

## **Menzies/Aviation Services**

### **Summary of provisional findings**

**Notified: 14 December 2018**

#### **Summary of provisional findings**

1. On 14 August 2018 the Competition and Markets Authority (CMA), pursuant to section 22 of the Enterprise Act 2002 (The Act), referred the completed acquisition by John Menzies plc (through its subsidiary Menzies Aviation (UK) Limited) (Menzies), of part of the business of Airline Services Limited (the Merger) for further investigation and report by a group of CMA Panel members.
2. In exercise of its duty under section 35(1) of the Act, the CMA must decide:
  - (a) whether a relevant merger situation has been created; and
  - (b) if so, whether the creation of that situation has resulted, or may be expected to result, in a substantial lessening of competition (SLC) within any market or markets in the United Kingdom (UK) for goods or services.
3. The statutory deadline for preparing and publishing our report is 28 January 2019.
4. We refer to Menzies and Airline Services collectively as ‘the Parties’.

#### **Background: the Parties and the industry in which they operate**

5. Menzies is a global supplier of aviation services, including ground handling services. It operates in 36 countries. In 2017, it earned £1,273.6 million in revenues in relation to aviation services worldwide. Menzies is listed on the main market of the London Stock Exchange. Menzies Aviation operates at 15 airports in the UK and provides ground handling, de-icing, aircraft presentation, cargo handling and cargo forwarding services to airlines.

6. Airline Services operates solely in the UK. It provides de-icing and aircraft presentation services at 16 UK airports. Airline Services provides ground handling services at only two UK airports, London Gatwick and Manchester. In the year ended 30 April 2017, Airline Services generated £34.9 million in turnover.
7. Prior to the Merger, Airline Services' largest investor was Lloyds Development Capital (LDC), the private equity arm of Lloyds Banking Group plc.
8. The Parties overlap in:
  - (a) Ground handling services, which comprise ramp and baggage handling, passenger services, and other related tasks involved in servicing the arrival and departure of an aircraft;
  - (b) De-icing services, which comprise the removal and prevention of build-up of ice on wings and fuselage;
  - (c) Aircraft presentation, which comprises cleaning, exterior washing and other cabin services.
9. The Parties overlap in ground handling services at London Gatwick (LGW) and Manchester (MAN). They also overlap in de-icing services at London Heathrow (LHR), Edinburgh (EDI) and Glasgow (GLA) airports (the 'overlap airports'). The overlap in aircraft presentation is only at MAN and is very limited. Therefore, aircraft presentation was not considered further.
10. The customers for these services are international and regional airlines operating at UK airports.

## **The transaction and the relevant merger situation**

### **The transaction**

11. John Menzies plc through its wholly owned subsidiary Menzies Aviation, acquired part of the business of Airline Services Limited (ASL), namely that in relation to de-icing, aircraft presentation and ground handling (Airline Services). There were a number of other bidders for Airline Services.
12. The Merger was implemented by means of an asset purchase agreement between ASL and Menzies Aviation on 4 April 2018, pursuant to which Menzies Aviation acquired all the relevant assets, contracts and employees relating to Airline Services.

## **The rationale for the transaction**

13. Airline Services was sold as it was owned by a private equity investor and the sale was part of the investment process.
14. Menzies stated that the Merger offered it an opportunity to expand its de-icing and aircraft presentation offerings, expand its geographical coverage in the UK and deepen its customer relationships at airports around the UK.

## **The relevant merger situation**

15. We found that as a result of the Merger, the Parties ceased to be distinct and that the share of supply test was met. We therefore provisionally concluded that a relevant merger situation had been created based on the share of supply test.

## **Counterfactual**

16. We assessed the overall financial position of Airline Services prior to the Merger and whether, had Menzies not bought Airline Services, it would have continued to provide a competitive constraint, either under alternative ownership or on a standalone basis.
17. Whilst the private equity investor which owned Airline Services had decided to exit its investment, there were alternative bidders for the business and there is no evidence that Airline Services would have exited the market in the absence of the Merger. We have therefore provisionally found that the counterfactual for Airline Services is the prevailing conditions of competition, with Airline Services under the ownership of one of the other bidders in the sale process, although it is not possible to say which bidder was most likely to acquire Airline Services.
18. We considered whether Menzies would continue to provide a competitive constraint to Airline Services at all of the overlap airports. Taking into account the available evidence, our provisional finding is that the counterfactual for Menzies is the prevailing conditions of competition at the time of the Merger, with Menzies continuing to operate and compete for customers at all overlap airports.

## **Theories of harm**

19. In this inquiry, we have focused on the following theories of harm:
  - (a) Loss of existing competition in ground handling services at LGW and MAN.

- (b) Loss of existing competition in de-icing services at LHR, EDI and/or GLA.
- (c) Loss of potential competition in ground handling services at UK airports.
- (d) Loss of potential competition in de-icing services at UK airports.
- (e) Potential foreclosure concerns.

## **Market definition**

20. The purpose of market definition in a merger inquiry is to provide a framework for the analysis of the competitive effects of the merger. The boundaries of the market do not determine the outcome of the analysis of the competitive effects of the merger.
21. Some airlines tender for bundled contracts involving ground handling and de-icing services. Some airlines may purchase those services across a network of airports. Our provisional view is that we do not need to define either a separate bundled ground handling/de-icing product market and/or de-icing network product market, but that we have taken the purchasing preferences of airlines into account in our assessment of competitive effects.
22. We have also considered whether self-supply of ground handling and/or de-icing should be considered as part of the relevant product market. While we note that self-supply, particularly for ground handling, may be an option for some airlines, we did not consider self-supply to be within the relevant product market. However, we considered the role of self-supply in our assessment of the competitive effects of the Merger.
23. In relation to the geographic market, we found that airlines tend to contract on the basis of a single airport for ground handling. It is more frequent for airlines to contract de-icing services across multiple UK airports, but many still contract on a single airport basis. In addition, the number and identity of suppliers of de-icing and ground handling services varies across UK airports. We therefore provisionally found that an airport-level geographic market is appropriate for both ground handling and de-icing. With respect to de-icing services at LHR, we considered whether the different terminals at which independent de-icing suppliers operate (that, is Terminals 2, 3 and 4) may be separate markets, but find that this is not the case because providers are able to operate across these terminals.
24. We have provisionally concluded that there are separate product markets for:

- (a) the supply of baggage, ramp, passenger and airside cargo handling services (together, ground handling services); and
  - (b) the supply of de-icing services
- 25. We have provisionally concluded that the appropriate geographic market is at an airport level.

## **Competitive assessment**

### **Analytical framework**

- 26. For both ground handling and de-icing service contracts, airlines seek bids from providers or they may choose to roll-over the contract with an existing provider. Providers may not be aware of the identity of rival bidders and will not usually know the value of the bids of rivals when bidding. In this situation, a provider must form expectations of the likely strength of rivals' bids based on the information available. Market shares and the results of previous tenders, as well as which firms competed (where known), may be used by bidding firms to assess the likely strength of rivals' bids. If a supplier has won recent tenders, this rival may be more likely to bid strongly for future tenders. As such, this supplier may provide a strong competitive constraint on rivals. Therefore, we used information on recent tenders and market shares in our assessment of the Merger.
- 27. On the other hand, past performance, as reflected in market shares and the outcomes of previous tenders, may not reflect competitive constraints exerted by suppliers not currently at the airport. Nor may market shares necessarily offer a full picture of the competitive conditions at the airport, particularly where suppliers serve different segments of the market. In addition, market shares which have changed significantly over time may be less useful in assessing the competitive constraint exerted by suppliers at an airport. Therefore, we did not use market shares and tender results mechanistically.
- 28. We also considered the competitive constraints which may arise from credible bidders not currently at the airport and from expansion by other suppliers currently at the airport. Related to this, we considered whether barriers to entry and expansion are sufficiently low such that entry and expansion may take place rapidly, thus increasing the constraint on current providers.

### **Ground handling at LGW**

- 29. LGW is the second-largest airport in the UK. The supply of ground handling services at LGW has changed in recent years. In 2016 Aviator, a large ground handler, exited the airport at short notice. Following this, BA, a major operator

at LGW, moved to self-supply as did Aurigny, a much smaller operator. Norwegian Air moved to a hybrid model of self-supply through a subsidiary, RED, which owns the equipment and manages the service, but is supplied with staff by a third-party provider, Omniserv. More recently, easyJet (the largest operator at LGW) adopted a variant of the hybrid model by contracting with DHL.

30. In addition, there are four independent suppliers of ground handling at LGW of which Menzies and Airline Services are the largest with substantially higher shares of supply than the two, Swissport and dnata. These shares are higher if the self-supply and hybrid models described above are excluded.
31. Concerns were raised about the Merger by some third parties that the Merger would remove important options for airline customers; in particular because the two other independent ground handlers at LGW, Swissport and dnata, may not be able to replace the competitive constraint of Airline Services.
32. We have found that competition at LGW is characterised by a recent history of entry, exit, and expansion, as well as substantial moves to different models of self-supply at LGW. There has also been significant entry by new providers serving hybrid models. We consider that this history of entry, expansion and exit is important when assessing the competitive constraints on the Parties. In particular, we consider that the threat of further entry and expansion is likely to provide a strong competitive constraint on the Parties. This view is supported by our assessment of barriers to entry and expansion, which we do not consider to be large.
33. Our engagement with other ground handlers not currently at LGW indicated that there were a number of credible bidders who have either already bid for contracts at LGW, or who would bid for attractive contracts in future.
34. Our tender analysis indicated that the Parties were involved in airline tenders more frequently than Swissport and dnata, but that no contracts had switched between the Parties in the last three years. We also observed that both Swissport and dnata have been growing and winning new contracts since their entry at LGW.
35. In relation to the position of smaller airlines, we observe that contracts with such airlines may be particularly attractive to incumbent ground handlers when their flight schedules fit with the schedule of flights already served by the ground handler. In this case, additional customers can be served without materially additional resources. Both Swissport and dnata have taken on contracts for airlines with relatively small operations at LGW. In addition, we

are aware that there are a number of tenders up for renewal in the next 12-24 months which may provide an attractive opportunity for entry.

36. Taking all this evidence into account, in particular the likelihood of new entry and expansion at LGW, we have provisionally concluded that the Merger has not resulted in, and may not be expected to result in, an SLC in the market for ground handling services at LGW.

### **Ground handling at MAN**

37. MAN is the busiest airport in the UK outside of London. In addition to the Parties, there are currently five other independent ground handlers at MAN. Self-supply and hybrid models are less prevalent than at LGW. Menzies is the second largest supplier of ground handling services at MAN, after Swissport. However, it has lost some major contracts recently. One of these contracts was to Airline Services, which led to Airline Services entering MAN in 2018. More recently, Menzies lost the easyJet contract to DHL, another new entrant.
38. The loss of the contract to Airline Services indicates that the Parties compete against each other. They have also been both involved in a small number of other tenders at MAN. One airline raised concerns about how the Merger would reduce their options and concerns that Menzies' ownership of Airline Services may lead to a reduction in the quality of service.
39. However, following the loss of the easyJet contract, the combined shares of supply of the Parties are not particularly high. There are also five other ground handlers operating at MAN: Swissport, Aviator, dnata, Premiere Handling and DHL. We consider that these alternative ground handlers will provide a competitive constraint on the merged entity.
40. In addition, there has also been recent entry at MAN; for example by Airline Services, DHL and Premiere Handling. Other ground handlers have expressed an interest in entering MAN if profitable opportunities arise, and some of these ground handlers have already bid on contracts at the airport. We consider these ground handlers to be credible suppliers and that further new entry is likely.
41. Taking all this evidence into account, we have provisionally concluded that the Merger has not resulted in, and may not be expected to result in, an SLC in the market for ground handling services at MAN.

### **De-icing services at LHR**

42. LHR is the largest airport in the UK. BA is the largest airline at LHR and self-supplies de-icing services. The independent de-icing providers at LHR are

Menzies, Airline Services, Aero Mag, and Cobalt. Menzies, Airline Services and Aero Mag are of roughly similar size at LHR, while Cobalt is considerably smaller.

43. The high shares of supply of each of the Parties may indicate that they place a strong competitive constraint on each other. In addition, some airlines raised concerns about the impact of the Merger on competition at LHR, observing that there were already limited options in terms of de-icing providers.
44. De-icing services are only required by airlines during the colder months of the year (October to April) but even then are only needed when the temperature drops sufficiently. Aircraft spending the night at the airport (night-stopping) have the most need, as temperatures drop overnight. We have also been told that LHR is one of the warmest airports in the UK, affecting the demand for de-icing services. Airlines have tended to contract on a 'pay-as-you-use' basis. This dependency on the weather and the mode of compensation makes revenues from de-icing services uncertain.
45. Menzies and Cobalt both provide ground handling services at LHR, alongside de-icing services. Menzies also supplies de-icing on a stand-alone basis to some customers. Cobalt only supplies de-icing services to customers for which it also supplies ground handling, but it does not supply de-icing services to all its ground handling customers. Airline Services and Aero Mag do not supply ground handling services at LHR.
46. Airline Services tends to serve airlines with night-stopping aircraft or those with larger operations at LHR (far more so than Menzies). In addition, many of Menzies' current contracts at LHR are bundled with full, or partial, ground handling services. Airline Services does not provide any ground handling services at LHR and therefore does not bid for such bundled contracts.
47. These factors indicate that, although both the Parties supply de-icing contracts, there is some difference in their focus with Airline Services focussing more on night-stopping aircraft and de-icing only contracts, in contrast to Menzies for whom these customers are less important than customers seeking bundled ground handling and de-icing contracts.
48. The tender analysis we undertook showed that the Parties were both involved in very few tenders since January 2016 on which we gathered data. On only one of these tenders, a very small tender for one flight every three days, the Parties bid head-to-head. On the other, Menzies chose not to bid and there were two other bidders. In addition, there were no instances of contracts being switched between the Parties in the last three years. Therefore, it

appears that there has been very limited competitive interaction between the Parties.

49. It appears that Aero Mag has been a stronger competitive force at LHR in recent years than the constraint provided by each of the Parties on the other. Aero Mag entered in 2013 and quickly grew. Aero Mag told us that it is interested in expanding at LHR, and does not see barriers to entry, although it would only bid for profitable opportunities.
50. Cobalt does not plan to grow its de-icing service at LHR and only supplies de-icing services to airlines which also use Cobalt for ground handling services. We do not consider Cobalt to provide a strong competitive constraint.
51. Overall, the evidence indicates that the Parties compete only to a very limited extent at LHR, and that Aero Mag provides a stronger competitive constraint on each for de-icing only contracts. Notwithstanding this provisional assessment, we considered the prospects for entry and/or expansion, as well as any countervailing buyer power which may exist post-Merger.
52. We considered barriers to entry at LHR. Similar to ground handling services, the absolute costs of entry are not particularly high – it would be necessary to have at least two rigs, trained staff, and a location where to store de-icing fluid. We have seen examples of entry, including sponsored entry, of de-icing providers in the UK. Aero Mag's entry at LHR was facilitated by the airport operator; IDS's entry at London Luton was supported by easyJet; and Menzies has recently entered into GLA after securing a contract with IAG at that airport. Nonetheless, the uncertainty of revenues may not make entry attractive unless the provider wins a large contract or is confident of winning many small contracts. We also see far fewer instances of entry than we observe in relation to ground handling services at LGW and MAN.
53. Our engagement with other de-icing suppliers not currently at LHR indicated that there are one or two credible potential bidders for de-icing contracts at LHR and that we would expect bidding by one or more of these credible bidders for large de-icing contracts at LHR but that entry for smaller scale contracts is less likely.
54. We also considered whether self-supply might be an option for airlines at LHR where BA currently self-supplies. While we are aware of other airlines self-supplying de-icing services at other airports, including through the use of hybrid models (Ryanair at London Stansted and Norwegian Air at LGW), we consider that self-supply is likely to be an option only for airlines for whom LHR is a major base.

55. Taking all this evidence into account, we have provisionally concluded that the Merger has not resulted in, and may not be expected to result in, an SLC in the market for de-icing services at LHR. In reaching this provisional conclusion, we placed significant weight on the evidence that there is very limited competitive interaction between the Parties.

### **De-icing services at EDI and GLA**

56. We note that there are many similarities between these two airports: both have the same three current de-icing suppliers (Swissport, Airline Services, Menzies); the tender data shows a similar pattern of bidding; and a number of comments from the Parties and third parties apply equally to both airports.
57. Both EDI and GLA are small to medium sized airports. There is currently no self-supply by airlines of de-icing services at either EDI or GLA. Two airlines raised concerns about the impact of the Merger on the supply of de-icing services at these airports.
58. The Parties have high shares of supply at both EDI and GLA. However, our analysis of tenders, market shares and switching of contracts indicates that the Parties do not appear to compete for de-icing contracts at either GLA or EDI.
59. At both airports, all of Menzies' contracts are for a bundle of ground handling and de-icing services whereas, at both airports, all of Airline Services' contracts are for de-icing services only, covering a network of UK airports. There have been no instances since January 2016 of contracts switching between the Parties at either airport.
60. Our tender analysis indicated no examples of both Parties being involved in the same tender. Moreover, Swissport appears to be a closer competitive constraint to each of the Parties than they are to each other.
61. Overall, the evidence indicates that the Parties do not compete at EDI or GLA. Notwithstanding this provisional assessment, we considered the prospects for entry and/or expansion, as well any countervailing buyer power which may exist post-Merger.
62. The main constraint on entry appears to be a lack of profitable opportunities to enter, which may require contract with sufficient scale and/or alongside the offer of other services. We note that EDI and GLA are both significantly smaller than LHR, and as such their respective de-icing markets may not be large enough to support a greater number of de-icing suppliers. This may therefore discourage entry. On the other hand, we note that EDI and GLA are

both colder airports than LHR. Colder weather implies that airlines will have a greater demand for de-icing services.

63. Our engagement with other de-icing suppliers not currently at EDI or GLA indicated that there were some who were interested in entering these airports provided there are suitable commercial opportunities. One noted the cold weather, and hence greater demand for de-icing, these airports experience. Menzies' recent entry into GLA to serve the IAG contract there indicates that entry with a relatively small operation is possible. We also noted the credible prospect of sponsored new entry at EDI and GLA.
64. Taking all this evidence into account, we have provisionally concluded that the Merger has not resulted in, and may not be expected to result in, an SLC in the market for de-icing services at EDI or GLA. In reaching this provisional conclusion, we placed significant weight on the lack of evidence of any existing competition between the Parties.

### **Loss of potential competition & foreclosure concerns**

65. We have also considered whether the Merger would be likely to result in a loss of potential competition at UK airports where the Parties do not currently overlap in ground handling or de-icing services.
66. In relation to Airline Services, our provisional view is that, whilst Airline Services had a general ambition to expand into new airports to provide ground handling services, the overall evidence suggests that any such expansion, if it had occurred, would have been incremental and limited in scope. Considering the evidence in the round, we do not consider that the loss of any potential entry by Airline Services would be such as to lead to an SLC in the supply of ground handling at additional UK airports.
67. In relation to Menzies, our provisional view is that, absent the Merger, Menzies would not have sought to enter additional UK airports to provide stand-alone de-icing services. In addition, we consider that Menzies was unlikely to enter additional UK airports to deliver de-icing services itself (alongside any 'bundled' ground handling services) as Menzies would have continued to focus on ground handling and out-sourcing any de-icing requirements to Airline Services. Accordingly, our provisional assessment is that the Merger will not lead to an SLC in the supply of de-icing at additional UK airports.
68. Lastly, we considered whether the Merger may lead to foreclosure of competitors through the merged entity not offering sub-contracted de-icing services (as Airline Services does now). When looking at the available

evidence, we considered that the merged entity is unlikely to have the ability or the incentive to foreclose competitors.

### **Provisional findings**

69. We have provisionally concluded that the Merger has not resulted in, and may not be expected to result in, an SLC in relation to ground handling or de-icing services in the UK.