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# Southdown Motor Services Limited

A report on the conduct of Southdown Motor Services Limited  
in respect of its operation of local bus services  
on routes 262 and 242 in Bognor Regis

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MONOPOLIES AND MERGERS COMMISSION

# **Southdown Motor Services Limited**

A report on the conduct of Southdown Motor Services Limited in respect of its operation of local bus services on routes 262 and 242 in Bognor Regis

**Presented to Parliament by the Secretary of State for  
Trade and Industry by Command of Her Majesty  
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17 March 1993**

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<sup>1</sup>These members formed the group which was responsible for this report under the chairmanship of Sir Sydney Lipworth.

## **Note by the Department of Trade and Industry**

In accordance with section 17(5) of the Competition Act 1980, the Secretary of State has excluded from the copies of the report, as laid before Parliament and as published, certain matters, publication of which appears to the Secretary of State to be against the public interest, or which he considers would not be in the public interest to disclose and which, in his opinion, would seriously and prejudicially affect certain interests. The omission is indicated by a note in the text.

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# 1 Summary

1.1. In a reference made on 3 September 1992 (and varied on 12 January 1993—see Appendix 1.1) the Director General of Fair Trading (DGFT) asked us to investigate the registration, operation and charging of uneconomic fares by Southdown Motor Services Limited (Southdown) on routes 262 and 242 in Bognor Regis, with the intention of undermining the viability of a competitor. We were asked to consider whether this course of conduct was anti-competitive and, if so, might be expected to operate against the public interest.

1.2. Southdown (now called Sussex Coastline Buses Ltd (Sussex Coastline), but referred to as Southdown throughout) is, and for many years has been, the main operator of bus services in Bognor Regis. In 1987, shortly after the deregulation of the bus industry, a new company, Strikeline Limited (Strikeline) (referred to by its trade name Easy Rider Minicoaches (Easy Rider)), started services in competition with Southdown on routes from the town centre of Bognor Regis to two residential areas, North Bersted to the north and Rose Green to the west of the town. Each company provided two buses per hour on these routes.

1.3. In July 1990 Southdown introduced a new service, the 262, timed shortly ahead of the Easy Rider service to Rose Green, but this was withdrawn in December 1990. In March 1991 Southdown introduced another new service, the 242, which ran shortly ahead of Easy Rider on its services both to North Bersted and Rose Green. After the introduction of the 242, Southdown was operating six buses per hour to North Bersted, and four to Rose Green. The 242 service made a substantial loss, but caused a significant deterioration in Easy Rider's financial position, following which, in May 1992, its proprietor sold the vehicles and goodwill to Southdown.

1.4. Southdown argued that it was forced to act as it did to defend itself in Bognor Regis. We, however, believe that the operation of the additional services provided by route 242, at revenues which did not cover even the costs of drivers' wages or provide any contribution to general expenses, with the purpose of driving out Easy Rider, was an anti-competitive practice, and a main cause of Easy Rider's withdrawal from the market.

1.5. Competition from Easy Rider had been to the benefit of passengers, resulting both in lower fares than elsewhere in Bognor Regis and in higher levels of service than Southdown had provided previously. The loss of competition may, in our view, be expected in due course to result in higher fares and lower levels and quality of service on the routes previously operated by Easy Rider, and the corridors adjacent to such routes. We have, therefore, concluded that Southdown's course of conduct may be expected to operate against the public interest.

1.6. We have recommended that firstly Southdown be required to limit fares increases on the affected routes to the increase in the Retail Price Index (RPI) for two years from the date of our report and, secondly, that it should undertake for a similar period not to reduce the levels of service on the affected routes below those operated by Southdown and

Easy Rider before the introduction of route 242. Additionally, Southdown should submit regular reports to the Office of Fair Trading (OFT) on changes in fares and levels of service, and on the profitability on the affected routes, and in the Bognor Regis area generally for purpose of comparison.

## 2 The relevant bus services

### Introduction

2.1. This chapter considers the operation of bus services operating between Bognor Regis and two residential areas, North Bersted and Rose Green, respectively to the north and west of Bognor Regis town centre (see Appendix 2.1). It relates to the situation arising from the deregulation of the bus industry following the Transport Act 1985 (the 1985 Act). Our inquiry centres on the response by the dominant operator to a new entrant in specific parts of the Bognor Regis area. Before outlining the relevant bus services of the two companies it is appropriate to summarize the regulations that govern bus operations and their application to the situation in Bognor Regis.

### Regulation of the industry

2.2. Between 1930 and 1981 anyone wishing to run a bus service needed a licence for each vehicle, a public service vehicle (PSV) licence for each driver and a road service licence (RSL) for each route. The grant of licences was, and continues to be, regulated by Traffic Commissioners, each Commissioner being responsible for a defined area.<sup>1</sup> Before issuing an RSL, Traffic Commissioners were required to consider the need for any proposed new service, taking account of existing services and the needs of the area as a whole. Local authorities and existing operators could object. There were also provisions for the Traffic Commissioners to specify fares. Local authorities provided financial support to local bus companies based on the expected shortfall in revenue in relation to costs. Revenue support grants were paid after taking account of any surplus made on profitable routes.

2.3. The Transport Act 1978 made limited changes to this licensing system, making it easier for minibuses using volunteer drivers to run local services (community buses) and facilitating car sharing. The Transport Act 1980 removed restrictions on the provision of long-distance express services and was intended to make it easier to operate a local service in competition with an existing licence-holder. It effectively removed fare controls and, with effect from April 1981, replaced individual vehicle licensing with PSV operator licensing.

2.4. In 1984 the Government published a White Paper entitled *Buses*.<sup>2</sup> This set out proposals designed to free bus services from restrictions on competition. It envisaged that competition would lead to lower fares, new services and more passengers and that the obstacles to enterprise, initiative and efficiency inherent in the existing system of regulation would be removed.

2.5. The 1985 Act provided for the deregulation of the bus industry on the lines set out in the White Paper. The 1985 Act's main provisions were:

- (a) the abolition of road service licensing for local services outside London and the introduction of local service registration;
- (b) the restriction of subsidy to local services which were not commercially registered but required to meet social need, such subsidy to be awarded on the basis of competitive tendering; and

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<sup>1</sup>Great Britain is divided into nine Traffic Areas, each of which has a Traffic Commissioner, a full-time salaried official appointed by the Secretary of State.

<sup>2</sup>*Buses*, Cmnd 9300, July 1984.

- (c) the National Bus Company (NBC) to be split up and privatized and local authority bus operations (ie those of municipal operators, including Scottish regional operators and Passenger Transport Executives) to be formed into separate passenger transport companies operating at arm's length from the local authorities.

2.6. Under the provisions of the 1985 Act there is, therefore, no longer any restriction on the quantity of local bus services supplied. Operators must now hold PSV operator licences and are simply required to register new services with the appropriate Traffic Commissioner, giving 42 days' notice of any intention to set up or to vary or withdraw a service. Information must be provided on the route, terminal points, timetable, stopping arrangements and type of vehicles to be used. The Traffic Commissioners retain their powers over the quality of service offered and over safety standards. They have powers to attach conditions to operator licences where operators fail to run local services in accordance with the registered details, intentionally interfere with the services of another operator, or operate services in a manner dangerous to the public. The conditions may prohibit the operator from providing services on certain routes, or even from providing local bus services of any description.

2.7. The 1985 Act changed the basis on which local authorities could subsidize the provision of local bus services. Subsidies can now only be paid for socially necessary services not provided by the commercial network. All contracts for subsidized services (except for *de minimis* arrangements and post and community buses) must be let by competitive tender, and specific information on tenders received must be published by the local authority. There is an express duty on local authorities not to inhibit competition between operators and potential operators when exercising their subsidy powers.

2.8. Local authorities have powers which enable them to provide concessionary fares, for instance for elderly and disabled people. Before the 1985 Act this was often given in the form of a blanket subsidy. Payments in respect of concessionary fares must now reflect the actual loss of revenue to the operator, plus any additional costs of carrying the extra passengers.

## The Bognor Regis area

2.9. Bognor Regis is a seaside resort on the Sussex coast, falling within the administrative area of Arun District Council. Most of the commercial and shopping facilities of Bognor Regis are located in the town centre, although there are two out-of-town supermarkets: Tesco in South Bersted and Sainsbury near Chichester. Bognor Regis has a population of around 56,000. There is a relatively high proportion of elderly residents; around one-third of the population is of pensionable age (see Table 2.1).

TABLE 2.1 Age of population

	<i>Percentage of residents of pensionable age or over*</i>
Bognor Regis	31.1
West Sussex	24.0
UK	15.7

Source: 1991 Census.

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\*65 years and over for men and 60 years and over for women.

2.10. The main focus of our investigation is bus services operating between Bognor Regis town centre and two residential areas, Rose Green and North Bersted. Rose Green is situated approximately 2½ miles west of the town centre. North Bersted, situated approximately 1½ miles north of the town centre, was originally a separate village but has become incorporated into Bognor Regis as the town has grown. We were told that both areas had a lower level of car ownership than other parts of Bognor Regis.

## **Bus operators in Bognor Regis**

2.11. Prior to deregulation Southdown (now called Sussex Coastline Buses Ltd, but referred to as Southdown throughout) was virtually the only operator of bus services in this part of West Sussex. Southdown had been a bus operator in Sussex since 1915 and as part of the privatization of the NBC was sold to four of its managers in a management buy-out in October 1987. In August 1989 Stagecoach (Holdings) Limited, now Stagecoach Holdings plc (Stagecoach), acquired Southdown. Including limited stop services Southdown operated ten routes from or through Bognor Regis town centre. These services are described in more detail in paragraphs 2.19 to 2.23. In January 1987 a new company, Strikeline Limited (referred to by its trade name Easy Rider), was formed by Mr Hunter which started two commercial bus services: the 01 which ran from North Bersted to the town centre and the 02 from Rose Green to the town centre. Easy Rider subsequently expanded its commercial services with the introduction of service 03 (from Stroud Green to the town centre) in January 1988 and service 04 (between Pagham and Bognor Regis) in November 1988. Service 03 was withdrawn, however, in August 1989 and the remainder of Easy Rider's services were discontinued in May 1992 when the assets and goodwill of the company were sold to Southdown. The services of Easy Rider are described in detail in paragraphs 2.24 to 2.30.

2.12. During 1992 the only other operator of commercial services in Bognor Regis was Blue Lake Coaches (Blue Lake). It operated a morning service from Chichester to Bognor Regis with a return journey in the evening. Blue Lake also ran a service from the town centre to the Tesco supermarket in South Bersted. In addition Blue Lake ran a service, number 243, from Bognor Regis to West Meads under contract to West Sussex County Council (WSCC). The tender for this contract expired at the end of October 1992. Southdown registered a commercial service offering two buses per hour as from 28 October 1992 and, as a result, Blue Lake withdrew its number 243 hourly service at the end of December 1992.

## **The OFT investigation and report**

2.13. In March 1991 Mr Hunter complained to the OFT that Southdown had registered and operated a service, number 242, which duplicated two of the routes operated by Easy Rider. Mr Hunter alleged that there was no financial justification for this registration since a previous attempt by Southdown to run a service (number 262) along part of the route had been withdrawn. Mr Hunter told the OFT that in his view the number 242 service was being run by Southdown at a continuing loss with the intention of removing Easy Rider from the market. On 25 February 1992 the DGFT announced an investigation of Southdown's services 242 and 262 under section 3 of the Competition Act 1980. During the course of this investigation Easy Rider ceased operating bus services in Bognor Regis on 16 May and Mr Hunter sold the assets and goodwill of Easy Rider to Southdown. As from 18 May 1992 Southdown operated its services to timetables similar to those of the former Easy Rider services.

2.14. In a report published in July 1992<sup>1</sup> the DGFT concluded that Southdown, in its operation of the two relevant bus services in Bognor Regis, was or had been pursuing a course of conduct which constituted an anti-competitive practice. The Competition Act 1980 defines an anti-competitive practice as a course of conduct which has, or is intended to have, or is likely to have the effect of restricting, distorting or preventing competition. The DGFT concluded that Southdown operated routes on an uneconomic basis with the intention of undermining the viability of the operations of a competitor. On 3 September 1992 the DGFT made a reference to the MMC under section 5 of the Competition Act 1980.

## **Operators' shares of registered bus miles**

2.15. At the time of its investigation the OFT was provided by WSCC with figures for the area of Arun District Council on the route mileage for each of the then three bus operators. The county council is a source of such data because it needs this information to apportion revenue under the concessionary fares scheme. On the basis of these figures Southdown was the dominant supplier with 66 per cent of the route mileage, as Table 2.2 shows.

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<sup>1</sup>An investigation under section 3 of the Competition Act 1980 by the DGFT: *Southdown Motor Services Ltd. The registration and operation of services 262 and 242 in Bognor Regis.* Office of Fair Trading, 15 July 1992.

TABLE 2.2 Proportion of route mileage for each bus operator in Arun district, for the year to April 1992

<i>Bus operator</i>	<i>Route mileage operated</i>	<i>Percentage of total mileage</i>
Southdown	269,051	66
Easy Rider	107,627	26
Blue Lake	31,200	8

Source: OFT report based on data from WSCC.

The data exclude two other services operated under contract, one to Sainsbury run by Hants & Sussex Motor Services and the other to Tesco operated by Sussex Bus Ltd (Sussex Bus), on the grounds that use of these services was free.

2.16. In its evidence to our inquiry Southdown disputed the accuracy of the bus mileage data supplied by WSCC, believing that the mileages for services 242 and 262 had been double counted. It also criticized the exclusion of other forms of transport such as rail and taxi. These other means of transport are considered in paragraphs 2.36 to 2.39.

2.17. Southdown submitted annual mileage data to us for each of its current routes in the Bognor Regis area. The total—470,796 miles per annum—includes service numbers 246, 247, 250 and 700 omitted from Table 2.2. The inclusion of the mileage on these routes would indicate that Table 2.2 understated Southdown's share of the local bus market.

2.18. A calculation of vehicle miles on commercial services was supplied to us by an officer of the Highways Department of WSCC for those bus routes west of Bognor Regis station and the High Street as at the end of October 1992. The Southdown share of the total bus mileage was 94 per cent. The only other competitor at this time was Blue Lake which has since withdrawn its one service. In the case of contract services (see paragraphs 2.32 to 2.35) Southdown now accounts for all current tendered services within the area of Arun District Council. Southdown is therefore in effect the only operator of bus services in Bognor Regis, except for occasional services into Bognor Regis from west of Chichester, school services, free services operated to and from two local supermarkets, and seasonal services to a local holiday complex.

### Southdown's local bus services

2.19. At the time of deregulation in October 1986 Southdown identified its commercial network as being half-hourly services along key corridors of the Bognor Regis area. The then Southdown West Sussex management were opposed to the use of minibuses and this acted as a major constraint on developing a wider network of services. Although Easy Rider charged lower fares when it entered the market in January 1987, Southdown told us that it had adopted a cautious 'wait-and-see' attitude to its rival on the services from North Bersted and Rose Green to Bognor Regis town centre. Not until May 1987 did it respond by retiming service 250 to arrive at North Bersted in front of Easy Rider service number 01.

2.20. Southdown made further changes to its frequencies and timings in March 1989 (see Table 2.5). However, it was not until Southdown was acquired by Stagecoach in August 1989 that the company dropped its reluctance to use minibuses. Thus in February 1990 the new Southdown management introduced rerouted minibus services from Bognor Regis town centre to North and South Bersted on a half-hourly basis—routes 244 and 245. A half-hourly frequency was also introduced on the number 260 service between Bognor Regis town centre and Pagham timed to run later than hitherto to be spaced further away from the Easy Rider service.

2.21. In July 1990, almost a year after the acquisition by Stagecoach, Southdown amended its route 260 to provide a quarter-hourly service between Rose Green and Bognor Regis, the additional services being renumbered as service 262. Southdown told us that this minibus service proved unreliable, given the company's commitment to an extension of a park-and-ride scheme in Chichester at the behest of the local authority. As a result the 262 service was withdrawn in December 1990.

2.22. When the Chichester park-and-ride scheme ended in March 1991, Southdown was able to redeploy the minibuses and staff to operate an improved network of services throughout the Bognor Regis area. Southdown started minibus service number 242 from North Bersted to Rose Green which provided, along with service number 260, a 15-minute frequency to Rose Green. At the same time the North Bersted service on routes 244 and 245 was enhanced to a quarter-hourly service. Together with a slightly rerouted number 242 service this meant that North Bersted was served by six buses per hour. The retimed 242 service covered the bulk of the route of the Easy Rider 01 and 02 services (see Appendix 2.2), running shortly ahead of both services (see Table 2.5). The result was that Rose Green was served by six buses per hour (four by Southdown and two by Easy Rider) and North Bersted by eight buses per hour (six by Southdown and two by Easy Rider).

2.23. On the withdrawal by Easy Rider of service 04 in January 1992 Southdown registered service 4 to link Rose Green and Pagham with Bognor Regis town centre. Easy Rider introduced a new service 04 to compete with Southdown's service number 260 to Chichester. This new service lasted for just over four months until May 1992 when the whole of Easy Rider's services ceased to operate as a result of the sale by Mr Hunter of the vehicles and goodwill to Southdown. When Easy Rider ceased to trade Southdown immediately operated replacements for the rival services 01, 02 and 04, before eliminating the duplication between the former Easy Rider services and its own bus frequencies in July 1992.

### **Easy Rider's local bus services**

2.24. Mr Hunter established the company to take advantage of the opportunities arising from the deregulation of the bus industry. Mr Hunter told us that he had identified the estates in Rose Green and North Bersted as areas which at that time were not served effectively by buses. Mr Hunter saw the potential in serving this market by using minibuses which could go into and through these estates, rather than pass them by as larger buses were obliged to do due to the narrow roads.

2.25. Easy Rider started operating from the residential estates in January 1987 running two services: the 01 ran from North Bersted to the town centre and the 02 from Rose Green to Bognor Regis. Fares and timetables for both these services remained largely unaltered until May 1992.

2.26. Mr Hunter told us that he needed very few passengers per trip to make these two services viable and that from the outset he had been anxious to avoid entering into conflict with Southdown wherever possible. He explained that, given that Southdown had withdrawn its previous two-hourly service covering the northern part of the North Bersted area (it later withdrew the service linking Rose Green, Nyetimber and Pagham), he had seen a gap in the market which would not involve direct competition with Southdown. However, the nature of the approaches to the town centre from both the north and west of Bognor Regis had meant that Easy Rider was unable to avoid overlap with the routes served by Southdown.

2.27. We calculate that about 70 per cent of Easy Rider's services overlapped with those of the existing Southdown services (see also the map of the routes at Appendix 2.1). Southdown said that, since Easy Rider's operations were entirely within 400 yards, and within 200 yards of Southdown's service 250, Easy Rider was not offering genuine new services in Bognor Regis.

2.28. Both Easy Rider's 01 and 02 services operated from Monday to Saturday with a half-hour frequency but there was no evening or Sunday service. In residential areas off the main roads each of the routes offered a hail-and-ride service whereby passengers were able to signal to the driver and the bus would stop anywhere along the route providing it was safe to do so.

2.29. In January 1988 Easy Rider introduced a third service, the 03, from Bognor Regis to Stroud Green in the north-west of the area, but this did not prove to be successful. It was withdrawn in August 1989. In November 1988 Easy Rider began to operate a minibus service from Bognor Regis to Pagham and in

January 1992 this was varied and extended to Chichester. This service continued until Easy Rider ceased to trade in May 1992. Table 2.3 summarizes the development of commercial bus services operated by Easy Rider in Bognor Regis.

TABLE 2.3 **Easy Rider's commercial bus services in Bognor Regis—a chronology**

26 January 1987	Easy Rider started two services, 01 from North Bersted to the town centre and 02 from Rose Green to the town centre
25 January 1988–25 August 1989	Service 03 operated between Bognor Regis and West Meads
28 November 1988	Service 04 started and operated between Bognor Regis and Pagham
25 July 1990	Southdown started service 262 from Rose Green to the town centre, using one minibus
2 December 1990	Service 262 was withdrawn
17 March 1991	Southdown started service 242 from North Bersted to Rose Green via the town centre using two minibuses
5 January 1992	Service 04 rerouted and extended to Chichester
16 May 1992	Easy Rider ceased operating bus services in Bognor Regis
17 May 1992	Southdown started operating services to similar timetables to those of former Easy Rider services

Source: Easy Rider.

## Timing of services

2.30. The Easy Rider 01 service to North Bersted began in January 1987 on a schedule of services timed to depart from Bognor Regis town centre eight minutes behind the then Southdown service and from North Bersted ahead of Southdown service 250. The 02 service to Rose Green was due to run four minutes ahead of the existing Southdown service. Table 2.4 shows the timing and frequency of Easy Rider's services.

TABLE 2.4 **Easy Rider's commercial bus services in Bognor Regis**

<i>Route</i>	<i>Time of first bus*</i>	<i>Time of last bus*</i>	<i>Frequency of service†</i>	<i>Timing of services‡</i>
01 North Bersted–Bognor	8.15	17.45	2	15,45
02 Rose Green–Bognor	8.15	17.45	2	15,45
03 Stroud Green–Bognor	8.18	17.48	2	18,48
04 Pagham Beach§–Bognor	8.25¶	17.25¶	1	25¶

Source: Easy Rider.

\*Time of first and last bus from Bognor High Street on weekdays.

†Buses per hour on weekdays.

‡Minutes past the hour from Bognor High Street.

§Route extended to Church Farm in April 1990 and rerouted and extended to Chichester in January 1992.

¶Timetable amended January 1992: first bus 8.23; last bus 17.39; timing 25 minutes past the hour throughout most of the day.

2.31. As stated in paragraph 2.21, Southdown made changes to the timings of its services in July 1990. These meant that its newly-introduced minibus service number 262 was due to run three minutes ahead of the Easy Rider 02 service. In March 1991 Southdown revised its Bognor Regis area services which resulted in the number 242, 244, 245 and 260 services being timed to operate between one minute and five minutes ahead of those scheduled by Easy Rider. Table 2.5 summarizes the timings of Southdown and Easy Rider's services during the daytime on weekdays.



TABLE 2.5 Timings of Easy Rider (ER) and Southdown (S) services: minutes past the hour, weekday, daytime

	Bognor– N Bersted		N Bersted (ER: Rowan Way S: Oak Grove) –Bognor		Bognor– Rose Green		Rose Green (ER: Gossamer Lane East S: Gossamer Lane West) –Bognor	
Easy Rider (01/02) (same times throughout)	15	45	25	55	15	45	05	35
Southdown 24/1/87	07	37(240/1) <i>ER 8 mins behind</i>	20	50(240/1) <i>ER 5 mins behind</i>	23	53(245/260) <i>ER 8 mins ahead</i>	09	34(245/260) <i>ER 4 mins ahead</i>
24/7/88	10	43(244/5) <i>ER 5 mins behind</i>	23	53(244/5) <i>ER 2 mins behind</i>	38	53(244/260) <i>ER 23-8 mins ahead</i>	58	34(244/260) <i>ER 7-1 mins behind</i>
March 1989	07	37(244/5) <i>ER 8 mins behind</i>	19	49(244/5) <i>ER 6 mins behind</i>	33	53(244/260) <i>ER 18-8 mins ahead</i>	54	34(244/260) <i>ER 11-1 mins behind</i>
Feb 1990	07	37(244/5)	19	49(244/5)	00	30(260) <i>Evenly spaced services</i>	13	43(260) <i>ER 8 mins ahead</i>
July 1990	07	37(244/5)	19	49(244/5)	00	30(260) 12 42(262) <i>New 262: 3 mins ahead of ER</i>	13	43(260) 28 58(262) <i>262: 7 mins ahead* of ER</i>
Dec 1990	07	37(244/5)	19	49(244/5)	00	30(260)	13	43(260)
March 1991	12	42(242)	24†	54†(242)	00	30(260)	01	31(242)‡
	20	50	32	02	10	40(242)	13	43(260)
	35	05(244/5) <i>New 242: 3 mins ahead of ER. Increased frequency 244/5</i>	47	17(244/5) <i>New 242: 1 min ahead of ER. In- creased frequency 244/5</i>		<i>New 242: 5 mins ahead of ER</i>		<i>242: 4 mins ahead of ER</i>
Jan 1992	12	42(242)	24†	54†(242)	00	30(260)	01	31(242)‡
	20	50	32	02	10	40(242)	13	43(260)
	30	05(244/5) <i>242: 3 mins ahead of ER</i>	47	17(244/5) <i>242: 1 min ahead of ER of ER</i>		<i>242: 5 mins ahead of ER</i>		<i>242: 4 mins ahead</i>

Source: MMC study from information provided by Southdown and Easy Rider.

\*3 minutes ahead at Gloucester Drive.

†Rowan Way, same route as Easy Rider.

‡Based on 4 minutes earlier departure time at Gloucester Drive; Gossamer Lane time not given.

Note: Easy Rider 04 and Southdown 4 routes not included in above analysis. The Easy Rider 04 route, introduced in November 1988, left Bognor at 25 minutes past the hour, returning from Pagham Beach at 02. It initially served different routes from Southdown's, but the route was changed to run over the 260 route, extended to Chichester, from Jan 1992, 5 mins ahead of the 260 service to Pagham (but more evenly spaced between the through 260 services to/from Chichester). Southdown introduced its own 4 service at this time, over the former Easy Rider 04 route. Southdown's 4 left Bognor Regis High Street at 24 minutes past the hour—1 minute before the Easy Rider 04, but now on a slightly different route to Pagham—and returned from Pagham 7 minutes before Easy Rider 04, but again via a different route.

## Local authority tendered services

2.32. Tendered services are services subsidized by the local authority where no commercial service is registered. The responsibility for tendering for services in Bognor Regis lies with WSCC. Currently all tendered services in Bognor Regis are operated by Southdown. All contracts for WSCC's tendered services are now awarded for three years. The contracts are awarded on a net cost (or minimum subsidy) basis. Under such contracts the operator retains the revenue from the bus service and is paid the tender sum which is calculated as the difference between estimated revenue and cost. Net cost contracts mean that the operator rather than the local authority bears the revenue risk. For each tendered service WSCC specifies the service to be operated, including the route, frequency and timetable. WSCC does not specify the level of fares to be charged. The performance of tendered services is monitored by WSCC.

2.33. Easy Rider had operated two subsidized services, number 390 from Elmer to Bognor Regis (one journey on Saturdays only) and number 375 from Pagham to Bognor Regis (on Sundays and public holidays), but Southdown had won the contracts when they came up for renewal in February 1988. As stated in paragraph 2.12, until October 1992 Blue Lake operated one service in Bognor Regis under contract to WSCC. It withdrew its number 243 service to West Meads in December 1992 following the decision by Southdown to register a commercial service on this route as from 28 October 1992.

2.34. The contracts held by Southdown are for early morning and evening services in the urban areas of Arun District Council.

2.35. An officer of the Highways Department of WSCC told us that a large operator like Southdown has an advantage in securing contracted services through the ability to submit bulk tenders covering a variety of bus routes.

### *Competition from other forms of transport*

2.36. Bus services in Bognor Regis face a degree of competition from other forms of transport: private car, taxi, train, and, for shorter distances, cycling and walking. Car ownership levels in the town are slightly higher than the national average but lower than in the rest of West Sussex (see Table 2.6).

TABLE 2.6 Car ownership

	Percentage of households with:		
	No car	1 car	2 or more cars
Bognor Regis	26.8	47.6	25.6
West Sussex	23.7	45.9	30.5
Great Britain	33.4	43.5	23.1

Source: 1991 Census.

2.37. Southdown pointed out that since deregulation in 1986 bus operators had experienced a decline in demand for bus services. Increased car ownership was seen as the main factor accounting for this contraction in the bus market. Competition from cars was only partly offset by the effect of town centre car parking regulation in discouraging car use.

2.38. A rail service connects Bognor Regis with London, Brighton and Portsmouth. Some London services run via Arundel and Horsham, the remainder via Worthing and Hove.

2.39. Southdown told us that bus operators in Bognor Regis faced keen competition from taxis. It pointed out that the Arun taxi fleet included 115 vehicles based in Bognor Regis. Southdown said that two passengers could save money by sharing a taxi for the short distance to the residential areas out of the town centre rather than each paying a bus fare.

### **Quality of bus services**

2.40. Southdown told us that it believed public transport services should meet high quality and safety standards and provide a well co-ordinated network. It regarded Easy Rider as being a low-cost, low-quality operator. Southdown was of the opinion that Easy Rider operated old buses which were not easy for elderly passengers to use and were cramped, and that it did not maintain a high standard of running to schedule.

2.41. Mr Hunter saw his hail-and-ride service as meeting the needs of those in the residential estates outside Bognor Regis. Elderly people were offered a regular service to the town, and those unable to walk long distances could be collected and returned by a minibus very close to their home. Those who patronized Easy Rider's services praised the courtesy of the drivers in assisting passengers to join and alight from buses, and helping with loading and unloading of shopping bags and other luggage. An officer of the Highways Department of WSCC said he understood that after a good start the quality and efficiency of Easy Rider's services had deteriorated.

2.42. The drivers of Easy Rider's minibuses were not physically separated from the passengers in a distinct compartment as is the case with larger buses. As a result the drivers could become well known to regular users of Easy Rider, and passengers could rely on being collected and returned from outside their home. Mr Hunter told us that he employed ex-coach drivers rather than bus drivers since coach drivers had a reputation for courtesy. This, he said, was reflected in the tips that coach drivers invariably received from passengers appreciative of efforts to oblige them when making journeys by coach.

## Information provision and marketing

2.43. Easy Rider told us that it published free timetables for each of its local bus services in Bognor Regis. It told us that these timetables were displayed on the main bus stands in Bognor Regis town centre and at the local Tourist Information Centre and were published in local newspapers. Timetables were also readily available to passengers along Easy Rider's routes from its own bus drivers. Easy Rider told us that it would not have been cost-effective to put up timetables at bus stops along its routes since the bulk of its passengers boarded buses on those parts of the routes that operated as a hail-and-ride service. Southdown told us that, unlike Easy Rider, it provided route numbers on all bus stops, timetable information on all main bus stops in the town centre and elsewhere on each route, and widely available free timetable booklets.

## Southdown's fares

2.44. Around 80 per cent of Southdown's revenue from local bus services in Bognor Regis is derived from cash fares,<sup>1</sup> ie single or return tickets (see Table 2.7); prepaid tickets account for the remaining 20 per cent. The range of prepaid tickets available on Southdown's services in Bognor Regis is shown in Table 2.8.

TABLE 2.7 Southdown's revenue from local bus services in Bognor Regis by ticket type\*

	£'000	%
Cash fares	1,009.1	82
Prepaid tickets:		
Scholars	157.4	13
General and local tickets	3.7	†
Concessionary	<u>55.4</u>	<u>5</u>
Total	1,225.6	100

Source: Southdown.

\*Excludes revenue from local authorities for tendered services. (Based on figures for Chichester depot for 1991/92.)  
 †Less than 0.5 per cent.

TABLE 2.8 Prepaid tickets available on Southdown's services in Bognor Regis

Explorer ticket	One day's unlimited travel ticket issued by Southdown and Coastline and accepted by ten other operators in the region. Adult Explorer, £4.40 (reductions for children, OAPs and families).
Senior Traveller ticket	Available to senior citizens and the disabled for six or twelve months permitting half-price fares except before 09.00 on weekdays.
Season ticket	Available to children under 16 years for travel to and from school during school terms. Available to adults at all times on all days.

Source: Southdown.

2.45. Arun District Council participates in the West Sussex Bus Pass scheme. A pass, available for either six months or one year, enables holders to travel on all services at half fare at all times other than before

<sup>1</sup>We distinguish between cash fares (including both single and return) and prepaid tickets. Prepaid tickets are tickets whereby the cost of travel is paid either fully or in part in advance. Prepaid tickets, therefore, include point-to-point season tickets, travelcards giving free travel and travelcards or concessionary passes offering half-price travel.

09.00 on weekdays. The scheme is available to the same passengers as the Southdown Senior Traveller ticket and permits travel on all services in West Sussex and to points outside the county providing the journey commences in West Sussex.

## Changes in fares

2.46. Southdown provided us with details of changes in fares since October 1986 for its services operated in Bognor Regis. The level of fares charged by Southdown compared with that of Easy Rider shows no consistent picture of one operator charging more than the other. There were periods when Easy Rider fares were undercut by Southdown and some Southdown return fares were below those of Easy Rider (see Table 2.9). As a generalization, however, single fares charged by Southdown were slightly above those charged by Easy Rider.

2.47. Southdown's fares on its services in Bognor Regis appear to have been influenced by the competition from Easy Rider. Southdown told us of a number of occasions when it had reduced fares or trimmed fares increases because of the presence of Easy Rider. For example, it made reductions to fares between North and South Bersted to Bognor Regis in the summer of 1988 in response to a cut in fares by Easy Rider. Southdown said that in the following year it had encountered customer resistance following a fares increase in March 1989. Having raised fares on all routes into Bognor Regis by about 5 per cent in June 1989, Southdown felt obliged within six months to rescind this fares increase on the routes served by Easy Rider's 01 and 02 services. At the same time Southdown reduced its fares on its service number 260 from Pagham to Bognor Regis given the competition from Easy Rider's recently-introduced 04 service.

2.48. Southdown announced fares increases of 6 per cent in June 1990 but these did not apply on the number 260 service where Easy Rider continued to offer competition. In October 1990 Southdown increased its fares by between 10 and 12 per cent on all routes except those serving North and South Bersted because it felt that this would lose it custom to Easy Rider. Southdown stated that it was concerned about the revenue generated on its Aldwick-Rose Green-Pagham service given the presence of Easy Rider. In March 1991 it felt unable to sustain the fares levels arising from the October 1990 increase on this route and thus again cancelled that fare adjustment.

2.49. In September 1991 Southdown raised its fares by 8 per cent except on the corridors into Bognor Regis where Easy Rider operated.

2.50. Following the withdrawal of Easy Rider from the market in May 1992 Southdown announced a general fares increase designed to achieve an overall increase of 4 per cent in fare level throughout rural areas of West Sussex. Fares on some of the routes in Bognor Regis on which Easy Rider had competed were increased in June 1992 by 5p (representing an increase of up to 25 per cent on the shortest distances). There were no increases on those local services in Bognor Regis where Easy Rider had not previously competed: fare levels to the east of Bognor Regis, for example, were unchanged.

2.51. Table 2.9 shows that representative fares on some routes in Bognor Regis have risen by up to 60 per cent over the last five years. On those routes where Easy Rider operated, fares increased by much less.

TABLE 2.9 Changes in Southdown single fares in Bognor Regis area (single fares from Bognor Regis High Street)

	Routes not operated by Easy Rider					Routes operated by Easy Rider					pence
	250 Royal Oak	260 Chichester	245/250 Felpham School	East of Bognor South Downs Hotel	Sea Lane	North of Bognor:*	260/242/262 West of Bognor				
Approx journey time	10m	40m	6m	10m	13m	8m	Aldwick X Roads	Gossamer Lane	Carlton Avenue	Church Way†	
26/10/86	40	125	30	47	N/A	40	47	57	62	67	
20/9/87	45	130	35	50	65	45 [N/A]	50 [N/A]	60 [N/A]	65 [N/A]	70	
31/1/88	48	138	37	53	69	48 [40]	53 [40]	64 [60]	69 [60]	74	
30/6/88	48	138	37	57	69	37 [40]	53 [40]	64 [60]	69 [60]	74	
26/3/89	48	152	40	60	74	40 [40]	57 [40]	63 [60]	74 [60]	80 [70]	
11/6/89	51	161	42	60	78	42 [40]	60 [40]	67 [60]	78 [60]	85 [70]	
24/7/89	50	160	42	60	78	37 [40]	60 [40]	67 [60]	67 [60]	78 [70]	
25/2/90	50	160	42	64	78	37 [40]	60 [40]	67 [60]	67 [60]	78 [70]‡	
27/6/90	55	175	45	72	85	40 [40]	65 [45]	70 [60]	70 [65]	85 [75]	
14/10/90	62	196	51	70	96	40 [40]	73 [45]	79 [60]	79 [65]	96 [75]	
17/2/91	60	195	50	70	95	40 [40]	70 [50]	75 [70]	75 [70]	95 [75]	
18/3/91	60	180	50	70	95	40 [40]	50 [50]	70 [70]	70 [70]	90 [75]	
28/7/91	60	180	50	70	95	40 [40]	50 [50]	70 [70]	70 [70]	90 [75]	
29/9/91	65	195	55	75	105	40 [40]	50 [50]	70 [70]	70 [70]	90 [75]	
5/1/92	65	195§	55	75	105	40 [40]	50 [50]	70 [70]	70 [70]	90 [75]	
19/4/92	65	195§	55	75	105	40 [40]	50 [50]	70 [70]	70 [70]	90 [75]	
28/6/92	65	210	55	75	105	45	55	70	70	90	
20/9/87– 19/4/92											per cent
% increase	+44	+50	+57	+50	+62	-11	0	+17	+8	+29	

Source: MMC study from information supplied by Southdown.

\*Various routes, eg 241/242/244/245/250. Royal Oak (column 1) is just beyond Central Avenue, to the North of Bognor.

†Easy Rider services via Church Way introduced in November 1988, to other destinations in January 1987.

‡Easy Rider reduced fares by 5p on 1 April 1990 until 14 October 1990.

§Easy Rider introduced a Chichester service from 6/1/92, with £1 single fare.

Notes:

1. RPI increased by 35 per cent from September 1987 to April 1992.

2. Table shows single fares only. A maximum return fare was also introduced on services to west of Bognor only in 1990. Between Bognor and Pagham, for example, return fares were reduced between 1987 and 1992.

3. Easy Rider fares where available in square brackets.

2.52. Southdown confirmed that with the withdrawal of Easy Rider it would aim to reduce some of the fare differentials that had emerged. It acknowledged that fares increases might stimulate a further loss of passengers to other forms of transport.

## Barriers to entry

2.53. Against this background we have considered the character of competition in the market for local bus services and in particular barriers to entry facing potential entrants to such markets. Southdown told us that it did not believe there were any significant barriers to entry into the market for local bus services either in general or in Bognor Regis in particular. It saw this belief demonstrated by the entry of Easy Rider where a new operator had acquired two 16-seat vehicles easily and had been able to run services to challenge existing operators.

2.54. Southdown did not consider that the 42 days' notice period required by prospective operators to register a new service constituted a barrier to entry. It did not feel that an incumbent operator had an undue advantage in being given advance notice of any need to plan a response to a new rival.

2.55. In Southdown's view the entry of Easy Rider also showed that access to an existing bus station was not necessary for a new entrant to become established: there was no bus station in Bognor Regis. Neither in its view was the need for depot and maintenance facilities a pressing problem.

2.56. Easy Rider confirmed to us that it provided very little roadside information about its services. On the residential estates of Rose Green and North Bersted Easy Rider became known as the minibus operator which could be hailed to stop outside one's home and therefore it was not necessary to walk any distance to a bus stop to use its service.

2.57. The existence of prepaid tickets, multi-ride tickets and local authority concessionary fare schemes could provide a barrier to entry for a potential bus operator depending on the travel patterns of local bus passengers. Easy Rider had, however, faced no such problems in Bognor Regis.

2.58. As we have observed in previous reports, the perceived financial strength of an incumbent and its willingness to fight to protect its market can be expected to have an effect on entry into a market. In particular, if an incumbent is believed to have the ability and willingness to withstand losses following a prospective entrant's appearance in a market then new entry may be deterred. Southdown did, however, point to entry elsewhere in its operating area as evidence that, in its view, entry could, nevertheless, still occur.

# 3 The companies

## Southdown

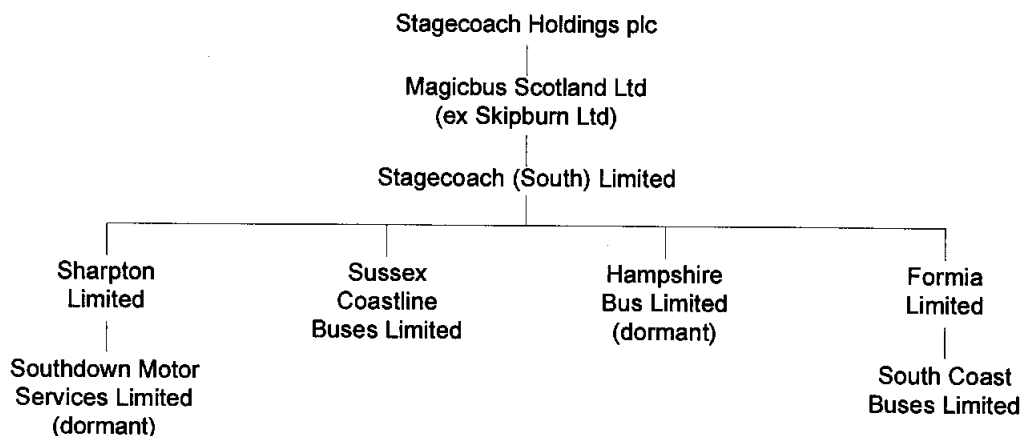
3.1. Southdown was established in 1915, running buses in the Brighton, Worthing and Bognor Regis areas. Operations were subsequently extended eastward as far as Eastbourne and westward to the Portsmouth area. In 1968 Southdown became part of the NBC, a public sector body formed under the provisions of the 1968 Transport Act. Southdown was then merged with a neighbouring bus company, Brighton & Hove & District Buses.

3.2. The 1985 Act provided for the splitting up and privatization of the NBC and in January 1987 Southdown was split up in order to promote competition. The engineering services (all component and mechanical overhauls, bodywork and repairs and stores procurement) were hived off into a separate company, as were the bus operations in Brighton and Hove. This left some 50 per cent of its former activities to be carried on by Southdown. As part of the privatization of the NBC, Southdown was sold in October 1987 to four of its managers who formed a company called Sharpton Limited (Sharpton) to undertake a management buy-out. In August 1989 Stagecoach (Holdings) Limited, now Stagecoach Holdings plc, acquired Sharpton and thus Southdown. Stagecoach is the second largest private operator of bus services in the UK, with, in the year ended 30 April 1992, a turnover of £140.7 million (1990/91, £103.4 million) and operating profit before interest and tax of £15.2 million (1990/91, £10.2 million).

3.3. On 30 April 1991, as part of a group reconstruction, the trade, assets and liabilities of Southdown were transferred to another subsidiary of Stagecoach, Stagecoach (South) Limited (Stagecoach (South)). Southdown's business is now operated by a subsidiary of Stagecoach (South), Sussex Coastline, and its Eastbourne operation was transferred to South Coast Buses Limited (South Coast Buses) at the end of April 1992: it is, however, referred to as Southdown throughout this report. The group structure of Stagecoach relevant to Southdown from 1 May 1992 is shown in Figure 3.1. The name of Southdown Motor Services Limited has been passed to another non-trading company (formerly Southdown Buses, which was formerly Portsmouth CityBus Limited).

FIGURE 3.1

### Stagecoach Holdings plc: group structure relevant to Southdown at 1 May 1992



Source: Southdown.

## Financial information on Southdown

3.4. Southdown's turnover, operating profit/(loss), profit/(loss) after interest and tax and return on turnover are summarized in Table 3.1. Detailed profit and loss accounts of Southdown are shown in Appendix 3.1. Southdown stated that the fall in turnover in 1990/91 was principally the result of the divestment of its Portsmouth operations, although there had been some rationalization of loss-making routes. Southdown's operating result changed from a loss of £281,000 in 1989/90 to a profit of £697,000 in 1990/91; Southdown stated that these results were not comparable because of the treatment of the Portsmouth results, but there had been an improvement of approximately £500,000 due to the cost rationalization that had started in August 1989 and continued to date. The 1992/93 budget figure of £782,000 is for Southdown's successor company, Sussex Coastline, and the Eastbourne operation which was previously part of Southdown but was transferred to South Coast Buses at the end of April 1992.

TABLE 3.1 Southdown: turnover, operating profit/(loss) before and after interest and taxation and before extraordinary items for the five years ended 25 April 1988 to 30 April 1992 and budget for the year to 30 April 1993

Years ended 25 April 1988 and 1989 and 30 April thereafter	£'000					
	Southdown				Sussex Coastline	Coastline & Eastbourne
	1988	1989	1990	1991	1992	1993 budget
Turnover	13,138	12,102	12,565	8,050	9,733	10,310
Operating profit/(loss) on ordinary activities before interest, taxation and extraordinary items	526	(969)	(281)	697	482	782
Profit/(loss) on ordinary activities after interest and taxation but before extraordinary items	434	(731)	(332)	491	410	*
						<i>per cent</i>
Return on turnover (operating profit/(loss) as a percentage of turnover)	4.0	(8.0)	(2.2)	8.7	5.0	7.6

Source: Southdown.

\*Stagecoach (South) stated that it did not budget for profit after all group interest and group tax.

3.5. Southdown estimated that its approximate turnover from local services for the calendar year ending 31 December 1992 (as distinct from its financial year) was £10,100,000 of which approximately £1,060,000 was accounted for by services operated wholly or mainly in the Bognor Regis area.

3.6. Southdown's capital employed consists primarily of PSVs. It is financed by shareholders' equity and by borrowings. The balance sheets of Southdown for the five years to 30 April 1992 are shown in Appendix 3.2. This shows that gearing (borrowings net of cash as a percentage of net equity) was 3.5 per cent at 30 April 1992. Southdown's return on average capital employed was negative in the years to 30 April 1989 and 1990 due to the operating losses made in those years, but Southdown returned to profitability, with positive returns on capital in 1990/91 and 1991/92. Southdown's capital employed and return on average capital employed are shown in Table 3.2. (Note: Stagecoach (South) said that it considered capital employed was more accurately reflected in a restated balance sheet which it had prepared and which is referred to further in paragraph 3.7.)



TABLE 3.2 Southdown: capital employed and return on average capital employed for the five years ended 25 April 1988 to 30 April 1992

Years ended 25 April 1988 and 1989 and 30 April thereafter	Southdown				Sussex Coastline
					£'000
	1988	1989	1990	1991	1992
Capital employed	5,658	5,641	2,577	2,386	1,927
Average capital employed	6,533	5,650	4,109	2,482	2,157
Operating profit/(loss)	526	(969)	(281)	697	482
					<i>per cent</i>
Return on average capital employed (operating profit/(loss) as a percentage of average capital employed)	8.1	(17.2)	(6.8)	28.1	22.3

Source: Southdown.

3.7. Stagecoach (South) prepared its own statement of capital employed and return on capital for Southdown, which differs from that shown in Appendix 3.2 and Table 3.2. Stagecoach (South) stated that the balance sheet of Southdown, based on statutory accounts, did not reflect the land and buildings it had used, and that the restated balance sheet included additional amounts for land and buildings. Stagecoach (South) also excluded inter-company debtors and creditors from the restated balance sheet of Southdown, which is shown in Appendix 3.3. Capital employed based on the restated balance sheet and return on capital are also shown in Appendix 3.3 and are summarized in Table 3.3. Stagecoach (South) considered that the restated capital employed more accurately reflected the true position. Table 3.3 shows a much lower, though still positive, return on capital, at 6.0 per cent for 1990/91 and 5.2 per cent for 1991/92, than in Table 3.2. However, the trend shown in return on capital over the years from 1987/88 to 1991/92 is similar, being a positive return in 1987/88 followed by negative returns in 1988/89 and 1989/90 and thereafter positive returns to 1991/92.

TABLE 3.3 Southdown: capital employed and return on average capital employed for the five years ended 25 April 1988 to 30 April 1992 based on Southdown balance sheet restated by Stagecoach (South)

Years ended 25 April 1988 and 1989 and 30 April thereafter	Southdown				Sussex Coastline
					£'000
	1988	1989	1990	1991	1992
Capital employed	6,101	6,321	14,047	9,263	9,200
Average capital employed	6,754	6,211	10,184	11,655	9,232
Operating profit/(loss)	526	(969)	(281)	697	482
					<i>per cent</i>
Return on average capital employed over the year (operating profit/(loss) as a percentage of average capital employed)	7.8	(15.6)	(2.8)	6.0	5.2

Source: Southdown.

### Financial information on route 242

3.8. Route 242 was introduced into Southdown's Bognor Regis town network on 17 March 1991. Southdown was unable to provide a detailed breakdown of route costs prior to late May 1991 because it did not until then have in place a system of route costing, and costs could not be disaggregated below depot level. However, route costings are available from 26 May 1991, prepared by Southdown for operational costing periods of or about four weeks each, with 13 costing periods in the year. The first full year for which these costings were kept was therefore the year to end May 1992. The year

to end May 1992 was also that in which Southdown's route 242 was in competition with Easy Rider's routes 01 and 02. Easy Rider ceased operating bus services in Bognor Regis on 16 May 1992.

3.9. Tables 3.4, 3.5 and 3.6 summarize route costings and show revenue, direct costs, the variable element of direct costs, contribution, overhead and profit or loss. These terms are defined in paragraph 3.10. Results from operating route 242 for the year to end May 1992 are summarized in Table 3.4. Costing periods subsequent to May 1992 are summarized in Table 3.5. Southdown's own costings show the cost components of direct cost but do not categorize these between 'variable' and 'semi-variable'. However, the variable element, as we have defined it, is shown in Tables 3.4 and 3.5 to show whether revenue has been sufficient to cover the variable costs of operating route 242.

3.10. Definitions of the headings used in Tables 3.4 and 3.5 and elsewhere in this chapter are set out below:

- *Revenue*: direct revenue and allocated revenue.
- *Variable costs*: drivers' wages, fuel and tyres.
- *Semi-variable costs*: engineering staff and materials, including maintenance; other operating costs and depreciation.
- *Direct costs*: variable plus semi-variable costs.
- *Contribution*: revenue minus direct costs.
- *Overhead*: depot overheads plus company overheads.
- *Profit/(loss)*: contribution minus overheads.

3.11. For the 52 weeks to 30 May 1992, the route costings summarized in Table 3.4 show that, for route 242, revenue at £30,079 was insufficient to cover the variable costs at £49,093 of operating buses on the route. Shortfall from variable costs was £19,014 (38.7 per cent of variable costs). A negative contribution was made and the operating loss for the year to end May 1992 was £62,718. The loss was more than double revenue for the year at 209 per cent of revenue.

3.12. The figures for 1991/92 are broken down in Table 3.4 into four groups of three costing periods each, plus the thirteenth costing period. Although revenue increased and loss as a percentage of revenue reduced over costing periods to 30 April 1992, loss was still 183 per cent of turnover over the three costing periods to 30 April 1992. In the last costing period of the year, to end May 1992, revenue still fell short of variable costs, though loss as a percentage of revenue was at its lowest for the year at 127 per cent.

TABLE 3.4 Southdown: service on route 242: revenue, costs, contribution and profit/(loss) for the year to end May 1992 subdivided into four groups of three costing periods (CPs) to 30 April 1992 and the CP to end May 1992

	CPs						£
	3 CPs to 17.8.91	3 CPs to 9.11.91	3 CPs to 1.2.92	3 CPs to 30.4.92	1 CP to 30.5.92	13 CPs to 30.5.92	
Revenue	5,336	6,455	7,034	7,947	3,307	30,079	
Direct costs	19,642	19,965	19,377	20,157	6,823	85,964	
of which variable	11,504	11,393	10,754	11,576	3,866	49,093	
Contribution	(14,306)	(13,510)	(12,343)	(12,210)	(3,516)	(55,885)	
Overhead	1,140	1,116	1,579	2,326	672	6,833	
Profit/(loss)	(15,446)	(14,626)	(13,921)	(14,537)	(4,188)	(62,718)	
Profit/(loss) as a percentage of revenue	(289)	(227)	(198)	(183)	(127)	(209)	

Source: Southdown.

3.13. Details of Southdown's revenue, costs and loss from operating the route 242 service separately for each of the 13 costing periods to end May 1992 are shown in Appendix 3.4. In every period, revenue fell short of variable costs, contribution was negative and loss exceeded revenue.

3.14. For periods subsequent to May 1992, revenue, costs and profit/(loss) from operating route 242 are shown in Table 3.5, with the year to May 1992 for comparison. Table 3.5 shows that Southdown's results from operating route 242 improved after May 1992. In particular:

- (a) Revenue has increased in subsequent costing periods over the average to end May. Revenue in the three costing periods to 22 August 1992 was some £15,400, an increase of some 190 per cent over revenue for the equivalent three costing periods in the previous year, to 17 August 1991, shown in Table 3.4, of some £5,300.
- (b) Revenue in the 13 costing periods to end May 1992 did not cover the variable costs of route 242, whereas in each of the costing periods since the end of May, shown in Table 3.5, revenue covered variable costs on the route. Revenue has, however, continued to fall short of direct costs since the end of May 1992.
- (c) Losses incurred in the operation of the route in each costing period since May 1992, shown in Table 3.5, are less than the average for the year to end May 1992.

### ***Financial information on route 262***

3.15. Southdown said that its route 262 service was introduced in July 1990 to use vehicles and drivers that were expected to be displaced from the park-and-ride service in Chichester, which was due to finish in October 1990, and to fill gaps in its existing service. However, before the park-and-ride scheme was due to finish, it was extended until March 1991 and Southdown withdrew its 262 service. As noted in paragraph 3.8, Southdown did not have detailed route costings available before the end of May 1991. Southdown did, however, provide details of the revenue and costs from operating route 262 for the four-week period ending 1 December 1990, which it specially calculated for the OFT. These are summarized in Table 3.6 and show that, although the 262 service covered its variable costs in the period, it was loss-making and made no contribution to overheads.

TABLE 3.5 Southdown: service on route 242: revenue, costs, contribution and profit/(loss) for the year to end May 1992 and for subsequent costing periods (CPs) for which figures are available to 9 January 1993

	Year to end May 1992	Average per CP, year to May 1992	CP					£'000
			27.6.92	25.7.92	22.8.92	19.9.92*	17.10.92	
Revenue	30.1	2.3	4.4	5.0	6.0	5.6	5.7	5.0
Direct costs	86.0	6.6	6.1	6.2	6.6	6.9	7.1	6.6
of which variable	49.1	3.8	3.5	3.4	3.7	3.7	3.9	3.8
Contribution	(55.9)	(4.3)	(1.7)	(1.2)	(0.6)	(1.3)	(1.4)	(1.6)
Overhead	6.8	0.5	0.8	0.9	1.0	1.5	1.0	1.0
Profit/(loss)	(62.7)	(4.8)	(2.5)	(2.1)	(1.6)	(2.8)	(2.4)	(2.6)
Profit/(loss) as a percentage of revenue	(209)	(209)	(57)	(43)	(27)	(50)	(43)	(52)
								per cent

Source: Southdown.

\*Southdown stated that route costings figures were not produced for periods 5, to 19.9.92, and 8, to 12.12.92.

Note: Percentages have been calculated on unrounded figures.

TABLE 3.6 Southdown: service on route 262: revenue, costs, contribution and loss for the four-week period ended 1 December 1990

	£'000
Revenue	1.6
Direct costs	2.1
of which variable	1.5
Contribution	(0.5)
Overhead	0.2
Profit/(loss) for the four-week period	(0.7)

Source: Southdown.

### *Financial information on all Southdown's routes in the Chichester area*

3.16. Appendix 3.4 also summarizes route costings for a number of other routes in the Chichester area and for the Chichester area in total. This shows revenue, costs and profit/(loss) over the period from June 1991 to August 1992. Appendix 3.4 shows that, for the Chichester area in total, Southdown's services made an operating loss of some £58,600 (3.6 per cent of revenue) in the 13 costing periods to the end of May 1992; but operating profits which totalled some £52,400 (12 per cent of revenue) over the three costing periods from June to August 1992. In the 13 costing periods to the end of May 1992, for the Chichester area in total, Southdown's operating loss of £58,600 was on revenue of £1,650,500; on route 242, Southdown's operating loss of £62,700 was on revenue of £30,100.

3.17. Table 3.7 summarizes the revenue and operating profits of the Chichester depot for the years to 30 April 1991 and 1992, for the year to end May 1992, for the three costing periods to 22 August 1992 and for the eight costing periods to 12 December 1992. This shows that the profitability of the Chichester area services in total changed from a profit in the year to 30 April 1991 to a loss in the years to 30 April 1992 and end May 1992, and a profit after May 1992. Operating profit was 11 per cent of revenue in the eight costing periods to 12 December 1992.

TABLE 3.7 Southdown: Chichester depot: revenue, operating profit/(loss) and operating profit/(loss) as a percentage of revenue for the years to 30 April 1991 and 1992, the year to end May 1992, the three costing periods to 22 August 1992 and the eight costing periods to 12 December 1992

	£'000				
	Year to 30.4.1991	Year to 30.4.1992	Year to 31.5.1992	3 costing periods to 22.8.1992	8 costing periods to 12.12.1992
Revenue	1,582	1,611	1,651	441	1,188
Operating profit/(loss)	36	(81)	(59)	52	131
Operating profit/(loss) as a percentage of revenue	2.2	(5.0)	(3.6)	11.9	11.0

Source: Southdown.

Note: Percentages have been calculated on unrounded figures.

## Easy Rider

3.18. Easy Rider Minicoaches was the trading name of Strikeline, incorporated in November 1985 and owned by Mr I Hunter, the operator of Easy Rider.

3.19. Tables 3.8 to 3.10 summarize the accounts of Strikeline, trading as Easy Rider, for periods to 31 March 1992. Profit and loss are summarized in Table 3.8. These show that, from 1987/88, Easy Rider's turnover increased yearly from £71,900 in 1987/88 and reached a peak in 1989/90 of £91,200. In 1990/91 Easy Rider's turnover fell by £12,800 (14.1 per cent) to £78,400, and in 1991/92 by a further £8,200 (10.4 per cent) to £70,200. In the period from its incorporation in November 1985 to 31 March 1987, Strikeline incurred an operating loss of £10,100. In each subsequent year operating profits were made of £5,100 in 1987/88, £2,100 in 1988/89, £3,900 in 1989/90 and £2,300 in 1990/91. In 1991/92 operating profits were £3,000; however, if, for example, director's remuneration had been charged in 1991/92 at the same rate as in the previous year, there would have been an operating loss in 1991/92 of £3,700 (see note 2 to Table 3.8).

TABLE 3.8 Strikeline: profit and loss accounts for the period from 13 November 1985 to 31 March 1987 and for the years ended 31 March 1988 to 31 March 1992

	13.11.85 to 31.3.87	1987/88	1988/89	1989/90	1990/91	1991/92*
						£'000
Turnover	7.6	71.9	85.5	91.2	78.4	70.2
Cost of sales	(6.9)	(38.7)	(53.5)	(58.0)	(49.9)	(47.8)
Administrative expenses	(10.8)	(28.1)	(29.9)	(29.3)	(26.2)	(19.4)
Operating profit/(loss)	(10.1)	5.1	2.1	3.9	2.3	3.0
Net interest	(0.7)	(4.1)	(3.6)	(2.2)	(0.6)	(0.1)
Taxation	0.0	0.0	0.0	0.0	0.0	0.0
Retained profit/(loss)	(10.8)	1.0	(1.5)	1.7	1.7	2.9
						per cent
Return on turnover (operating profit/(loss) as a percentage of turnover)	(133.4)	7.0	2.5	4.3	2.9	4.3

Source: Strikeline.

\*1991/92 figures are taken from draft unaudited accounts.

Notes:

1. Percentages calculated on unrounded figures.
2. Director's remuneration and national insurance contribution (NIC) is shown in the draft 1991/92 accounts at £3,782, compared with £10,479 in 1990/91. If, for example, director's remuneration and NIC had been the same in 1991/92 as in 1990/91, there would have been, instead of the operating profit of £3,000 shown above, a loss of £3,700 and a negative return on turnover of (5.3) per cent.

3.20. Strikeline's capital employed and sources of capital are shown in Table 3.9. Net tangible fixed assets consisted almost entirely of motor vehicles, financed partly by funds generated by Easy Rider, but mainly by leasing and hire purchase contracts and director's current account. After deducting net liabilities other than borrowings, Strikeline's capital employed varied between £39,400 at 31 March 1987 and £10,200 at 31 March 1992. At every year end from 31 March 1987 to 31 March 1992, Strikeline had net borrowings in excess of its capital employed and a deficit on its share capital and reserves.

**TABLE 3.9 Strikeline: capital employed, net borrowings and net deficit for the six years ended 31 March 1987 to 1992**

	Year ended 31 March						£'000
	1987	1988	1989	1990	1991	1992	
Tangible fixed assets	40.0	42.7	33.0	22.8	17.0	12.8	
Net liabilities other than borrowings	<u>(0.6)</u>	<u>(3.5)</u>	<u>(5.2)</u>	<u>(5.1)</u>	<u>(2.6)</u>	<u>(2.6)</u>	
Capital employed	39.4	39.2	27.8	17.7	14.4	10.2	
Net borrowings	<u>(50.2)</u>	<u>(48.1)</u>	<u>(38.1)</u>	<u>(26.3)</u>	<u>(21.3)</u>	<u>(14.2)</u>	
Net deficit	<u>(10.8)</u>	<u>(8.9)</u>	<u>(10.3)</u>	<u>(8.6)</u>	<u>(6.9)</u>	<u>(4.0)</u>	
Share capital less accumulated loss	(10.8)	(8.9)	(10.3)	(8.6)	(6.9)	(4.0)	

Source: Strikeline.

*Notes:*

1. Net borrowings consist of director's current account, bank overdraft and lease and hire purchase obligations, less cash.
2. 1992 figures are taken from draft unaudited accounts.

3.21. Strikeline's returns on average capital employed for the five years to 31 March 1992 are shown in Table 3.10. This shows positive returns on average capital employed over the period to 1991/92, varying between 6.4 per cent in 1988/89 and 17.3 per cent in 1989/90. Although return on average capital employed for 1991/92 is shown at 24.3 per cent, if, for example, director's remuneration had been charged in 1991/92 at the same level as in the previous year there would have been an operating loss and return on capital would have been negative (see note 2 to Table 3.10).

**TABLE 3.10 Strikeline: returns on average capital employed for the five years from 1987/88 to 1991/92**

	Year ended 31 March					£'000
	1987/88	1988/89	1989/90	1990/91	1991/92	
Operating profit	5.1	2.1	3.9	2.3	3.0	
Average capital employed	39.3	33.5	22.7	16.0	12.3	
Return on average capital employed (operating profit as a percentage of average capital employed)	12.9	6.4	17.3	14.3	24.3	<i>per cent</i>

Source: Strikeline.

*Notes:*

1. Percentages are calculated on unrounded figures.
2. Director's remuneration and NIC is shown in the draft 1991/92 accounts at £3,782, compared with £10,479 in 1990/91. If, for example, director's remuneration and NIC had been the same in 1991/92 as in 1990/91, there would have been, instead of the operating profit of £3,000 shown above, an operating loss of £3,700 and a negative return on average capital employed of (30.2) per cent.

3.22. Strikeline's sources and application of funds for the three years to 30 March 1990 are shown in Appendix 3.5 and show that Strikeline's sources of funds were almost entirely absorbed by applications over this period. No more recent funds or cash flow statements are available as Strikeline took advantage of the exemption from preparing these offered to small companies by Financial Reporting Standard number 1.

3.23. Table 3.9 shows that Strikeline had an excess of net borrowings over capital employed and a net deficit on shareholders' funds since its commencement. Strikeline's draft accounts at 31 March 1992 showed net tangible fixed assets of £12,800; net liabilities and borrowings totalled £16,800,

including an amount owing by Strikeline to its director of £15,000. Cash at bank and in hand at 31 March 1992 shown by the draft accounts was £750. In May 1992 Southdown purchased the goodwill and assets of Easy Rider for a total consideration of £[ \* ].

## Comparison of the revenues and costs of Southdown and Easy Rider

3.24. A comparison of the revenues and costs of Southdown and Easy Rider for the period from June 1991 to May 1992 is shown in Appendix 3.6. This shows average weekly revenues and costs and average per mile and per hour, based on average miles travelled and average operating hours per week, of Southdown's service 242 and Easy Rider's services 01 and 02. Appendix 3.6 is based on Table 2.3 of the DGFT's report. However, comments by both Southdown and Mr Hunter showed that the average operating hours in that table required amendment. The amended figure of 123 average operating hours per week, based for both Southdown and Easy Rider on two vehicles operating on the routes, was accepted by both Southdown and Mr Hunter and the amended table is now shown in Appendix 3.6.

3.25. Detailed route costings had not been maintained by Easy Rider in respect of its routes; however, the OFT estimated the figures for Easy Rider, in the absence of route costings, from information provided by Mr Hunter. Mr Hunter considers the figures for Easy Rider to be about right, subject to the reservation in paragraph 3.26, and Southdown does not dispute that Easy Rider's operation was a lower cost operation than Southdown's.

3.26. Appendix 3.6 is summarized in Table 3.11. This shows that during the period from June 1991 to May 1992 Southdown's revenue did not cover variable costs, but Easy Rider's revenue covered both variable and semi-variable costs and made a contribution to overheads. The table shows operating losses on the routes being made by both operators in the period. Table 3.11 shows that Easy Rider's average revenue per week was more than double Southdown's. Easy Rider's average direct costs (variable plus semi-variable costs) per week were lower than Southdown's, although the overhead costs as allocated by Southdown were less than Easy Rider's as estimated by the OFT. Mr Hunter considers it anomalous that Easy Rider's overhead costs should appear greater than Southdown's.

TABLE 3.11 **Southdown and Easy Rider: comparison of average revenue and costs from operating services on routes 242 and 01 and 02 between June 1991 and May 1992**

	<i>Southdown route 242</i>			<i>Easy Rider routes 01 and 02</i>		
Average miles per week	1,680			1,671		
Average operating hours per week	123			123		
PVR* (minibus)	2			2		
	<i>Average per week £</i>	<i>Average per mile ppm†</i>	<i>Average per hour £ph‡</i>	<i>Average per week £</i>	<i>Average per mile ppm†</i>	<i>Average per hour £ph‡</i>
Revenue	533	31.7	4.3	1,191	71.3	9.7
Direct costs	1,640	97.6	13.3	1,086	65.0	8.8
of which variable	933	55.5	7.6	702	42.0	5.7
Contribution	(1,107)	(65.9)	(9.0)	106	6.3	0.9
Overhead	113	6.7	0.9	253	15.1	2.1
Operating profit/(loss)	(1,220)	(72.6)	(9.9)	(147)	(8.8)	(1.2)

Source: OFT from information provided by Southdown and Mr Hunter.

\*Peak vehicle requirement.

†Pence per mile.

‡£ per hour.

\*Figure omitted. See note on page iv.



3.27. We have not been able to reconcile the OFT figures fully from information from Strikeline's Annual Report and Accounts, but this information indicates that Easy Rider had lower costs and higher revenues per mile than those shown for the Southdown route 242. The fact that Strikeline's draft 1991/92 accounts show a small profit, whereas the estimated figures for routes 01 and 02 show a loss, is partly explained by lower director's remuneration (referred to in paragraph 3.21), the different time periods involved and the inclusion in the accounts of the results of operating Easy Rider route 04, not included in the OFT figures.

## 4 Views of other parties

### West Sussex County Council

4.1. An officer of the Highways Department of WSCC told us that only a few operators made bids for the county's tendered bus services in Bognor Regis. Tendered services tended to be 'add-ons', and indeed there was now only one all-day service under contract to WSCC and this was operated by Southdown. Southdown had the majority of contracts for tendered services in Bognor Regis, partly because other operators were not interested in those routes, and partly because Southdown bulk tendered, often for 10 to 15 contracts, at a heavily discounted price if they won them all.

4.2. WSCC did not believe that Easy Rider's withdrawal from the market had led to a reduction in the competition for tendered services. Easy Rider had operated only one short journey on a Saturday and a Sunday service for the council, which fitted in with an existing schedule, for a short time, and had rarely tendered for any other work. WSCC noted that, at the expiry of Blue Lake's contract for a tendered service between West Meads and Bognor Regis, Southdown had registered an all-day commercial service. The council did not consider that Blue Lake's decision to continue to compete on this route on a commercial basis between West Meads and Bognor Regis would benefit bus passengers. There had never been sufficient passengers for the route to sustain competition.

4.3. WSCC found it difficult to comment on whether competition from Easy Rider in the commercial sector had benefited fare-paying passengers, as WSCC had not controlled fares since deregulation. However, it did consider that services had improved overall since Easy Rider had reintroduced routes from which Southdown had withdrawn, and had routed buses down smaller roads and through estates which had not previously been served by buses. WSCC said that, although it had no first-hand evidence, it understood that the quality and reliability of the Easy Rider service had deteriorated after a good start. Easy Rider had certainly been deficient in its marketing: timetables had been virtually non-existent and, where its routes had overlapped with Southdown's, it had used existing bus stops, operating a hail-and-ride service elsewhere.

4.4. WSCC thought that Southdown was still operating Easy Rider's former services, although there had been some rationalization. WSCC did not believe that Southdown would abuse its position, at least in the short term, if it established itself as virtually the sole operator in Bognor Regis.

4.5. WSCC did not consider that there were any significant barriers to entry in the Bognor Regis local bus services market. The seeming lack of competitive penetration was, it thought, due more to the fact that existing operators were not prepared to take on the large commitment of operating a bus service, preferring the relative simplicity of operating coaches. Similarly, although WSCC invited tenders widely, there was little or no interest from newcomers wishing to compete. There had been more interest in the early days of deregulation, but even then Easy Rider had been the only moderately successful new entrant in the Bognor Regis area.

4.6. Although WSCC had noted Southdown's competitive action elsewhere, it did not consider that Southdown's action in Bognor Regis truly deterred entry, since much depended on the degree of determination of the potential new entrant; any operator entering the market and duplicating routes must expect Southdown to retaliate, as any incumbent anywhere in the country could be expected to do. Even if Southdown raised fares and reduced services in Easy Rider's former operating area, the opportunity available to a potential new entrant would be limited.

4.7. Supporting the concept of bus companies running networks, which it saw as encouraging the use of public transport, WSCC agreed with Southdown's view that it had been unreasonable for the OFT to consider service 242 in isolation because Easy Rider's routes overlapped with Southdown's and abstracted revenue from Southdown's other routes.

4.8. We asked WSCC to consider possible remedies on a hypothetical basis, should Southdown's action be found to be anti-competitive. WSCC foresaw difficulties if Southdown were prohibited from operating a service at a loss, for example by deliberately undercutting competitors. The effect of such a remedy, which would be hard to enforce, would depend on fare scales; these tended to be fixed by what the market would bear rather than by rates per mile. Southdown would doubtless argue that it was competing 'with its hands tied behind its back'. There was evidence that operators competed as much on the frequency of a service as they did on fares.

4.9. WSCC did not believe that it would be effective for Southdown to give an undertaking that, if it introduced temporary fares reductions or increases in services in response to competition, it should maintain them for a year or more. WSCC thought that Southdown would do this anyway and cited the Westrings Coaches case: when Westrings Coaches had eventually withdrawn from the Chichester to Wittering route, Southdown had kept fares low and they were probably still lower than they would otherwise have been. A problem here was that there was no readily identifiable index to which prospective fares increases could be related.

4.10. WSCC also foresaw difficulties with a remedy which would not allow Southdown to respond to a new entrant that ran a service just in front of its own. The Transport Act provided for operators to register services to run at whatever times they notified to the Traffic Commissioner, but if they varied the timing by more than five minutes the registration would have to be amended. Any such remedy would need careful wording and Southdown could argue that it would be unfair. WSCC noted that there was an apparent conflict between the Transport and Competition Acts: whereas the former encouraged competition, it appeared that the latter could discourage it, at least in the bus industry.

4.11. It was WSCC's considered and long-held view that the franchising of networks would improve local bus services. There would still be competition in tendering but it would eliminate the waste of resources involved in operators competing with each other on the same routes.

### **Bognor Regis Town Council**

4.12. Bognor Regis Town Council told us that its Environment and Leisure Committee had suggested that the district council should have the power to fix bus fares in the same way that it had with taxi fares. Fixed fares, the committee believed, would allow companies to compete on the basis of service, punctuality, comfort and safety without the problems that had arisen through an unfettered market following deregulation.

### **Bersted Parish Council**

4.13. Bersted Parish Council (Bersted) told us that, in addition to supporting Easy Rider's complaint to the OFT, it had approached Southdown in September 1991 requesting that the timetables be altered to make a more sensible gap between the Southdown and Easy Rider services. Southdown had also been asked to look at other routes which had been identified as needing a service, rather than duplicating Easy Rider's. Both requests had been refused.

4.14. Bersted had also asked Southdown to consider using smaller buses. Easy Rider's 16-seater buses had been much more suitable for use on the narrow estate roads than the vehicles used by Southdown. Southdown had stated that it would use its smallest buses which were 23-seaters. It had also responded negatively to an informal suggestion by the Clerk of the Council that, when upgrading its stock, it should consider purchasing smaller buses.

## **Pagham Parish Council**

4.15. Pagham Parish Council said that, had Southdown's buses been scheduled at equal intervals between Easy Rider's services, the community would have benefited from a more frequent service. However, the timing of Southdown's services had been similar to Easy Rider's and had not benefited the community at all.

### **Easy Rider**

4.16. Mr I Hunter, the proprietor of Easy Rider, told us that, after contemplating and eventually dismissing the idea of a rural bus service, he had started routes 01 and 02 in Bognor Regis as hail-and-ride services because he had identified a gap in the market. Southdown had withdrawn its service covering the northern parts of the North Bersted area and some services covering sections of Rose Green, Nyetimber and Pagham. He considered that, in both cases, the areas had been left with very few buses. Mr Hunter said that he had designed services to cover those areas not served by Southdown, aiming to bring them as close as possible to people's homes; Easy Rider had therefore used minibuses on the narrow roads of the residential estates. He had been anxious not to enter into conflict with Southdown and had consequently kept off Southdown's routes wherever possible; the nature of the approaches to the town centre had, however, made some overlap unavoidable.

4.17. Mr Hunter explained how, by providing a good friendly service, Easy Rider had secured loyal passenger support: hail-and-ride had meant that passengers could be taken directly to their houses; drivers had often helped by lifting shopping on and off the bus; and Easy Rider had become part of the community. This had been in contrast to Southdown which, prior to its take-over by Stagecoach and the advent of Easy Rider, had had a very poor reputation, particularly concerning the unhelpfulness of the drivers.

4.18. Mr Hunter agreed with the OFT report's finding that Easy Rider's services had been more efficient than Southdown's. It had been a far smaller operation and costs could be more easily contained; maintenance, workshop and administrative costs had been monitored carefully and acted upon quickly.

4.19. Mr Hunter considered that Easy Rider's dissemination of information and marketing of its services had been satisfactory. Timetables had been printed in the newspapers and had been available on the buses; information had been available by telephone; and passengers had soon come to know the times of Easy Rider's services, as they had remained unchanged throughout the period of operation.

4.20. In July 1990 Southdown had introduced its service 262 in direct competition with Easy Rider's 02 Rose Green service. Service 262 had been withdrawn in December 1990, but in March 1991 a new half-hourly Southdown service 242 had been registered, covering Easy Rider's 01 and 02 routes. Whilst Southdown's entry had led to a fall in revenue, Easy Rider had not been concerned about fares or bus frequency; the main problem had been timing, because Southdown's services had been registered to run about two minutes ahead of Easy Rider's. Although Mr Hunter had been advised to retaliate by reregistering Easy Rider's timings, he had not done so. He had always wanted to run a legitimate business and he believed that continual unnecessary reregistering would merely have led to Easy Rider and Southdown playing leap-frog, and consequential loss of revenue.

4.21. At this stage Mr Hunter complained to the OFT that Southdown had adopted, for its service 262, almost identical timing and exactly the same route as Easy Rider's route. Moreover he had been sure that Southdown had taken predatory action by running service 262 at a loss and had anticipated that its subsequent service 242 would be run in a similar fashion.

4.22. Mr Hunter told us that, since April 1991, following Southdown's intense competition and with the effects of the recession, Easy Rider had been losing money and the company had barely been breaking even. Easy Rider had never made anything more than a reasonable profit and it had been clear to him that Southdown was determined to contest the routes to the end. He had finally offered to sell the assets of Easy Rider to Southdown, and Southdown had agreed to purchase Easy Rider's

three buses and goodwill. Mr Hunter had sought and received Southdown's assurance that it would maintain the routes for a reasonable period and he had undertaken not to restart bus services on the same routes within one year. Mr Hunter told us that he would consider running another bus service despite Southdown's incumbency. He did not consider that there were significant barriers to entry other than Southdown acting anti-competitively.

4.23. Mr Hunter said that he had competed for tendered services and would consider doing so again. Easy Rider had been awarded a Sunday service to Pagham beach and a Saturday morning service east of Bognor Regis, which had formerly been operated by Southdown and which had later fallen away as a tendered service because Southdown had decided to operate it commercially. He had been aware that Southdown competed for tendered services, offering deep discounts for successful bulk tenders and thereby taking routes from incumbent operators.

4.24. Mr Hunter could not completely accept the argument that Easy Rider had extracted revenue from Southdown's total route network in Bognor Regis. He believed that it had tapped a new market of passengers who would not have used Southdown's services; but inevitably, given that its route went to Bognor Regis town centre, there had had to be an overlap with Southdown, and he did not consider that Easy Rider should have declined to pick up passengers on the overlapping section of its route. Similarly Mr Hunter could not accept that Easy Rider had undermined the viability of Southdown's co-ordinated network in Bognor Regis. In his view there was room for two companies to operate in the area.

4.25. On the question of hypothetical remedies, Mr Hunter believed that a requirement for Southdown not to operate services at a loss would be beneficial. However, he foresaw difficulties in monitoring and thought that such a remedy probably went against the spirit of deregulation. He also pointed out that there were many variables which affected the costing of a route. Mr Hunter said that if Southdown, even operating at a loss, were to keep its timing at a reasonable distance from that of another operator, that would simply be competitive behaviour. What was unacceptable was that Southdown, while operating at a loss, could alter its bus timings and thus effectively smother the competitor.

4.26. When we asked Mr Hunter about a remedy which would require Southdown to maintain fares or frequencies for a minimum period if they had been introduced in response to competition, he said that this would not have prevented the demise of Easy Rider. He thought that Southdown would be willing to maintain fares or frequencies for a year to see off a competitor. A broader undertaking or more specific control of the timing was needed.

4.27. In Mr Hunter's view a more effective remedy would be for the Traffic Commissioner to be empowered to prevent a competitor registering a service, say, two minutes in front of an existing service. On receipt of an application for a local service, the Commissioner's office should compare it with other services and if necessary stipulate that the service should run at a different time in the interest of the public. Provided that the timings came within the Commissioner's overall control and were evenly spread, Mr Hunter would even find it acceptable for an operator greatly to increase the frequency of a service.

4.28. Mr Hunter did not regard restricting fares increases to increases in the RPI as an appropriate remedy, and, indeed, did not consider any remedy concerning fares to be crucial; passengers were already price sensitive and in Easy Rider's experience even small fares increases turned customers away.

## **Sussex Bus**

4.29. Mr J Belson, Managing Director of Sussex Bus, who formed the company in 1985, told us that his objective was to take advantage of the opportunities arising from bus deregulation. Operating eight buses, Sussex Bus runs services in the Chichester area and to Midhurst, Horsham and Brighton, and accounts for approximately 12 per cent of bus miles in the Chichester district.

4.30. Sussex Bus said that during the period of the OFT investigation it had a contract with Southdown to operate a 260 service during peak hours. Whilst this contract had ended, there was still an arm's length commercial arrangement between the two companies. Sussex Bus explained that it used Southdown's bus station, but not the repair facilities. It discussed with Southdown the state of the local market, its future shape and any known forthcoming changes that might offer opportunities to Sussex Bus.

4.31. Southdown had previously typeset the Sussex Bus timetable, although it had not done so for the latest version. Where convenient and appropriate Sussex Bus had added its flags to those owned by Southdown on the council-owned bus stops, and the companies' tickets were interchangeable where appropriate.

4.32. Sussex Bus told us that before deregulation it had been in competition with Southdown when it had started a niche operation. Currently, for instance, it operated a tendered Sunday service on a weekday Southdown route, the service appearing in Southdown's timetable. Sussex Bus did not compete head-on with Southdown because the local market was too small.

4.33. Sussex Bus told us that it did not believe that Easy Rider had contributed anything to the benefit of bus users. Asked to expand, Sussex Bus explained that Easy Rider and Southdown had both run half-hourly services; their buses had reached bus stops within five minutes of each other, which was of no benefit to passengers. Sussex Bus considered that Easy Rider had marketed itself poorly; timetables had been hard to find and drivers often had not kept to them; information had been disseminated by word of mouth. In Sussex Bus's opinion Easy Rider's 16-seater vehicles had been too small. Despite these drawbacks Easy Rider had seemingly built up a high degree of passenger loyalty and support. Sussex Bus thought that this had come about because of the nature of the Easy Rider operation, notably the hail-and-ride service sometimes deviating from the route to passengers' front doors, and its generally caring attitude. Moreover Southdown had initially allowed Easy Rider to operate unhindered.

4.34. Sussex Bus said that an operator entering the market had to decide on its scale of operation. If it wanted to compete on equal terms with a dominant incumbent it had to invest large sums. If it merely wanted to be a niche operator it should declare its interest, serve an area not already covered without significant overlap, and establish its own market base. Easy Rider had appeared to want both roles; having established itself as a niche operator, it had challenged Southdown directly, taking passengers from the main route into Bognor Regis.

4.35. In Sussex Bus's view Easy Rider had not operated efficiently, and it had in fact been surprised by the OFT finding that Easy Rider's services were more efficient than Southdown's. Sussex Bus accepted that Easy Rider had scope to be more efficient in that it had lower overheads and did not have the expense of printing, bus-stop flags and other peripherals. Fares on routes 242 and 262 did not appear to be a factor; although both companies appeared to have kept fares artificially low, there had not been a price war. Sussex Bus considered that, had Easy Rider invested sufficiently in its routes, it would probably have been able to hold its market position.

4.36. Sussex Bus noted that, prior to its acquisition by Stagecoach, Southdown's operation had been merely adequate. Following the take-over, however, Southdown had made efforts to hold its market share and regain its former position. Passenger loadings and timetables had been overhauled and new midibuses had been deployed on the main feeder and estate routes in Bognor Regis, although admittedly not to all passengers' front doors.

4.37. Tendered services in the Bognor Regis area were undoubtedly dominated by Southdown. Sussex Bus thought that this was because no other operators were prepared to run short peak-hour services and because Southdown submitted bulk tenders, bidding for a number of services for a fixed discounted sum. Sussex Bus did not consider that Easy Rider's withdrawal would affect potential competition for tendered services.

4.38. Sussex Bus did not think that there were any significant entry barriers. To enter the market was relatively straightforward; the problem for a new entrant was to develop its market in the face of probable retaliation from the incumbent operator.

4.39. A dominant incumbent should be allowed, in Sussex Bus's view, to defend its area, preventing smaller operators from entering and creaming off the easy pickings. Larger operators, like Southdown, had invested heavily, building up an integrated network with good vehicles and staff. Sussex Bus saw competition as leading to a lower quality of service: with the smaller operator extracting revenue from the dominant company's income, neither company was able to do well. Despite the possibility of lower fares in the short term, this solution would be to the overall detriment of the travelling public.

4.40. Sussex Bus believed that this highlighted a possible conflict between the Transport and Competition Acts over what was reasonable competition. Given that competing on price was impractical, operators could only compete on service, offering a better service at a more convenient time, more frequently or just ahead of the opposition. If the incumbent offered a poor-quality service which did not improve, an efficient smaller operator could enter the market, establish itself and successfully hold its market share.

4.41. Sussex Bus accepted the argument that Southdown's retaliatory action in Bognor Regis could deter market entry. But it did not believe that this charge could be levelled only at Southdown. Any dominant incumbent in Southdown's situation would retaliate vigorously if competitors entered the market on a good commercial route and began creaming off easy profits. Any potential competitor should expect no less.

4.42. Asked to comment on possible remedies, Sussex Bus responded that a requirement not to run a route at a loss would undermine an incumbent's ability to compete. It was not always understood that isolating one route ignored the other, probably more profitable, services which made up the complete network.

4.43. Sussex Bus considered that the public would at least gain some benefits from a remedy whereby a company which ousted another by reducing fares or increasing frequency should have to maintain the new fare levels or frequency for a stipulated period.

4.44. Sussex Bus also accepted as feasible a hypothetical requirement that no operator should be allowed to reregister a route so that its buses kept just ahead of those of its competitor. Sussex Bus saw the possibility of such registrations as a deficiency in the Transport Act. Traffic Commissioners should have powers to control competition, and to arbitrate between conflicting registrations, amending timetables which clashed.

## **Other operators**

4.45. We also heard from a small operator elsewhere in Sussex, who told us that another Stagecoach subsidiary, Hastings & District Transport Ltd (H&D), had started a service which was virtually identical to the small operator's own service, and which H&D ran contrary to the service registration.

## **South Yorkshire Transport Ltd**

4.46. South Yorkshire Transport Ltd (SYT) was concerned about the respective roles of small and large bus companies and the charges of predatory pricing being levelled at large bus companies.

4.47. SYT considered that care should be taken when comparisons were made. There was a common perception that bus companies of different sizes competed principally with each other and supplied the same product but in different volumes. This argument was fallacious. A larger bus company in general produced a product, which was a network of services serving the community; an individual route was only part of this whole product. A small bus company, however, produced only a single route, or sometimes two.

4.48. In pricing its product, the bus company must have regard to the cost of production and to competition. Competition differed depending on the size of the operator. Typically a small company set out to obtain business at the expense of a larger operator; accordingly it priced its services to

attract custom away from a small part of the large company's network. On the other hand, the large company competed not only with smaller operators but other forms of transport. Consequently it priced its network to cover costs and make profits as a totality. SYT believed that it was wrong to look at the fares on a particular route in terms of predatory pricing, when it formed part of a network of services and it was the costs of the whole network which the large operator tried to cover.

4.49. SYT noted that Bognor Regis traditionally had a high population of retired people and a temporary summer population, both of which were dependent on bus transport. An interrelated network of services was thus important, enabling such passengers to use more than one route in making a journey. Furthermore a network allowed an operator to organize staff and vehicles so as to maximize efficiency.

## **Bus and Coach Council**

4.50. The Bus and Coach Council (BCC) believed that the reference had highlighted the difficulties in applying existing competition legislation to the bus industry. Article 75 of the Treaty of Rome recognized that special circumstances affected transport, but it did not define them. It recognized the importance of market stability and consumer satisfaction in the transport sector, which was an indispensable ancillary activity to other industrial sectors.

4.51. The supply of bus transport was inelastic due to its perishable nature; this produced a conflict in applying the full freedoms of competition, which was exacerbated by the interchangeability of transport services. Although Article 85(3) of the Treaty enabled some agreements to be entered into for the benefit of the passenger, the general prohibition under Article 85 continued to be a source of complaint from user groups.

4.52. The BCC believed that the stability of the bus transport market was of concern to the Government and that the ease by which new companies entered and left the market should be balanced against the long-term stability provided by major operators. The public interest could be best served by a review of the application of competition legislation to the bus industry. Until such action was taken there was a danger that a number of technically sound decisions taken on competition grounds would continue to work against the public interest.

4.53. Under the new definition of 'subsidiarity' reached at the Edinburgh Summit, the issues of Southdown would not be matter for the EC; nonetheless there was still a requirement to comply with the general rules laid down in Article 5 of the Treaty. In the policy discussion document for 'The Future Development of the Common Transport Policy' (COM(92)494 final) the Commission had stated that it intended to modify some aspects of competition legislation, especially Regulation 1017/68, in order to allow more co-operation in the field of transport.

## **National Federation of Bus Users (NFBU)**

4.54. Dr Caroline Cahm attended a hearing on behalf of the NFBU and Buswatch. The NFBU is a bus users' body which was established in 1985 to promote the interests of passengers. It currently has about 30 affiliated groups and 200 individual members. Buswatch is a passenger-monitoring organization which has monitored local bus services from the point of view of passengers since 1986.

4.55. Asked to comment on the effects of competition on local bus services, the NFBU said that it did not consider that generally reduced fares had resulted, and that passengers did not like the type of competition which resulted in the duplication of services. Operators competed fiercely on all aspects except fares, fearing that fare cutting would cause them to go out of business. They did compete, however, in the area of non-transferable bargain saver tickets, effectively tying passengers to a particular service. The NFBU was not convinced that competition led to the opening up of new routes. This might happen initially, but there was a general tendency for the original network to be progressively re-established.



4.56. The NFBU told us that in its experience passengers preferred a coherent network of services, not necessarily provided by a single monopoly operator, but possibly through operators co-operating and services complementing one another. It would be beneficial if the law could be amended to encourage co-operation between operators in ticketing and to establish networks.

4.57. We asked the NFBU whether a single operator running a coherent network might raise fares. The Federation believed that this would be unlikely, particularly in the current economic situation. Passengers were price sensitive and operators would lose custom if they charged what were perceived as high fares. The NFBU agreed with the argument which had been put to us that networks offered the advantage of integrated routes and destinations, travel cards and onward travel facilities. The population generally was becoming more mobile and there was a growing demand for travel beyond the immediate area. Smaller operators tended to operate best within a smaller framework where timetables were less important and service information could be passed on by word of mouth.

4.58. Whilst the NFBU did not have specific evidence regarding the Easy Rider and Southdown services, its Chairman had visited the area and spoken to passengers. Undoubtedly Easy Rider was seen as having provided a friendly and seemingly reliable service, whereas Southdown was viewed rather more negatively. However, the NFBU thought that Easy Rider's almost personal service, virtually eschewing timetables, lacked professionalism and that Southdown was much more effective in its dissemination of information through timetables and leaflets. Passengers did not appear to have been interested in fares.

4.59. Easy Rider had operated three 16-seater minibuses, later acquiring a 19-seater. Having seen the vehicles the Chairman of the NFBU felt that, while these were perfectly legal, they were not completely safe; they had low roofs and small aisles and easily became overcrowded. Passengers, particularly the elderly, had difficulties getting on and off such buses. To judge from the extensive rusting on the exteriors the NFBU thought that maintenance of the vehicles might not have been as thorough as it should have been. The fact that the vehicles had been kept out of doors had not facilitated maintenance. It was the NFBU's general experience that smaller operators, like Easy Rider, were under-resourced and did not invest sufficiently in maintenance.

4.60. The NFBU agreed that, since its take-over of Easy Rider, Southdown had changed some of its services and increased some fares. But it was the NFBU's general impression that passengers were now favourably disposed towards Southdown whose attitude had become far more positive and friendly. Moreover the Federation did not consider that if Southdown became the only operator in Bognor Regis it would abuse its position: it would not be in Southdown's interests to do so. Southdown wanted a network that would engender passenger loyalty; changing services and increasing fares would have the opposite effect. Fares were very much influenced by the market, and generally operators raised them only when necessary since fares increases usually led to fewer passengers.

4.61. Asked about barriers to entry, the NFBU told us that there were virtually none, although it accepted that a larger operator had the capacity to run a smaller one off the road. It considered that, if a large operator saw a small operator extracting revenue by taking passengers and generally affecting its network, it would almost inevitably react as Southdown had done.

4.62. The NFBU could not readily accept the argument that Southdown's widely-known retaliation against competitors acted on its own as an effective barrier. Most of the larger operators had such a reputation and matters had been exacerbated by the depth of the economic recession. Possibly when the economy recovered there could be a case for restricting some of the actions of the larger operators.

4.63. Commenting on hypothetical remedies if we concluded that Southdown had been carrying out an anti-competitive practice, the NFBU favoured changes to the competitive framework to prevent any operator from abusing the market, rather than specific remedies aimed at Southdown. A change in the service registration system was advocated, whereby services and changes would be registered on particular dates. Operators beginning a new service would have to give a commitment to maintain it for a minimum period. The NFBU argued that the six weeks' notice period to introduce, withdraw or change a service should be extended to three months.

4.64. Concentrating on specific hypothetical remedies, the NFBU thought it reasonable that Southdown should not be permitted to run at a loss. A possibility might be the imposition of a fare for a route. Similarly, on consistency grounds the NFBU subscribed to the concept of a remedy which would prevent a company from providing an excellent service and cheap fares with the purpose of driving out a competitor, only to remove them after the competitor's departure. Lastly the NFBU agreed that the prospect of a remedy which would peg fares increases to the rate of inflation was theoretically a reasonable objective.

### **Members of the public**

4.65. We received letters from 17 members of the public, 12 of whom had contributed to the OFT's investigation. Only one correspondent thought that Southdown's service was satisfactory since the Easy Rider take-over, but wondered how long it would remain so.

4.66. All the remaining respondents believed that Bognor Regis had benefited greatly from Easy Rider's services, particularly the elderly, young mothers with their children, and schoolchildren.

4.67. Respondents commented how, unfairly in their opinion, Southdown had rescheduled its services to run just in front of Easy Rider's. Most respondents also said that, since the take-over of Easy Rider, Southdown's service had deteriorated in comparison with Easy Rider's, particularly as regards the helpfulness of the drivers, and its fares had been increased.

# 5 Views of Southdown

5.1. This chapter summarizes the views of Southdown, as stated in its submission and in oral evidence to the MMC.

## The factual basis

5.2. Southdown told us of a number of operators that had registered local bus services in the Bognor Regis area following deregulation in October 1986. Although most of these had presented only limited competition, Easy Rider's services 01 and 02, which had commenced on 26 January 1987, had been seen as a direct threat to Southdown's commercial network. Southdown believed that the OFT report was misleading in suggesting that there was 'limited overlap' between Southdown's operations and those introduced by Easy Rider, since, at the time when Easy Rider had commenced operation, over 70 per cent of its route length had exactly duplicated Southdown services. The remainder had been within 200 yards of Southdown services, which Southdown argued could also be regarded as overlapping. Southdown said that the initial Easy Rider services had been timed to depart from Bognor Regis eight minutes ahead of Southdown services 245 and 260, and that Easy Rider's services in the opposite direction had been timetabled to run just in front of Southdown's. In practice Easy Rider's services had in general tended to run shortly ahead of Southdown's. Southdown considered that this demonstrated the weakness of the OFT argument that Easy Rider's services had only limited overlap with Southdown's, and believed that Easy Rider did not cater for a separate market. Indeed, the closeness of the timings suggested to Southdown that Easy Rider's services were designed to abstract revenue from services 245 and 260.

5.3. In Southdown's view the OFT report was invalidated because it incorrectly stated that there was no overlap and later indicated that, in its response to Easy Rider's entry, Southdown had basically duplicated Easy Rider's services. This showed that the OFT was adopting a different answer to the two circumstances. Southdown believed that its response to Easy Rider's entry had been quite reasonable, and that, in so far as it was covering much the same ground that Easy Rider had covered, it was merely because Easy Rider had itself covered much of Southdown's route in the first place. In Southdown's view Easy Rider had found a few new passengers by taking minibuses into the Rose Green and Bersted estates with a hail-and-ride service, but this new facility was provided on the back of about 90 per cent of its business 'creamed' from Southdown's services. Southdown told us that it had established an 04 service on Easy Rider's original 04 route only when it had learned that Easy Rider was extending its 04 service to Chichester on the route of Southdown's 260 service.

5.4. On the question of competition from other forms of transport, Southdown pointed out that there were over 115 taxis based in Bognor Regis, which was a large number for a small town. Since the distances were short, taxi fares for journeys within Bognor Regis were not high; indeed it was known in the bus industry that it was common for two people shopping together to realize that, by getting a taxi home, they could travel as cheaply as by catching a bus.

5.5. When we put it to Southdown that the costs figures in a corrected version of Table 2.3 of the OFT report (reproduced as Appendix 3.6 to this report) supported the conclusion that Easy Rider's was a lower-cost operation than Southdown's, Southdown said that it would not dispute that a small operator like Easy Rider, using smaller vehicles, would be operating at lower costs. Services 242, 244 and 264 were still not covering their direct costs and the rate of loss on 242 and 264 was too high; however, Southdown was seeking to develop services in the Bognor Regis area and could not simply

increase fares and halve the frequency on these routes. It believed that the market was definitely contestable and that it would never be able to recoup its past losses on the routes. It did not believe that the market was robust enough to sustain the sort of changes that would be necessary to make those services pay.

5.6. Southdown believed that there was not room for two operators on the former Easy Rider routes, as the evidence since Easy Rider's departure demonstrated. Southdown was still running a service at greater frequency and lower fares than the market would actually sustain even at Easy Rider's level of costs. In an ideal world Southdown would reduce the service or put up fares, or both, but it had no current plans to make any further changes to these services. The company acknowledged that it would therefore continue to sustain losses on these services, its reason for doing so being solely to protect the totality of its existing markets. It would never be able to make predatory gains from these routes, but it hoped that, by service development and by judicious rationalization, it would eventually obtain some contribution from them. Any change which it made on the former Easy Rider routes would be as little and as late as possible to ensure that the maximum benefit remained to the public. If it stepped away in the slightest degree from what the market itself found acceptable, then the market would be contested. Southdown believed that the previous presence of Easy Rider as a competitor in Bognor Regis made the market even more contestable for the future.

### **The course of conduct**

5.7. Southdown confirmed that it had registered and operated services 242 and 262 as described in the OFT report. It accepted that the services operated, in isolation, on an uneconomic basis, but said that since fare levels were set for the whole area, it did not accept that uneconomic fares were charged. Nor, by extension, did it accept that the operations as a whole, including services 242 and 262, were uneconomic. Southdown did not accept that the course of conduct was anti-competitive; it believed that not to have responded to Easy Rider's entry would have been anti-competitive. Southdown considered that predatory pricing could only be said to have taken place when monopoly profits had been extracted, and this was not the case. It believed that users now had a far better service taking all factors into account.

5.8. Southdown emphasized that its operation was a highly-integrated network, within which it was necessary to maintain comparability, consistency and compatibility between all the services concerned. Inevitably fares had to be based on the area as a whole, and it was appropriate to look at Bognor Regis at large as a profit centre. Although the viability of routes was judged on an individual basis, the company was not necessarily in a position to take action on that judgment. All bus operations had a mixture of profitable and unprofitable routes and it was not possible to separate one out from the others. Cross-subsidy was unavoidable and judgments had to be based on the needs of the market as a whole. In this particular case the results on the reference routes were the least satisfactory in the area, but if a route failed to contribute it would not necessarily be dropped because of the cross-subsidizing and integration effects on other services.

5.9. Southdown said that it had never intended to undercut Easy Rider's fares; in fact it had never been able to fully establish what Easy Rider charged. In almost all cases its fares had been higher than Easy Rider's.

5.10. We asked Southdown for its view on the definitions of 'uneconomic' and 'predatory pricing'. It saw 'uneconomic' as related to time: the covering of direct costs was relevant to the short term, semi-variable costs to the medium term, and total costs to the longer term. Southdown did not think that cost was the relevant criterion by which to establish predatory pricing; it understood that monopoly profits flowed from predatory pricing, and this was not feasible in the present case. Moreover costs related only to one small part of the total operation.

### **Motive and intent**

5.11. On its motive and intent in running service 242 at a significant loss and only a few minutes ahead of Easy Rider, Southdown said that it had acted to defend the business as a whole. It

considered that the OFT conceded that the concept of predatory pricing could not exclude motive and intent, since uneconomic pricing on its own was consistent with a legitimate competitive response to the new entrant. Southdown said that in this case the 'evidence' of motive and intent was provided by what it had said at its meeting with the OFT, referred to in the OFT report, namely that Easy Rider's entry had forced it to take action to defend itself. Southdown believed that motive and intent of this sort was meaningless in determining whether there was predation since it applied in most cases where an incumbent was faced with a new competitor. Southdown criticized the analysis of motive and intent in the OFT report, arguing that motive and intent were meaningful only in relation to the incumbent's strategy after the new entrant had left the market. However, the OFT report contained no evidence of Southdown's intention to put prices up to 'supra-competitive' levels. In fact no such evidence existed, as predation in an economic sense was not feasible in this market: 'supra-competitive' prices or reductions in frequency would simply encourage new entry into the market or cause loss of passengers to other forms of travel, such as taxis or walking. In failing to observe the critical distinction that motive and intent must relate to behaviour after the exit of the new entrant, the OFT had falsely characterized Southdown's behaviour as predatory when it had in fact been a legitimate and necessary competitive response.

5.12. Southdown emphasized that it had been seeking to protect itself against a 'classic creaming operation' which, had it been allowed to succeed, would have seriously damaged the overall interests of the business, and would have sent clear signals to others to indulge in a 'cream skimming operation'. The financial situation which Stagecoach had inherited when it purchased Southdown had been poor; the company had been badly managed and had failed to defend itself adequately, adopting a cautious 'wait-and-see' approach to Easy Rider. One of the new management's objectives had been to defend its revenue base more effectively. Now that there was only one operator on the route, Southdown hoped that it would maintain as much as possible of the revenue that the departed operator had taken. When we put it directly to Southdown that it had protected its business by pushing its competitor out, it accepted that this was a description of the competitive process.

5.13. Southdown told us that the bus market in Bognor Regis had declined to a greater extent than the average in the south of England, which was itself considerable, and that the company was seeking to rebuild that market by providing better levels of service. It did not believe that there was room for more than one operator in that type of market. If Easy Rider had in fact won, and had pushed Southdown off the road, which is what Southdown believed would have happened had it operated additional uneconomic services, Southdown would have had to have made cuts elsewhere because it would have had less revenue to cover its fixed overheads. That would have encouraged more new entrants like Easy Rider, and there would have been more competition; but the eventual net result would have been to find only one operator in any given area. Southdown believed that, had it not acted as it did, either there would have been only one operator left in West Sussex or, more probably, there would in the medium term have been one operator in each of the main towns at a lower level of quality and co-ordination. As a result the credibility of public transport, which had deteriorated since deregulation, would have declined even further, and the remaining dominant single operators in any given sub-market would have had to cut services or raise fares.

### **The effect on the public interest**

5.14. Southdown argued that the outcome of the competition in Bognor Regis, had Southdown not acted to conserve its business, would have been that the public interest would have been less well served: the remaining operation would not have been economically sustainable unless at a lower level, with a poorer quality of service. Southdown thought it questionable why a new operator, 'creaming' rather than seeking to develop a new market, should be defended. It believed that there was room for other operators, but that they had to find the appropriate space; they should not expect, simply because they were small, to get the constant protection towards which the OFT's line appeared to be leading. In that respect the system was not working properly.

5.15. Southdown acknowledged that Easy Rider's service had been different in some ways from its own, but believed that some 90 per cent of Easy Rider's revenue represented 'creaming'. Where Southdown encountered other operators which had sought and developed a niche market, it did not pursue part of that market, largely because the niche operator was probably able to serve it better.

In the case of Easy Rider, most of the people boarding its buses had done so at places served by existing Southdown services and less than 10 per cent on the estates.

5.16. Southdown argued strongly that it was not against the public interest to take measures to protect existing business from 'creaming' operations. It believed that it was in the public interest to provide public transport services meeting high quality and safety standards, properly managed, coordinated and controlled, offering a reasonable prospect of continuity. Southdown also believed that, had it not taken steps to protect its market in Bognor Regis, its whole Chichester and Bognor Regis area operations would have been at risk, leading to a proliferation of low-quality operations of a type already widespread in the county. This could be potentially very damaging to the market as a whole and to the needs of the individual passenger, particularly in West Sussex where county council policies were not notably pro-public transport. Southdown therefore considered that a strong professional commercial sector was vital for the public transport market and users in the Bognor Regis and Chichester areas. Southdown, by holding costs in 1992 to 1982 levels (a reduction of more than 30 per cent in real terms), had been able to provide 40 new 'user-friendly' buses in West Sussex in 1992. Part of the strategy which was needed to be able to make such improvements was to respond effectively to 'creaming' operations. In making such a response, Southdown would not wish to do anything which it considered to be against the customers' interests. It had consistently maintained that it would act as a professional operator and had said, in other competitive situations, that it would not tolerate a situation where its drivers raced those of another company, or anything of that sort on the road. Southdown considered that in the long run it was working to what it believed was the Government's intention in terms of promoting and improving the public transport network.

### *Fares and services*

5.17. On the question of fares and services, Southdown did not consider that its course of conduct had resulted in any adverse effect on fares, levels or standards of service. Southdown argued that the overall price elasticity of demand for bus travel and potential competition from new entrants would be sufficient to prevent fares increases following the withdrawal of Easy Rider, and told us that, for these reasons, the Stagecoach group's policy was not to increase fares in the current year. A modest increase in fares had in fact taken place after the withdrawal of Easy Rider, but this had been in line with fares increases in the remainder of the area. Southdown accepted that these fares would probably not have been increased in June 1992 had Easy Rider remained in the market. Fares on the reference routes had remained lower than the area norm, and both the level and standard of service had been improved. Southdown confirmed that it would wish to reduce some of the fare differentials that had emerged as a result of competition over the previous five years, although it believed that its ability to do this would be restricted by the potential for competition from new entry or loss of passengers to other forms of transport. The raising of fares to 'supra-competitive' levels was simply not conceivable in this particular market in the light of the absence of barriers to entry and the high percentage of car ownership.

5.18. Southdown observed that Easy Rider had provided a low fare, and the competition had led to Southdown's fares being held lower; but the quality of service provided by Easy Rider had not been very satisfactory, with no significant addition to existing services. If the type of service provided by Easy Rider had continued, it would have been with cramped minibuses with high entrance steps, whereas Southdown was now providing, throughout most of West Sussex, modern vehicles with low entrance steps which were very acceptable to customers. If the passenger market were not satisfied with the relationship between fares and quality of service offered by Southdown, then another operator would enter with lower-quality vehicles and attempt to take that market. If, as had happened in Bognor Regis, Southdown defended its position and the competitor ceased operating, there would be a situation in which Southdown was providing (again, as in Bognor Regis) a higher-quality service at a lower fare. Since that would be unsustainable in the long run, the public would either opt for a lower quality of service (which would be all Southdown or another operator could afford to run at the low fares), or accept that a higher quality of service could sustain higher fares.

5.19. Southdown accepted that, at the time when Easy Rider had entered the market, the reliability and general quality of Southdown's service had not been as good as it should have been, and said that the scope of its services had been limited by the then management's opposition to the use of

minibuses. Since 1991, however, the quality of Southdown's services had been very good, with monitoring of timing by roving inspectors, and quality checks. Southdown alleged that Easy Rider's departure times from main points had been fairly flexible.

5.20. While acknowledging that some users found Easy Rider's drivers more helpful, Southdown explained that, since Southdown used more vehicles, and therefore more drivers, inevitably the drivers would be less well known to passengers. With some of Southdown's vehicles it would not be as easy for the driver to help passengers on and off the bus as it was for Easy Rider's drivers, but the access to and from Southdown's vehicles was much easier, and they provided more storage space for such items as shopping trolleys and pushchairs.

5.21. Southdown told us that, on taking over Easy Rider's vehicles, it considered that none of them was fit for the road; moreover it believed that passengers did not like them because they were cramped. When Easy Rider services had been extended to Chichester, Southdown's staff at Chichester Bus Station had monitored Easy Rider's timing and found the timetables virtually impossible to maintain. Southdown considered that its services provided better vehicles, more realistic timetables and greater safety, and that it offered the public a genuine prospect of continuity of service. There was no doubt that Southdown now provided a better service due to the fact that it faced competition in Bognor Regis; because the market was contestable, it would not make the same mistake as the company's former owners and allow service levels to deteriorate.

5.22. Southdown said that the North Bersted services, on some parts of which there were now six buses per hour, provided access to the North Bersted area by different routes (the 242, 244 and 245), including the route from Elmer which had shown considerable growth. Frequency on routes 244 and 245 had grown from two-hourly four years ago, firstly to half-hourly and now to quarter-hourly. The increase in patronage which had accompanied the eightfold multiplication of services on routes 244 and 245 had given Southdown some faith that its increases in frequencies throughout Bognor Regis were increasing the overall level of patronage.

5.23. When we asked Southdown how long it had been prepared to maintain eight services per hour on the former Easy Rider 01 route and six per hour on the former 02 had Easy Rider not backed away, the company said that it would probably have been for up to another year; there came a point at which any defence became too expensive.

### *Acquisition of Easy Rider*

5.24. Southdown told us that in March 1992 Mr Hunter had offered for sale the assets and goodwill of Easy Rider, which Southdown had subsequently purchased. No written agreement had been entered into and, in particular, no restrictions had, in Southdown's view, been agreed on the future activities of Strikeline, Easy Rider or Mr Hunter; indeed, Mr Hunter still maintained his operator's licence and could therefore re-enter the market at any time. Southdown had taken on two Easy Rider drivers and had given a verbal undertaking, which it had met, not to let Easy Rider's passengers down or to make any immediate changes.

### **Market entry**

5.25. Southdown did not believe that there were any significant barriers to entry into the market for local bus services, either in general or in Bognor Regis in particular. It was relatively easy for a new operator to acquire and operate vehicles without any significant or even proper facilities, as Easy Rider had shown. With respect to particular points:

- (a) the 42-day notice period applied to all operators and was not a barrier to entry;

- (b) access to bus stations was rarely required by new operators, and where it was the Southern Vectis<sup>1</sup> case had set acceptable guidelines; Easy Rider was an example of an operator able to operate without proper depot facilities;
- (c) information about demand was best obtained by physical observation, the method regularly used by Southdown, and did not constitute a barrier to entry (as had been demonstrated in many places in the UK); and
- (d) the reaction of existing operators was not seen as a barrier because new operators continued to enter the local bus market in various places; the reaction of existing operators had clearly not deterred the most enterprising of the new entrants.

5.26. Southdown said that Easy Rider's departure made it clear to any would-be new entrant that it would 'not take new entry lying down'. However, Easy Rider's operations had shown that barriers to entry were low, and Southdown did not believe that any operator would be deterred from entering any of Southdown's markets if it failed to provide either value for money or a quality service; nor did it believe that the withdrawal of Easy Rider had reduced potential competition in any meaningful way: many operators provided tendered services in West Sussex, and the tender system provided an excellent springboard for commercial operations. Southdown told us that although, when bids were invited for tendered services, it attempted to provide multiple tender options to the county council, in cases where the council had accepted such an arrangement it had clearly decided that the balance of advantage was in so doing. In Southdown's experience councils were anxious to maintain as high a number of potential bidders as possible, and the facility of tender operation had led to a significant reduction in entry barriers.

5.27. Southdown noted that it had shown its willingness to buy new entrant companies and that this might be said to tend to increase the contestability of the market and encourage entry. Evidence would suggest that no large operators were likely to enter the market, because they tended not to be interested in distant small businesses. However, smaller local companies were potential competitors. Another potential entrant would be a taxi operator offering a taxi-bus service. In Worthing, for example, a niche operator was using at least six eight-seat taxis, acting as buses and covering roads which were too narrow for Southdown's vehicles.

## Remedies

5.28. We invited Southdown to comment on the hypothetical remedies set out in Appendix 5.1 on the basis that they were possible remedies were the MMC to find that the course of conduct specified in the reference represented an anti-competitive practice from which effects adverse to the public interest might be expected to result. We indicated that it might be found, for example, that the loss of competition from the withdrawal of Easy Rider might be expected to result in higher fares, and lower levels and quality of service, on those routes previously operated by Easy Rider, and on a corridor of within some 200 yards of those routes.

5.29. Southdown responded that it had not at any stage had the intention of restricting competition. The real issue in its view was what it was likely to do in the future, and its understanding of the predatory cycle was that a company had to be able to complete that cycle by making monopoly profits through undue price increases before it could be regarded as exploiting a monopoly position. It considered that an anti-competitive practice should emphasize the likelihood of the predatory cycle being completed, and that any proposed remedies should only be sought if the problems for which they were designed were actually likely to occur.

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<sup>1</sup>See report published by the OFT on 17 February 1988, *The Southern Vectis Omnibus Company Limited—Refusal to allow access to Newport Bus Station, Isle of Wight*.



5.30. Southdown noted that events since the MMC report on the merger of Stagecoach and Formia Ltd<sup>1</sup> had shown clearly that, where Stagecoach had a dominant position, it had not carried out those actions which the MMC had been concerned that it might carry out; in particular it had not lowered service levels and had no power to raise prices. Southdown also drew attention to the fact that, since Easy Rider's departure in May 1992, commercial competitors had entered the local bus market in Havant and Midhurst, and between Chichester and Bosham. The company argued that this showed that entry barriers were low, that the market was contestable, and that any actions which it might have taken had not had any impact on market entry. Moreover, where a previous competitor in Chichester had left the market two years previously, Southdown was still providing services at a higher level than the market warranted, and at a lower fare than that required to make a proper contribution, because the company knew that the local market would not stand an increase in fares or a reduction in service to more realistic levels. In these circumstances Southdown did not believe that it was possible to reach a finding that Southdown had carried out an anti-competitive course of conduct, unless the 'elimination' of Easy Rider itself satisfied the statutory definition. In its own view such a finding would, when accompanied by any of the possible remedies, actually undermine the competitive process.

5.31. Furthermore, Southdown did not consider the likelihood that the hypothetical effects to which the MMC had referred would actually occur to be sufficiently high as to give the MMC adequate reason to seek remedies that would interfere with the market. If the OFT were given a monitoring role, it could act in any case if a problem arose, using the Competition Act or the monopoly provisions of the Fair Trading Act. Southdown noted that any investigation by the OFT into a response to a competitor such as Easy Rider would be misconceived if it simply identified low costs with users' or the public interest, since the user was unaware of the hidden costs of choosing a low-cost option.

5.32. Southdown did not accept that its actions in Bognor Regis had been uneconomic: its additional services in the town had been part of an area-wide improvement in services and, while the position on routes where Easy Rider had operated was obviously complex, the improved services on the other side of Bognor Regis had clearly led to improved patronage. The company would be even more concerned about the possible remedies if the MMC were to examine the economics of its operation on the basis of the limited area, and viability at one point in time, rather than on a longer-term basis.

5.33. On the individual hypothetical remedies set out in Appendix 5.1, Southdown said that (a) would be acceptable as long as it was not unduly onerous, although the company did not believe any of the proposed remedies to be necessary or desirable since the market was fully contestable. It did not regard (b) as acceptable since it would be too restrictive given the level of interworking required to enable a bus network to be run easily; nor did it consider (c) to be a reasonable suggestion since it would merely encourage a new competitor to indulge in a 'hit-and-run' operation, emerging elsewhere to compete with Southdown, which would be inhibited from responding. The company regarded (d) and (e) as imposing totally unacceptable restrictions on its freedom to compete with any new entrants, which would in effect be subsidized. Southdown told us that it would find (f) acceptable provided that the monitoring was not unduly onerous and that it was limited in its geographical scope to the anti-competitive practice described in the report.

5.34. In discussion we sought Southdown's views on a number of alternatives to the hypothetical remedies listed in Appendix 5.1. As a variant of option (b) we suggested that a minimum level of service might be prescribed with the condition that Southdown would not reduce it below the level of services which had prevailed when Easy Rider was operating. Southdown commented that any such proposal would be a form of re-regulation of the market, which it would consider inappropriate. It would also regard as unacceptable a remedy which would prohibit it from responding to a new competitor by adopting the same behaviour which had arguably resulted in the previous competitor's departure. Any remedy which constrained Southdown's ability to respond to the new competition which regularly emerged would make it virtually impossible for the company to run its business.

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<sup>1</sup>Stagecoach (Holdings) Ltd and Formia Ltd: A report on the acquisition by Stagecoach (Holdings) Ltd of Formia Ltd, Cm 1382, December 1990.

Southdown said that the MMC were unlikely to have powers to recommend that it should withdraw from a particular route.

5.35. Finally we put to Southdown hypothetically a combination of remedy (a), controlling fares, and remedy (f), providing for monitoring, which would include the provision of information on route profitability. Southdown confirmed that it would have no practical problem with such a combination provided that there was no widening of the area in respect of which information would be required. However, the fact that it was willing to entertain the possibility of (a) and (f) did not mean to say that it agreed that the MMC should make such a recommendation because it regarded the premises on which all the possible remedies had been based as unsound in the context of the local bus market.

# 6 Conclusions

## The reference

6.1. On 15 July 1992 the Director General of Fair Trading (DGFT) published a report on the registration and operation by Southdown Motor Services Limited (now called Sussex Coastline Buses Ltd, but referred to as Southdown throughout) of two bus services in the Bognor Regis area.<sup>1</sup> Complaints about unfair trading by Southdown had first been made to the Office of Fair Trading (OFT) in March 1991 by the owner of a competing bus company, Easy Rider Minicoaches (Easy Rider). A formal inquiry under section 3(1) of the Competition Act 1980 (the Act) was begun in February 1992. The DGFT's subsequent report concluded that Southdown had been pursuing a course of conduct which constituted an anti-competitive practice, in that it operated routes on an uneconomic basis with the intention of undermining the viability of the operations of a competitor; the course of conduct specified was the registration, operation and charging of uneconomic fares on services 262 and 242.

6.2. Southdown having failed to offer undertakings which he considered satisfactory, the DGFT, in exercise of his powers under section 5 of the Act, made a reference to the MMC on 3 September 1992 (see Appendix 1.1). The reference required the MMC to investigate Southdown's local bus services in the Bognor Regis area, and the course of conduct to be investigated was specified as 'the registration, operation and charging of uneconomic fares on local bus services with the intention of undermining the viability of the operations of a competitor'. Following an application by Southdown for judicial review of the terms of reference, and its determination, the terms of reference were varied on 12 January 1993 under section 6(6) of the Act, and we were required to exclude any course of conduct 'other than the registration, operation and charging of uneconomic fares on routes 262 and 242, or on any route substantially the same as route 262 or 242 operated by Southdown, with the intention of undermining the viability of the operations of a competitor'.

6.3. By virtue of the reference as varied and of section 6(5) of the Act, we are required to investigate and report:

- (a) whether, at any time during the period of 12 months ending on 3 September 1992, Southdown was pursuing, in relation to the services specified, the course of conduct specified in the reference, or any other course of conduct which appears to be similar in form and effect to the one so specified;
- (b) whether, by pursuing such a course of conduct, Southdown was at any time during that period engaging in an anti-competitive practice; and
- (c) whether, if Southdown was engaging in an anti-competitive practice, the practice operated or might be expected to operate against the public interest.

By virtue of section 2(1) of the Act, an anti-competitive practice arises if, in the course of business, a person pursues a course of conduct which has, or is intended to have, or is likely to have the effect of restricting, distorting or preventing competition in connection with the supply or securing of services in the UK or any part of it.

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<sup>1</sup>An investigation under section 3 of the Competition Act 1980 by the DGFT: *Southdown Motor Services Ltd. The registration and operation of services 262 and 242 in Bognor Regis.* Office of Fair Trading, 15 July 1992.

## Background to the reference

### *Southdown*

6.4. Southdown was part of the National Bus Company group until 1987, operating buses in Sussex and East Hampshire, and coach services. In preparation for privatization, Southdown was split up. The bus operation within Brighton and Hove and the engineering services were set up as separate companies, and the remaining part was sold to four of its managers in 1987. It was purchased in August 1989 by Stagecoach (Holdings) Limited, now plc (Stagecoach), one of the largest bus companies in the UK. From April 1991 Southdown was operated as a subsidiary of one of the companies in the Stagecoach group. Following a reorganization in May 1992, Southdown was renamed Sussex Coastline Buses Ltd, and its Eastbourne operation combined with another subsidiary, Hastings & District Transport Ltd, to form a new company, South Coast Buses Ltd—see also Figure 3.1. In 1990 the MMC investigated and reported on the acquisitions by Stagecoach of Portsmouth Citybus Ltd<sup>1</sup> and of Formia Ltd,<sup>2</sup> both involving Southdown.

6.5. As shown in Chapter 3, consolidated turnover of the Stagecoach group was some £103 million in 1990/91, and £141 million in 1991/92; its operating profit (before interest and tax) was some £10.2 million in 1990/91 and £15.2 million in 1991/92. Southdown's turnover was some £9.7 million in 1991/92, with an operating profit (before interest, tax and extraordinary items) of £0.5 million. The Chichester depot, from which Southdown's Bognor Regis services are operated, made only a small operating profit in 1990/91, and—as shown in Appendix 3.4—was unprofitable in the following year, with a turnover of some £1.7 million.

### *Bus services in Bognor Regis*

6.6. Bognor Regis is a town with a population of some 56,000 situated on the coast in West Sussex. At the time of deregulation of the bus industry in October 1986 (see Chapter 2), Southdown operated virtually all bus services in Bognor Regis.

6.7. Of main relevance to our inquiry are the services between the town centre of Bognor Regis and Aldwick and Rose Green to the west of the town, and between the town centre and North Bersted to the north of the town (see Appendices 2.1 and 2.2). At deregulation, Southdown operated half-hourly services on both these corridors, provided by the 245 and the 260 (which continued to Chichester and Midhurst) to Rose Green, and the 246 and 247 to North Bersted. As well as a relatively limited overall level of service, Southdown acknowledged to us that the quality of service under the then management was poor. The scope of services was also limited by the aversion of that management to use of minibuses.

6.8. Southdown told us that a number of firms had attempted to enter the market at deregulation. The company of main relevance to our inquiry is Strikeline Ltd (Strikeline) (which we have referred to by its trade name, Easy Rider) which introduced two services in January 1987: 01 between Bognor Regis High Street and North Bersted, and the 02 between the High Street and Rose Green. Both these services were half-hourly. As is apparent from Appendix 2.1, much of the Easy Rider routes—some 70 per cent—followed those of existing Southdown services, but, by using minibuses, Easy Rider developed 'hail-and-ride' services on roads previously unserved. These roads were within 200 yards of existing Southdown routes, which Southdown argued could still be regarded as overlapping with its existing services. As shown in Table 2.5, the 01 to North Bersted was registered to run some five to eight minutes behind the existing Southdown services; the 02 to Rose Green ran some four to eight minutes ahead of the existing Southdown services. Mr Hunter, the sole shareholder of Strikeline, told us that Easy Rider's routes were registered at times to keep out of Southdown's way; Southdown claimed that in practice Easy Rider tended to run shortly in front of its services. Easy Rider's fares

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<sup>1</sup>Stagecoach (Holdings) Ltd and Portsmouth Citybus Ltd: a report on the acquisition by Stagecoach (Holdings) Ltd of Portsmouth Citybus Ltd, Cm 1130, July 1990.

<sup>2</sup>Stagecoach (Holdings) Ltd and Formia Ltd: a report on the acquisition by Stagecoach (Holdings) Ltd of Formia Ltd, Cm 1382, December 1990.

were initially somewhat below Southdown's. Easy Rider introduced a third service—the 03—to the north-west of Bognor Regis in January 1988. This was less successful, and it was withdrawn in November 1989. In November 1988 it introduced a fourth service—the 04—between Bognor Regis and Pagham.

6.9. Southdown told us that, under its previous ownership, it had adopted a cautious 'wait-and-see' approach to Easy Rider. Various changes were made to Southdown services up to 1990. For example, the 245 was withdrawn in July 1988, with part of the former route to Rose Green operated by the 246, and there were a number of changes in routeings and the introduction of minibuses on services to North Bersted. As shown in Table 2.5, until July 1990 Southdown continued to operate two services per hour on the corridors both to Rose Green and to North Bersted, with the same frequency as Easy Rider's 02 and 01 services.

6.10. In July 1990 Southdown—now a subsidiary of the Stagecoach group—introduced a new minibus service, the 262, on an identical route between Bognor Regis and Rose Green to the Easy Rider 02, and timed about three minutes ahead of the 02. The service covered the costs of drivers' wages, fuel and tyres (the variable costs referred to in the DGFT's report), but made a significant operating loss after taking into account other direct (or 'semi-variable') and indirect (or 'fixed') costs (as defined in paragraph 3.10). Reliability was poor, and the service was withdrawn in December 1990. Since this was more than 12 months before the date of the current reference to us, it is not open to us to consider whether the operation of the 262 could be regarded as a course of conduct constituting an anti-competitive practice.

6.11. In March 1991 Southdown introduced a major revision to bus services in Bognor Regis. The services to North Bersted, now the 244 and 245 which also ran to Middleton and Elmer to the east of Bognor Regis, were doubled to a quarter-hourly frequency. Route 242, the other service specified in the revised terms of reference, was introduced to run half-hourly between Rose Green, Bognor Regis town centre, and North Bersted. The bulk of the 242 served the same route as the Easy Rider 01 and 02 service, including the narrower roads on estates not previously served by Southdown, the services also being timed between one and five minutes ahead of Easy Rider. As shown in Table 3.4, revenues for the 242, some £30,000 in the year to the end of May 1992, fell far short of variable costs (£49,000 over the period). After allowing for semi-variable and overhead costs, there was a loss of some £63,000 over that 12-month period.

6.12. The Easy Rider 01 and 02 services remained unchanged throughout their period of operation. In January 1992 the 04 service was rerouted and extended to Chichester on the route of Southdown's 260 service. Mr Hunter told us that this was because he believed Southdown intended to duplicate his 04 service. Southdown established a service 4, on the original Easy Rider 04 route, but only, it told us, when informed of the change in the Easy Rider service. By spring 1992, therefore, Southdown operated six buses per hour to North Bersted (on the 242, 244 and 245 services), and Easy Rider two buses per hour (on its 01 service). On the routes to Rose Green, Southdown operated four buses per hour on the 260 and 242, and Easy Rider two buses per hour on the 02; Easy Rider also had one bus per hour on its 04 service, as did Southdown on its service 4.

6.13. The fares charged on these services are illustrated in Table 2.9. There were periods in which some Easy Rider single fares were undercut by Southdown and some Southdown return fares were more consistently below those of Easy Rider (although restricted to off-peak periods): in April 1992, for example, the Southdown return fare to Rose Green was £1.10 compared with £1.20 on Easy Rider. Generally Southdown single fares remained slightly above those of Easy Rider. However, Southdown fares were clearly influenced by competition from Easy Rider: increases on those services affected by competition—existing services such as the 244, 245, 250 and 260 as well as the more recent 242 and 262 services—were much lower than on comparable routes where Southdown faced no competition. Southdown told us of a number of occasions on which it had reduced fares, or limited fares increases, because of this competition.

6.14. As shown in Chapter 3, Easy Rider's turnover was £70,000 in 1991/92, with an operating profit of about £3,000. This represented a slight increase in profit on the previous year, but only after a significant reduction in director's remuneration. From July 1991, on the figures we have seen, Easy Rider operated services 01 and 02 at an average loss of about £150 per week (see Appendix 3.6).

6.15. In view of the worsening financial position of his company, Mr Hunter offered the business for sale to Southdown during the period of the OFT inquiry. The vehicles and the goodwill of the Easy Rider operation were sold to Southdown in May 1992 for a substantial sum. No written agreement was signed, but Southdown agreed verbally to maintain the routes for a reasonable period; it also took on some of the staff. Southdown told us that there was no restriction on Mr Hunter re-starting operations; Mr Hunter said that he agreed not to restart the business within one year.

6.16. Following the sale, the duplication between the former Easy Rider and Southdown services was ended on 26 July 1992, the Easy Rider 01 and 02 services being slightly retimed and renumbered 241, and the 242 being withdrawn. The Easy Rider 04 service was deregistered and replaced by an additional through service to Chichester on the 260. Although the number of services was reduced, there remained six buses per hour to North Bersted, and four buses per hour on routes 242 and 260 to Rose Green (plus an additional bus on the 04 which generally serves a slightly different route). Fares on some of the routes on which Easy Rider had competed were increased in June 1992 by 5p (up to 25 per cent on the shortest distances). There were few increases in fares on comparable local services elsewhere in the Bognor Regis area, although some fares on rural services in West Sussex were increased at this time.

6.17. There has subsequently been no change to services or fares on the affected routes. On the last figures available (to January 1993), route 241, the successor to route 242, was covering its variable, but not its semi-variable, cost.

6.18. In October 1992 Southdown started a new service, the 243, between Bognor Regis and West Meads. This service had been operated by Southdown at deregulation, but it had subsequently been operated under tender to West Sussex County Council by Blue Lake Coaches (Blue Lake). Southdown registered the commercial operation of the service when the tender period expired. With Blue Lake's withdrawal from this route, Southdown became the only operator of commercial services in Bognor Regis, except for occasional services into Bognor from west of Chichester, school services, free services operated to and from two local supermarkets, and seasonal services to a local holiday complex.

## **The course of conduct**

6.19. Our terms of reference, as revised, confine us to considering 'the registration, operation and charging of uneconomic fares on routes 262 and 242, or on any route substantially the same as route 262 or 242 operated by Southdown, with the intention of undermining the viability of the operations of a competitor'. Southdown confirmed that it had operated services 262 and 242 as described in the DGFT's report. The operation of route 262, however, fell outside the time-scale relevant to our investigation. We have, therefore, to consider whether by the registration, operation and charging of uneconomic fares on route 242, with the intention of undermining the viability of a competitor, Southdown was engaging in an anti-competitive practice.

6.20. Southdown argued that its operation of route 242 could not be regarded as predatory, as characterized in the DGFT's report. Its views are extensively summarized in Chapter 5. Southdown accepted that, looked at in isolation, route 242 operated on an uneconomic basis. However, it argued that routes could not be looked at in isolation, but were part of the local network, and fares were set for the area as a whole. It did not, therefore, accept that uneconomic fares were charged, nor that the operations as a whole, including the specified routes, were uneconomic. We could not accept this argument. We do not consider that fares could be regarded as set solely on a network basis, given the extent to which account has clearly also been taken of competition on particular routes. We agree that bus networks will have a mix of routes of varying degrees of profitability—as is, indeed, the case with Southdown's Chichester operation in general. Some routes that may appear to be uneconomic will be operated in order to generate revenue for the network as a whole—on return tickets, or through tickets, for example—or to make use of unproductive resources, the level of which is determined by the more profitable services. However, no evidence was provided to us of any significant 'network' benefits from the operation of route 242. On the contrary, Southdown's stated intention was to put pressure on Easy Rider by increasing the frequency of its services.

6.21. Southdown further argued that it was forced to take action to defend itself. It referred to Easy Rider's services as a 'classic creaming operation', abstracting revenue from Southdown's existing services and indeed putting the maintenance of Southdown's entire Chichester-based operation at risk. We cannot accept this argument. We accept that there was substantial duplication between Easy Rider and Southdown's existing service: indeed the geography of Bognor Regis is such that no competitor could develop services in any of the outlying estates without running on the same corridors as Southdown on the route into the town centre. A degree of 'creaming' therefore was an inevitable consequence of competition. Easy Rider, however, provided substantial benefits to passengers when it entered the market. It was the first operator to use minibuses in Bognor Regis, and to develop hail-and-ride services through estates previously served only on the main roads, to the considerable benefit particularly of elderly users. It innovated, therefore, rather than merely duplicated the existing services. Even when it did overlap with Southdown's existing services, it added to frequency and, in the opinion of many passengers who gave evidence to us, provided a better quality of service—for example, helpfulness of drivers—at a time when Southdown's quality of service, in particular reliability and punctuality, was acknowledged to be poor.

6.22. At the time Stagecoach acquired Southdown, Easy Rider was an established operator; through contributing to service improvements since deregulation, it could be regarded as helping to 'create the cream'. This is not, therefore, a case of a new entrant undermining the viability of an existing profitable and efficient operator: but a large operator wishing to enhance his profitability by eliminating an established smaller competitor.

6.23. We can see no economic benefit to users in Southdown, a higher-cost operator, driving out a competing low-cost operator; indeed Southdown's route 241—the amalgam of the previous Easy Rider 01 and 02 services and Southdown's 242 route—is still failing to cover its semi-variable costs or contribute to overheads. Similarly, we find it difficult to regard the mere substitution of Southdown for Easy Rider's lower-cost services as having contributed significantly to the improved viability of Southdown's Chichester operation as a whole.

6.24. Southdown argued that it was entitled to respond vigorously and with all legal means at its disposal to any new entrant: if it did not, it argued, the viability of its network would be threatened because failure to respond would encourage the new entrant to expand, or would induce further entry. There is clearly a difference, however, between a vigorous competitive response, which transmits the benefits of competition to consumers, and a response designed to drive new entrants from the market by running uneconomic services: Southdown indeed told us that it would probably have continued running its extra services at a loss for up to another year. Southdown told us that the only new entry it would not respond against would be entry into niche routes and those Southdown did not wish to serve. If this argument were accepted, it would leave negligible scope for competitors in Bognor Regis, denying consumers there the long-term benefits of competition.

6.25. Southdown also criticized the analysis of motive and intent in the DGFT's report. Motive and intent, Southdown argued, were meaningful only in relation to the incumbent's behaviour after the new entrant had left the market. The report, in its view, contained no evidence of Southdown's intention to put prices up to 'supra-competitive' levels. Indeed Southdown further argued that predation was not feasible in this market, since 'supra-competitive' prices or reductions in frequency would simply encourage new entry into the market, or cause loss of passengers to other forms of travel such as taxis or walking.

6.26. In our view anti-competitive behaviour, as defined in section 2(1) of the Act, does not rely on the characteristics of predatory behaviour put forward by Southdown. We have ourselves seen no evidence that Southdown—or its owner, Stagecoach—aims to make excessive profits on the affected routes: indeed the Bognor Regis local services currently remain loss-making. The benefits of competition are not, however, confined to ensuring that operators do not make excessive profits. Competition also provides a mechanism to ensure lower costs, innovation in service, and an adequate quality of service. The information available to us suggests that Easy Rider was a lower-cost operator, and that it had both innovated and improved the level and quality of service in Bognor Regis. Its removal from the market could, therefore, adversely affect both fares and services, even though Southdown's profits may remain no more than reasonable; it is sufficient for the purposes of this

section that there was a course of conduct that has or was intended to have the effect of preventing, restricting or distorting such competition, whatever the effect on profitability.

6.27. We discuss ‘contestability’—ie the ease of entry into and exit from the market—and the substitutability of bus travel with other forms of transport in evaluating the effect of loss of competition on the public interest, in paragraphs 6.38 to 6.41; we do not accept that either of these factors would be as effective as the previous competition from Easy Rider in limiting fares or profits, or preventing deterioration in levels or quality of service.

6.28. The circumstances of the case can be summarized as follows. The former management of Southdown had neglected services to the north and west of Bognor. Easy Rider had seen the gap in the market, and provided innovation and competition on entering the market in 1987. The two companies had co-existed, although neither had earned substantial profits. Following its acquisition by Stagecoach, Southdown saturated the services with the introduction of the 242, increasing its own frequencies on routes to Rose Green to four per hour, and to North Bersted to six per hour, including the additional frequencies on its other services. The effect on Easy Rider was all the greater by the operation of the service shortly before Easy Rider’s services. There was no increase in demand to justify the new service, or marketing justification; on the contrary, the addition to services from the introduction of the 242 resulted in heavy losses, the service failing even to cover its variable costs, of drivers’ wages, fuel and tyres. The sole purpose was to drive out Easy Rider. A company of the size of Southdown, backed by the considerable resources of the Stagecoach group, is clearly in a position to maintain routes on such an uneconomic basis far longer than a small company such as Easy Rider can sustain the resultant loss of revenue. Although fares on the 242 were the same as on Southdown’s other services on these routes and similar to those charged by Easy Rider, in our view they were clearly uneconomic, in the sense in which that word is used by the DGFT in his report and the reference, in that they did not cover the variable costs referred to above and therefore inevitably made no contribution to general expenses and produced a loss. The extra services, in both their frequency and timing, contributed to the deterioration in Easy Rider’s financial position and were a main cause of its withdrawal from the market, despite its record of lower costs and a quality of service welcomed by many of its passengers.

6.29. We have concluded, pursuant to section 8(2)(a) of the Act, that the operation of route 242 by Southdown in the 12 months up to the reference to us, as we have described in paragraph 6.28, at fares which did not cover costs and in order to drive out Easy Rider, was a course of conduct which falls within the terms of reference, namely the registration, operation and charging of uneconomic fares on that route with the intention of undermining the viability of the operations of a competitor.

6.30. Alternatively, we have concluded that the registration and operation on route 242 of uneconomic services, that is services that did not cover their variable costs referred to above and therefore inevitably made no contribution to general expenses and produced a loss, with that intention, was a course of conduct similar in form and effect to that set out in the reference.

6.31. We find that the course of conduct we have described in paragraph 6.29 is an anti-competitive practice, or alternatively that the course of conduct described in paragraph 6.30 is an anti-competitive practice.

6.32. We conclude therefore that, by pursuing the course of conduct specified in the reference, Southdown was engaging in an anti-competitive practice. We have therefore to consider whether that practice operated or might be expected to operate against the public interest.

### **The effect on the public interest**

6.33. Southdown argued strongly to us that it was not against the public interest to protect existing business from ‘creaming operations’. It believed that it was in the public interest to provide public transport services meeting high quality and safety standards, properly managed, co-ordinated and controlled, and offering a reasonable prospect of continuity. It saw a strong, professional commercial sector as vital for the public transport market and users in the Bognor Regis and Chichester areas: an argument supported by some third parties. Were its services in those areas to be at risk, there



could be a proliferation, it argued, of low-quality operations in those areas from which it withdrew and these markets would be monopolized by low-quality operators. It saw smaller operators therefore as confined to 'niches'—market sectors that small operators could serve better than Southdown.

6.34. The efforts made by Southdown to improve services, particularly since its acquisition by Stagecoach, are clearly to be welcomed. Southdown referred to its recent investment in 40 new buses, of undoubted benefit to users, particularly with their improved ease of access. Within the Bognor Regis area the frequency of services has much improved since 1990, particularly on services from North Bersted to Elmer and Middleton; Southdown also took some pride in improved quality of service such as punctuality and reliability, and its provision of information to users through widely available timetables and information on bus stops; Easy Rider, in contrast, relied on passengers' familiarity with its services and the publication of its timetables in newspapers.

6.35. We do not, however, believe that improvements to services require, or justify, the elimination of effective local competitors such as Easy Rider. As discussed in paragraph 6.21, Easy Rider had itself contributed to improved services in the Bognor Regis area, by seizing the opportunities presented by the shortcomings of Southdown's former management. Although its vehicles were older and may in some ways have been less suitable for passengers than Southdown's current fleet, other aspects of its service—such as the helpfulness of drivers—were clearly appreciated by its users. Such aspects of quality of service should clearly be for users to decide, competition giving users a choice between the services offered by Easy Rider and Southdown.

6.36. As well as the effect on service, competition had a beneficial effect on the level of fares in Bognor Regis. As shown in paragraph 6.13 and Table 2.9, whereas fares on some non-competitive routes in Bognor Regis have risen by up to 60 per cent over the last five years, those on routes in competition with Easy Rider have increased by one-half of that amount, or even fallen, providing a substantial benefit to passengers. Some fares, in consequence, are as much as one-third lower as a result of competition. Since the loss of that competition, some fares have increased; Southdown acknowledged that it might have had difficulty in making such increases had there still been competition. It also confirmed, however, that it would wish to reduce some of the differentials that had emerged as a result of competition over the last five years, although it believed its ability to do so would be limited by the potential for competition from new entry or loss of passengers to other forms of transport.

6.37. In our view, given the significant benefits of competition to fares over the last five years on those corridors where Easy Rider operated, the loss of that competition gives rise to a real risk of fares increases or reductions in frequency to recover the lost ground. The effect of competition on fares was indeed not confined to routes 262 and 242 as specified in the reference, but is also noticeable on Southdown's other services on these corridors—the 260 (as far as Pagham) and 264, the 244 and 245 to North Bersted, and the 250 on Chichester Road, formerly served by Easy Rider en route to North Bersted. Indeed, given Southdown's higher costs, it is difficult to see how undermining the viability of Easy Rider could prove profitable to Southdown unless it were to result in higher fares, or reduced service levels.

6.38. Southdown argued that the overall price elasticity of demand for bus travel and potential competition from new entrants would be sufficient to prevent fares increases following the withdrawal of Easy Rider: indeed, Southdown told us that, for these reasons, the policy of the Stagecoach group was not to increase fares in the current year. We are not confident that such factors would prevent fares increases. The differential fare movements shown in Table 2.9, for example, show that whereas actual competition from Easy Rider held fares increases to the increase in the Retail Price Index (RPI) or below on those corridors on which it operated, fares elsewhere in Bognor Regis tended to increase by above RPI despite the prospect of potential competition from other operators, or competition from other forms of transport.

6.39. Although fares and frequency can affect bus usage to an extent—Southdown indeed told us that increased frequencies on services to the east of Bognor Regis had resulted in increased passenger numbers—in our view alternatives to bus travel are unlikely to prove as effective a constraint on fares or service levels as competition between operators. It may well be profitable for a dominant operator to charge higher fares or provide poorer frequency and carry fewer passengers.

6.40. We also do not accept that the prospect of new entry in this case is sufficient to provide an effective constraint on fares. Although there are few formal barriers to entry to the industry, in our view a major deterrent is the prospect of retaliation by existing operators: the viability of entry will indeed depend, not on the current level of fares or profits on a service, but on the expected level of fares and services following entry, depending on the response of the incumbent.

6.41. There are a number of niche operators but no major bus operators within 20 miles of the Bognor Regis area, and Southdown acknowledged that no major operator was likely to enter the market. Although the possibility of entry cannot be precluded, the risk of retaliation by the incumbent operator makes the viability of entry and hence the prospects of entry, particularly by smaller operators, much more uncertain. The particular action taken against Easy Rider is itself, in our view, likely to deter new entry on to the routes we are considering.

6.42. Southdown's course of conduct on service 242 was a main cause of the withdrawal of Easy Rider, and had the effect of eliminating competition to Southdown not only from Easy Rider's 01 and 02 services, but also from Easy Rider's other service—the 04—at least as far as Pagham. That competition had been to the benefit of passengers both in lower fares and higher levels of service. As we mentioned in paragraphs 6.27 and 6.39, alternatives to bus travel, or the prospects for new entry into the market, are unlikely in our view to prove effective constraints on the levels of fares charged, or of services operated: the action taken against Easy Rider is indeed itself likely to deter entry on to the affected routes. We do not believe that adverse effects have yet occurred—the services have been rationalized, but there has to date been no unreasonable reduction in service levels, nor has the fares increase that has subsequently occurred been on a sufficient scale to be regarded as against the public interest. We consider, however, that the loss of competition from Easy Rider may, in due course, be expected to result in higher fares and lower levels and quality of service than would otherwise have occurred on those routes previously operated by Easy Rider and on the Southdown services currently operating on these routes and the corridors adjacent to such routes.

6.43. We conclude therefore that the anti-competitive practice identified may be expected to operate against the public interest, by reason of the adverse effects identified in paragraph 6.42.

## Remedies

6.44. We are therefore required to consider what action (if any) should be taken for the purpose of remedying or preventing the adverse effects identified in paragraph 6.42. We have not identified any significant adverse effects that have arisen to date, but effects that might be expected to occur in future. It would not therefore be appropriate in the current case to take immediate action to require Southdown to reduce its activities, which could indeed impact adversely on users in the short term.

6.45. We have concluded that loss of competition from Easy Rider may be expected to result in higher fares or lower quality of service on those routes previously operated by Easy Rider, and the corridors adjacent to such routes. Undertakings on fares or service would directly remedy these adverse effects. We therefore recommend that:

- (a) Southdown (by which we refer throughout this section to Sussex Coastline Buses Ltd and any associated company supplying bus services on the affected routes) be required for two years from 17 March 1993 (the date of our report) to limit any increase in fares above the levels charged on that date to the increase in the RPI. This would apply to services on all roads served by Easy Rider, and a corridor of 200 yards around these roads: hence to the present services 244, 245, 250 (as far as Central Avenue, North Bersted), 260 (as far as Pagham) and 264 as well as the 241.
- (b) Southdown undertake that for two years from 17 March 1993 it will not reduce the level of services on the affected routes below that operated by Southdown and Easy Rider together immediately before the introduction of route 242 by Southdown (as illustrated in Table 2.5). This would also apply to services on all roads served by Easy Rider, and a corridor of 200 yards around those roads, as listed above.

6.46. The remedies we have proposed are consistent with Southdown's expectation that it could not increase fares, and its statement that it currently had no plans to reduce service. The minimum level of service we have put forward is indeed below the current level of services on routes to North Bersted, which benefited also from the increase in frequency on routes other than the 242: we have no reason to believe Southdown would reduce services to this level, but our recommendation would prevent a more significant reduction to the service levels prevailing before Easy Rider entered the market. Southdown argued that any such requirement on service levels would be both unnecessary and restrictive: we regard it as fully justified to ensure that users do not lose the benefit which competition from Easy Rider brought to the market. Such a remedy would clearly be limited in duration, but to go beyond a two-year period would seem unreasonable, given the possibility of changes in the pattern of demand requiring adjustment of services.

6.47. We acknowledge, however, that neither of the remedies suggested above may be regarded as fully adequate for the adverse effects we have identified: the time-scale of any such requirements imposed on Southdown must be limited, since circumstances can change significantly. In our view, therefore, the measures outlined above should be supplemented by a requirement that Southdown undertake to submit regular reports to the DGFT on changes in fares or levels of service and on the profitability of the routes affected, and in the Bognor Regis area generally for purpose of comparison. It would also be desirable that similar information on levels of fares and services should be submitted to West Sussex County Council.

6.48. We considered a number of other possible remedies, summarized in Appendix 5.1, with a view to preventing a similar course of conduct in future. In the present case, however, confined to a limited number of routes, any similar situation could be easily identified and action taken without the need to put any such further measures in place at the present time.

6.49. We have, however, drawn attention in previous reports to the limited powers to stop or deter an anti-competitive course of conduct. The current case, where the matter was referred to us only after Easy Rider had withdrawn from the market, illustrates in our view the benefit of a provision for interim relief during investigation of alleged anti-competitive behaviour.

M S LIPWORTH (*Chairman*)

A FERRY

J S METCALFE

D MILLER

S N BURBRIDGE (*Secretary*)

17 March 1993

APPENDIX 1.1  
(referred to in paragraphs 1.1 and 6.2)

**The reference**

1. On 3 September 1992 the DGFT sent to the MMC the following reference:

The Director General of Fair Trading has published a report under section 3 of the Competition Act 1980 ('the Act') stating in accordance with section 3(10) of the Act that a course of conduct pursued by Southdown Motor Services Limited, now called Sussex Coastline Buses Limited ('Southdown'), constitutes an anti-competitive practice and that it is appropriate for him to make a reference to the Monopolies and Mergers Commission ('the Commission') under section 5 of the Act. The Director General of Fair Trading has not accepted from Southdown any undertaking which covers the course of conduct described in the report as constituting an anti-competitive practice. Therefore in the exercise of his powers under section 5 of the Act he hereby makes a reference to the Commission as follows:

- (a) the person whose activities are to be investigated by the Commission is Southdown;
- (b) the services to which the investigation is to extend are local bus services in the Bognor Regis area (that is to say the area shown on the map on page 8 of the report);
- (c) the course of conduct to be investigated is the registration, operation and charging of uneconomic fares on local bus services with the intention of undermining the viability of the operations of a competitor.

A report on this reference is to be made within the period ending on 18th December 1992.

*(signed)* BRYAN CARSBURG  
Director General of Fair Trading  
Date 3 September 1992

2. Following an application by Southdown for judicial review of the reference, the Secretary of State for Trade and Industry granted the MMC a further period, until 17 March 1993, for the submission of a report on the reference. The High Court heard the application on 18 November 1992 and ruled on 11 January 1993 that the OFT had extended the inquiry unlawfully: once the terms of an investigation under the Act had been set by reference to a specific geographic area it could not be widened in making the reference to the MMC. Therefore on 12 January 1993 the DGFT sent to the MMC the following variation to the reference which restricted the investigation on the course of conduct to routes 262 and 242 (or any route substantially the same as these):

**VARIATION UNDER THE COMPETITION ACT 1980 SECTION 6(6)  
OF A REFERENCE UNDER SECTION 5(1)**

Whereas:

(1) on 15th July 1992 the Director General of Fair Trading ('the Director General') published a report ('the report') under section 3(10) of the Competition Act 1980 ('the Act') stating that a course of conduct pursued by Southdown Motor Services Ltd, now called Sussex Coastline Buses Ltd ('Southdown'), constituted an anti-competitive practice and that it was appropriate for him to make a reference to the Monopolies and Mergers Commission ('the Commission') under section 5(1) of the Act;

(2) the Director General did not accept from Southdown any undertaking under section 4(3) of the Act which covered the course of conduct described in the report as constituting an anti-competitive practice; and

(3) on 3rd September 1992 the Director General in exercise of his powers under section 5(1) of the Act made a reference to the Monopolies and Mergers Commission specifying:

- (a) the person whose activities were to be investigated by the Commission as Southdown;
- (b) the services to which the investigation was to extend as local bus services in the Bognor Regis area (that is to say the area shown on the map on page 8 of the report);
- (c) the course of conduct to be investigated as the registration, operation and charging of uneconomic fares on local bus services with the intention of undermining the viability of the operations of a competitor;

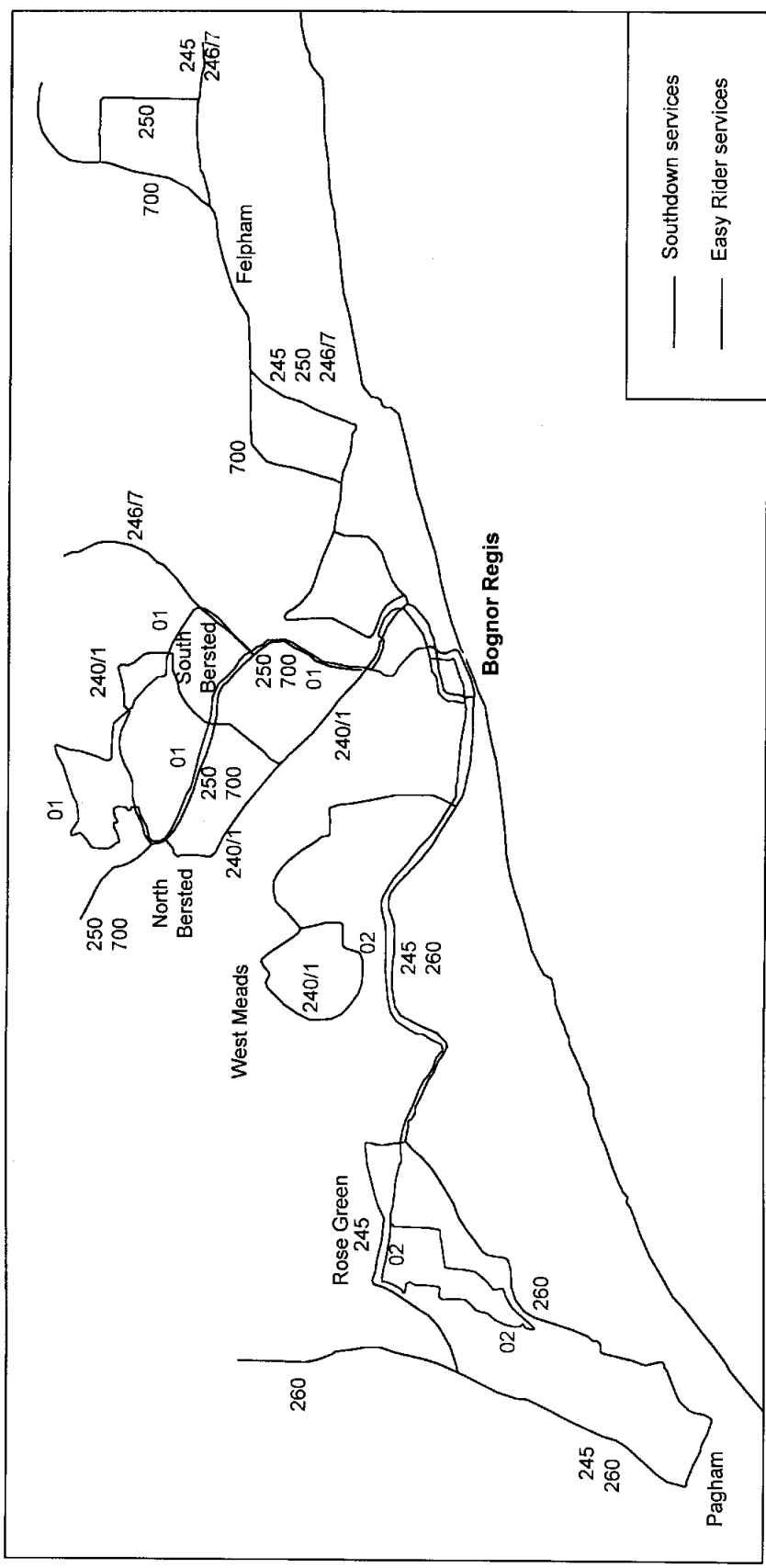
Now therefore the Deputy Director General of the Office of Fair Trading, having been authorised by the Director General under paragraph 7 of Schedule 1 to the Fair Trading Act 1973, in exercise of the power under section 6(6) of the Act hereby restricts the scope of the said reference by excluding any course of conduct other than the registration, operation and charging of uneconomic fares on routes 262 and 242, or on any route substantially the same as route 262 or 242 operated by Southdown, with the intention of undermining the viability of the operations of a competitor.

*(signed)* J W PRESTON  
*Deputy Director General of the Office of Fair Trading*  
12 January 1993

3. The composition of the Group of members responsible for the present investigation and report is indicated in the list of members in the preface.
4. Notices inviting interested parties to submit evidence to the MMC were placed in the *Chichester Observer*, *Bognor Regis Observer*, *Bognor Guardian* series, *Coach & Bus Week* and *Bus & Coach Buyer*.
5. We received written evidence from West Sussex County Council, Bognor Regis Town Council, two parish councils, Mr Ian Hunter (the proprietor of Easy Rider), Sussex Bus, another bus company in Sussex, South Yorkshire Transport, the Bus and Coach Council, the National Federation of Bus Users and 17 members of the public.
6. We received written submissions from Southdown and the company attended two hearings. We also held hearings with West Sussex County Council, Mr Hunter, Sussex Bus and the National Federation of Bus Users.
7. We would like to thank all those who helped in our inquiry.

APPENDIX 2.1  
 (referred to in paragraphs 2.1, 2.27, 6.7 and 6.8)

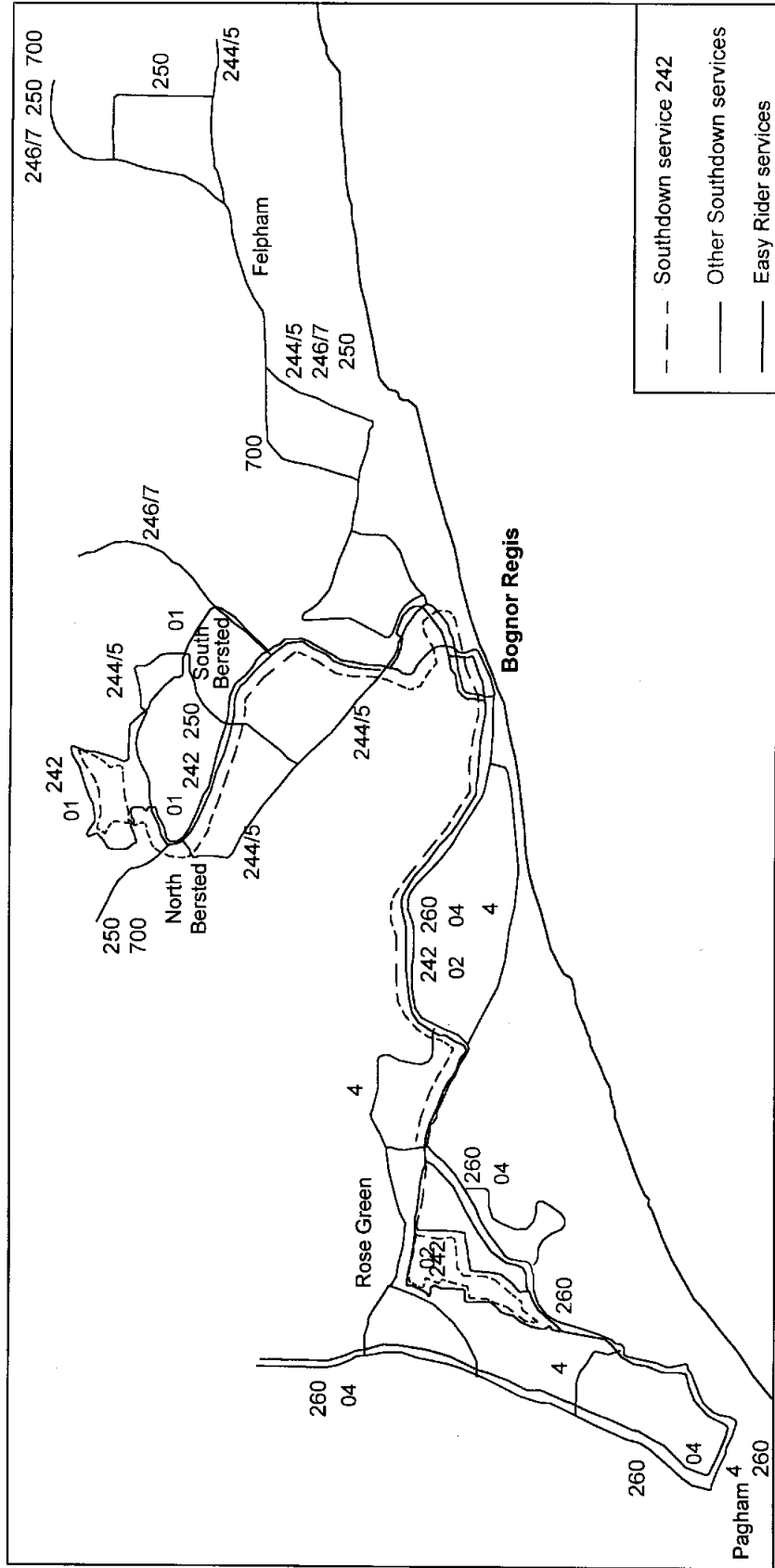
**Southdown and Easy Rider services, January 1987**



Source: Southdown.

APPENDIX 2.2  
*(referred to in paragraphs 2.22 and 6.7)*

**Southdown and Easy Rider services, end April 1992**



Source: Southdown.

APPENDIX 3.1  
(referred to in paragraph 3.4)

**Southdown: profit and loss accounts for the five years to 30 April 1992**

	£'000				
	Year to 25 April 1988 and 1989 and 30 April thereafter				Sussex Coastline
	Southdown				
	1988	1989	1990	1991	1992
Turnover	13,138	12,102	12,565	8,050	9,733
Other operating income	334	467	407	645	214
Operating costs	(12,946)	(13,538)	(13,218)	(8,001)	(9,464)
Amortization of goodwill	<u>0</u>	<u>0</u>	<u>(35)</u>	<u>3</u>	<u>(1)</u>
Operating profit/(loss) before interest, tax and extraordinary items	526	(969)	(281)	697	482
Interest payable and similar charges	(133)	(125)	(138)	(206)	(72)
Profit/(loss) on ordinary activities before taxation	393	(1,094)	(419)	491	410
Taxation (charge)/credit	<u>41</u>	<u>363</u>	<u>87</u>	<u>0</u>	<u>0</u>
Profit/(loss) on ordinary activities after taxation	434	(731)	(332)	491	410
Extraordinary items	<u>0</u>	<u>0</u>	<u>(470)</u>	<u>(1,139)</u>	<u>0</u>
Profit/(loss) for the financial year	434	(731)	(802)	(648)	410
Retained profit/(loss) at beginning of year	38	1,172	441	(361)	(633)
Transfer from revaluation reserve	2,700	0	0	376	0
Dividend paid	<u>(2,000)</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>
Retained profit/(loss) at end of year	1,172	441	(361)	(633)	(223)

Source: Southdown.

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*Note:* Southdown stated that the extraordinary items in 1990 and 1991, which included loss from and on disposal of discontinued operations, reorganization costs and amounts written off investments less provisions made on acquisition, would now have to be reported as operating costs under Financial Reporting Standard number 3.



APPENDIX 3.2  
(referred to in paragraphs 3.6 and 3.7)

**Southdown: balance sheets for the five years to 30 April 1992**

	Year to 25 April 1988 and 1989 and 30 April thereafter Southdown				Sussex Coastline
	1988	1989	1990	1991	1992
	£'000				
Tangible fixed assets	2,634	2,585	5,622	3,656	3,191
Stock and debtors less creditors other than borrowings	<u>3,024</u>	<u>3,056</u>	<u>(3,045)</u>	<u>(1,270)</u>	<u>(1,264)</u>
Capital employed	5,658	5,641	2,577	2,386	1,927
Investments	22	108	1,422	1,552	1,545
Goodwill	0	0	1,170	26	24
Borrowings net of cash	<u>(532)</u>	<u>(1,621)</u>	<u>(1,578)</u>	<u>(947)</u>	<u>(119)</u>
Net assets	5,148	4,128	3,591	3,017	3,377
Share capital and reserves	4,772	4,041	3,389	2,967	3,377
Provisions for liabilities and charges	<u>376</u>	<u>87</u>	<u>202</u>	<u>50</u>	<u>0</u>
Net equity	<u>5,148</u>	<u>4,128</u>	<u>3,591</u>	<u>3,017</u>	<u>3,377</u>
Average capital employed	<u>6,533</u>	<u>5,650</u>	<u>4,109</u>	<u>2,482</u>	<u>2,157</u>
Gearing (borrowings net of cash as a percentage of net equity)	10.3	39.3	43.9	31.4	3.5

Source: Southdown.

APPENDIX 3.3  
(referred to in paragraph 3.7)

**Southdown: balance sheets for the five years ended  
25 April 1988 to 30 April 1992 restated by Stagecoach**

	£'000				
	<i>Years ended 25 April 1988 and 1989 and 30 April thereafter</i>				
	1988	1989	1990	1991	1992
Fixed assets	2,634	2,585	5,622	3,656	3,191
Land and buildings not included above	<u>3,771</u>	<u>3,710</u>	<u>9,601</u>	<u>6,203</u>	<u>6,203</u>
Fixed assets employed	<u>6,405</u>	<u>6,295</u>	<u>15,223</u>	<u>9,859</u>	<u>9,394</u>
Stock and debtors less creditors other than borrowings	3,024	3,056	(3,045)	(1,270)	(1,264)
Adjusted to remove inter-company debtors	(3,328)	(3,030)	(5,316)	(2,293)	(81)
Adjusted to remove inter-company creditors	-	-	<u>7,185</u>	<u>2,967</u>	<u>1,151</u>
	<u>(304)</u>	<u>26</u>	<u>(1,176)</u>	<u>(596)</u>	<u>(194)</u>
Revised capital employed	6,101	6,321	14,047	9,263	9,200
Average capital employed	6,754	6,211	10,184	11,655	9,232
Operating profit/(loss) before interest and tax	526	(969)	(281)	697	482
				<i>per cent</i>	
Return on capital employed (operating profit/(loss) as a percentage of average capital employed	7.8	(15.6)	(2.8)	6.0	5.2
				<i>£'000</i>	
Investments	22	108	1,422	1,552	1,545
Goodwill	0	0	1,170	26	24
Borrowings net of cash	(532)	(1,621)	(1,578)	(947)	(119)
Sub-total	(510)	(1,513)	1,014	631	1,450
Net assets = net equity	5,591	4,808	15,061	9,894	10,650
				<i>per cent</i>	
Gearing (borrowings net of cash as a percentage of net equity)	9.5	33.7	10.5	9.6	1.1

Source: Stagecoach.

APPENDIX 3.4  
(referred to in paragraphs 3.13, 3.16 and 6.5)

**Profitability of Southdown routes in Chichester area, including Bognor Regis**

	Costing periods ended:														Year to			£'000		
	22.6.	20.7.	17.8.	14.9.	12.10.	9.11.	7.12.	4.1.	1.2.	29.2.	28.3.	30.4.	30.5.	end	27.6.	25.7.	22.8.			
	91	91	91	91	91	91	91	92	92	92	92	92	92	May 92	92	92	92			
<b>Route 242</b>																				
Revenue	1.5	1.8	2.0	2.1	2.2	2.2	2.4	2.3	2.4	2.5	2.5	2.9	3.3	30.1	4.4	5.0	6.1			
Direct costs	7.0	6.1	6.6	6.5	6.7	6.7	6.5	6.3	6.6	6.6	6.3	7.2	6.8	86.0	6.1	6.2	6.6			
<i>Of which variable</i>	3.8	3.8	3.9	3.8	3.8	3.8	3.7	3.6	3.4	3.7	3.7	4.2	3.9	49.1	3.5	3.4	3.7			
Contribution	(5.4)	(4.3)	(4.6)	(4.5)	(4.5)	(4.5)	(4.1)	(4.1)	(4.2)	(4.1)	(3.8)	(4.3)	(3.5)	(55.9)	(1.7)	(1.2)	(0.6)			
Overhead	0.4	0.4	0.3	0.4	0.3	0.4	0.5	0.5	0.6	0.7	0.6	1.1	0.7	6.8	0.8	0.9	1.0			
Profit/(loss)	(5.9)	(4.7)	(4.9)	(4.8)	(4.8)	(4.9)	(4.6)	(4.6)	(4.8)	(4.8)	(4.4)	(5.3)	(4.2)	(62.7)	(2.5)	(2.1)	(1.6)			
<i>Profit as % revenue</i>	(378)	(257)	(250)	(232)	(222)	(225)	(190)	(202)	(202)	(194)	(173)	(181)	(127)	(208)	(57)	(43)	(27)			
<b>Route 244</b>																				
Revenue	10.7	12.4	12.2	12.0	12.4	12.5	12.7	11.3	11.2	11.9	12.2	14.0	14.0	159.5	14.2	14.8	14.5			
Direct costs	14.9	13.1	14.0	14.0	14.3	14.4	13.9	13.5	14.4	14.5	13.9	15.9	15.1	186.0	13.6	13.6	14.6			
<i>Of which variable</i>	8.4	8.2	8.5	8.3	8.2	8.3	8.1	7.8	7.7	8.3	8.3	9.6	8.8	108.4	7.9	7.7	8.5			
Contribution	(4.2)	(0.7)	(1.9)	(2.0)	(1.9)	(1.9)	(1.2)	(2.1)	(3.2)	(2.6)	(1.7)	(1.9)	(1.1)	(26.5)	0.6	1.2	(0.2)			
Overhead	2.5	2.3	1.9	1.9	1.8	2.2	2.4	2.3	2.6	3.0	2.6	4.6	2.7	32.9	2.4	2.6	2.3			
Profit/(loss)	(6.7)	(3.0)	(3.8)	(3.9)	(3.6)	(4.1)	(3.6)	(4.4)	(5.8)	(5.6)	(4.4)	(6.5)	(3.7)	(59.5)	(1.8)	(1.4)	(2.5)			
<i>Profit as % revenue</i>	(63)	(24)	(31)	(33)	(29)	(33)	(29)	(39)	(52)	(47)	(36)	(46)	(27)	(37)	(13)	(10)	(17)			
<b>Route 250</b>																				
Revenue	32.5	31.5	32.2	32.9	39.0	34.4	35.2	27.7	18.5	17.7	18.1	18.1	17.4	355.1	17.5	15.7	12.4			
Direct costs	29.5	25.1	27.3	27.2	27.9	27.8	26.9	25.6	10.1	10.0	9.6	10.9	10.4	268.4	9.3	9.3	10.7			
Contribution	3.0	6.4	4.9	5.7	11.1	6.5	8.3	2.1	8.3	7.8	8.4	7.2	7.0	86.7	8.2	6.4	1.7			
Overhead	7.0	5.8	5.2	5.2	5.0	5.5	6.3	5.0	3.1	3.2	2.8	4.6	2.6	61.5	2.3	2.5	1.8			
Profit/(loss)	(4.0)	0.6	(0.3)	0.4	6.0	1.0	1.9	(2.9)	5.2	4.5	5.7	2.6	4.4	25.2	5.9	3.9	(0.04)			
<i>Profit as % revenue</i>	(12)	2	(1)	1	15	3	5	(10)	28	25	31	14	25	7	34	25	0			
<b>Route 260</b>																				
Revenue	34.2	34.7	32.6	34.5	40.5	38.8	39.5	30.5	34.2	33.8	34.9	33.5	37.9	459.7	37.3	36.4	34.5			
Direct costs	29.0	25.1	27.1	27.5	27.7	27.7	26.8	25.7	22.6	22.3	21.6	25.4	24.8	333.3	21.7	21.7	25.3			
Contribution	5.2	9.6	5.5	7.0	12.8	11.1	12.7	4.8	11.6	11.5	13.4	8.1	13.1	126.4	15.6	14.6	9.3			
Overhead	6.6	5.6	4.9	5.1	4.9	5.5	6.2	5.2	6.1	6.6	5.6	9.0	5.5	76.8	4.8	5.4	5.2			
Profit/(loss)	(1.4)	4.0	0.7	1.9	7.9	5.5	6.5	(0.4)	5.5	4.8	7.7	(0.8)	7.6	49.6	10.8	9.3	4.1			
<i>Profit as % revenue</i>	(4)	12	2	6	19	14	17	(1)	16	14	22	(2)	20	11	29	25	12			
<b>Route 4</b>																				
Revenue	-	-	-	-	-	-	-	-	0.9	1.1	1.2	1.5	1.8	6.5	2.0	2.3	2.0			
Direct costs	-	-	-	-	-	-	-	-	3.3	3.3	3.2	3.6	3.4	16.8	3.1	3.1	3.3			
Contribution	-	-	-	-	-	-	-	-	(2.4)	(2.2)	(2.0)	(2.1)	(1.6)	(10.3)	(1.0)	(0.8)	(1.3)			
Overhead	-	-	-	-	-	-	-	-	0.2	0.3	0.3	0.6	0.4	1.8	0.4	0.4	0.3			
Profit/(loss)	-	-	-	-	-	-	-	-	(2.7)	(2.5)	(2.3)	(2.6)	(2.0)	(12.1)	(1.4)	(1.2)	(1.6)			
<i>Profit as % revenue</i>	-	-	-	-	-	-	-	-	(311)	(229)	(191)	(172)	(109)	(177)	(70)	(54)	(78)			
<b>Easy Rider routes 01/04</b>																				
Revenue	-	-	-	-	-	-	-	-	-	-	-	-	2.1	2.1	3.7	3.9	-			
Direct costs	-	-	-	-	-	-	-	-	-	-	-	-	6.9	6.9	10.2	9.6	-			
Contribution	-	-	-	-	-	-	-	-	-	-	-	-	(4.8)	(4.8)	(6.5)	(5.6)	-			
Overhead	-	-	-	-	-	-	-	-	-	-	-	-	0.4	0.4	0.7	0.8	-			
Profit/(loss)	-	-	-	-	-	-	-	-	-	-	-	-	(5.2)	(5.2)	(7.2)	(6.4)	-			
<i>Profit as % revenue</i>	-	-	-	-	-	-	-	-	-	-	-	-	(249)	(249)	(195)	(162)	-			
<b>Other Chichester area</b>																				
Revenue	36.8	40.3	50.4	42.5	44.3	42.7	43.2	34.8	55.9	56.1	57.7	70.2	62.6	637.5	65.0	72.3	77.2			
Direct costs	36.2	31.6	34.1	34.1	35.1	35.1	34.9	32.4	50.9	50.2	48.5	54.0	50.8	527.8	45.3	45.5	45.9			
Contribution	0.7	8.7	16.3	8.4	9.3	7.6	8.3	2.3	4.9	5.9	9.2	16.2	11.8	109.8	19.7	26.8	31.3			
Overhead	6.6	5.8	6.6	5.5	4.8	5.4	6.0	5.3	10.3	11.6	9.7	17.1	9.7	104.2	9.0	9.5	10.8			
Profit/(loss)	(6.0)	2.9	9.7	3.0	4.5	2.2	2.3	(3.0)	(5.4)	(5.7)	(0.5)	(0.9)	2.1	5.5	10.7	17.3	20.5			
<i>Profit as % revenue</i>	(16)	7	19	7	10	5	5	(9)	(10)	(10)	(1)	(1)	3	1	17	24	26			
<b>Chichester area total</b>																				
Revenue	115.8	120.8	129.3	123.9	138.4	130.5	133.0	106.5	123.0	123.2	126.6	140.3	139.1	1,650.5	144.1	150.4	146.7			
Direct costs	116.6	101.0	109.0	109.3	111.7	111.8	108.1	103.5	108.0	106.9	103.2	117.0	118.2	1,424.3	109.3	109.0	106.5			
Contribution	(0.7)	19.8	20.3	14.6	26.7	18.7	24.9	3.0	15.0	16.2	23.5	23.3	20.9	226.2	34.8	41.4	40.2			
Overhead	23.3	19.9	18.9	18.1	16.8	19.0	21.5	18.3	23.0	25.5	21.7	36.9	21.9	284.8	20.4	22.2	21.5			
Profit/(loss)	(24.0)	(0.1)	1.4	(3.4)	9.9	(0.3)	3.4	(15.3)	(8.0)	(9.3)	1.8	(13.6)	(1.0)	(58.6)	14.4	19.2	18.8			
<i>Profit as % revenue</i>	(21)	0	1	(3)	7	0	2	(14)	(6)	(7)	1	(10)	(1)	(4)	10	13	13			

Source: MMC study from information provided by Southdown.

Note: The various routes are as follows: 242 Bognor Regis local service—the subject of the OFT report, fully in competition with Easy Rider. 244 Bognor Regis local service—the North Bersted section of which was in competition with Easy Rider. 250 Chichester–Bognor–Littlehampton, limited overlap with Easy Rider on approach to Bognor. 260 Midhurst–Chichester–Pagham–Bognor, in competition with Easy Rider between Pagham and Bognor. 01/04 Easy Rider ceased operation 17.5.92; its services were run by Southdown until 26.7.92 when amalgamated with other services. Other Chichester area: Chichester–Witterings; Chichester–Selsey; Chichester local (including temporary service to Bosham); tendered service around Bognor; limited stop Portsmouth–Chichester–Bognor–Brighton; and Chichester–Goodwood Races.

APPENDIX 3.5  
(referred to in paragraph 3.22)

**Strikeline: sources and application of funds for the  
three years ended 30 March 1990**

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	<i>Year ended 30 March</i>		
	1988	1989	1990
<i>Source of funds</i>			
Funds generated from operations:			
Profit/(loss) before tax	946	(1,450)	1,717
Items not involving the movement of funds:			
Depreciation	14,107	10,837	7,465
Adjustment on disposal of fixed assets	<u>0</u>	<u>0</u>	<u>2,754</u>
Total generated from operations	15,053	9,387	11,936
Funds from other sources			
Issue of shares	998	0	0
Working capital movements:			
Increase in creditors	4,842	0	0
Increase in bank overdraft	0	2,574	0
Reduction in debtors	<u>0</u>	<u>219</u>	<u>136</u>
Total sources	<u>20,893</u>	<u>12,180</u>	<u>12,072</u>
<i>Applications</i>			
Purchase of fixed assets	16,861	1,093	0
Working capital movements:			
Reduction in creditors	0	11,742	11,558
Reduction in bank overdraft	3,199	0	328
Increase in debtors	<u>27</u>	<u>0</u>	<u>0</u>
Total applications	20,087	12,835	11,886
Movement in cash balance, increase/(decrease)	806	(655)	186

Source: Strikeline.

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*Note:* Strikeline's Annual Reports and Accounts state that it did not prepare a funds flow statement in 1990/91 or a cash flow statement in 1991/92 as it took advantage of the exemption offered by Financial Reporting Standard number 1.

APPENDIX 3.6

(referred to in paragraphs 3.24, 3.26, 5.5 and 6.14)

Revenue and cost comparison from June 1991 to May 1992

	Southdown route 242		Easy Rider routes 01 and 02	
	Average per week £	Average per mile ppm	Average per week £	Average per mile ppm
Average miles per week		1,680		1,671
Average operating hours per week		123		123
PVR (mini)		2		2
		Average per hour £ph		Average per hour £ph
Fares	510	30.3	1,147	68.7
Seasons tickets etc	23	1.4	44	2.6
Tenders	0	0.0	0	0.0
Total revenue	533	31.7	1,191	71.3
Variable costs				
Drivers' wages	853	50.8	614	36.8
Bus operating costs	80	4.7	88	5.3
Total	933	55.5	702	42.0
Contribution to semi-variable costs	(400)	(23.8)	489	29.3
Semi-variable costs				
Maintenance	330	19.7	266	15.9
Other operating costs	268	15.9	0	0.0
Depreciation	109	6.5	118	7.1
Total	707	42.1	384	23.0
Contribution to fixed costs	(1,107)	(65.9)	106	6.3
Fixed costs				
Depot overheads	87	5.2	109	6.5
Company overheads	26	1.6	144	8.6
Total	113	6.7	253	15.1
Operating profit/(loss)	(1,220)	(72.6)	(147)	(8.8)

Source: OFT from information provided by Southdown and Mr Hunter.

## APPENDIX 5.1

(referred to in paragraphs 5.28, 5.33, 5.34 and 6.48)

### Possible remedies on which the MMC sought Southdown's views

- (a) Southdown (by which we also refer to its successor company, Sussex Coastline Buses Ltd, and any associate company involved in bus services on the affected routes) be required to limit fares increases on those routes affected to the increase in the RPI for two years, from May 1992 before the withdrawal of Easy Rider. This would apply to services on all roads served by Easy Rider, and a corridor of 200 yards around these roads: hence to the present routes 244, 245, 250 (as far as Central Avenue, Bersted), 260 (as far as Pagham) and 264, as well as the 241.
- (b) Southdown undertake to maintain the levels of service operated by Southdown for two years, from May 1992 before the withdrawal of Easy Rider. This would also apply to services on all routes served by Easy Rider, and a corridor of 200 yards around those routes, as listed above. It would, for example, require Southdown to maintain six services per hour to South Bersted, four services per hour to Rose Green via Aldwick Road, plus the one service per hour on the present route 04, within the hours of operation of these services in May 1992.
- (c) In order to protect any further new entrants from retaliation in the form of temporary reductions in fares or increases in frequency, Southdown undertake that, should it reduce fares or increase frequencies against a new entrant on the affected routes, fares should not be increased relative to RPI, nor frequencies reduced for a two-year period should the competitor withdraw. Such an undertaking should last for [five] years from the date of Easy Rider's withdrawal in May 1992, and similarly apply to those roads previously served by Easy Rider, and to a corridor within 200 yards of those roads and to the services listed above. Southdown should, however, be able to seek release from any such undertakings should there be any material change in circumstances on the affected roads.
- (d) [Alternative to (c)] At the time the undertakings to maintain fares and frequency expire, Southdown should in our view be allowed to establish fares and frequencies at what it considers a competitive level but only if moves are taken to ensure that if a new entrant wishes to start a new service, action will not be taken against him. Similar measures could also apply to the period of the above undertakings. Southdown should further, therefore, undertake that should a competitor commence services on the affected routes at any time within the next five years, Southdown will not reduce fares, nor increase frequencies from the levels prevailing [two months] before the commencement of such services, at least until the expiry of the five-year period.
- (e) As an alternative to (a) to (d): Southdown should, we believe, be free to adjust its fares or services in the short term but only if moves are taken to ensure that if a new entrant wishes to start a new service, action will not be taken against him. Southdown should undertake that should a new entrant commence services on the affected routes as listed above at any time within [five] years starting in May 1993, it will not reduce fares nor increase frequencies from the levels prevailing [two months] before the commencement of such services, at least until the expiry of the five-year period.
- (f) The measures outlined above should be supplemented by an undertaking by Southdown to submit regular reports to the OFT and West Sussex County Council on changes in fares or levels of service, on the routes affected and in the Bognor Regis area generally, for purpose of comparison. Should monitoring of these reports reveal any abuse by Southdown of its monopoly position on the routes affected, it would be open to the Director General to consider the use of other powers available under the Fair Trading Act.





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