Anticipated acquisition by David Lloyd Clubs of 16 Virgin Active gyms

Decision on relevant merger situation and substantial lessening of competition

ME/6679/17

The CMA's decision on reference under section 33(1) of the Enterprise Act 2002 given on 19 May 2017. Full text of the decision published on 26 May 2017.

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

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SUMMARY

1. David Lloyd Clubs Limited (**David Lloyd**, or **DL**) has agreed to acquire the business and assets of 16 gyms (together the **Target Gyms**) from Virgin Active Limited (**Virgin Active**, or **VA**) (the **Merger**). David Lloyd and the Target Gyms 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. The CMA identified seven local areas where a David Lloyd gym and a Target Gym overlapped within a 20-minute drive time: Berkshire, Brighton, Clearview, Hampshire, Lancashire, Northwood and Surrey (**Overlap Areas**). The CMA then assessed, for each Overlap Area, whether sufficient competition would remain post-Merger or whether concerns might arise from the loss of David Lloyd or the Target Gym as an independent competitor.

4. In undertaking this assessment, and consistent with past decisional practice, the CMA adopted as a starting point a product frame of reference of all gyms. However, as in previous cases, the CMA noted that the level of constraint and closeness of competition between gyms will vary according to a number of factors, including offering, price and location.

5. Both Parties operate gyms towards the ‘premium’ end of the market, offering a range of facilities including ‘gym’ facilities (eg exercise machines and a weights area), ‘wet’ facilities (ie a swimming pool) and exercise classes, and many also offer additional facilities such as a crèche, childcare facilities, a sauna and racquet courts. Therefore, for each Overlap Area, the CMA first identified which competitor sites offered at least a gym, a swimming pool and exercise classes (the **Core Facilities**). The CMA then compared the precise facilities available at each of these rival sites with those offered at the relevant sites of the Parties. The CMA also took into account the location, size (as indicated by square footage, the number of pieces of equipment and the number of members) and the membership price of these facilities.

6. In four of the Overlap Areas (Berkshire, Hampshire, Lancashire and Surrey), and in relation to the overlaps between Virgin Active Clearview and each of David Lloyd Basildon and David Lloyd Dartford, the CMA was satisfied, on the basis of information and analysis provided by David Lloyd and Virgin Active and third party market testing, that the Parties were not particularly close competitors and that sufficient competitive constraints would remain post-

Merger. The CMA found that there were a number of rivals offering the Core Facilities which are geographically closer to the Parties than the Parties are to each other.

7. In the remaining three Overlap Areas (Brighton, Clearview (in relation to the overlap with David Lloyd Gidea Park) and Northwood), the CMA found from its initial analysis that the Parties' sites were closer competitors and the number of rivals offering the Core Facilities was more limited. The CMA therefore undertook a more detailed assessment of these areas, which included a survey of the Parties' members in each of these Overlap Areas.

8. In summary, the CMA found that:

(a) In Brighton, the Parties' gyms are approximately 16-18-minutes' drive time from one another, internal David Lloyd documents [✂], the facilities are similar, and the home locations of their members significantly overlap. Responses to the survey indicated that the Parties are close competitors, with only one alternative significant competitor for each party (Withdean for Virgin Active and The Gym for David Lloyd).

(b) In Clearview, the Virgin Active Clearview site and the David Lloyd Gidea Park[1] site are approximately 10-15-minutes' drive time from one another, internal David Lloyd documents [✂], the facilities are similar, and the home locations of their members show some considerable overlap. Responses to the survey indicated that the Parties are close competitors, with only one alternative significant competitor for each party (DW Fitness for Virgin Active and Hornchurch Sports Centre for David Lloyd).

(c) In Northwood, internal David Lloyd documents [✂], the facilities are similar, and the home locations of their members show some overlap. However, the Parties' gyms are approximately a 22-minute drive time from one another and their membership pricing is not similar (average price per member of £[✂] at David Lloyd compared with £[✂] at Virgin Active). Responses to the survey also indicated that the Parties are not particularly close competitors and that a number of other competitors would continue to constrain the Parties post-Merger.

9. On the basis of this evidence, the CMA believes that the Merger gives rise to a realistic prospect of a substantial lessening of competition (**SLC**) as a result of horizontal unilateral effects in the supply of gyms in the local areas around Virgin Active Brighton and Virgin Active Clearview (ie between Virgin Active

[1] As explained in the competitive assessment below, the CMA did not identify competition concerns with regard to the overlap between Virgin Active Clearview and other David Lloyd sites in the area.

Clearview and David Lloyd Gidea Park), but not in relation to Virgin Active Northwood. The CMA has not found competition concerns in relation to any of the other overlaps.

10. The CMA is considering whether to accept undertakings under section 73 of the Enterprise Act 2002 (**the Act**). The Parties have until 26 May 2017 to offer an undertaking to the CMA that might be accepted by the CMA. If no such undertaking is offered, then the CMA will refer the Merger pursuant to sections 33(1) and 34ZA(2) of the Act.

ASSESSMENT

Parties

11. David Lloyd is controlled by TDR Capital LLP (**TDR**). It operates 83 gyms in the UK and 12 gyms in Europe. It has approximately [✂] members and employs around 6,200 staff. The turnover of David Lloyd in 2015 was around €[✂] million, of which approximately €[✂] million was generated in the UK.

12. Virgin Active operates 61 gyms in the UK and a further 184 in 9 other countries. It has approximately [✂] members in the UK and [✂] members overall. The turnover of the Target Gyms in 2016 was around £[✂] million, all of which was generated in the UK.

Transaction

13. The proposed transaction involves the acquisition by David Lloyd of the business and assets of the Target Gyms. The Merger was announced in a Press Release on the David Lloyd website on 7 February 2017.[2]

Jurisdiction

14. As a result of the Merger, the enterprises of David Lloyd and the Target Gyms will cease to be distinct.

15. The Parties submitted that the share of supply test is met with regard to the Overlap Area around the David Lloyd Basildon gym, by virtue of David Lloyd and Virgin Active Clearview together accounting for 25% or more of the share of supply of gyms in a 15-minute drive time catchment.[3] The relevant

[2] www.davidlloyd.co.uk/press/virgin-active.

[3] The Parties relied upon a datasource from Leisure Database Company (http://www.leisuredb.com/) and applied the size filters used to determine the initial fascia counts in *Pure Gym/LA Fitness*, looking only at gyms which offer group exercise facilities (ie group cycling or a dance studio) and a dedicated car park.

catchment area has a population of over 200,000. The Parties submitted that the wider Basildon/Clearview area is of sufficient size and significance to constitute a substantial part of the UK. In addition, David Lloyd and Virgin Active together account for more than 25% of the supply of private gyms with Core Facilities in a 20-minute drive time catchment centred on the Virgin Active gym in each of Clearview and Brighton. The CMA considers that these areas together are a substantial part of the UK.[4] The CMA considers that on either of the above grounds the share of supply test in section 23 of the Act is met.

16. 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.

17. The initial period for consideration of the Merger under section 34ZA(3) of the Act started on 21 March 2017. The statutory 40 working day deadline for a decision is therefore 19 May 2017. The Merger was considered at a Case Review Meeting.[5]

Counterfactual

18. 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.[6]

19. In the present case, there is no evidence supporting a different counterfactual, and the Parties and third parties have not put forward arguments in this

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[4] CMA2 at 4.62 notes: "In line with the approach taken previously by the CC and OFT, there is no need in the application of the share of supply test for the substantial part of the UK to constitute an undivided geographic area. This interpretation gives effect to the purposes of the Act. The economic significance of a merger, in terms of a substantial lessening of competition, does not necessarily depend on whether several localities are contiguous or separated."

[5] See *Mergers: Guidance on the CMA's jurisdiction and procedure* (CMA2), January 2014, from paragraph 7.34.

[6] *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).

respect. Therefore, the CMA believes the prevailing conditions of competition to be the relevant counterfactual.

Frame of reference

20. 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 merging 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.[7]

21. The Parties overlap in the provision of gyms. Both Parties offer gym facilities (eg exercise machines and a weights area), swimming pools, exercise classes, racquet facilities, health and beauty spas, crèches and childcare facilities, with the facilities varying to some extent by site.

Product scope

22. The supply of gyms has been considered most recently in *Pure Gym/LA Fitness* and *Pure Gym/the Gym*.[8] In both cases the CMA adopted a product frame of reference encompassing all gyms but noted that the closeness of competition between the parties and between the parties and their competitors varied according to a number of factors, including the offering, price and location.

23. In *Pure Gym/the Gym,* the CMA identified a number of broad groups of gyms: budget gyms, mid-range gyms, premium gyms, public gyms and specialised gyms. In the present case, the Parties both operate premium gyms, as indicated by the range and quality of the facilities on offer and the membership rates charged. Due to this differentiation, the CMA believes that the Parties may face less of a constraint from budget and mid-range gyms (which do not offer the same range or quality of facilities).

24. The CMA believes that the approach adopted in these recent cases (ie to identify a wide set of all-gym competitors but then to consider their

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[7] *Merger Assessment Guidelines*, paragraph 5.2.2.

[8] Anticipated combination of Pure Gym Limited and The Gym Limited, CMA decision 26 June 2014.

differentiation by considering the competitive constraint posed by other operators offering Core Facilities[9]) is appropriate in this case.[10]

25. The Parties submitted that the CMA's perspective in these previous cases was conservative as it failed to give any recognition to the competitive pressures they faced from non-gym health and fitness providers, such as private personal trainers, boutique group fitness and spinning studios and outdoor boot camps.[11] The CMA has not seen evidence to support widening the frame of reference in this way.

Conclusion on product scope

26. For these reasons, the CMA has adopted a product frame of reference of all gyms as its starting point, noting that the extent of the competitive constraint between gyms will vary according to a number of factors, including offering, price and location.

Geographic scope

27. In *Pure Gym/LA Fitness* and *Pure Gym/The Gym*, the CMA assessed the impact at both the national and local level.

28. In the present case, the CMA does not believe that the Merger could give rise to competition issues at the national level.[12]

29. At a local level, the CMA notes that the decisions in *Pure Gym/The Gym* and *Pure Gym/LA Fitness* did not reach a conclusion on the exact boundaries of the relevant geographic market. However, in these cases, the CMA identified overlaps where gyms were located within a 40-minute walk time or a 20-minute drive time (outside of London).

30. In the present case, the Parties said that a 20-minute drive time catchment around each of the Target Gyms would provide a reasonable starting point for identifying overlaps. Membership data from the Parties was consistent with this as, for the majority of their sites, over 80% of members live within a [✂] drive-time.[13] The '80% catchment area' was slightly wider in two local areas

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[9] In the *Anticipated acquisition by Virgin Active Holdings Limited of Esporta Racquets and Non-Racquets Holdings*, OFT decision 11 July 2011, it was decided that the relevant frame of reference was private clubs with the 'core' facilities of a gym, exercise classes and a swimming pool.

[10] *Pure Gym/the Gym, paragraphs 35 to 36.*

[11] Final Merger Notice, 20 March 2017, paragraph 12.1.2.

[12] Virgin Active will remain a significant national competitor post-Merger with 45 gyms.

[13] To identify overlaps, the CMA usually uses catchment areas that capture 80% of members. *Retail Mergers Commentary*, paragraph 2.20.

(Northwood and Surrey), [✂]. Applying this distance resulted in both these areas being identified as Overlap Areas.

Conclusion on geographic scope

31. For the reasons set out above, the CMA has assessed the impact of the Merger at a local level in each of the Overlap Areas of Berkshire, Brighton, Clearview, Hampshire, Lancashire, Northwood and Surrey.

Conclusion on frame of reference

32. As set out above, for each Overlap Area, the CMA has assessed the impact of the Merger using a starting point of the supply of all gyms and has taken into account any differentiation between the different types of gyms in the competitive assessment.

Competitive assessment

Horizontal unilateral effects

33. 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.[14] Horizontal unilateral effects are more likely when the merging parties are close competitors. The CMA has 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 unilateral horizontal effects in the provision of gyms at a local level.

The Overlap Areas

34. The CMA has assessed the impact of the Merger in the following seven Overlap Areas (by reference to the name of the Virgin Active gym):[15]

   (a) **VA Berkshire** (Royal Berkshire Health & Racquets club, Nine Mile Ride, Bracknell RG12 7PB), which overlaps with David Lloyd Reading.

   (b) **VA Brighton** (Brighton Health & Racquets club, Village Way, Brighton BN1 9SG), which overlaps with David Lloyd Brighton.

[14] *Merger Assessment Guidelines*, from paragraph 5.4.1.

[15] Drive times are estimated from the David Lloyd site to the Target Gym. The drive time from the Target Gym to David Lloyd site may be slightly different.

(c) **VA Clearview** (Clearview Health & Racquets club, Hall Lane, Little Warley, Brentwood CM13 3EN), which overlaps with David Lloyd Gidea Park, David Lloyd Basildon and David Lloyd Dartford.

(d) **VA Hampshire** (Hampshire Health & Racquets club, Botley Road, West End, Southampton SO30 3XA), which overlaps with David Lloyd Southampton.

(e) **VA Lancashire** (Lancashire Health & Racquets club, Heywood Old Road, Middleton, Manchester M24 4TH), which overlaps with David Lloyd Manchester Trafford City and David Lloyd Bolton.

(f) **VA Northwood** (Northwood Health & Racquets club, Ducks Hill Road, Northwood, London HA6 2DR), which overlaps with David Lloyd Bushey.

(g) **VA Surrey** (Surrey Health & Racquets club, Hannibal Way, Croydon CR0 4RW), which overlaps with David Lloyd Cheam.

35. Given the relatively small number of overlaps in the present case, the CMA considered them individually and did not employ a fascia count or other filter to exclude overlaps unlikely to raise concerns.

The approach to assessing competition in each Overlap Area

36. In each Overlap Area, the CMA assessed the closeness of competition between the Parties and the extent of the competitive constraint that will remain post-Merger, including by reference to the facilities offered, the location of the Parties' members[16], internal documents, the price of membership and third party views. The CMA also undertook a survey in three Overlap Areas to ascertain the level of likely diversion of Virgin Active members to David Lloyd and vice versa.

37. The CMA noted that, in each Overlap Area, the Parties' sites offer the Core Facilities so, as a first step in seeking to identify those competitors which would impose the greatest competitive constraint on the Parties, the CMA identified competitors offering the Core Facilities. Consistent with *Pure Gym/The Gym*, the CMA also identified whether competitors have more than 50 pieces of equipment and more than 500 members as, given the large-scale nature of the Parties' sites, small sites are less likely to impose a material

[16] The Parties submitted geographic heat maps for each Overlap Area showing the home locations of their respective members.

constraint on the Parties. The CMA also considered where relevant whether competitor sites had racquet facilities.

The survey

38. The CMA carried out a survey of Virgin Active and David Lloyd members at each of the Parties' gyms in Brighton, Clearview[17] and Northwood, with the assistance of the Parties. In line with the CMA's usual practice, survey respondents were asked what they would do if their gym closed and,[18] for those who indicated that they would go elsewhere, which of 11 other named gyms they would go to (including that of the other merging party) or to any other gym.[19] The survey opened on 24 March 2017 and closed on 7 April 2017. 3404 members responded.

39. A relatively high proportion of respondents said either that they did not know what they would do if their gym closed[20] or that they would go elsewhere but did not know where. The responses of respondents who said that they would go elsewhere but did not know where were redistributed across the remaining answer options (including 'other'). This is in line with the previous survey practice of the CMA and its predecessor organisations.

40. The Parties submitted that the CMA's estimated diversion ratios overstated the extent of diversion between their gyms and that this was exacerbated by the CMA's redistribution of 'don't knows'. The Parties also submitted that:

(a) respondents would be more likely to choose the 11 listed gyms (which included, in each case the other party's closest site) rather than another gym which was not specifically listed;

(b) respondents were aware of the Merger and the Parties' brands, which would bias them towards identifying the Parties' gym as their alternative; and

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[17] As potential competition concerns were identified only with regard to the overlap between VA Clearview and DL Gidea Park, the survey was limited to these sites and members of the other DL sites in that local area (DL Basildon and DL Dartford) were not surveyed.

[18] Respondents could respond: 'take out membership elsewhere'; 'go elsewhere and pay per visit'; 'not go anywhere else'; or 'don't know'.

[19] The CMA invited the Parties to identify which 10 alternative gyms in each local area were likely to be the closest competitors to their own gyms. These alternative gyms were listed in order of distance from the relevant David Lloyd or Virgin Active gym where the respondent was a member. Respondents were also able to say that they would go elsewhere but that they didn't know where.

[20] These members' responses were redistributed across all remaining responses (including those saying 'not go anywhere else').

(c) an analysis of David Lloyd members leaving David Lloyd Brighton between May 2015 and December 2016 showed that only between 1-5% subsequently joined Virgin Active Brighton in the same period.

41. However, the CMA believes that the survey results remain probative to its competitive assessment, as:

(a) whilst the 'framing effects' identified above could increase responses for gyms listed relative to gyms not listed, the CMA mitigated this by accepting the Parties' list of alternative competitors and listed the gym of the other merging party last (since respondents may be more likely to choose a gym listed earlier rather than later);[21]

(b) it is unclear the extent to which members of specific sites were aware of the Merger or the effect this could have had on their responses;

(c) the reallocation of 'don't knows' across all remaining answer options is appropriate within a Phase 1 assessment;[22] and

(d) limited weight can be placed on the Parties' analysis of members leaving David Lloyd Brighton for Virgin Active since, on the one hand, the Parties did not submit any evidence to explain whether its members left due to competition from other gyms in the local area or other factors and, on the other, it was not possible to ascertain what proportion of members diverted to Virgin Active as compared to other gyms in the local area.

42. Further, the CMA believes that the high level of responses to the survey increases its reliability, while acknowledging that the high level of 'don't knows' indicates a degree of uncertainty among respondents about the alternatives. The evidence from the survey is included in the analysis of Brighton, Clearview and Northwood below.

Berkshire, Hampshire, Lancashire and Surrey

43. In four of the Overlap Areas (and in relation to the overlaps between Virgin Active Clearview and each of David Lloyd Basildon and David Lloyd Dartford, discussed in the section on Clearview below), the CMA was satisfied, on the

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[21] With two exceptions: David Lloyd Gidea Park was 6th out of 11 in the list of alternatives for Virgin Active Clearview. Virgin Active Clearview was 10th out of 11 in the list for David Lloyd Gidea Park.

[22] The response 'other' (which also included a text box to write in the name of the other gym) appeared immediately before 'don't know' as a possible response and therefore it is not clear that a higher proportion of respondents who chose 'don't know' would have gone to an unlisted gym rather than one of the gyms stated compared with the proportion who knew their preference. Moreover, while a different allocation of 'don't knows' would have reduced diversion ratios between the Parties, it would also have reduced diversion to other listed gyms including the closest other alternatives. It therefore would not have affected the CMA's assessment of whether there were closer alternatives to the Parties' gyms.

basis of information and analysis provided by David Lloyd and Virgin Active and third party market testing, that competition concerns would not arise. These four areas are discussed in turn below.

Berkshire

44. Virgin Active Berkshire is located approximately 20-minutes' drive from David Lloyd Reading. The Parties submitted an analysis of member locations, which indicated that the majority of Virgin Active Berkshire's members are drawn from a separate geographical area to that of David Lloyd Reading. David Lloyd's internal documents show that [✄]. Only one competitor submitted that it was concerned that the Merger would reduce competition and the offering to members. No other third party in this area expressed any competition concerns about the Merger.

45. Post-Merger, 18 gyms offering the Core Facilities will remain within a 20-minute drive of Virgin Active Berkshire. All 18 gyms offering the Core Facilities are at a shorter drive time to Virgin Active Berkshire than David Lloyd Reading, including other large health and fitness club operators with a similar offer.

46. The CMA therefore believes that there is sufficient competition in the Berkshire area to constrain the Parties post-Merger.

Hampshire

47. Virgin Active Hampshire is located approximately 17-minutes' drive from David Lloyd Southampton. The Parties submitted an analysis of member locations, which indicated that the majority of Virgin Active Hampshire's members are drawn from a separate geographical area to that of David Lloyd Southampton. David Lloyd's internal documents show that [✄]. No third party in this area has expressed any competition concerns in relation to the Merger.

48. Post-Merger, 19 gyms offering the Core Facilities will remain within a 20-minute drive of Virgin Active Hampshire, of which seven also offer racquet facilities. 17 gyms offering the Core Facilities are at a shorter drive time to Virgin Active Hampshire than David Lloyd Southampton, including other large health and fitness club operators with a similar offer.

49. The CMA therefore believes that there is sufficient competition in the Hampshire area to constrain the Parties post-Merger.

Lancashire

50. Virgin Active Lancashire is located approximately 19-minutes' drive from David Lloyd Manchester Trafford City and approximately 20-minutes' drive from David Lloyd Bolton. The Parties submitted an analysis of member locations, which indicated that the majority of Virgin Active Lancashire's members are drawn from a separate geographical area to that of either David Lloyd Manchester Trafford City or David Lloyd Bolton. David Lloyd's internal documents show that [✂]. No third party in this area has expressed any competition concerns in relation to the Merger.

51. Post-Merger, 47 gyms offering the Core Facilities will remain within a 20-minute drive of Virgin Active Lancashire, of which eight also offer racquet facilities. 39 gyms offering the Core Facilities are at a shorter drive to Virgin Active than the closest overlapping David Lloyd gym (Manchester Trafford City), including other large health and fitness club operators with a similar offer.

52. The CMA therefore believes that there is sufficient competition in the Lancashire area to constrain the Parties post-Merger.

Surrey

53. Virgin Active Surrey is located approximately 22-minutes' drive from David Lloyd Cheam and approximately 25-minutes' drive time from David Lloyd Beckenham[23]. The Parties submitted an analysis of member locations, which indicated that the majority of Virgin Active Surrey's members are drawn from a separate geographical area to that of David Lloyd Cheam. However, the CMA noted some overlap in member locations between Virgin Active Surrey and David Lloyd Beckenham, despite a significant drive time between these sites. David Lloyd's internal documents show that [✂]. No third party in this area has expressed any competition concerns in relation to the Merger.

54. Post-Merger, 18 gyms offering the Core Facilities will remain within a near 20-minute drive of Virgin Active Surrey, of which three also offer racquet facilities. 13 gyms offering the Core Facilities are at a shorter drive time to Virgin Active Surrey than the closest overlapping David Lloyd gym (Cheam), including other large health and fitness club operators with a similar offer.

55. The CMA therefore believes that there is sufficient competition in the Surrey area to constrain the Parties post-Merger.

[23] Virgin Active Surrey is also located at a 29.6-minute drive time to David Lloyd Raynes Park.

Brighton, Clearview and Northwood

56. In the remaining three Overlap Areas, the CMA found from its initial analysis that the Parties' sites were closer competitors and the number of rivals offering the Core Facilities was more limited. The CMA therefore undertook a more detailed assessment of these areas.

Brighton

57. Virgin Active Brighton is located approximately 18-minutes' drive from David Lloyd Brighton. The Parties submitted an analysis of member locations, which indicated that there is a significant overlap in the geographical areas from which the Parties draw their members.

58. David Lloyd's internal documents showed that David Lloyd monitored multiple competitors which it classified either as 'high threat' or 'medium threat'.

59. Virgin Active Brighton offers racquet facilities whereas David Lloyd Brighton does not. Their other offerings are very similar.

60. The average monthly membership fees for Virgin Active Brighton and David Lloyd Brighton are very similar (£[✂] and £[✂] respectively).

61. Table 1 shows the CMA's estimated diversion ratios for Virgin Active Brighton and David Lloyd Brighton using evidence from the survey.[24] Diversion ratios estimate the degree of substitution between one provider of a product or service and a potential substitute.[25]

[24] Diversion ratios from Virgin Active to David Lloyd include diversion to all David Lloyd gyms. Diversion ratios from David Lloyd to Virgin Active have not been adjusted to exclude diversion to other David Lloyd gyms.

[25] *Merger Assessment Guidelines*, from paragraph 5.2.15.

Table 1: Estimated diversion ratios from Virgin Active Brighton and David Lloyd Brighton

	VA			DL	
	Number	%		Number	%
Not go anywhere else	132	21%	Not go anywhere else	45	18%
Falmer Sports Complex	8	2%	The Gym (Brighton)	18	11%
University of Sussex Sports Complex	3	1%	Livingwell Health Club (Brighton)	6	4%
The Gym	3	1%	Pure Gym	3	2%
Fitness First Health Club	3	1%	Prince Regent Swimming Pool	10	6%
Prince Regent Swimming Pool	23	5%	Fitness First Health Club	4	2%
Pure Gym	3	1%	Underground Gym	11	6%
Withdean Sports Complex	89	20%	Coral Health and Fitness	1	1%
Coral Health and Fitness	4	1%	Sports Direct	5	3%
Underground Gym	11	2%	University of Sussex Sports Complex	1	1%
Sports Direct Fitness	5	1%	Withdean Sports Complex	4	2%
David Lloyd	89	20%*	Virgin Active Brighton	61	36%
Other	112	25%	Other	15	9%
Don't Know	158	N/A	Don't Know	69	N/A

Note: Includes all other DL gyms. DL Brighton was listed in the survey as one of the 11 alternative gyms. Additionally, some respondents who responded that they would go to an 'other' gym said this was a David Lloyd gym.*

62. These diversion ratios indicate that the Parties are each other's closest competitor in the Brighton area. Specifically, the survey found that:

    (a) in the event of closure of Virgin Active Brighton, 20% of members would divert to David Lloyd and 20% of members would divert to Withdean Sports Complex; and

    (b) in the event of closure of David Lloyd Brighton, 36% of members would divert to Virgin Active Brighton and 11% would divert to The Gym.

63. Post-Merger, seven gyms offering the Core Facilities will remain within a 20-minute drive of Virgin Active Brighton, with six offering the Core Facilities at a shorter drive time to Virgin Active Brighton than David Lloyd Brighton. Four gyms offering the Core Facilities will remain within a 20-minute drive of David Lloyd Brighton, with all four offering the Core Facilities at a shorter drive time to David Lloyd Brighton than Virgin Active Brighton. However, the survey evidence shows low levels of diversion to other gyms with the Core Facilities in the Brighton area, indicating that consumers are unlikely to view them as close alternatives to the Parties.

64. The Parties submitted that there are differences between the locations of the Parties' members and actual diversion ratios are likely to be significantly lower

than suggested by the survey. The Parties said that there is evidence of members switching to different gyms in Brighton, although the Parties could not provide details to explain why these members may be switching. The Parties submitted that there are many gyms in the Brighton area with all the Core Facilities, and many more gyms which may not possess all the Core Facilities but nonetheless exert competitive pressure.

65. The survey evidence indicates that, in relation to the Parties' sites in Brighton, few members would divert to a gym without the Core Facilities, suggesting that these gyms provide a limited constraint on the Parties. The survey identified those gyms with the Core Facilities which appear to constrain the Parties, indicating that each of the Parties has two significant competitors, one of which in each case is the other party to the Merger. The CMA notes that this evidence is consistent with David Lloyd's internal documents (see paragraph 58.

66. The Parties also submitted that two existing operators are likely to be stronger competitors in the future as King Alfred Leisure Centre is undergoing a £40 million investment, and The Triangle is undergoing a £3.1 million refurbishment. The CMA considered these submissions but noted that the facilities which these gyms will offer and how they will be perceived by the members of Virgin Active Brighton and David Lloyd Brighton remains very unclear.

67. On the basis of the evidence set out above, and in particular on the basis of evidence indicating strong competition between the Parties and a limited constraint from other existing operators in the area, the CMA believes that the Merger gives rise to a realistic prospect of an SLC in the provision of gyms in the Brighton area.

Clearview

68. Virgin Active Clearview is located approximately 10-minutes' drive from David Lloyd Gidea Park, 14-minutes' drive from David Lloyd Basildon and 15-minutes' drive from David Lloyd Dartford.[26] The Parties submitted an analysis of member locations, which indicated that there is a significant overlap between the geographical areas from which Virgin Active Clearview and David Lloyd Gidea Park draw their members, but no significant overlap

[26] Travelling in the opposite direction results in the following drive times: 12.7-minutes from Virgin Active Clearview to David Lloyd Basildon, 14.6-minutes from Virgin Active Clearview to David Lloyd Gidea Park, and 19.5-minutes from Virgin Active Clearview to David Lloyd Dartford.

between the geographical areas from which Virgin Active Clearview, David Lloyd Basildon and David Lloyd Dartford draw their members.

69. Post-Merger, 18 gyms offering the Core Facilities will remain within a 20-minute drive of Virgin Active Clearview, of which three also offer racquet facilities. There is one gym (DW Fitness) at a shorter drive time (approximately seven minutes) to Virgin Active Clearview than the nearest David Lloyd gym (Gidea Park, at approximately 10-minutes). DW Fitness offers a membership fee of £[✂], compared with £[✂] at Virgin Active Clearview and £[✂] at David Lloyd Gidea Park.[27] All of the other gyms offering the Core Facilities within a 20-minute drive of Virgin Active Clearview appear to be priced at significantly lower membership fees, which may reflect a lower quality of facilities.

70. David Lloyd's internal documents show that David Lloyd monitored multiple competitors which it classified either as 'high threat' or 'medium threat'.[28] Similarly, David Lloyd's internal documents show that [✂]. This evidence would suggest that Virgin Active Clearview is a significant close competitor to David Lloyd Gidea Park, a less significant close competitor to David Lloyd Basildon and no competitor to David Lloyd Dartford. The CMA notes that David Lloyd Dartford is located south of the river Thames, while Virgin Active Clearview (and the other two David Lloyd sites) are all located north of the river.

71. All four of the Parties' gyms in this area offer the Core Facilities, as well as racquet facilities. Virgin Active Clearview, David Lloyd Basildon and David Lloyd Gidea Park also offer crèche facilities.

72. In light of the evidence from internal documents, the location of members and local competitors, the CMA believes that there is sufficient competition to constrain the Parties post-Merger in relation to the overlaps between Virgin Active Clearview and each of David Lloyd Basildon and David Lloyd Dartford. However, in relation to the overlap between Virgin Active Clearview and David Lloyd Gidea Park, the CMA conducted a more detailed assessment (as with Brighton and Northwood), which included a survey of members.

[27] Source: LDC Database July 2016. The monthly membership rate collected by LDC is the adult peak no contract rate (if offered) or if not, the shortest adult peak rolling contract. These figures tend to be higher than the average membership fee paid for the Parties' gyms which are £55 per month for Virgin Active Clearview and £81 per month for David Lloyd Gidea Park. Reasons for this include that membership prices in the LDC Database may not reflect any discounting offered in exchange for a longer duration of contract or any negotiation that may occur at the point of sale.

[28] [✂].

73. Table 2 shows the CMA's estimated diversion ratios for Virgin Active Clearview and David Lloyd Gidea Park using evidence from the survey.

Table 2: Estimated diversion ratios from Virgin Active Clearview and David Lloyd Gidea Park

	VA Clearview			DL Gidea Park	
	Number	Per cent		Number	Per cent
Not go anywhere else	43	12%	**Not go anywhere else**	38	15%
Spirit Health Club	6	3%	**Ab Salute (Romford)**	7	4%
DW Fitness	15	8%	**Fitness First Health Club**	9	5%
Ab Salute (Brentwood)	10	5%	**Better Gym**	3	2%
Ab Salute (Romford)	1	1%	**LDG Fitness Centre**	1	1%
Better Gym	5	3%	**Nuffield Health**	31	18%
David Lloyd	51	26%*	**Ab Salute (Brentwood)**	1	1%
Pure Gym	2	1%	**Central Park Leisure Centre**	4	2%
Bannatynes Health Club	6	3%	**YMCA**	4	2%
Central Park Leisure Centre	7	4%	**Hornchurch Sports Centre**	26	15%
Fitness First Health Club	5	3%	**Virgin Active Clearview**	46	26%
Basildon Sporting Village	10	5%	**DW Fitness**	1	1%
Other	51	26%	**Other**	16	9%
Don't Know	138	N/A	**Don't Know**	72	N/A

Note: Includes all other DL gyms. DL Gidea Park was listed in the survey as one of the 11 alternative gyms. Additionally, some respondents who responded that they would go to an 'other' gym said this was a David Lloyd gym.*

74. These diversion ratios indicate that the Parties are each other's closest competitor. Specifically, the survey found that:

(a) in the event of closure of Virgin Active Clearview, 26% of members would divert to David Lloyd and 8% of members would divert to DW Fitness; and

(b) in the event of closure of David Lloyd Gidea Park, 26% of members would divert to Virgin Active Clearview and 18% would divert to Nuffield Health Romford.

75. The Parties submitted that there is limited overlap between the locations of the Parties' members, and that 16 gym operators with Core Facilities were excluded from the survey, seven of which have racquet facilities. The Parties also submitted that they are constrained by a high number of operators which may not possess all the Core Facilities but nonetheless exert competitive pressure.

76. The survey evidence indicates that, in relation to Virgin Active Clearview and David Lloyd Gidea Park, few members would divert to a gym without the Core

Facilities, suggesting that these gyms provide a limited constraint on the Parties. The survey identified those gyms with the Core Facilities which appear to constrain the Parties, indicating that each of the Parties has two significant competitors, one of which in each case is the other party to the Merger. The CMA notes that this evidence is consistent with David Lloyd's internal documents (see paragraph 70).

77. The Parties submitted that nine gyms have opened in the Clearview area in the past two years, one of which has Core Facilities, and two gyms with the Core Facilities (one of which also has racquet facilities) have undergone significant recent refurbishment. The Parties also submitted that a new £25 million operator will enter in Romford early in 2018, which will have the Core Facilities. This operator will be located within a 20-minute drive time of both Virgin Active Clearview and David Lloyd Gidea Park. The CMA considered these submissions but noted that the facilities which these sites will offer and how they will be perceived by the members of Virgin Active Clearview and David Lloyd Gidea Park remains very unclear.

78. On the basis of the evidence set out above, and in particular on the basis of evidence indicating strong competition between the Parties and a limited constraint from other existing operators in the area, the CMA believes that the Merger gives rise to a realistic prospect of an SLC in the provision of gyms in the Clearview area, specifically between Virgin Active Clearview and David Lloyd Gidea Park.

Northwood

79. Virgin Active Northwood is located approximately 22-minutes' drive from David Lloyd Bushey.[29] Both Parties' gyms offer the Core Facilities and racquet facilities. The average membership price paid is £[✄] at Virgin Active Northwood and £[✄] at David Lloyd Bushey. The Parties submitted analysis of member locations, which indicates that, whilst there is some overlap, the majority of Virgin Active Northwood's members are drawn from a separate geographical area to that of David Lloyd Bushey. David Lloyd's internal documents show that David Lloyd monitored multiple competitors which it classified either as 'high threat' or 'medium threat'.

80. Table 3 shows the CMA's estimated diversion ratios for Virgin Active Northwood and David Lloyd Bushey using evidence from the survey.

[29] Travelling in the opposite direction, from Virgin Active Northwood to David Lloyd Bushey, the drive time is 21.7-minutes.

Table 3: Estimated diversion ratios from Virgin Active Northwood and David Lloyd Bushey

	VA Northwood			DL Bushey	
	Number	%		Number	%
Not go anywhere else	126	20%	**Not go anywhere else**	19	8%
The Northwood Club	70	18%	**Bushey Grove Leisure Centre**	15	11%
William Penn Leisure Centre	18	5%	**The Gym**	1	1%
Fitness First	16	4%	**West Herts Squash and Fitness**	1	1%
Anytime Fitness	6	2%	**The Village Gym**	46	33%
Highgrove Pool and Fitness Centre	29	8%	**Aspire Leisure Centre**	2	1%
West Herts Squash and Fitness	1	0%	**Watford Leisure Centre**	6	4%
YMCA	1	0%	**Nuffield Health**	4	3%
Pump Gym	2	1%	**Pure Gym**	1	1%
The Gym	2	1%	**Westminster Lodge Leisure Centre**	2	1%
Bushey Grove Leisure Centre	9	2%	**The Northwood Club**	2	1%
David Lloyd	57	15%*	**VA Northwood**	23	17%
Other	95	25%	**Other**	22	16%
Don't know	211	N/A	**Don't Know**	81	N/A

Note: Includes all other DL gyms. DL Bushey was listed in the survey as one of the 11 alternative gyms. Additionally, some respondents who responded that they would go to an 'other' gym said this was a David Lloyd gym.*

81. These diversion ratios indicate that, while Virgin Active Northwood and David Lloyd compete closely, they are not each other's closest competitors, since:

(a) in the event of closure of Virgin Active Northwood, 18% of members would divert to The Northwood Club and 15% of members would divert to David Lloyd; and

(b) in the event of closure of David Lloyd Bushey, 33% of members would divert to The Village Gym, 17% would divert to Virgin Active Northwood, and 11% would divert to Bushey Grove Leisure Centre.

82. Post-Merger, four gyms offering the Core Facilities will remain within a near 20-minute drive of Virgin Active Northwood, with all four gyms offering the Core Facilities at a shorter drive time to Virgin Active Northwood than David Lloyd Bushey. 29 gyms offering the Core Facilities will remain within a near 20-minute drive of David Lloyd Bushey, with 28 gyms offering the Core Facilities at a shorter drive time to David Lloyd Bushey than Virgin Active Northwood. The Parties submitted that 86 gym operators with Core Facilities were not on the survey list, 29 of which have racquet facilities.

83. On the basis of the evidence set out above, and in particular the survey evidence indicating that the Parties are not each other's closest competitor,

which is supported by the limited member area overlap between the Parties and the differentiation in their average prices, 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 provision of gyms in the Northwood area.

Barriers to entry and expansion

84. Entry, or 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. In assessing whether entry or expansion might prevent an SLC, the CMA considers whether such entry or expansion would be timely, likely and sufficient. In terms of timeliness, the CMA's guidelines indicate that the CMA will look for entry to occur within two years.[30]

85. Evidence provided by competitors suggested that the costs associated with building a new gym are large, particularly if the gym features a swimming pool and/or racquet facilities. The main factors associated with setting up a new gym are obtaining a suitable location and gaining planning approval. One competitor said that it can take between three to six months to open a gym and, although costs will vary depending on the location, size and facilities, they will range between £1 million and £2 million.

86. Internal documents from Virgin Active note that [✄].[31] [✄] [32] [✄].

87. The Parties submitted that the barriers to entry are low in the gym industry. They added that the market is already characterised by the presence of numerous operators with Core Facilities, and that there are many possibilities for expansion. These comments have been taken into account where appropriate in the location-specific competitive assessment above.

88. The CMA believes that the expansion of existing operators in Brighton and the entry of new operators in Clearview may mitigate the initial effect of the Merger to an extent. However, this is in the context of strong current competition between the Parties and limited current alternative constraints in these areas. As noted in the analysis above, there are many other existing gyms in the Brighton and Clearview areas which offer a limited constraint on the Parties and, in this context, the extent of the constraint which the new or expanded sites will offer remains very unclear.

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[30] *Merger Assessment Guidelines*, paragraph 5.8.11.

[31] [✄].

[32] [✄].

89. For these reasons, the CMA believes that entry or expansion is not sufficient to prevent the realistic prospect of an SLC as a result of the Merger.

Third party views

90. The CMA contacted competitors of the Parties. Approximately half of the competitors which responded to the CMA raised concerns regarding a reduction in competition at the top end of the market and that the reduction may lead to higher membership fees or a reduction in the quality or types of facilities currently offered by the Parties in the Overlap Areas. No other third parties raised concerns about the Merger.

91. Third party comments have been taken into account where appropriate in the competitive assessment above.

Decision

92. Consequently, the CMA believes 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.

93. The CMA therefore believes that it is under a duty to refer under section 33(1) of the Act. However, the duty to refer is not exercised[33] whilst the CMA is considering whether to accept undertakings[34] instead of making such a reference. The Parties have until 26 May 2017[35] to offer an undertaking to the CMA.[36] The CMA will refer the Merger for a phase 2 investigation[37] if the Parties do not offer an undertaking by this date; if the Parties indicate before this date that they do not wish to offer an undertaking; or if the CMA decides[38] by 2 June 2017 that there are no reasonable grounds for believing that it might accept the undertaking offered by the Parties, or a modified version of it.

Rachel Merelie
Acting Executive Director, Markets & Mergers
Competition and Markets Authority
19 May 2017

[33] Section 33(3)(b) of the Act.

[34] Section 73 of the Act.

[35] Section 73A(1) of the Act.

[36] Section 73(2) of the Act.

[37] Sections 33(1) and 34ZA(2) of the Act.

[38] Section 73A(2) of the Act.