrants, including CB Richard Ellis, Jones Lang LaSalle and Macro.

55. Since it does not affect the outcome in this case, the OFT has not found it necessary to conclude on the strength of barriers to entry in FM services.

**Fleet car hire and management**

56. The parties presented to the OFT a ranking of the top 20 FCH contract hire companies in the UK (by fleet size). Neither of the parties featured in this list and after the merger Carillion will have a fleet of around 17,500 cars (Lex, the market leader, has a fleet size of about 260,000 cars) and will

[17] Carillion bids for around [>1000] FM contracts a year while McAlpine bids for around [0-100] per year.

account for less than [0-5] per cent of total supply (ranking near the bottom of the top 20 list).

57. The parties also submitted that the large majority (around 80-90 per cent) of their fleets are used for internal purposes.

58. The parties were not aware of any instance in which they competed against each other for the same customer contract.

Barriers to entry and expansion

59. Competitors told the OFT that barriers to entry in FCH services are low. Examples of requirements to enter the supply of FCH services include having adequate funding in place and having a reliable IT system.

60. Since it does not affect the outcome in this case, the OFT has not found it necessary to conclude on the strength of barriers to entry in FCH services.

## VERTICAL ISSUES

61. The parties submitted that in theory vertical issues may be present since McAlpine supplies aggregates, pitched roofing tiles and architectural stone products (for floors, paving and cladding), all of which may be used as inputs by construction firms in their activities. The OFT was told by the parties that McAlpine is currently in the process of selling off these lines of business. [End note 1]

62. The parties also submitted that the merger will not materially change Carillion's ability or incentive to foreclose rivals (for example, by refusing supply or increasing input costs). In north Wales (where McAlpine's aggregates quarry is located) McAlpine's share of the supply of aggregates is around [5-15] per cent.[18] Similarly, McAlpine accounts for less than [0-10] per cent of the supply of pitched roofing tiles on a national basis, and less than [0-5] per cent of the supply of architectural stone products.

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[18] On a 50 miles radius. Other OFT decisions have examined aggregates on a local basis – for example, OFT decision of 29 September 2004, Anticipated acquisition by Anglo American plc of Johnston Group plc.

63. No third party raised concerns with the OFT over foreclosure or other vertically related issues.

64. The OFT does not consider that vertical concerns arise in this case since McAlpine accounts for a very small share of these inputs. Additionally, McAlpine is already an integrated supplier and the OFT has not received any evidence that it had tried to foreclose rivals previously.

**THIRD PARTY VIEWS**

65. No third parties raised competition concerns with the OFT about this merger.

66. In respect of construction services, customers generally told the OFT that there was sufficient choice within the marketplace for them to select a competitive provider of construction services.

67. In relation to FM services, some customers said that they award contracts via a competitive tender and enjoy a degree of countervailing buyer power.

68. In relation to FCH services, customers told the OFT that the marketplace was competitive. Customers and competitors named a number of credible, in some cases much larger, rivals including Lex, ALD, Lloyds, Arval and Lombard.

**ASSESSMENT**

69. The parties overlap in a wide range of construction activities. The OFT has not found it necessary to conclude on the scope of the product market in this case since the outcome of its competition assessment does not vary according to the product market definition used.

70. Regardless of how construction activities are measured, after the merger Carillion's share of supply will, with two exceptions, be low. In the North East and East Midlands, Carillion's share of infrastructure work post-merger will be relatively significant ([25-35] per cent and [15-25] per cent respectively) but bidding information submitted by the parties indicate that Carillion and McAlpine have not been particularly close competitors, including in these two regions of the country. The OFT therefore considers

that any loss of competition arising from this merger will not be substantial. Nor does the OFT consider that the merger will create or strengthen coordinated behaviour within the industry.

71. Customers are unconcerned about the impact of this merger on construction services, and sufficient choice will remain from large, established construction firms like Balfour Beatty, Skanska, Bovis Lend Lease, Laing O'Rourke and Sir Robert McAlpine to offset any loss of competition arising from this merger.

72. After the merger, Carillion will not account for a high share of supply in FM services. Bidding information from the parties indicate that they have not been close competitors and customers are unconcerned. After the merger a considerable number of rivals will remain to offer customers choice and act as a competitive constraint on Carillion.

73. The parties presented to the OFT a ranking of the top 20 FCH contract hire companies in the UK (by fleet size). Neither of the parties featured in this list, and after the merger Carillion will have a fleet of around 17,500 cars (Lex, the market leader, has a fleet size of about 260,000 cars) and will account for less than [0-5] per cent of total supply.

74. The parties also submitted that the large majority (around 80-90 per cent) of their fleets are used for internal purposes.

75. The parties were not aware of any instance in which they competed against each other for the same customer contract.

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

**DECISION**

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

**End note**

1. After the OFT had taken its decision the parties informed the OFT that these lines of business have been sold.