

# COMPLETED ACQUISITION BY ELECTRO RENT CORPORATION OF MICROLEASE INC. AND TEST EQUIPMENT ASSET MANAGEMENT LIMITED

## Issues statement

**23 November 2017**

### The reference

1. On 19 October 2017, the Competition and Markets Authority (CMA), in exercise of its duty under [section 22\(1\)](#) of the Enterprise Act 2002 (the Act), referred the completed acquisition by Electro Rent Corporation (Electro Rent) of Microlease Inc. and Test Equipment Asset Management Limited (Microlease) for further investigation and report by a group of CMA panel members (the inquiry group).
2. The CMA must decide:
  - (a) whether a relevant merger situation has been created; and
  - (b) if so, whether the creation of that situation has resulted, or may be expected to result, in a substantial lessening of competition (SLC) within any market or markets in the UK for goods or services.
3. In this statement, we set out the main issues we are likely to consider in reaching our decisions, having had regard to the evidence gathered to date including evidence set out in the phase 1 decision to refer the acquisition of Microlease by Electro Rent for further investigation (the reference decision<sup>1</sup>). This does not preclude the consideration of any other issues which may be identified during the course of our inquiry, which will include the gathering of further evidence.
4. Throughout this document, where appropriate, we refer to Electro Rent and Microlease collectively as ‘the Parties’.

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<sup>1</sup> See [Reference decision](#), 19 October 2017 (and published on the CMA website on 30 October 2017). (Note, on 14 June 2017, the CMA announced that the merger would be referred for a phase 2 investigation unless the Parties offered acceptable undertakings to address the competition concerns identified. The full text of this decision was published on 7 July 2017 and is referred to in this document as the [CMA phase 1 decision](#).)

## Background

5. On 31 January 2017 Electro Rent acquired the whole of the issued share capital of Microlease (the merger).
6. The Parties both supply testing and measurement equipment (TME) which incorporates a wide range of equipment used to test and measure electronic devices in order to validate their performance, across sectors such as telecommunications, aerospace and defence, industrial, and information technology. The Parties operate globally in the supply of TME for purchase, leasing and rental.
7. Electro Rent is owned and controlled by funds managed by investment firm Platinum Equity LLC, and is based in the US (California). It supplies TME, offering such products for sale (either as new or used equipment), for lease and for rental in the UK and worldwide. It has calibration laboratories but no manufacturing facilities. In the UK, it has premises in Sunbury, and supplies products to the UK market from a warehouse in Belgium.
8. Microlease is based in the UK. It supplies TME – offering such products for sale (either as new or used equipment), for lease and for rental – and asset management services, in the UK and worldwide. Microlease has an office, warehouse and calibration laboratory in the UK. It has no manufacturing facilities.
9. More information on the Parties can be found in paragraphs 8 and 9 of the CMA phase 1 decision.<sup>2</sup>

## Frame of reference

10. 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 CMA's analysis of the competitive effects of the merger in any mechanistic way. In assessing whether a merger may give rise to an SLC, the CMA may take into account factors such as constraints outside the relevant market, segmentation within the relevant market, and other ways in which some constraints are more important than others.<sup>3</sup>

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<sup>2</sup> See [CMA phase 1 decision](#), 14 June 2017.

<sup>3</sup> See [Merger Assessment Guidelines](#) (CC2/OFT 1254), September 2010, paragraph 5.2.2.

11. In general, we note that market definition and the analysis of competitive effects are both driven by considerations relating to the ‘closeness’ of substitution between the Parties’ offers and those of alternatives.
12. The Parties overlap in the:
  - sale of new TME;
  - sale of used TME;
  - rental of TME; and
  - leasing of TME.
13. As set out in paragraphs 24 to 29 of the CMA phase 1 decision,<sup>4</sup> the Parties submitted that the appropriate product frame of reference in this case should be the supply of TME (irrespective of the form of supply), but consider that the narrowest plausible candidate product market is the rental of TME in the UK. They also submitted that a UK market for TME rental is the narrowest appropriate geographic frame of reference.
14. Given Electro Rent’s minimal revenues from sales and leasing in the UK, our current intention is to focus on the overlap in rental activities. However, we will also take account of Microlease’s more significant sales of TME in the UK.
15. We will investigate the extent to which different forms of supply of TME are alternatives to TME rental for UK customers, and therefore whether the product frame of reference should be widened from rental of TME to include other forms of supply on the basis of demand-side substitution. In this regard, we will also consider the scope for supply-side substitution between different forms of TME supply.
16. Given the wide range of TME we will also consider whether there are sufficient differences in competitive conditions between different types of TME such that it is appropriate to distinguish between different types of TME in the frame of reference.
17. We will also consider the extent to which the market for TME is wider than the UK.

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<sup>4</sup> See [CMA phase 1 decision](#), 14 June 2017.

## Assessment of the competitive effects of the merger

### *Counterfactual*

18. We will assess the possible effects of the merger on competition compared with the competitive conditions in the counterfactual situation (ie the competitive situation in the absence of the merger). We will therefore consider what would have been likely to have happened if the merger had not taken place and what would have been the likely conditions of competition in the foreseeable future.
19. For completed mergers the CMA generally adopts the pre-merger 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.
20. As set out in paragraph 17 of the CMA phase 1 decision,<sup>5</sup> we have seen no evidence supporting a different counterfactual to the pre-merger conditions, and the Parties have not put forward any arguments in this respect. Therefore, we currently believe the pre-merger conditions of competition to be the relevant counterfactual.

### *Theory of harm: Horizontal unilateral effects through the loss of actual competition*

21. Theories of harm describe the possible ways in which an SLC could arise as a result of the merger and provide the framework for our analysis of the competitive effects of the merger. We have set out below the theory of harm which we intend to investigate, and welcome views.
22. The removal of one party as a competitor in the supply of TME could provide the incentive for the Parties to deteriorate elements of their competitive offering in the UK; these could include:
  - (a) increasing the price of rental of TME; and/or
  - (b) deteriorating another competitive parameter that matters to customers, such as quality or service levels.

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<sup>5</sup> See [CMA phase 1 decision](#), 14 June 2017.

23. We will examine the following factors:

- (a) Closeness of competition between Microlease and Electro Rent: in particular, we will consider whether the Parties are the best alternative supplier for each other's customers, and whether competition between the Parties influences how they set prices or other aspects of their service. We will also consider the possibility that Electro Rent may have become a closer competitor to Microlease in the UK since the opening of Electro Rent's UK premises and the resulting potential for Electro Rent to become a closer competitor to Microlease in the UK by scaling up the UK operation.
- (b) Closeness of competition from other rental suppliers and other forms of TME provision: we will consider the extent to which other rental suppliers and/or other forms of TME provision are alternatives for the Parties' customers.
- (c) The ability of the Parties to price discriminate between customers: in particular, their ability to identify and set different prices for customers who have no, or few, alternative options.

### ***Countervailing factors***

24. We will consider whether there are countervailing factors which are likely to prevent or mitigate any SLC that we may find.

### ***Entry and expansion***

25. We plan to investigate the likelihood of entry and expansion, and whether new competitors to the Parties are likely to emerge. We will consider in this context the process and outcome of the Undertakings in Lieu given by Electro Rent during Phase 1,<sup>6</sup> given that the proposed divestment did not take place.

26. In order for entry and/or expansion to offset an SLC, entry and/or expansion would need to be timely, likely and sufficient.

27. To investigate this issue, we intend to collect information on:

- the history of entry, expansion and exit, in particular the opening of Electro Rent's UK premises in 2015 and subsequent development of its UK business;

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<sup>6</sup> See [Reference decision](#), 19 October 2017, paragraphs 3–12.

- the steps involved in new entry or expansion into the supply of new product lines or new geographies, and costs of doing so;
- the likelihood of future entry/expansion in this market;
- the barriers to entry and expansion, including:
  - the role played by supply relationships with OEMs;
  - what physical facilities are needed and whether these need to be in the UK;
  - what level of stock holding and type of stock is required to be held;
  - working capital/investment costs;
  - staff levels;
  - logistics network;
  - what additional services may be required to accompany product lines;
  - whether effective entry can be made in only one sector or type of equipment, or is a presence in more than one sector or type of equipment necessary to be an effective competitor; and
- customers' preferences to switch supplier (eg cost of switching, length of existing contracts, and importance of an established relationship).

#### *Buyer power*

28. In order for countervailing buyer power to offset an SLC, customers would have to have sufficient buyer power that could offset any attempt of the Parties to increase prices or reduce quality and/or innovation.
29. We will examine how negotiations are carried out between the Parties and customers and how frequently these happen in order to determine if there are sufficient outside options for customers to switch to post-merger and therefore exercise countervailing buyer power of a scale to be sufficient to offset an SLC.

#### *Efficiencies*

30. We will examine any submissions made in relation to efficiencies arising from the merger. In particular, we will examine whether any potential efficiencies are rivalry-enhancing and could be expected to offset any loss of competition.

## *Other*

31. We are not currently aware of any other countervailing factors, and none have been suggested by the Parties.

## **Possible remedies and relevant customer benefits**

32. If we conclude provisionally that the merger has resulted, or may be expected to result, in an SLC in any market(s), we will consider whether, and if so what, remedies might be appropriate, and will issue a further statement.
33. In any consideration of possible remedies, we may have regard to their effect on any relevant customer benefits in relation to the merger and, if so, what these benefits are likely to be and which customers would benefit.

## **Responses to the issues statement**

34. Any party wishing to respond to this issues statement should do so in writing, by no later than **5pm on Thursday 7 December 2017**. Please email [ElectroRent.Microlease@cma.gsi.gov.uk](mailto:ElectroRent.Microlease@cma.gsi.gov.uk) or write to:

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