

**Compass Group PLC
and
Rail Gourmet Holding AG,
Restorama AG and Gourmet Nova AG**

A report on the merger



COMPETITION COMMISSION

Compass Group PLC and Rail Gourmet Holding AG, Restorama AG and Gourmet Nova AG

A report on the merger

**Presented to Parliament by the Secretary of State for
Trade and Industry by Command of Her Majesty
July 2002**

Members of the Competition Commission as at 17 June 2002

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¹These members formed the Group which was responsible for this report under the chairmanship of Mrs D P B Kingsmill. Mr M R Webster ceased to be a member of the Group on 23 April 2002 as he was unable for a substantial period to perform his duties as a member of the Group. The conclusions in this report are those of the remaining members of the Group.

Note by the Department of Trade and Industry

In accordance with section 83(3) and (3A) of the Fair Trading Act 1973, 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 she considers would not be in the public interest to disclose and which, in her opinion, would seriously and prejudicially affect certain interests.

The omissions are indicated by a note in the text or, where space does not permit, by the symbol ✂.

Contents

	<i>Page</i>
Part I—Summary and Conclusions	
<i>Chapter</i> 1	Summary3
2	Conclusions.....7
Part II—Background and evidence	
3	The acquisition and the companies concerned..... 19
4	The market..... 39
5	The views of Compass..... 61
6	Views of other parties..... 85
	List of signatories 101
<i>Appendices</i>	(The numbering of the appendices indicates the chapters to which they relate.)
1.1	The reference and background 103
3.1	Compass: profit and loss account..... 105
3.2	Compass: balance sheet 106
3.3	Compass: cash flow 107
3.4	RGUK: profit and loss account 108
3.5	RGUK: balance sheet 109
3.6	RGUK: cash flow 110
3.7	RGUK: revenue and contribution by contract—excluding Eurostar 111
	Glossary 113

Part I

Summary and Conclusions

1 Summary

Introduction

1.1. On 26 March 2002, the Secretary of State for Trade and Industry referred to the Competition Commission (CC) for investigation and report under the merger provisions of the Fair Trading Act 1973 the proposed acquisition by Compass Group PLC (Compass) of Rail Gourmet Holding AG, Restorama AG and part of Gourmet Nova AG. Compass completed the final stage of its acquisition of the companies on 5 April 2002. Our terms of reference are at Appendix 1.1. We were required to report by 17 June 2002.

1.2. This reference to the CC followed the notification of the proposed acquisition of these companies to the European Commission under Article 9 of the European Community Merger Regulation. The European Commission cleared this transaction on 26 February 2002, except in respect of that part of the acquisition which related to the supply of on-train food services in the UK. This was referred to the competent UK competition authorities.

1.3. The companies acquired by Compass were part of the Swissair group. We established that only Rail Gourmet UK Limited and Rail Gourmet Waterloo International Limited (RGUK), the UK subsidiaries of Rail Gourmet Holding AG, had any involvement in the supply of on-train food services in the UK, and our investigation was therefore only concerned with the impact that the acquisition of RGUK would have on the supply of on-train food services in the UK.

1.4. On-train food services consist of procuring food and drink and supplying it to the trains (logistics), and serving it to passengers on the trains (on-board catering service). The services provided on the trains are of two kinds: a full meals, buffet and trolley service (MBT) on main or longer routes, and a trolley-only service. Both are backed up by a logistics service.

1.5. Following the privatization of rail services in the UK, there was a management buyout in 1995 of the On Board Services division of British Rail, which had provided all the on-train food services. This was renamed European Rail Catering (ERC). During the privatization process the on-board catering staff providing MBT services transferred to the train operating companies (TOCs), while ERC remained responsible for the logistics, including the operation of trolley-only services. ERC, together with its initial contracts with the TOCs, was acquired by Rail Gourmet Holding AG in 1997. Contracts are now renegotiated or retendered by the TOCs in relation to their own franchises. RGUK still holds the contracts to supply most of the TOCs with logistics and trolley services. It has also held the contract to provide logistics to support the food service on Eurostar since 1992. We found that its share of these logistics and trolley service contracts by value was about 80 per cent.

1.6. Compass has previously acquired one small logistics contract (with Scotrail) giving it about 3 per cent of the value of these contracts. It also has a 49 per cent interest in a joint venture with Cremonini to provide on-board catering services for Eurostar. We found that this service was essentially different from the logistics and trolley service contracts. We therefore

concluded that the effect of the acquisition was to increase the share of supply of the merged entity from 80 to 83 per cent.

1.7. Our inquiry focused on the question whether the acquisition would create any barriers to entry for a competitor wishing to provide on-train food services. This is essentially a bidding market. Any increase in share of supply would not be the critical factor in determining the effect on competition, but rather any increase in market power in relation to competitors and to the TOCs letting the contracts.

1.8. We looked at the existing competitive constraints. It appeared that there had been a number of new entrants to provide trolley services, including relatively small operators compared with RGUK. However, there had, so far, been less competition for the larger contracts to provide logistics for MBT services, which made up the bulk of the market value. One of these contracts had been won by a competitor, Sodexho UK, and a number of others are expected to be tendered in the next two to three years. We found little interest among potential competitors in bidding for these contracts, although in principle there are a large number of suppliers of general food and logistics services who could be in a position to provide these services. We concluded that this was partly because the market had not yet fully developed from its origins in a nationalized monopoly supplier. There were also perceptions of difficulties in dealing with the rail industry. A major factor could be uncertainty about profitability, especially given the risk involved in dependency on rising passenger numbers, affected by rail crashes in recent years.

1.9. It was clear that the TOCs have considerable market power in relation to any supplier, as they set all the conditions for the supply of the service, control the facilities, insist on open book contracts and retain the possibility of bringing the logistics supply in-house. The TOCs see provision of food services as part of their own brands, and there is no scope for any supplier to develop their own brands or provide alternatives. We concluded that the competitive constraints described above, and in particular the tight control exercised by the TOCs over the conditions under which on-train food is supplied, could discourage a firm wishing to bid for a contract.

1.10. We considered whether the acquisition created further barriers to entry. Although RGUK had some competitive advantages as the experienced incumbent, this was dependent on the TOCs' continued satisfaction with its service rather than any intrinsic market power. The acquisition of RGUK by Compass made no difference to this position.

1.11. Compass does, however, have a large share of the supply of food on railway stations, with about 62 per cent of the concessions let by Railtrack and the TOCs, under a number of brand names. We considered whether this would give Compass increased market power in relation to TOCs or competitors in respect of the on-train food service. This could be the case if it were able to affect the pricing of on-train food, or close off access from competitors. However, its share of station concessions is falling as the stations are opened up to more competition by Railtrack and the TOCs. The product ranges for on-train and on-station food only overlap to a limited extent, and it would be physically very difficult to combine the support operations. Above all, we concluded that the conditions which the TOCs attach to the use of service centres would prevent Compass from using its on-station concessions to block competitors for the provision of the on-train food service.

1.12. We therefore concluded that the acquisition by Compass of RGUK will not in itself discourage other potential competitors from bidding for the on-train food service contracts, or give rise to opportunities for the combined entity to exercise market power in a way which would be detrimental to competition.

1.13. We concluded that the acquisition does not operate against the public interest. In doing so, we noted that more might be done, in the interest of the consumers of railway food, to

encourage the TOCs to innovate, and to bring more players into the provision of food on trains, with a view to increasing quality and variety, and improving the creativity with which this aspect of their business is managed. We noted that the Strategic Rail Authority (SRA) has said that it could consider requiring operators to retender their contracts for on-board catering more frequently to try to encourage growth in the number of players in the market. We suggest that the SRA should consider constructive ways to ensure that there is more frequent competition to provide more innovative on-train food services.