

Summary of provisional findings

1. On 3 August 2004 the Office of Fair Trading referred the proposed acquisition by Arriva plc of the business of the Hertfordshire bus operator, Sovereign Bus & Coach Company Ltd (Sovereign), to the Competition Commission for investigation and report. The reference was made under section 33(1) of the Enterprise Act 2002 (the Act). We are required to publish our final report by 17 January 2005.
2. Arriva plc provides local bus services in Hertfordshire through two subsidiary companies, Arriva The Shires Limited (ATS) and Arriva East Herts & Essex Limited (AEHE), operated together under the trading name 'Arriva the Shires & Essex' (we refer to ATS and AEHE collectively as 'Arriva'). Arriva has five depots in Hertfordshire, at Hitchin and Stevenage in north Hertfordshire, Watford and Hemel Hempstead in south-west Hertfordshire and Ware in east Hertfordshire. The depot at Stevenage is held on a lease due to expire at the end of 2007 and Arriva understands that the lease will not be renewed by the landlord. Arriva has the right to terminate the lease early, in December 2005, and proposes to exercise this right if the merger goes ahead. Arriva's objective through the proposed merger is to increase profitability and its service offering to customers, but it stated that this increase in profitability was in no way contingent upon any increase in fares.
3. Sovereign is a wholly-owned subsidiary of Blazefield Holdings Limited (Blazefield), a privately-owned company operating bus services mainly in Yorkshire and Lancashire. Within the last two to three years Blazefield has disposed of all of its bus operations in London and the Home Counties apart from Sovereign; the St Albans business of Sovereign was sold to Centrebus Limited (Centrebus) in January 2004. Sovereign currently operates six commercial bus services, including an inter-urban service, linking Hitchin, Stevenage, Welwyn Garden City, Hatfield, St Albans and Hemel

Hempstead, and a Stevenage town centre service. Sovereign's commercial and tendered services are operated from leased depots in Stevenage and Hatfield. The lease for the Stevenage depot is due to expire in 2022 whilst the (informal) lease for that part of the Hatfield depot used by Sovereign is subject to three months' notice to/from Universitybus Limited (Universitybus).

4. Under a business sale agreement announced on 23 June 2004, ATS is to acquire from Sovereign and Blazefield the assets of the Sovereign business, including 46 vehicles. Total consideration was less than £5 million. Completion of the transaction is conditional on any regulatory outcome being satisfactory to Arriva and on written consent from the landlord of the Stevenage depot authorizing Blazefield to sublet it to Arriva.
5. The acquisition would result in the enterprises concerned ceasing to be distinct and we found that, as Arriva already accounts for over 25 per cent of the supply of bus services in Hertfordshire, a share which will be increased as a result of the merger, the share of supply test was satisfied in respect of a substantial part of the UK for the purposes of the Act. The parties did not contest this. We concluded that arrangements are in progress which, if carried into effect, will result in the creation of a relevant merger situation.
6. We defined the relevant markets affected by the proposed merger to be the supply of bus services on point-to-point journeys and broader network markets in Hertfordshire which, for fare-paying passengers, are no wider than the six towns linked by Sovereign's inter-urban service and their surrounding areas. It is appropriate to segment these markets between commercial and tendered services; with respect to the latter, network markets include not only the six towns and surrounding areas but also the county of Hertfordshire as a whole.

7. Both the parties and a number of third parties, including Hertfordshire County Council (HCC), explained to us that Hertfordshire was not 'good bus territory', mainly due to the general prosperity, dispersed population and relatively high level of car ownership within the county, as well as the fact that some of the towns with which we were concerned, such as Welwyn Garden City and Stevenage, were specifically designed around the car. In addition, there are labour and depot shortages, and higher costs, arising in part from the proximity of London. There was also a decline in bus passenger numbers.
8. Of the 30 bus operators listed by HCC, many provide only tendered services; currently, the main operators of commercial services in Hertfordshire apart from Arriva and Sovereign are Centrebus, Universitybus and Transit Group (operating primarily in Stevenage). As a result of the merger, Arriva's overall share of commercial services, which has remained more or less stable over the last four years, would rise from 55 to 70 per cent and its total share of commercial and tendered services from 51 to 63 per cent (both measured by registered mileage within Hertfordshire). Market concentration in all Hertfordshire districts is already high and, in those (few) districts where Sovereign currently operates, the merger would give rise to significant increments in concentration, particularly in Stevenage.
9. Were the merger not to go ahead (the counterfactual), Blazefield, we concluded, would continue the Sovereign business, albeit in a reorganized form to increase its profitability to a level in line with the rest of the Blazefield group. Arriva would maintain its current services in the relevant markets and would remain in occupation of its current Stevenage depot until the end of 2007. Thereafter Arriva would operate the services based there from its other Hertfordshire depots.

10. At the individual route level, any head-to-head competition between Arriva and Sovereign is confined to flows on parts of Sovereign's routes, overlaps which to a substantial extent occur as an unintended effect of road configuration (for example, a single road into a town centre). The parties told us that they had never in any event set out to compete with one another by design. We identified (as did Arriva) 31 overlap flows between Arriva and Sovereign services. Our analysis confirmed that there is no material direct competition between Arriva and Sovereign on most of these flows and that on the remainder there is effective competition from third parties. We do not therefore expect the merger to result in a substantial lessening of competition (SLC) due to any loss of actual competition on individual flows.
11. As regards potential competition in commercial services, three of us did not expect the merger to result in any SLC. Arriva and Sovereign have not in the past sought to compete directly with each other, and the three of us did not expect the position to change in the future, particularly given Blazefield's plans to reorganize Sovereign's operations if the merger did not proceed. The three did not believe that an alternative owner would take a different approach. In addition, the three accepted Arriva's continuing need to maintain and improve the quality of its services in order to achieve its long-term aim of attracting new passengers on to buses from their cars.
12. In the view of the other two of us, however, Sovereign is currently and, in the absence of the merger, would continue to represent an important competitive constraint obliging Arriva to maintain its standards of performance, customer service and fare levels broadly in line with Sovereign's (and vice versa). Further, the presence of a business with a combination of the size, quality and profitability of a restructured Sovereign would, in the view of the two of us, provide a key opportunity for a competitor to enter the market at the scale necessary to provide more effective

competition to Arriva. On both of these grounds, the two expected the elimination of Sovereign through the merger to give rise to an SLC in bus markets in Hertfordshire.

13. As to competition in tendered services, HCC considered that there was enough competition on the whole, whilst recognizing that, on a localized basis, predominantly in the Stevenage area, Sovereign was one of Arriva's main competitors in this market. The three of us mentioned in paragraph 11 noted that there were relatively few occasions on which the only bidders were Arriva and Sovereign and further that Blazefield intended to reorganize Sovereign's operations if the merger did not proceed. The three further noted the overall lack of concern on the part of HCC in particular, and also that in the period that we reviewed there had been over 30 bidders for HCC contracts and barriers to entry into tendered services were relatively low. Accordingly the three concluded that the merger may not be expected to give rise to an SLC in relation to tendered services.
14. The other two of us, however, believed that Arriva would be in a position to win contracts with higher bids than would be the case without the merger. The two were concerned that there were three contracts for which Arriva and Sovereign were the only bidders; that in 16 out of 22 cases where both tendered a bid, one of them was awarded the contract; and that between them the parties held a substantial share of contracts in the Stevenage area. Hence the two expected the merger to result in an SLC due to the elimination of Sovereign as a major competitor for tendered services contracts awarded by HCC.
15. We took the view that in Hertfordshire there is a shortage of existing depot facilities of a particular type, namely those adequate for the needs of an operator with more than about ten buses, and that this is exacerbated by local authority planning restrictions. However, smaller operators appear to be able to find suitable sites for their needs.

The three of us mentioned in paragraph 11 did not believe that the merger would affect the position. In the view of the other two of us, the lack of depot facilities represents a significant barrier to entry or expansion in Hertfordshire; and Arriva's enhanced ability to redeploy buses from its Hertfordshire depots as a result of the merger, aggravated by this lack of depots, would result in a deterrent to potential entrants. The two accordingly concluded that the merger may be expected to result in an SLC in bus markets in Hertfordshire due to the raising of barriers to entry or expansion.

16. In summary, the majority of us concluded that the proposed merger may not be expected to result in an SLC within any market in the UK for goods or services.