
Anticipated acquisition by MTR Laing Railway Company Limited of the Thameslink/Great Northern Franchise

The OFT's decision on reference under section 33(1) given on 8 July 2005. Full text of decision published 15 July 2005.

Please note that square brackets indicate information excised or replaced by a range at the parties' request.

PARTIES

1. **Laing Railway Company Limited (Laing)** is a wholly-owned subsidiary of **John Laing Plc (JL)**. JL is involved in the development, investment and operation of infrastructure (e.g. accommodation, roads and rail). Laing owns Chiltern Railways, a train operating company (TOC) running passenger franchise services out of London Marylebone to Aylesbury, Birmingham and the West Midlands. Laing also owns a 40 per cent stake in CGL Rail plc, which designed, built, financed and maintains the City Greenwich Lewisham Rail link for Docklands Light Railway Limited. Other Laing projects include the station development at Warwick Parkway and Project Evergreen II, a design, build, finance and transfer project for infrastructure enhancements on the Chiltern network.
2. **MTR** is a wholly-owned subsidiary of **MTR Corporation (No.2) Limited (MTR)**. MTR is a public company 76 per cent owned by the Government of Hong Kong. It is engaged in two main business areas: railway operations and property development. MTR's principal business is the operation of Hong Kong's mass transit railway system; it currently has no rail operation in the UK. However, MTR owns a 29 per cent share in Greater South Eastern Railway Limited (GSER), a joint venture with GNER Holdings Ltd (which owns 71 per cent). GSER was set up to bid for and operate the Integrated Kent Franchise (IKF).
3. **MTR Laing Railway Company Limited (MTRLaing)** is a newly-incorporated 50:50 joint venture company established by MTR and Laing solely for the purpose of bidding for and operating the Thameslink/Great Northern franchise (TGN).
4. **Thameslink/Great Northern Rail Franchise (TGN)** encompasses routes from King's Lynn, Peterborough, Welwyn Garden City and Hertford to London and from Bedford through London to Brighton. It will consolidate the passenger rail services on the networks currently operated by Thameslink Rail Limited and residual routes

operated by West Anglia Great Northern Railway Limited (WAGN) within a single franchise. The revenues for the TGN franchise are expected to be around £275 million in aggregate.

TRANSACTION

5. The anticipated merger arises from a competitive bidding process for the TGN franchise put out to tender by the Strategic Rail Authority (SRA). The SRA announced the 5 pre-qualified bidders (National Express Group plc, FirstGroup plc, Stagecoach Group plc, Danish Railways/EWS Railways and, MTRLaing) on 1 April 2005. The SRA published the Invitation to Tender (ITT) on 1 June 2005 and bidders are required to submit bids in response by 6 September 2005. It is anticipated that the final franchise agreement with the preferred bidder will be signed during Winter 2005/2006.
6. The parties notified the transaction on 26 April 2005 and the 40-working day administrative timetable expires on 8 July 2005.

JURISDICTION

7. By virtue of section 66(3) of the Railways Act 1993, MTRLaing and TGN will cease to be distinct. This transaction qualifies on the turnover test in that the annual turnover of TGN is expected to significantly exceed the £70 million threshold.

RELEVANT MARKET

Product market

8. The prospects of substitution between rail and other forms of transport for a given journey are specific to the routes and passenger profiles in question. Passengers' choice of transport on any journey depends on a number of different factors, including (convenience of) access to a particular means of transport (either at the boarding or disembarkation point), personal preference, value of time and relative costs of the available alternatives.
9. As regards private transport, evidence collated by the CC in its FirstGroup/ScotRail and NEG/Greater Anglia merger inquiries suggests that there is limited substitutability between public and private transport in response to changes in relative price, although the exact extent of substitutability varies depending on, among other things, the level of car ownership in the particular area and whether the relevant journey is urban or rural.

10. Bus services tend to be more frequent than rail services. Bus and coach travel tends to be cheaper than travel by train, although journeys are generally longer due to a larger number of stops or congestion delays.
11. As well as varying by route, the degree of substitutability between different transport modes is also dependent upon characteristics of the user.¹
12. In the absence of any evidence to suggest that an alternative approach might be appropriate, The OFT, in line with previous practice, has taken as the relevant frame of reference for assessing the competitive effects of the proposed acquisition the supply of passenger transport services on point-to-point flows.

Geographic market

13. In making a journey, passengers wish to travel from a particular point of origin to a specific destination. The CC concluded in its report on the First/ScotRail merger that point-to-point journeys were considered the relevant geographic frames of reference for competition assessment in relation to the bus/rail overlaps in that case. Point-to-point frames of reference have consistently been employed in relation to various modal combinations such as coach/rail and rail/rail.²
14. The OFT has not received any evidence in this case that warrants departing from the point-to-point approach, which the parties endorse.

HORIZONTAL ISSUES

Bus-on-rail

15. There are no overlaps between bus and rail on this case. Neither JL, Laing or MTR have any bus operations in the UK.

Rail-on-rail

16. Based on the SRA's current Invitation to Tender (ITT) for each of the TGN and IKF franchises, there is the potential for a total of six rail-on-rail overlap flows if (i) MTRLaing is the successful bidder for the TGN franchise, and (ii) the bidding vehicle in which MTR has a minority interest (GSER) wins the IKF franchise (the 'overlap scenario'). On this basis, MTR would own stakes in the TOCs operating the TGN (50 per cent) and IKF (29 per cent) franchises respectively. Assuming that each pre-qualified bidder were to stand an equal chance of winning the relevant

¹ Of particular relevance in the CC's NEG/Greater Anglia report, where coach-on-rail overlaps were prevalent, was the distinction between leisure passengers, commuters and business travellers who exhibited different sensitivities to journey times. The evidence collated by the CC in its FirstGroup/ScotRail inquiry also suggested that train and local buses were at least potentially substitutable on some routes.

² See, for example, CC report in NEG/Greater Anglia, OFT decisions in First/ICEC, Virgin/ICEC, Arriva/Wales and Borders, South Eastern Railways/IKF.

franchise, the probability that the overlap scenario will occur is small. The following nevertheless proceeds on the basis that overlaps will arise.

Blackfriars – Elephant and Castle – Herne Hill

17. This route gives rise to three such potential overlap flows. However, the fact that the overlaps between the IKF and the TGN on this route would only occur at peak times, when all fares are regulated, eliminates the scope for price increases by the rail operators on these flows (i.e., outside of increases permitted under regulation). Similarly, service levels are tightly regulated. While the presence of regulation appears to preclude any merger effects on the flows in question, two further points also support the conclusion that no competition concerns arise: first, most passengers are likely to be using travelcards as all stations are within Transport for London (TfL)'s Travelcard zone; second, bus and/or the underground appear to be viable travel alternatives for a large number of passengers.

London Bridge and Redhill via East Croydon

18. According to the ITT for IKF,³ the SRA anticipates that this route may be transferred to a Brighton mainline TOC (currently Southern), which would remove the overlap between the IKF and the TGN. Given that at the time of investigation this is only a proposal, it has been assumed for the sake of caution that the route will be included in the TGN, giving rise to three overlap flows.
19. If the overlap scenario occurs, the increment (e.g. in terms of service frequency) created by the merger is limited, and MTR would continue to face competitive discipline from Southern, currently the predominant operator by revenue (accounting for over [] per cent of total revenue and over [] per cent of season ticket revenue on any of the given flows).⁴

Conclusion

20. The OFT does not believe there is a realistic prospect of a substantial lessening of competition on the above flows due to the factors identified above. In addition, MTR does not have outright control of the bid vehicles for either the IKF or the TGN franchise. In these circumstances, it is far from clear that MTR would have the ability to engineer anti-competitive outcomes, such as co-ordinated price increases, since these would not necessarily be in the interest of its joint venture partners.

³ See the IKF Stakeholder Briefing document (Jan 2005)

⁴ These figures refer to the years 2003 and 2004

Barriers to entry and expansion

21. The OFT has previously acknowledged⁵ that whilst there may be some scope for entry to the rail sector via open access agreements, the likelihood of such entry appears low and no evidence of such entry has been put forward by the parties.

VERTICAL ISSUES

22. This transaction does not raise any vertical competition concerns.

THIRD PARTY VIEWS

23. There were no concerns from third parties.

ASSESSMENT

24. The rail on rail overlaps examined above will only occur only if the bidding vehicles in which MTR has an interest are the successful bidders for both the IKF and TGN franchises. This scenario is uncertain for two reasons: (1) it is impossible to predict whether or not MTR's bids will be successful; (2) even if they win the IKF, the exact map of the franchise has yet to be determined, with the SRA envisaging that certain flows⁶ may be transferred to Southern in advance of the start of the IKF franchise.
25. Furthermore, MTR only has a 29 per cent minority stake in GSER and does not have outright control of MTRLaing. Even if both relevant consortia were to win their respective franchises, it is far from clear that MTR would have the ability to engineer anti-competitive outcomes, such as co-ordinated price increases, since this would not necessarily be in the interests of its joint venture partners.
26. In any event, high proportions of regulated fares and strict service level prescription appear to remove the possibility of merger specific effects in relation to one set of overlap flows, while in relation to the other, post-merger, the parties will continue to face competitive pressure from Southern, the lead operator on the flows in question.
27. Consequently, the OFT does not believe that it is or may be the case that the creation of this merger situation may be expected to result in a substantial lessening of competition within a market or markets in the United Kingdom.

⁵ See South Eastern Railways/IKF, 31 March 2005.

⁶ See the IKF Stakeholder Briefing document (Jan 2005)

DECISION

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