

Anticipated acquisition by Bretagne-Angleterre-Irlande S.A of certain assets used by P&O Ferries on its Portsmouth to Le Havre service

The OFT's decision on reference under section 33 given on 7 December

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Please note square brackets indicate exact figure replaced by a range at the parties' request.

**PARTIES**

1. **Brittany Ferries (Bretagne-Angleterre-Irlande S.A. (BAI))** operates a fleet of seven ferries between France and the UK and Ireland respectively, and between the UK and Spain. BAI's 2003 turnover was approximately €325 million (£227 million).
2. **P&O Ferries (P&O)** is a unit of the Peninsular and Oriental Steam Navigation Company (P&O Group). P&O operates ferries in the North Sea and English Channel between UK and Continental ports and in the Irish Sea. The P&O Group is also active in the operation of ports worldwide and has cold logistics and property development divisions. In 2003, the P&O Group had a turnover of approximately £4,138 million of which £1,081 million was in ferry services.

**TRANSACTION**

3. On 28 September 2004, P&O announced its intention to close three of its Portsmouth-based ferry routes serving the French ports of Le Havre, Caen and Cherbourg respectively.<sup>1</sup> In respect of its overall cross-Channel ferry operations, P&O's intention is to remain active on the so-called 'Short French Sea' (specifically, its Dover to Calais route) while withdrawing entirely from the 'Western Channel' with effect from 2005 – with the exception of its Portsmouth to Bilbao route.<sup>2</sup>

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<sup>1</sup> P&O press release of 28 September 2004 entitled Ferries: Outcome of Review.

<sup>2</sup> The ferry industry refers to the principal sea routes between the UK and France via the Dover Straits as the 'Short French Sea' (e.g. Dover to Calais, Dunkirk or Boulogne) and to the longer cross-Channel routes further west as the 'Western Channel'. Western Channel

4. On the same day, BAI signed a Memorandum of Understanding with P&O for the acquisition of an assets package comprising P&O's Portsmouth - Le Havre route, including two multipurpose ferry vessels, associated port berths, infrastructure, staff and a non-compete clause (the MOU). The turnover associated with these assets was [ ]<sup>3</sup> in the 2003 financial year.
5. The effective date of notification was 13 October 2004 when a satisfactory submission was received. The 40 working day administrative deadline is 7 December 2004.

## JURISDICTION

6. The OFT takes the view that the assets package subject to the MOU is an enterprise within the meaning of section 129 of the Enterprise Act 2002 (the Act) and that the share of supply test in section 23 of the Act is met in relation to the supply of ferry services on the Western Channel to freight and tourist customers respectively.
7. The OFT believes, therefore, that it is or may be the case that arrangements are in progress or in contemplation which, if carried into effect, will result in the creation of a relevant merger situation for the purposes of section 33(1)(a) of the Act.

## RELEVANT MARKET

### Product market

8. The parties overlap in the supply of ferry services to freight and tourist customers on the Western Channel. Previous cases in this sector have distinguished between freight ferry services and tourist ferry services.<sup>4</sup> The OFT has received no new evidence in this case that would suggest departing from this approach.
9. **Freight** ferry services consist of the provision of roll-on/roll-off (ro/ro – for wheeled freight) and lift-on/lift-off (lo/lo – for containers) port-to-port maritime transport services. Ferry freight is either 'accompanied' (by a driver of a rigid or articulated lorry) or 'unaccompanied' (a lorry trailer, lift tank or steel container). Freight ferry

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ports include Portsmouth, Southampton, Poole and Plymouth (UK) and Le Havre, Radicatel, Caen, Cherbourg, St. Malo and Roscoff (France).

<sup>3</sup> Information excised at the parties' request.

<sup>4</sup> See the EC decisions in *P&O Stena Line* OJ L163/61 29/6/99; *P&O/P&O Stena Line*, Case M.2838 7/8/02, and the UK decisions in *P&O/Stena Line*, November 1997, Cm 3664 (MMC), and *P&O/Stena Irish Sea*, February 2004 (CC). The EC decision refers to 'tourist passengers', the MMC report refers to 'passenger services' and the CC report to tourists. All of these categories appear to refer to the same type of services. In this decision, tourist ferry services refers to all non freight services.

services are provided by multipurpose vessels, ropaxes, freighters, lo/lo ferries and Eurotunnel freight shuttles.<sup>5</sup>

10. **Tourist** ferry services consist of the provision of ro/ro port-to-port maritime transport services for foot passengers and tourist vehicles (cars, coaches, caravans, camper vans and motorcycles). Tourist ferry services are provided by multi-purpose vessels, ropaxes, freighters, fastcraft and Eurotunnel tourist shuttles. Tourist ferry services can be further segmented between day trips, short stays (5 days or less) and main holidays (5 days or more). The majority of tourist customers on the Western Channel are main holiday.
11. As between vessel types, multipurpose vessels generally offer extensive on-board passenger services (catering, entertainment, retail etc.) and cabins (to provide sleeping accommodation for longer crossing times), whereas ropax and fastcraft have more limited on-board amenities and tend to devote less, if any, space to cabins.
12. In relation to tourist customers, the parties further submit that **low-cost airlines (LCAs)** significantly constrain the supply of Western Channel ferry services both at the level of competition (i) for holiday destinations and (ii) for mode of transport to a given destination. These propositions have some evidentiary support in the form of recent ferry industry initiatives showing an awareness of the need for cross-Channel ferry operators to react to LCAs, as well as tourist marketing, analyst commentary and media coverage.<sup>6</sup> Against that, however, is evidence (i) that the merging parties do not benchmark or otherwise adapt their Western Channel prices in response to LCA prices and (ii) that the rapid growth of LCA travel – which may be expanding the size of the holiday sector – does not appear to have come at the expense of Western Channel tourist volumes, which have been relatively static (see paragraph 17 and onwards below).
13. Overall, the evidence may bear out the proposition that LCAs are a medium-to-long term competitive constraint on ferry operators on the Western Channel, and more so in respect of weekend or short break than main holiday (5 days or more) customers. The evidence does not however permit the conclusion that LCAs are currently a short-term constraint,<sup>7</sup> i.e. that sufficient tourists would switch to

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<sup>5</sup> See para. 25 below for explanations of the different vessel types.

<sup>6</sup> Growth in UK air travel to the Continent has been very rapid. In 2003, the ferry industry established the [www.silanddrive.com](http://www.silanddrive.com) website targeting fly/drive customers and commissioned an industry report into adapting to the LCA challenge, while Speed Ferries, a small ferry operator on the Short French Sea, is thus far unique in adopting a LCA-style pricing model. The parties also note that camping holiday suppliers, historically using ferry transport, now include air travel as an option.

<sup>7</sup> See para. 3.14 OFT *Mergers: substantive assessment guidance*, which states that the OFT would expect short term price constraints to be active within one year.

LCAs to render unprofitable a 5-10 per cent price increase by a hypothetical ferry monopolist on the Western Channel.<sup>8</sup>

14. There is a question as to whether Eurotunnel rail shuttle services from Folkestone to Fréthun should be included in the scope of the product frame of reference for the competition assessment of this transaction. Previous decisional practice has established that the **Eurotunnel** is an immediate competitive constraint on Short French Sea ferry services and in the same product market for both tourist and freight customers.<sup>9</sup> Evidence available to the OFT suggests that this view remains valid. The constraint on Western Channel services imposed by Eurotunnel therefore turns on the extent to which Short French Sea operations constrain Western Channel ferry services, which is considered further at paragraph 15 and onwards, below.

### Geographic market

15. The parties submit, citing prior decisional practice among other evidence, that cross-Channel services are one geographic market in respect of both tourist and freight services because **Short French Sea** operations are immediate constraints on their Western Channel counterparts.
16. As to decisional practice, the 2004 Competition Commission report involving P&O relates to the Irish Sea. The MMC's 1997 findings on the P&O/Stena joint venture – limited to the Short French Sea – do suggest that such routes are substitutes for Western Channel freight customers on those routes but not for tourist customers.<sup>10</sup> The 1999 EC decision<sup>11</sup> in relation to the same transaction is consistent in this respect on freight but notes that Short French Sea tourist prices do constrain corresponding Western Channel prices (though its emphasis in that case was that the reverse was not true).<sup>12</sup> As the present case is the first that relates to an overlap in the Western Channel and in light of the parties' submission that the sector is dynamic, the OFT has considered afresh whether current evidence supports a Channel-wide geographic frame of reference.

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<sup>8</sup> Indeed, competition from air travel for main holiday customers (accounting for over 60 per cent of Western Channel volumes) has existed for some time through package holidays but volumes have remained fairly steady.

<sup>9</sup> See *ibid* at footnote 4.

<sup>10</sup> See paras. 2.47ff and 5.64 for freight, noting that price/volume data support 'the proposition that Short French Sea routes offer a substantial degree of substitutability for Western Channel and North Sea routes and that all these sectors could be regarded as part of the same market' and paras. 5.52-53 for tourist customers, noting that P&O and Stena had experienced significant price reductions on the Dover-Calais route, and Stena had a marked reduction in prices on the Newhaven-Dieppe route, while 'by contrast, prices on the Western Channel do not exhibit a significant downward trend'.

<sup>11</sup> Commission decision IV/36.253 – P&O Stena Line of 26 January 1999, OJ L 163/61, 29/6/99.

<sup>12</sup> See *ibid*, para.48.

17. To complement the mixed views of third parties on switching behaviour among Western Channel tourist and freight customers, the OFT also reviewed a substantial volume of evidence from the parties.<sup>13</sup> The parties were able to provide only limited data comparing prices and volumes on the Western Channel and Short French Sea over time. These appear to show that the closest substitute for the Portsmouth-Le Havre route is Portsmouth-Caen, rather than the Short French Sea. Furthermore, as with LCAs, the parties do not engage in any form of benchmarking of prices directly in relation to prices on the Short French Sea.<sup>14</sup> P&O's price shock analysis, covering a very limited period of 2004, is broadly consistent with the other price and volume data, showing comparatively little loss in Western Channel volumes given the magnitude of price reductions on the Short French Sea.
18. The OFT also considered secondary sources in more detail. A French government report (2000)<sup>15</sup> provided by the parties contains narrative which, in places, suggests that Western Channel operators are constrained by the Short French Sea, yet the report's quantitative data shows that Western Channel tourist and freight prices were relatively insulated from dramatic price falls on the Short French Sea over the period 1993-98 – Short French Sea prices falls over 1993-98 of around 42 per cent in freight and 60 per cent in tourist correspond to price and volume drops in the Western Channel of around 5 per cent in tourist and 5-7 per cent in freight. In respect of tourist volumes, the same relative insulation is suggested by the Ferry Industry Association's report on LCAs, which includes data up to the end of 2002 and depicts Western Channel tourist volumes as essentially stable even as Eurotunnel capacity appears to have prompted sharp reductions in the Short French Sea ferry volumes. Other data from the parties, customers and competitors, much of it qualitative, is equivocal or inconclusive and tends not to undermine the quantitative evidence discussed here.
19. In summary, the overall weight of evidence on demand-side switching is not strong enough to conclude that sufficient tourist or freight customers would switch to Short French Sea ferry or Eurotunnel services to render unprofitable a 5-10 per cent price increase by a hypothetical ferry monopolist on the Western Channel.

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<sup>13</sup> The evidence included (i) drive time and journey cost data via Short French Sea and Western Channel for various tourist origin/destination pairings; (ii) data and surveys of the actual origin and destination of the parties' tourist customers; (iii) P&O documents detailing freight customer switching; (iv) evidence on Western Channel volume changes in relation to a recent price shock on the Short French Sea; and (v) various third party studies and reports.

<sup>14</sup> Ferry operators do monitor the prices on Short Sea but there is no evidence that they price change in reference to this monitoring.

<sup>15</sup> *Etude de la part maritime dans les échanges transmanche*, Ministère de l'Équipement, des Transports et du Logement, November 2000.

20. As to supply-side switching, the parties indicate that no switching of vessels has occurred from the Short French Sea to the Western Channel and their arguments highlight the substantially divergent economics and operational differences between the two sectors. Overall, the evidence suggests that Short French Sea ferry service providers would not be able readily to switch their operations to the Western Channel within one year due to the costs and time involved in vessel reconfiguration (conversely, switching vessels between Western Channel routes is easier as vessel reconfiguration is not required).

## **Conclusion**

21. The evidence available to the OFT suggests that the cumulative weight of the potential constraints identified above do not appear sufficient to discipline a hypothetical ferry monopolist on the Western Channel. Accordingly, the frame of references employed in this case to inform the competitive assessment are the supply of ferry services on the Western Channel to tourist and freight customers, respectively.

## **HORIZONTAL ISSUES**

### **Non-coordinated effects**

22. The addition of P&O's Portsmouth-Le Havre route volumes to BAI's volume share of ferry services on the Western Channel gives rise to shares of supply of [70-75 per cent] (increment [20-25 per cent] and [75-80 per cent] (increment [20-25 per cent]) for tourist and freight customers respectively. However, these data might understate the strength of BAI's post-merger position since, aside from Portsmouth-Le Havre, P&O is also withdrawing from its Portsmouth-Cherbourg and Portsmouth-Caen routes.
23. Given their small scale, the remaining two Western Channel competitors, Transmanche and Channel Freight Ferries (CFF), do not appear to pose a sufficient constraint to discipline BAI post-merger. In 2003, Transmanche's share of Western Channel tourist passengers was [0-5 per cent] and of the freight sector was [10-15 per cent]. CFF does not serve tourist customers. Its share of the freight sector is currently estimated at approximately [10-15 per cent]. Equally, while the accumulation of the constraints identified under market definition are relevant (LCAs, Short French Sea ferries, Eurotunnel), these appear insufficient in scope and timeliness to eliminate by themselves concerns of market power on the part of BAI post-merger.
24. Accordingly, it may be that post-merger BAI will have the ability and incentive unilaterally to raise prices significantly above pre-merger levels across the board to tourist and freight customers respectively. In particular, the merger may facilitate

targeted price increases in relation to certain classes of tourist customer less likely to switch to alternatives, given that the parties' prices do currently vary substantially according to the duration of stay, number of passengers and size and type of vehicle. Finally, non-price factors such as route frequency and on-board service levels may also change to customers' detriment as a result of the merger.

### Barriers to entry and expansion

25. Initial competition concerns may be allayed if entry or expansion would be timely, likely and sufficient to constrain any market power. Here, entry must be understood in relation to the three main types of vessel in operation on the Western Channel:

- **multipurpose vessels:** the traditional ferry type carrying the majority of cross channel traffic. They are flexible in that they can adjust ferry space between tourist and freight traffic at relatively short notice;
- **ropax:** designed to carry ro/ro freight but are adaptable to carry tourists. They are a substitute for multipurpose vessels for freight customers but less so for tourists as the on board facilities are limited for relatively long crossing times; and
- **fastcraft:** small craft designed for tourists, they do not carry freight. These vessels have fewer on board facilities and no cabins; however the shorter crossing time makes them a viable alternative for tourist customers.

26. As regards *de novo* entry, barriers to entry appear to be high if using multipurpose vessels because of the high (particularly sunk) costs and risk of commissioning such a large vessel, the specialist expertise needed to operate it and the down time involved in configuring a vessel for use on the Western Channel. Barriers to entry using a ropax vessel appear to be lower but it takes a considerable amount of time to find and/or configure a vessel to suit a particular route. Entry appears easier in fastcraft, of which there seems to be a surplus on the world market. Of the two recent examples of entry on the Western Channel, CFF entered the relatively niche market of unaccompanied freight in 2003 but cannot be expected to provide a strong post-merger constraint on BAI outside this niche (even should it expand in due course).<sup>16</sup> Transmanche began supplying ferry services to the freight and tourist sectors via ropaxes in 2001. Entry barriers to the freight sector alone appear to be lower due to factors such as: the lower cost of vessels; less seasonality of demand; lower marketing costs required to attract customers; and lower staff costs.<sup>17</sup> Furthermore, although the heightened demand of tourist

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<sup>16</sup> See OFT Mergers Substantive Assessment Guidance (2003), para. 4.22.

<sup>17</sup> Entry barriers in relation to freight on the Western Channel may be lowered in the future as drivers sleep on the longer crossings to comply with the EC Working Time Directive which is currently before the European Parliament. As this occurs, freight demand on the

customers in busy periods of the year may encourage seasonal entry (and thus offer an alternative for peak season travellers) this is not a constraint during the remainder of the year.

27. Expansion by an existing operator appears easier than *de novo* entry due to benefits of previous expertise, an established reputation and customer base, and possible economies of scale and scope. Furthermore, it is conceivable that the exit of P&O may encourage entry and expansion by 'freeing-up' demand that was previously being satisfied by them. Conversely, ferry overcapacity on the Western Channel and the substantial losses sustained by some operators may discourage entry or expansion.
28. The evidence and third party views on prospects for entry are mixed, even as between existing operators. In any event, the balance of evidence suggests that *de novo* entry via a multipurpose vessel(s) would not be suitably likely or timely to allay the concern of post-merger market power of BAI, while it is questionable whether entry or expansion via other vessels, even if both timely and likely, would be sufficient in scope to do so.

#### **Buyer power**

29. The parties argue that post-merger BAI will also be constrained by its buyers. However, to the extent that any of the parties' customers had pre-merger buyer power, it will be eroded or eliminated as buyers' two principal Western Channel choices will be reduced to one, denying them any credible alternative to which they could (threaten to) switch.

#### **Conclusion**

30. The above analysis indicates a potential for serious competition concerns and suggests that customers may be exposed to higher prices or reduced service levels compared to those that have prevailed to the end of 2004 (the date of P&O's exit).

#### **COUNTERFACTUAL**

31. In order to decide, however, whether or not it may be the case that the merger may be expected to result in a substantial lessening of competition, the OFT consider the merger's impact relative to the situation expected to prevail absent the merger (i.e. the counterfactual). Generally speaking, this will be prevailing conditions of competition, but in this case, P&O has submitted that it will exit the

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Western Channel may increase, providing greater opportunity for profitable new entry or expansion.

Western Channel regardless of the BAI transaction. In order to treat this submission as the appropriate counterfactual for assessment of the merger situation, the OFT considers that sufficient compelling evidence is required, particularly as the postulated counterfactual involves the exit of one of the merging parties.<sup>18</sup> In effect, in such circumstances parties are arguing that to the extent competitive harm may arise, the merger is not the cause of that harm as it would in any event occur. Where absence of causation from merger to lessening of competition is alleged, the OFT will seek a high level of supporting evidence (although the standard of belief relevant to the assessment of that evidence remains the same as that set out in the reference test of the Act). This is appropriate given the asymmetry of information on such a key point: such claims are easily made but difficult independently to verify.<sup>19</sup>

### P&O's inevitable exit?

32. P&O has submitted a number of factors to support the assertion that its exit from the Western Channel is irrevocable and unconnected to BAI's acquisition of these two vessels (and associated elements):

- P&O has publicly announced its decision to exit from the entire Western Channel at the end of 2004.<sup>20</sup> A reversal of such a strategy, made by new P&O management, would trigger a loss of shareholder and investor confidence and cause substantial detriment to P&O far in excess of potential gains, thus rendering such action wholly unrealistic from a commercial perspective;<sup>21</sup>
- the Western Channel business has made losses every year since 1994;<sup>22</sup> a cumulative total (1994-2004) of over [ ].<sup>2324</sup> P&O explained that 2003 and the summer of 2004 have seen the most dramatic losses to date<sup>25</sup> prompting

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<sup>18</sup> See also Taminco/Air Products, decision of 16 July 2004; Arcelor/Corus, decision of 9 September 2004.

<sup>19</sup> See further the OFT's treatment of evidence required to meet the conditions of its failing firm defence (*Mergers: substantive assessment guidance*, para. 4.36-39). The analysis below tracks these criteria.

<sup>20</sup> Save for its Portsmouth/Bilbao route [Information excised at the parties' request].

<sup>21</sup> P&O has requested that we stress that all of the route closures are, as a matter of law, subject to the necessary employee consultation.

<sup>22</sup> The parties put forward several factors to explain these losses, including: strong competition particularly from the Short Sea; material and increasing over-capacity on the Short Sea; increases in French tobacco duty; loss of duty free; arrival of the Channel Tunnel; increasing competition from LCAs and high-speed trains; and increases in the price of crude oil which have had a negative impact on bunker fuel costs (a key fixed cost).

<sup>23</sup> Information excised at the parties' request.

<sup>24</sup> However, it should be noted that the OFT has less evidence in terms of the profitability of individual routes.

<sup>25</sup> [Information excised at the parties' request] forecast final for 2004.

P&O to follow earlier independent consultants' recommendations, and exit the Western Channel as soon as possible;

- employee negotiations on the issue of closure have already started in both the UK and France;
  - P&O started the (recent) consideration of the options for its ferry business on the Western Channel in March 2004, well before the start of any discussions with BAI;
  - the MOU with BAI is non-binding and will only become so following the satisfactory conclusion of employee consultations, discussions with the owners of the vessels, and negotiations with Portsmouth City Council;
  - every serious prospect of reorganising the business has been exhaustively examined and discounted throughout its 10 years of loss-making and, more recently, in the course of the fundamental business review which started in March 2004, well before discussions with BAI and other potential buyers.
33. In the light of the above, the OFT is satisfied that P&O has genuinely explored all serious prospects of re-organising the business and that it will exit the Western Channel routes (and specifically Portsmouth-Le Havre) even in the absence of the transaction with BAI.

#### **Less anti-competitive alternatives to the merger**

34. In the present case however, given BAI's existing position on the Western Channel, it appears that any other realistic buyer would result in lower post-merger concentration levels and potentially represent a less anti-competitive alternative to the merger. In order to be satisfied that no realistic or credible alternative purchaser exists, the OFT has sought to gather sufficient compelling evidence on this point, including evidence that 'all possible options have been explored'.<sup>26</sup> On the balance of the evidence, the OFT believes that it may be the case that such a purchaser exists. In this connection, the following points are relevant:

- Prior to entering the MOU with BAI and its public exit announcement, P&O explained that it approached (informally and in confidence) the operators which, based on its market knowledge, it judged might potentially be interested in acquiring the sub-chartering arrangements. P&O contends that,

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<sup>26</sup> See *Mergers: substantive guidance* paras. 4.36-37. This evidentiary standard is also consistent with the US. Horizontal Merger Guidelines failing firm and division defence referred to by P&O, whose 'competitively preferable purchaser' criterion requires the allegedly failing firm/division to make 'unsuccessful good-faith efforts to elicit reasonable alternative offers of acquisition of the assets' above liquidation value: see paras. 5.1-5.2.

despite some interest from other operators, BAI is and was the only party willing to buy the sub-charter for the operation of the vessels on the Western Channel.

- The OFT accepts that to qualify as a less anti-competitive purchaser the bidder must be expected to deploy the assets on the Western Channel, and accepts that it may, on further investigation, be correct that BAI is and was the only party able to benefit from the economies of scale and scope necessary to render this route profitable and that it was, accordingly, the only realistic purchaser for use of the assets covered by the MOU on the Western Channel.
  - Set against P&O's quite plausible assertions, however, are certain uncontested facts: a significant number of other ferry operators in the Western Channel and Short French Sea and indeed elsewhere, were not contacted by P&O prior to the MOU announcements or at all.<sup>27</sup> It is also difficult to verify whether those buyers contacted had no interest in the Western Channel (discussions with them were not fully explored in lieu of P&O's pursuit of the BAI transaction).
  - Moreover, the OFT's investigation elicited evidence from third parties to suggest that other ferry operators may have been realistic buyers had they been contacted prior to announcement of the MOU with BAI, a choice of purchaser which some third parties perceived as a *fait accompli*. Indeed, notwithstanding high *de novo* barriers to entry via multipurpose vessels, the assets at issue present a potential purchaser with proportionately less risk because the package goes beyond the mere vessels to include crew, staff, associated port berths, infrastructure, and a customer base accustomed to a Portsmouth-Le Havre service.
35. If P&O exits the market, the merger does not proceed, and no-one sub-charters the vessels for use on the Western Channel, the result will be a reduction in capacity which would not, in itself, be in the interest of customers. While it is theoretically conceivable that P&O's exit may promote competition between incumbents and/or make entry more viable to capture freed-up demand, this appears somewhat speculative: on this point, the parties contend that BAI has sufficient capacity to meet all of P&O's current demand in the Western Channel and that the record of P&O's ongoing losses on these routes and its ultimate exit may continue to discourage entry and/or expansion.
36. Overall, it is entirely possible that there is no realistic outcome less anti-competitive than acquisition by BAI, even though this creates a predominant supplier on the Western Channel. However, the OFT did not receive sufficient

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<sup>27</sup> The OFT has taken note of P&O's point that a more exhaustive or public process may have been problematic in this case.

compelling evidence to dispel the belief that it may be the case that there is a less anti-competitive alternative to the merger, namely a purchaser other than BAI.

### **CUSTOMER BENEFITS**

37. The parties argue that the transaction will lead to tangible customer benefits in that it will ensure an experienced operator will provide a year-round service for tourist and freight customers on this route, and that BAI will be able to extend its network to a new port in France and thus develop more efficient sailing schedules which will offer greater choice to customers. The parties contend that the conditions of the market are such that BAI will be forced to pass on these benefits to consumers. However, it is far from clear that such benefits would outweigh the customer detriment that would result if the merger substantially lessens competition.

### **THIRD PARTY VIEWS**

38. Several freight customers are very concerned about the possibility of a reduced service on the route, price rises and a lack of ability to barter on price between BAI and P&O. Several tourist customers are similarly concerned about potential price rises and reduced services. The majority of competitors have some concerns about the transaction, particularly the increased strength of BAI on the Western Channel.

### **ASSESSMENT**

39. The proposed transfer of P&O's assets on its Portsmouth-Le Havre route to BAI arises in the context of P&O's publicly announced withdrawal from ferry routes in the Western Channel between UK and France. BAI, whose operations are confined to the Western Channel, will represent over 70 per cent of post-merger supply on such routes, both in the tourist and freight sectors.
40. This case poses two key questions. First, could BAI exercise market power once P&O's exit and sale to BAI has taken place (or would it be constrained from doing so)? Second, if so, would such an outcome have arisen in any event – i.e. even absent the merger?
41. As to the first question, the OFT has examined evidence on the degree to which constraints – including Short French Sea operations, LCAs, and entry into or expansion within the Western Channel by rival ferry operators – would offset any potential competition concerns. The weight of evidence available suggests that such constraints are indeed relevant to the analysis; but it does not support the belief that such constraints would be timely, likely and sufficient in scope to discipline BAI's post-merger competitive conduct. Accordingly, the merger may in the OFT's view raise potential competition concerns.

42. As to the second question, the OFT has concluded that the typical benchmark against which merger effects are assessed – prevailing conditions of competition – is inappropriate here, because P&O has provided sufficient compelling evidence that it will exit the Western Channel regardless of the proposed merger. Given BAI's position, the question therefore is whether there may be a less anti-competitive alternative to the proposed merger. The OFT has not been able to conclude that there is no realistic prospect of an alternative buyer whose purchase of the assets would represent an outcome significantly better for competition than a sale to BAI. Accordingly, it may be the case that substantial lessening of competition may be expected to result from the merger.

## **DECISION**

43. Consequently, the OFT believes that it may be the case that the merger may be expected to result in a substantial lessening of competition within a market or markets in the United Kingdom.
44. This merger will therefore **be referred** to the Competition Commission under section 33(1) of the Act.