
Anticipated acquisition by Virgin Active Group Limited of Holmes Place Health Clubs Limited

The OFT's decision on reference under section 33(1) given on 19 October 2006. Full text of decision published 27 October 2006.

PARTIES

1. Virgin Active Group Limited (Virgin Active) is the holding company of the Virgin Active group which operates health and fitness clubs in the UK, South Africa, Italy and Spain. Virgin Active currently operates 24 clubs in the UK. Virgin Active is controlled by the Virgin Group, which is active in a wide range of businesses including travel, tourism, mobile telephones and financial services.
2. Holmes Place Health Clubs Limited (Holmes Place) is part of the Holmes Place Group whose parent company is Health Club Group plc. The Holmes Place Group operates health and fitness clubs in the UK, Switzerland, Austria, France, Germany and the United States. Holmes Place operates the Holmes Place Group's 44 health and fitness clubs located in the UK. Holmes Place (through group companies) is also contracted to manage five other sports and leisure centres in the UK on an outsourced basis. Holmes Place's UK turnover was £111 million in 2005.

TRANSACTION

3. Virgin Active proposes to acquire Holmes Place via a private sale and purchase agreement. The parties notified the transaction to the OFT on 4 September 2006. Therefore the administrative deadline is 30 October 2006.

JURISDICTION

4. As a result of this transaction Virgin Active and Holmes Place will cease to be distinct. The UK turnover of Holmes Place exceeds £70 million, so the turnover test in section 23(1)(b) of the Enterprise Act 2002 (the Act) is satisfied. The OFT therefore believes 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.

RELEVANT MARKET

5. The European Commission (the Commission) has previously considered an acquisition involving a combination of the Holmes Place and Virgin Active businesses in *Bridgepoint Capital/Permira/Holmes Place* (the Bridgepoint Decision).¹ In that case, the Commission stated that a product market comprising all sports and leisure centres, including publicly and privately owned clubs seemed to be too broad. The Commission commented that there appeared to be some important differences between publicly and privately owned clubs in terms of the facilities and charging structures offered, although in some instances a degree of convergence seemed to be taking place. Ultimately however, the precise product market definition was left open.
6. In relation to the relevant geographic market, the Commission considered that a 1.5 kilometre isochrone/radius around the respective Virgin Active and Holmes Place clubs equalling a journey time of 15 minutes by foot should be used to identify the narrowest possible geographic market. The Commission noted that if travel by car or public transport were taken into account, this would result in wider catchment areas. Ultimately, however, the precise geographic scope was left open. In its assessment, the Commission calculated market shares within a 1.5 kilometre isochrone of each of the merging parties' clubs both on the basis of all privately owned clubs and also on the basis of all privately owned clubs with comparable facilities.²

¹ Case No COMP/M.3169, July 2003.

² In assessing which private clubs did not have comparable facilities, the Commission commented that some clubs did not have a gym and some did not offer exercise classes.

Product scope

7. In this case the parties submitted that the relevant product scope is the health and fitness market. This encompasses all centres offering exercise activities including those public leisure centres that offer equivalent facilities, services and charging structures to private clubs.
8. The evidence before the OFT suggests that in general, public and private clubs view each other as secondary rather than primary competitors. Therefore, although some third party responses suggest that there is a degree of overlap in the offerings of public and private facilities, the OFT has taken a cautious approach and has considered public and private clubs separately. However, the OFT has considered the degree of competitive constraint exerted by all clubs, both public and private, in the areas which have been examined in more detail.
9. Within the private club sector, the OFT has also taken a more cautious approach and considered a narrower product scope of private clubs with comparable facilities. Third party responses indicated that in order to be a strong competitor, a private club must provide a combination of most or all of the following facilities: (i) a gym; (ii) exercise classes; (iii) a swimming pool; (iv) a sauna; (v) a café/bar; (vi) a crèche; and (vii) beauty/spa treatments.

Management contracts

10. Holmes Place currently operates five management contracts, three of which are on behalf of Rochford Council and two on behalf of private clubs.³ Internal Holmes Place documents indicate that the aim is to operate these clubs with facilities and services comparable to other Holmes Place clubs, albeit that there are certain differences (such as offering pay-as-you-go membership). Although the OFT recognises that there are certain differences between the privately run and managed clubs, it has adopted a

³ The two private clubs are the National Badminton Club in Milton Keynes (on behalf of the National Badminton Association) and the Holmes Place Marylebone Health Club (on behalf of the Jury Hotel in Marylebone).

cautious approach and has treated these managed clubs in the same way as other Holmes Place clubs for the purposes of this investigation.

Geographic scope

11. The parties submitted that competition in this sector has a national dimension because some suppliers operate on a national basis with national brands.
12. The evidence before the OFT suggests that national competition is limited and that competition within the health and fitness industry takes place predominantly at the local level. This has been verified both by third party responses and external research. Therefore, the OFT has conducted its assessment primarily at the local level, consistent with the Commission's approach in the Bridgepoint Decision.
13. As mentioned above, the Commission considered 1.5 kilometre radii, equalling a journey time of 15 minutes by foot, to constitute the narrowest geographic market in the Bridgepoint Decision, but also looked at wider drive time catchments.
14. Third party evidence indicates that there is broad support for the 15 minute journey time used by the Commission in the Bridgepoint Decision. However, some third parties suggested that this boundary may be too narrow, particularly when considering locations outside of London. Third party responses suggested that walk times may be more relevant than drive times within London. However, it is not clear what proportion of members walk, drive or use public transport. Therefore the OFT has taken a cautious approach and has considered journey times of 15 and 20 minutes by foot (1.5 and 2 kilometre radii) and also by car/public transport centred around each of the parties' clubs in all areas.

HORIZONTAL ISSUES

National issues

15. The parties have a combined share of supply of private clubs of 2.5 per cent (with an increment of 0.9 per cent) in the UK. Evidence provided by the parties, and supported by third party responses, indicates that the health and fitness sector is large and highly fragmented in the UK.

Local issues

16. The OFT has assessed competition at the local level on the basis of a fascia test, consistent with the Commission's approach in the Bridgepoint Decision. The OFT has taken a cautious approach and has considered in more detail those local areas where the merger would result in a reduction in fascia from five to four or less, on the basis of all private clubs with comparable facilities that are located within 15 or 20 minute walk or drive times of each of the parties' clubs.
17. Applying this test, the OFT has identified the following three areas where the transaction raises cause for further analysis: (i) Thundersley in Essex; (ii) Wandsworth/Putney in London; and (iii) Merton Abbey/South Wimbledon/Streatham in London. The competitive dynamics in these areas are considered in more detail below.

Thundersley

18. Virgin Active has one club in Thundersley and another in nearby Chelmsford. Holmes Place does not have any clubs in the area, but manages three facilities on behalf of Rochford Council. As discussed above, the OFT has adopted a cautious approach and has treated these managed clubs in the same way as other Holmes Place clubs for the purposes of this investigation. However, the OFT recognises that public leisure centres offer a slightly differentiated service and therefore may be weaker competitors than other private Holmes Place clubs.
19. Within 15 and 20 minute walk times, the parties' clubs do not overlap. However, on the basis of a 15 minute drive time, the merger would result in a reduction in fascia from four to three around the Raleigh Leisure

Centre⁴ and from five to four around the Virgin Active club in Thundersley. However, if the isochrone is flexed to a 20 minute drive time, several comparable private clubs are included. On this basis, post merger there would be a reduction in fascia from eight to seven or higher. In addition, the OFT considers that there are a number of other private clubs in the area which, despite offering only a few of the comparable facilities outlined above, nevertheless offer sufficient facilities to exert a degree of competitive constraint on the parties.

20. None of the third parties who were contacted during the course of this investigation raised any competition concerns in relation to this local area.

Wandsworth/Putney

21. Virgin Active has one club located in Wandsworth, within one kilometre of the Holmes Place club in Putney. The merger would result in a reduction in fascia from four to three centred around the Virgin Active club and from three to two around the Holmes Place club on the basis of a 15 minute walk time.
22. An analysis of the local area indicates that post merger, there are likely to be sufficient competitive constraints to alleviate any prima facie competition concerns. Within two kilometres there are two privately run local authority leisure centres - Wandle Recreation Centre and Putney Leisure Centre, which offer a gym, swimming pool and sauna facilities. They also offer a membership scheme. Although the OFT has taken a cautious approach and has considered public and private clubs separately, the OFT considers that these public leisure centres provide a degree of competitive constraint on the merging parties, albeit that the constraint may be less than that posed by a comparable private club. This contention is supported by Holmes Place's internal documents.
23. In addition, the parties provided membership data for the Wandsworth and Putney clubs which demonstrate that only 55 per cent and 68 per cent of members respectively travel from within a boundary of 1.5 kilometres. The parties submitted that for each of these clubs, 80 per cent of members live within a boundary of three kilometres. On this basis the merger would result in a reduction in fascia around the two clubs of eight to seven and

⁴ This leisure centre is managed by Holmes Place.

six to five respectively. This indicates that drive times are also relevant in this area. On the basis of a 15 minute drive time, the merger would result in a reduction in fascia from seven to six if only comparable clubs are considered. If this is flexed to 20 minutes, the number of fascia would reduce from ten to nine around each of the parties' clubs post merger. In addition, if all private clubs within 15 and 20 minute drive time isochrones are considered, several additional clubs would be included in the analysis. Despite offering slightly different facilities, the OFT considers that these additional clubs would exert a degree of competitive constraint on the parties.

24. The OFT also considers that the clubs in this area are also likely to be constrained to some extent by clubs located close to their members' place of work. In addition, there are multiple Cannons, Esporta and Fitness First clubs within a 20 minute drive time.
25. None of the third parties who were contacted during the course of this investigation raised any competition concerns in relation to this local area.

Merton Abbey/South Wimbledon/Streatham

26. Virgin Active has one club located in Merton Abbey, within one kilometre of the Holmes Place club in South Wimbledon. The merger would result in a reduction in fascia from three to two centred around the Virgin Active club and from four to three around the Holmes Place club in South Wimbledon on the basis of a 15 minute walk time.
27. An analysis of the local area indicates that post merger, there are likely to be sufficient competitive constraints to alleviate any prima facie competition concerns. Within two kilometres of the Merton Abbey and South Wimbledon clubs, there are two privately run local authority leisure centres - Tooting Leisure Centre and Wimbledon Leisure Centre, which offer a gym, swimming pool and sauna/spa facilities. They also offer a membership scheme. Although the OFT has taken a cautious approach and has considered public and private clubs separately, the OFT considers that these public leisure centres provide a degree of competitive constraint on the merging parties, albeit that the constraint may be less than that posed by a comparable private club.

28. In addition, the parties provided membership data for the Merton Abbey and South Wimbledon clubs which demonstrate that only 56 per cent and 46 per cent of members respectively travel from within a boundary of 1.5 kilometres. The parties submitted that for each of these clubs, 80 per cent of members live within a boundary of three kilometres. The merger would result in a reduction in fascia around the two clubs of seven to six and eight to seven respectively if a boundary of three kilometres were considered. This indicates that drive times are also relevant in this area. On the basis of a 15 or 20 minute drive time, the merger would result in a reduction in fascia from seven to six. In addition, if all private clubs in the area are considered, the merger would result in a reduction in fascia from six to five within a 20 minute walk time and from ten to nine within a 15 or 20 minute drive time.
29. Third party responses have also suggested that, particularly in London, a high proportion of members use a gym close to their place of work rather than where they live. Therefore the OFT considers that the clubs in this area are likely to be constrained to some extent by clubs in central London. Furthermore, there are multiple Cannons, Esporta and Fitness First clubs within a 20 minute drive time.
30. None of the third parties who were contacted during the course of this investigation raised any competition concerns in relation to this local area.
31. Holmes Place also has a club in Streatham which overlaps with the Virgin Active club in Merton Abbey at the edge of a 20 minute drive time. On the basis of an isochrone centred on the Holmes Place club, the merger would result in a reduction in fascia from four to three. However, a similar isochrone centred on the overlapping Virgin Active club would result in a reduction in fascia from seven to six. In addition, there are two private clubs (Esporta and Cannons) located close to the Virgin Active club, but outside of the isochrone centred around Holmes Place Streatham, which the OFT considers will provide a strong competitive constraint on the parties post merger. In addition, none of the third parties who were contacted during the course of this investigation raised any competition concerns in relation to this local area.

Barriers to entry and expansion

32. Third party responses indicate that barriers to entry in this sector are relatively low. Third party competitors were in general agreement that the main barrier was finding an appropriate site and being awarded planning permission. However, given there are sufficient post-merger competitive constraints in each local area, no conclusion need be drawn on barriers to entry.

Buyer power

33. The OFT contacted several third party corporate members during the course of its investigation. The majority of these respondents indicated that they would consider switching to an alternative company if prices were to increase by 5 to 10 per cent. However, given there are sufficient post-merger competitive constraints in each local area, no conclusion need be drawn on buyer power.

VERTICAL ISSUES

34. The parties submit that they do not have more than a 15 per cent share of supply of any inputs or outputs in a vertical supply chain. Therefore this transaction does not raise any vertical concerns.

THIRD PARTY VIEWS

35. None of the third party competitors who were contacted during the course of this investigation raised any competition concerns about this merger. All agreed that the market was large, highly fragmented and very competitive. One third party competitor commented that barriers to exit exist in this sector because long term leases of premises make it very difficult to leave the sector.
36. The OFT received complaints from two members of Holmes Place. These members were concerned that post merger Virgin Active customers would be able to use Holmes Place clubs, whilst continuing to pay Virgin Active membership rates which are significantly less than Holmes Place rates. In addition, the customers raised concerns about the quality of service and investment in facilities that Virgin Active would provide post merger. However, at the very most, a proportion of Holmes Place members would

be tied to the club for a maximum of one year, after which point they would be free to switch to alternative clubs. Moreover, as outlined above, the evidence before the OFT indicates that post merger, customers would have a sufficient number of alternative clubs to which they could switch in the event that they were unhappy with the service and/or facilities offered by Virgin Active post merger.

ASSESSMENT

37. The OFT has considered public and private clubs to comprise separate product frames of reference. Within the private club sector, the OFT has also considered a narrower product scope of private clubs which it could be ascertained had comparable facilities, that is, clubs which offer a combination of most or all of the following facilities: (i) a gym; (ii) exercise classes; (iii) a swimming pool; (iv) a sauna; (v) a café/bar; (vi) a crèche; and (vii) beauty/spa treatments.
38. The effects of this merger have been considered at the national and also the local level. At the local level, the OFT has considered 15 and 20 minute walk and drive times centred around each of the parties' clubs.
39. At the national level, the parties have a combined share of supply of private clubs of 2.5 per cent (with an increment of 0.9 per cent). In addition, evidence provided by the parties, which has been supported by third party responses, indicates that the health and fitness sector is large and highly fragmented in the UK.
40. At the local level, there are three areas where the merger would result in a reduction in fascia from five to four or less.
41. In two areas of South London (Merton Abbey/South Wimbledon and Putney/Wandsworth) the merger would result in a reduction in fascia from five to four or less within the narrowest radii. However, a detailed analysis of each area suggests that within 15 or 20 minute walk times, there are publicly run facilities and other fitness centres which provide a degree of competitive constraint. Furthermore, the evidence before the OFT suggests that drive times are relevant to these areas. On the basis of 15 or 20 minute drive times, the merger would result in a reduction in fascia of seven to six or higher. Finally, the clubs in these areas are likely to be constrained to some extent by the clubs located close to their members'

place of work. Therefore, taking into account all of these factors, the OFT considers that sufficient post merger competitive pressure is expected to remain to discipline the merged entity.

42. In Thundersley, the parties' clubs do not overlap within the narrowest radii. However, the merger would result in a reduction in fascia from four to three around the Raleigh Leisure Centre and from five to four around the Virgin Active club on the basis of a 15 minute drive time. However, if the isochrone is flexed to 20 minutes, the merger would result in a reduction in fascia from eight to seven or higher.
43. None of the third party competitors who were contacted during the course of this investigation raised any competition concerns about this merger. The OFT received complaints from two members of Holmes Place. Their concerns have been addressed above.
44. Consequently, the OFT does not believe that it is or 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.

DECISION

45. This merger will therefore not be referred to the Competition Commission under section 33(1) of the Act.