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## Completed acquisition by Alexander Dennis Limited of Transbus Ltd

The OFT's Decision on reference under section 22 of the Enterprise Act 2002 given on 23 September 2004

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Please note square brackets indicate figures either removed or replaced by a range at the request of the parties'.

### PARTIES

- 1 **Transbus International Ltd (Transbus)**, a supplier of bus bodywork and chassis was bought out of administration by **Alexander Dennis Ltd (ADL)**, a company originally set up as a bid vehicle for the purpose of the acquisition, ADL only acquired the bus body and chassis business of Transbus and not the coach body and related aftermarket activities. The annual UK turnover of the acquired business is estimated by ADL to be [ $> \pounds 70$ million]. **Stagecoach Group plc** is an international transportation group, covering bus, train, tram, coach, taxi and ferry operations.

### TRANSACTION

- 2 On 21 May 2004, ADL acquired Transbus. Two of the parties to the bid vehicle, Brian Souter and Ann Gloag have a shareholding which gives them a material influence over ADL. Both these investors already have material influence over Stagecoach. The extended statutory deadline expires on 23 September 2004 and the transaction was notified to the OFT on 9 August 2004 with the administrative deadline falling after the statutory deadline.

### JURISDICTION

- 3 As a result of this transaction Transbus and Stagecoach have ceased to be distinct since the shareholding in ADL grants Brian Souter and Ann Gloag (who have material influence over Stagecoach) the ability materially to influence the policy of Transbus (now trading as ADL). The UK turnover of Transbus exceeds  $\pounds 70$  million, so the turnover test in section 23(1) (b) of the Enterprise Act 2002 (the Act) is satisfied. The OFT therefore believes that it is or may be the case that a relevant merger situation has been created.

## RELEVANT MARKET

- 4 There is no horizontal overlap between the parties to this merger. The OFT has therefore concentrated its assessment on the vertical relationship between Transbus (hereafter referred to under its post-acquisition name ADL) as a manufacturer of bus bodies and chassis and Stagecoach as a bus and coach operator and a purchaser of bus bodies and chassis.

### Product market

#### Bus manufacturing

- 5 Bus manufacturing for UK customers can be subdivided into supply of bus chassis and bus bodies. A bus operator's purchase of a new bus is based on what it perceives to be the optimal mix of bus chassis and particular bodywork design for the routes it operates. A purchaser has a choice of sourcing chassis and bodies from different or the same manufacturer(s), with some manufacturers producing both (such as ADL or Evobus), some only producing chassis for the UK market (such as Volvo), and some only producing bodies (such as East Lancashire Coachworks (ELC)). As shown in the share of supply tables below, bus body manufacturing for supply in the UK tends to take place in the UK while bus chassis manufacturing for supply in the UK takes place on a European basis.
- 6 Bus sales can be broken down into three main sub groups: midibuses (including mini buses), single deckers and double deckers. Midibuses are small single deckers used for low volume routes, typically carrying between 12 and 40 passengers. The choice of using either single or double deckers will usually be driven by capacity requirements. The distinction between single deckers and double deckers from a demand perspective has blurred in recent years due to the introduction of larger single deckers, especially imported high capacity 'bendy' buses. Nevertheless, many operators still favour double decker buses for high volume predominantly urban routes.
- 7 Bus operators purchase their vehicles from a range of body and chassis manufacturers in a number of different combinations, their decisions being based on a combination of specification and price. Bus operators invite manufacturers to tender for orders which can range from a few buses to several hundred. The evidence shows that the major operators have purchased vehicles from a number of different manufacturers in the last three years. None of the large bus operators believed that ADL's product range had any specific features which was not or

could not be replicated by other manufacturers and none of the operators or other manufacturers canvassed believed that ADL held any particular patents or any product advantage which could not be replicated by other manufacturers.

- 8 Existing import penetration into the UK is principally due to large multi national bus manufacturers such as Volvo and Daimler Chrysler (Mercedes and Evobus), from operations mainly based in Continental Europe. The OFT's investigation found no basis for concluding that these manufacturers would have any long term capacity constraints preventing an increase in their level of supply to the UK. In addition, a growing number of worldwide producers are introducing right hand drive vehicles (both bodies and chassis) with the intention of exporting to the UK: examples of recent new or intended importers to the UK market are BMC of Turkey, King Long of China and Hispano of Brazil.
- 9 The cost of market entry for chassis producers is higher than for bodywork producers due to the greater complexity of the work involved. Market entry for bodywork manufacture is relatively cheap (estimated at £250,000 per production line by one manufacturer). Evidence that successful market entry is possible is supported by the fact that Wrights have entered the market for double decker bus bodywork in the last five years and now supply approximately [15-25%] per cent of the double decker bodies sold in the UK.

#### Bus operators

- 10 Stagecoach's subsidiary bus companies control a number of UK bus and coach operators, consisting of both local timetabled services and long distance scheduled services.
- 11 The UK bus operators' sector is dominated by five large national operators which account for 69 per cent of the sector (see table 1 below). The remaining 31 per cent of the sector is supplied by a diverse range of operators ranging from relatively large operators with a strong local presence such as Tellings Golden Miller in South West London to hundreds of small operators, running up to a few dozen buses.

| <b>Operator</b>         | <b>share (% of total revenues)_</b> |
|-------------------------|-------------------------------------|
| First Group plc         | [20-30%]                            |
| Arriva plc              | [15-25%]                            |
| Stagecoach              | [10-20%]                            |
| The Go- Ahead Group plc | [0-10%]                             |
| National Express        | [0-10%]                             |
| Others                  | 31%                                 |

**Table1: Source: OFT analysis of published data**

- 12 For the purposes of this assessment the relevant frame of reference is taken to be the supply of bus bodies and bus chassis to UK customers (bus operators) on a UK-wide basis and European-wide basis, respectively.

### **VERTICAL ISSUES**

- 13 The potential competition issue which arises in a transaction such as this is whether a combination of the upstream manufacturer of bus chassis and bodies and a downstream bus operator could foreclose competition in the downstream market for bus services by, for example, charging higher prices for new ADL buses to Stagecoach's competitors (raising rivals' costs) or withholding spares to maintain existing ADL buses (refusal to supply).

#### **Bus chassis**

- 14 Bus chassis are manufactured by a number of companies such as Volvo, Scania, Evobus and ADL. Estimates of shares of supply are detailed in table 2 below. Between 2001-2003 ADL had a high, but declining, share in both the midibus chassis segment (average [60-70 per cent]) and the double decker chassis segment (average [45-55 per cent]). ADL's share of the single decker bus segment was low at only [<5 per cent] for this period.

|               | 2001     | 2002     | 2003     | Build location |
|---------------|----------|----------|----------|----------------|
|               | %        | %        | %        |                |
| Midibus       |          |          |          |                |
| ADL           | [70-80%] | [60-70%] | [55-65%] | UK             |
| Optare        | [10-20%] | [20-30%] | [25-35%] | UK             |
| DAF           | [5-15%]  | [5-15%]  | [5-15%]  | Holland        |
| Others        | [ < 5%]  | [ < 5%]  | 0        |                |
|               |          |          |          |                |
| Single decker |          |          |          |                |
| ADL           | 0        | [ < 5%]  | [ < 5%]  | UK             |
| Volvo         | [35-45%] | [45-55%] | [5-15%]  | Sweden         |
| Scania        | [20-30%] | [10-20%] | [40-50%] | Sweden         |
| Evobus        | 0        | [5-15%]  | [20-30%] | Holland        |
| Others        | [30-40%] | [15-25%] | [20-30%] |                |
|               |          |          |          |                |
| Double decker |          |          |          |                |
| ADL           | [50-60%] | [45-55%] | [40-50%] | UK             |
| Volvo         | [25-35%] | [40-50%] | [35-45%] | Sweden         |
| Scania        | 0        | 0        | [0-10%]  | Sweden         |
| Others        | [10-20%] | [5-15%]  | [5-15%]  |                |

Table 2: UK shares for chassis manufactures – source OFT estimates using data supplied by ADL

#### Bus bodies

- 15 As can be seen from table 3 below, ADL has a similarly high but more stable share of supply for bus bodies for midibuses (2001-2003 average [45-55 per cent]) and a high but declining share for double decker bus bodies (2001-2003 average [70-80 per cent]). It has a stronger presence in the manufacture of single decker bodies than chassis, but its share is still relatively low at [10-15 per cent].

|               | 2001     | 2002     | 2003     | Build location |
|---------------|----------|----------|----------|----------------|
|               | %        | %        | %        |                |
| Midibus       |          |          |          |                |
| ADL           | [45-55%] | [45-55%] | [45-55%] | UK             |
| Optare        | [10-20%] | [20-30%] | [25-35%] | UK             |
| Wrights       | [5-15%]  | [5-15%]  | [5-15%]  | UK             |
| Others        | [20-30%] | [25-35%] | [15-25%] |                |
|               |          |          |          |                |
| Single decker |          |          |          |                |
| ADL           | [5-15%]  | [0-10%]  | [5-15%]  | UK             |
| Wrights       | [60-70%] | [60-70%] | [30-40%] | UK             |
| Evobus        | 0        | [5-15%]  | [20-30%] | Holland        |
| Others        | [20-30%] | [20-30%] | [50-60%] |                |
|               |          |          |          |                |
| Double decker |          |          |          |                |
| ADL           | [75-85%] | [65-75%] | [60-70%] | UK             |
| Wrights       | [< 5%]   | [5-15%]  | [15-25%] | UK             |
| ELC           | [5-15%]  | [10-20%] | [10-20%] | UK             |
| Others        | [< 5%]   | [5-15%]  | [10-20%] |                |

Table 3: UK shares for body manufacture – source OFT estimates using data supplied by third parties

Note: The high correlation between ADL's shares of supply for both midi buses and double decker chassis and bodywork manufacture is in part explained by the fact that a large proportion of ADL's sales are for an integrated offering.

- 16 The OFT has been informed that completed new buses (body and chassis) can range in price from £85k per vehicle to £180k per vehicle. Spare parts are typically around £2-5k per annum depending on a number of factors such as wear and tear and operating environment. Buses will typically have a life span of about ten years, but again this varies with operating environment.<sup>1</sup>
- 17 Of the big five operators, Stagecoach purchased the highest proportion of its fleet from the former Transbus operations (between 1999-2001, 73 per cent for chassis and 93 per cent for bodywork).<sup>2</sup> The proportion of the other big four operators' fleets supplied by ADL is significantly lower and declining. In addition to the constraint offered by ADL's UK competitors, all the big five bus operators have purchased imported buses in the last five years, either chassis, bodies or both.

<sup>1</sup> Buses used in urban areas tend to have a shorter life, unless reconditioned.

<sup>2</sup> Source: OFT estimates using data from Bus Monitor.

- 18 For many smaller operators the majority of their fleet is sourced from second hand suppliers such as Ensign or Purfleet. There is a large pool of second hand buses available. The use of second hand vehicles is only constrained by the minimum requirement imposed by some Local Authorities (LAs) in relation to routes benefiting from a subsidy. Some LAs require that operators are Transport Act 2000 compliant and stipulate that buses must not be more than eight years old. Other LAs have no requirement in relation to the age of buses used. LAs sometimes stipulate that a particular type of bus should be used (in terms of capacity) but do not stipulate a make or model. Whilst this raises the possibility that a small operator could compete for a subsidised route with Stagecoach and prefer to use an ADL built bus for the route, the ability of ADL to impact the competitive position of the small bus operator is limited. The bus operator can purchase an alternative equivalent product elsewhere or even a second hand version of the ADL product.
- 19 Availability of spare parts is important to maintaining buses. The OFT does not consider that it is plausible that ADL would pursue a strategy to deny access to its spare parts. Most operators believed that denying such access would not be a successful long term strategy as, given the alternative products available, it would lead them to cease purchasing any new buses from ADL. One operator suggested that ADL was in reality only an assembler of buses and that components could be sourced from other suppliers.
- 20 Finally, the nature of competition among bus operators militates against foreclosure effects. The large bus operators tend to engage in competition at the margins of their geographic area or on a few specific routes. Smaller competitors to Stagecoach often buy second hand vehicles. Even assuming other shareholders in ADL would not frustrate any attempts by the common shareholders in ADL and Stagecoach to use the former to favour the latter, it is difficult to see that it would be profitable for ADL potentially to decrease its sales of buses to possibly generate some additional profits for Stagecoach on a subset of all Stagecoach's routes.

### **Buyer power**

- 21 The concentrated nature of the bus operating sector means that there is some buyer power, at least for the big five operators. The four largest operators, other than Stagecoach, have a collective market share of 53 per cent with the result that all manufacturers need to win orders from as many of these operators as possible. Crucially, the 'lumpy' nature of orders can give buyers more leverage if manufacturing capacity is not being fully utilised. As discussed above, most operators operate a diverse fleet of buses sourced from a range of manufacturers.

### THIRD PARTY VIEWS

- 22 The response of third party manufacturers and bus operators who responded to our enquiries was consistent. All believed that the common ownership of Stagecoach and ADL would not present any competition problems. In fact, the majority of responses welcomed the investment in ADL by Brian Souter and Ann Gloag as pro competitive: there was concern that if one of the other existing manufacturers had bought Transbus then there might have been a reduction of competition in the market.
- 23 Because the main direct competitors to Stagecoach are small operators with overlapping routes several of these were contacted to assess whether they had any specific concerns. None of the smaller bus operators canvassed had concerns in relation to the purchase of new buses.
- 24 In terms of spare parts, none of the bus operators canvassed believed that ADL had the incentive to raise prices to raise Stagecoach's competitor's costs.

### ASSESSMENT

- 25 The investment by Brian Souter and Ann Gloag, as part of a consortium of investors, in ADL means that the largest UK manufacturer of buses now shares common ownership with Stagecoach, one of ADL's largest customers and the third largest UK bus operator. The potential competition concern raised is whether Stagecoach could attempt to foreclose competition in the downstream bus market by raising its competitors' costs in relation to bus or spare parts purchases. Among other factors discussed above, the presence of strong competitors to ADL in the supply of both bus body and chassis manufacturing to UK customers suggests that ADL would not realistically be able to impact significantly on competition between the bus operators. ADL does not, according to any of its customers or competitors, possess any unique products which cannot be replicated from other sources.
- 26 Consequently, the OFT does not believe that it is or may be the case that the merger has resulted or may be expected to result in a substantial lessening of competition within a market or markets in the United Kingdom.

### DECISION

- 27 This merger will therefore **not be referred** to the Competition Commission under section 22(1) of the Act.