

Anticipated acquisition by DHL Supply Chain Limited of the enterprise constituted by the secondary distribution assets of Carlsberg Supply Company UK Limited

Decision on relevant merger situation and substantial lessening of competition

ME/6628/16

The CMA's decision on reference under section 33(1) of the Enterprise Act 2002 given on 13 January 2017. Full text of the decision published on 9 February 2017.

Please note that [X] indicates figures or text which have been deleted or replaced in ranges at the request of the parties for reasons of commercial confidentiality.

SUMMARY

1. DHL Supply Chain Limited (**DHL**) has agreed to acquire the enterprise constituted by certain secondary distribution assets and workstreams of Carlsberg Supply Company UK Limited (**CUK**) as part of an outsourcing agreement (**OA**) (the **Merger**). DHL and CUK are together referred to as the **Parties**.
2. The Competition and Markets Authority (**CMA**) believes that it is or may be the case that the Parties will cease to be distinct as a result of the Merger, that the share of supply test is met and that, accordingly, arrangements are in progress or in contemplation which, if carried into effect, will result in the creation of a relevant merger situation.
3. DHL provides contract logistics in the United Kingdom (**UK**), including through its subsidiary Tradeteam Limited (**Tradeteam**), which has a particular focus on drinks distribution. CUK's main focus is on the production and promotion of drinks brands and wholesaling, but it also has a logistics network. The OA involves the outsourcing to DHL of the secondary distribution element of CUK's logistics network.

4. The Parties overlap in the supply of portering services to certain retail on-trade¹ customers and brewers in the UK. Portering refers to the provision of secondary drinks distribution logistics services (ie delivery only) to the retail outlets of on-trade customers. Such customers (eg pub companies) procure the drinks themselves directly from brand owners and contract with the logistics provider to fulfil the delivery (or portering) element only.
5. The Parties do not overlap in relation to the supply of wholesaling services² or portering services to customers that require a mixture of wholesale and portering services (DHL does not compete for these customers as it does not buy or sell the relevant products). Therefore, the Parties overlap in portering-only services.
6. DHL operates throughout the UK but CUK does not provide portering in Northern Ireland (**NI**). Therefore, the Parties only overlap in the provision of portering-only services in Great Britain (**GB**).
7. The CMA investigated whether the Merger may give rise to competition concerns as a result of horizontal unilateral effects in the supply of portering-only services in GB.
8. Although, historically, CUK was one of three suppliers of portering-only services in GB, in [REDACTED] CUK decided to cease providing these services. Consequently, the CMA believes that CUK has not since this date been a constraint in the supply of portering-only services. The CMA therefore believes that no significant change to the competitive conditions in the supply of portering-only services will arise as a result of the Merger. In addition, DHL will continue to face constraints from Kuehne + Nagel's Drinks Logistics (**KNDL**), possibly from other contracts logistics providers and/or from the threat of customers self-supplying their portering needs.
9. For these reasons, the CMA believes the Merger does not give rise to a realistic prospect of a substantial lessening of competition (**SLC**) as a result of horizontal unilateral effects in portering-only services in GB.
10. The Merger will therefore **not be referred** under section 33(1) of the Enterprise Act 2002 (the **Act**).

¹ 'On-trade' refers to premises such as pubs, bars, restaurants, hotels etc. where drinks are purchased and consumed on site.

² Wholesaling refers to the provision of a bundled drinks and delivery service to on-trade customers for one price. Some brewer-wholesalers choose to outsource the actual delivery. CUK will continue to offer wholesale services post-Merger but will outsource the delivery (secondary logistics) to DHL.

ASSESSMENT

Parties

11. DHL is owned by Exel Investments Limited and ultimately by Deutsche Post AG, a company incorporated in Germany which offers global logistics services. In the UK, Deutsche Post provides contract logistics services through DHL and its subsidiaries, including Tradeteam. In 2015, DHL's annual turnover in the UK was around £4 billion.
12. CUK is owned by Carlsberg UK Holdings Limited and ultimately by Carlsberg A/S, incorporated in Denmark. The Carlsberg group is a global drinks brand owner and producer, whose brands include Carlsberg, Tuborg, Somersby Cider and Holsten. CUK's main focus is on the production of drinks, the promotion of its brands and wholesaling, but it also has a logistics network to support the secondary distribution of its products.
13. CUK has been unable to estimate the revenues attributable to the secondary distribution service that will be outsourced to DHL under the OA. However, DHL expects to achieve annual revenue from the OA of over [X] in years [X], [X] thereafter.

Transaction

14. The Merger involves the outsourcing to DHL of the secondary distribution element of CUK's logistics network.
15. The Merger is being effected by way of an OA pursuant to which DHL will provide contract logistics services to CUK [X]. The Parties envisage that integration of CUK's secondary distribution network with that of DHL will begin in [X], and from [X], DHL will be CUK's [X] secondary distribution logistics provider in GB (subject to certain exceptions outlined in the OA).
16. The OA was the result of a competitive tender process run by CUK. As the successful bidder, DHL will provide secondary logistics for the delivery of goods for CUK's wholesaling business to its on-trade customers. In addition, DHL will provide secondary logistics for:
 - (a) a portorage-only contract³ with [X] that will continue until [X];

³ All other CUK portorage-only business will have ceased by the time of the Merger [X].

- (b) [X] arrangement that CUK has with [X] under which [X] can enter into agreements for the supply of CUK brands, wholesaling of third party brands and delivery; and
- (c) [X] portage contracts for CUK's hybrid customers (ie customers who require portage services alongside wholesaling services).

17. The OA includes:

- (a) the transfer of the CUK's leases of [X] of CUK's depots;
- (b) the fixed assets and fittings at these depots for [X];
- (c) the novation of a number of leases and hire contracts of [X] equipment at these depots; and
- (d) the TUPE⁴ transfer of [X] CUK employees dedicated to its secondary logistics operations, [X].⁵

Jurisdiction

18. DHL is acquiring depots, machinery and employees, who will be transferred from CUK under TUPE. DHL is also gaining some ongoing workflow (CUK is outsourcing to DHL the performance of certain portage contracts until [X] and all of CUK's other secondary distribution activity until [X]). [X] There is therefore economic continuity between the logistical activities of CUK prior to the Merger and the activities that DHL will carry out after the Merger.
19. Accordingly, the CMA believes the assets being transferred, together with employees, constitute an enterprise as defined in section 129 of the Act.⁶ Therefore, as a result of the Merger, the enterprises of DHL and the business being acquired from CUK will cease to be distinct.
20. The Parties estimated that their combined share of supply of secondary distribution of drinks in the UK was approximately [30–40]% ([5–10]% increment).⁷ The CMA therefore believes that the share of supply test in section 23 of the Act is met.

⁴ *Transfer of Undertakings (Protection of Employment) Regulations 2006* as amended by the *Collective Redundancies and Transfer of Undertakings (Protection of Employment) (Amendment) Regulations 2014*.

⁵ No portage-only contracts are moving from CUK to DHL as part of the Merger as existing portage obligations are being sub-contracted.

⁶ *Mergers: Guidance on the CMA's jurisdiction and procedure* (CMA2), January 2014, paragraph 4.9.

⁷ The Parties' estimate is based on the revenues that DHL expects to achieve from the OA.

21. The CMA 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.
22. The initial period for consideration of the Merger under section 34ZA(3) of the Act started on 7 December 2016 and the statutory 40 working day deadline for a decision is therefore 3 February 2017.

Counterfactual

23. The CMA assesses a merger's impact relative to the situation that would prevail absent the merger (ie the counterfactual). For anticipated mergers the CMA generally adopts the prevailing conditions of competition as the counterfactual against which to assess the impact of the merger. However, the CMA will assess the merger against an alternative counterfactual where, based on the evidence available to it, it believes that, in the absence of the merger, the prospect of these conditions continuing is not realistic, or there is a realistic prospect of a counterfactual that is more competitive than these conditions.⁸
24. CUK decided in [redacted] to cease providing portorage services and that, with the exception of [redacted] hybrid contracts and its contract with [redacted], it would no longer seek to renew existing portorage contracts or compete to secure new ones. [redacted]. Consequently, CUK submitted that there is no relevant or realistic counterfactual in which CUK would continue to compete for portorage contracts. CUK said that it would have ceased providing portorage services regardless of the Merger.
25. CUK also submitted that [redacted].
26. The CMA has not found it necessary to conclude on the relevant counterfactual because the CMA does not believe that there is a realistic prospect that the Merger will result in an SLC within a market or markets in the UK on the basis of any realistic counterfactual. Therefore, the CMA conducted its assessment on the basis of the prevailing conditions of competition, taking into account the current competitive position of CUK after its decision to exit portorage.

⁸ *Merger Assessment Guidelines* (OFT1254/CC2), September 2010, from paragraph 4.3.5. The *Merger Assessment Guidelines* have been adopted by the CMA (see *Mergers: Guidance on the CMA's jurisdiction and procedure* (CMA2), January 2014, Annex D).

Frame of reference

27. Market definition provides a framework for assessing the competitive effects of a merger and involves an element of judgement. The boundaries of the market do not determine the outcome of the analysis of the competitive effects of the merger, as it is recognised that there can be constraints on merger parties from outside the relevant market, segmentation within the relevant market, or other ways in which some constraints are more important than others. The CMA will take these factors into account in its competitive assessment.⁹

Introduction

28. The Merger relates to the outsourcing of CUK's secondary logistics, both for CUK's wholesaling contracts and CUK's portering contracts (sometimes alongside a wholesaling contract (hybrid) and sometimes portering-only).
29. CUK will continue to compete in the wholesaling of drinks to the on-trade sector. DHL does not compete in this service as it does not buy or sell drinks. Therefore, there is no change to competition in the wholesale supply of drinks as a result of the Merger.
30. CUK will also continue to compete for customers which require the wholesale supply of drinks and, alongside that service, portering services for drinks sourced from another provider (hybrid customers). DHL does not compete for these customers as it cannot supply the wholesale service which is typically the primary element of the contract. Therefore, there is no change to competition in the supply of wholesale and portering (combined) services as a result of the Merger.
31. The only area of overlap between the Parties is in the supply of portering-only services to on-trade customers.

Product scope

32. The Parties submitted that the appropriate frame of reference is wider than portering and should encompass all contract logistics,¹⁰ in line with previous

⁹ [Merger Assessment Guidelines](#), paragraph 5.2.2.

¹⁰ The Parties defined contract logistics as 'the part of the supply chain process that plans, implements and controls the efficient, effective flow and storage of goods, services and related information from the point of origin to the point of consumption in order to meet customers' requirements'.

decisions by the European Commission¹¹ and on the basis of supply-side substitution. In particular, the Parties submitted that:

- (a) the requirements of drinks distribution customers are the same as those of customers needing the distribution of other goods;
- (b) customers' switching costs are low; and
- (c) expanding from supplying logistics for other goods into drinks logistics would not involve significant sunk costs or additional specialised assets or investment.

Porterage services and contract logistics

- 33. The CMA first considered whether the relevant frame of reference might be broader than all porterage services to include other, or all, contract logistics.
- 34. On the demand side, customers were not clear on whether they could switch to other contract logistics providers.
- 35. On the supply side, about half of the contract logistics suppliers which responded to the CMA's questions noted that drinks distribution does not require any special assets or equipment. The other half noted that there may be some types of drinks (in particular kegs) which require certain equipment, such as reinforced floors, drop mats and extra strapping. No contract logistics supplier thought that the assets were difficult to acquire on the open market. However, the CMA has not seen any evidence of expansion by other contract logistics providers into drinks distribution.
- 36. On a cautious basis, the CMA has investigated the impact of the Merger on the supply of porterage services separately from other contract logistics.

Porterage services alongside wholesale services to hybrid customers

- 37. The CMA also assessed whether the frame of reference should include porterage services which are offered alongside wholesale services to hybrid customers.
- 38. On the demand side, hybrid customers require both wholesaling and porterage services typically because they have a preference for limiting the number of drinks deliveries they receive; in addition, hybrid customers may be

¹¹ See, for example, M.3492 Exel/Tibbett & Britten, M.4232 Scottish and Newcastle/ Kuehne & Nagel JV, and M.3496TNT Forwarding Holding AB/Wilson Logistics Holding AB.

able to obtain better prices for some products directly with drinks manufacturers than they are able to obtain through the wholesaler.

39. On the supply side, third parties indicated that a portering-only supplier would need to set up a wholesaling business in order to be able to compete for hybrid customers, which would not be easy. This would involve negotiating the purchase and primary delivery of drinks from various drinks manufacturers and marketing a very different proposition.
40. For these reasons, the CMA believes that the frame of reference for considering the Merger should be limited to the provision of portering-only services (ie excluding portering services offered alongside a wholesale service to hybrid customers).

Segmentation by customer type

41. The CMA also considered whether portering-only services should be segmented by customer type, since these can be provided to drinks manufacturers, wholesalers or retail outlets.
42. The CMA found that all these customers contract for the same essential portering service, which is to deliver drinks from one point to another, and the assets used in this service are the same. For this reason, the CMA has not segmented by customer type. Nevertheless, the CMA notes that [§] and the CMA has taken into account the difference in the Parties' customer bases in its competitive assessment.

Conclusion on product scope

43. Given that the CMA has found no competition concerns on any basis, it was not necessary for the CMA to reach a conclusion on the appropriate product frame of reference. However, given the narrow overlap between the Parties and for the reasons set out above, the CMA assessed the impact of the Merger in a narrow frame of reference for portering-only services.

Geographic scope

44. The Parties submitted that the geographic market for contract logistics is the European Economic Area (EEA). However, they did not submit a view on the geographic frame of reference for portering-only services.
45. The CMA notes that the supply of portering-only services requires making multiple small deliveries and, for this reason, a local network may be necessary. Therefore, on a cautious basis, the CMA believes that the frame of

reference is unlikely to be wider than national. The CMA considered whether the frame of reference for portage-only services could be regional or narrower but found that all competitors have a national presence, and that many customers require deliveries to be made nationally.

46. DHL operates in NI while CUK has only one customer in NI: [X], which is part of a UK-wide contract. CUK does not have any distribution network in NI and fulfils its contract with [X] through a third party. CUK does not compete for portage in NI and so the Merger raises no realistic prospect of an SLC in NI. Therefore, the Parties only overlap in the provision of portage-only services in GB.
47. Therefore, the CMA investigated the impact of the Merger in GB (excluding NI).

Conclusion on frame of reference

48. For the reasons set out above, the CMA assessed the impact of the Merger in the supply of portage-only services in GB.

Competitive assessment

Horizontal unilateral effects

49. Horizontal unilateral effects may arise when one firm merges with a competitor that previously provided a competitive constraint, allowing the merged firm profitably to raise prices or to degrade quality on its own and without needing to coordinate with its rivals.¹² Horizontal unilateral effects are more likely when the merger parties are close competitors.
50. The CMA assessed whether it is or may be the case that the Merger has resulted, or may be expected to result, in an SLC in relation to horizontal unilateral effects in the supply of portage-only services in GB.

CUK's decision to cease providing portage-only services

51. Internal documents provided by CUK indicate that the core purpose of CUK's secondary logistics network has been to support its wholesale business. [X] As CUK's portage business grew, the revenue from these contracts failed to cover the cost of servicing them, [X].

¹² [Merger Assessment Guidelines](#), from paragraph 5.4.1.

52. In [X], CUK [X] agreed [X] to withdraw from its secondary logistics operations by: (a) outsourcing its logistics requirements for its wholesale and hybrid customers; and (b) ceasing all supply of portering-only services. [X]
53. [X]

Shares of supply

54. The three main suppliers of portering-only services in GB are the Parties and KNDL. The Parties estimated that, in 2015, KNDL had [40–50]% of portering-only sales in GB (by volume, in hectolitres), DHL had [30–40]%, and CUK had [20–30]%. However, by the end of 2017, CUK will have only [5–10]% of supply as it will continue to service only [X].¹³ Table 1 shows that CUK has not bid for any portering-only contracts [X].

Table 1: Number of bids for portering only contracts in 2010–2016

Party	2010	2011	2012	2013	2014	2015	2016
DHL	[X]	[X]	[X]	[X]	[X]	[X]	[X]
CUK	[X]	[X]	[X]	[X]	[X]	[X]	[X]

Source: Parties' bidding data.

Notes: Number of successful bids in parentheses.¹⁴

55. Given that [X], the CMA does not believe that historical shares of supply are informative when considering the competitive position of the Parties on a forward-looking basis. Moreover:
- (a) Given that no portering-only contracts are moving from CUK to DHL as part of the Merger (existing portering obligations are being sub-contracted), [X], and the assets transferring to DHL are only a small proportion of CUK's secondary logistics network ([X]), DHL will gain little advantage in bidding for portering-only services from the Merger. CUK will retain its contract with [X], with the portering element of these sales outsourced to DHL.¹⁵

¹³ CUK technically considers its [X] contract a portering-only service [X]. However, the CMA believes that CUK's relationship with [X] is a hybrid relationship as both wholesale and portering occurs, such that DHL would not have been able to compete for this contract.

¹⁴ The information reflects the most accurate information the Parties have, but given neither Party keeps systematic records of past tenders the data may be fully complete or accurate.

¹⁵ All of CUK's contracts which require secondary distribution (wholesale, hybrid or portering-only) will continue to be held by CUK.

- (b) While shares of supply can be informative, the CMA notes that in bidding markets shares can change substantially as contracts change hands through tenders, particularly if there are only a few tenders (as shown in Table 1).

Closeness of competition

56. DHL is not a wholesaler and therefore does not compete for hybrid customers. DHL also submitted that [REDACTED]. Consequently, the CMA believes that there will be no change to competition as a result of the Merger in the supply of wholesaling services or the supply of portorage services to hybrid customers.
57. Prior to [REDACTED], both Parties competed for portorage-only customers.¹⁶ On the basis of CUK's internal documents, the CMA believes that CUK's decision in [REDACTED] was driven by [REDACTED] and, although related to the decision to outsource its secondary logistics requirement, it was not dependent on this. The CMA notes that CUK could have continued to compete for portorage-only contracts with the intention of outsourcing the fulfilment of these contracts alongside the fulfilment of its wholesale and hybrid contracts, [REDACTED], which is confirmed by the bidding data shown in Table 1. [REDACTED]
58. Consequently, the CMA believes that CUK has not been constraining other suppliers of portorage-only services since [REDACTED]. Therefore, the Merger will lead to no significant change in competition in the supply of portorage-only services in GB.
59. The CMA notes that, given CUK is merely subcontracting its remaining portorage-only contracts and [REDACTED], had CUK reached an outsourcing agreement with a different contract logistics operator, this rival would have gained little advantage in bidding against DHL and KNDL for future portorage-only services; [REDACTED], and third parties told us that, workflow aside, the assets being acquired are readily available in the open market.
60. The CMA also notes that DHL will continue to face constraints from KNDL post-Merger, possibly from other contracts logistics providers and/or the threat of customers self-supplying their portorage needs (although it has not been necessary for the CMA to conclude on the strength of these constraints).

¹⁶ [REDACTED]

Conclusion on horizontal unilateral effects

61. For the reasons set out above, the CMA believes that the Merger does not give rise to a realistic prospect of an SLC as a result of horizontal unilateral effects in the supply of portering-only services in GB.

Barriers to entry and expansion

62. Entry, or the expansion of existing firms, can mitigate the initial effect of a merger on competition, and in some cases may mean that there is no SLC.¹⁷
63. In this case the CMA has not had to conclude on barriers to entry or expansion as the Merger does not give rise to competition concerns on any basis.

Third party views

64. The CMA contacted customers and competitors of the Parties. Third party comments have been taken into account where appropriate in the competitive assessment above.

Decision

65. Consequently, the CMA does not believe that it is or may be the case that the Merger may be expected to result in an SLC within a market or markets in the UK.
66. The Merger will therefore **not be referred** under section 33(1) of the Act.

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¹⁷ [Merger Assessment Guidelines](#), from paragraph 5.8.1.