

**THE ACQUISITION BY BUCHER INDUSTRIES AG OF  
JOHNSTON SWEEPERS LIMITED MERGER INQUIRY**

**Provisional findings report**

Published: 5 August 2005

The Competition Commission has excluded from this published version of the provisional findings report information which the inquiry group considers should be excluded having regard to the three considerations set out in section 244 of the Enterprise Act 2002 (specified information: considerations relevant to disclosure). The omissions are indicated by ✂.

# Provisional findings report

## The acquisition by Bucher Industries AG of Johnston Sweepers Limited

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## Summary

1. On 6 April 2005 the Office of Fair Trading (OFT) referred to the Competition Commission (CC) for investigation and report (under section 22(1) of the Enterprise Act (the Act)) the acquisition by Bucher Industries AG (Bucher) of Johnston Sweepers Limited (Johnston). Our terms of reference are set out in Appendix A. We are required to publish our final report by 20 September 2005.
2. Bucher is a publicly-listed company with its headquarters in Niederweningen, Switzerland. One of its business divisions is Bucher Municipal, which specializes in vehicles for clearing and cleansing traffic areas, and is the largest manufacturer of outdoor sweepers in Europe. Johnston was, prior to the merger, owned by Ennstone plc (Ennstone). It is the largest supplier of outdoor sweepers in the UK.
3. Bucher and Johnston both manufacture a similar range of sweepers. Their main uses are in cleaning roads, car parks and pedestrian walkways; they also have certain other specialist uses. Local authorities are the main end-users of these sweepers; about two-thirds purchase or hire sweepers, the remainder contract out street-cleaning services to companies that purchase or hire sweepers for those contracts.
4. On 18 February 2005 Bucher announced that it had acquired the European and Australian sweeper business of Johnston Group plc (Johnston Group) from Ennstone for a total of £20.5 million (on a debt-free basis). The acquisition was completed on 31 March 2005. As a result of the transaction, Bucher and Johnston ceased to be distinct enterprises. In the years 2001 to 2004 Johnston achieved a share of supply of truck-mounted sweepers in the UK in excess of 50 per cent each year, and Bucher achieved a share of supply of between 1 and 10 per cent. Adding Bucher's supply of truck-mounted sweepers to Johnston's results in a small increment to a share of

supply which is already greater than one-quarter. We therefore concluded that a relevant merger situation had been created.

5. We concluded that the product market primarily affected by the merger was no wider than the market for outdoor sweepers. We found conflicting evidence on whether there were a number of smaller product markets within this broad definition, but that our analysis was not affected by whether there are one or more product markets. We concluded that the market was no wider than the UK.
6. Buyers in the UK market generally attach more importance to reliability and performance of sweepers than price. The ability to source sweepers from a UK distributor and the presence of an after-sales service network (for spare parts sales and, for some, servicing) are considered to be extremely important. Customers consider a supplier's reputation in meeting all these criteria to be important, and often prefer to use suppliers with which they have had an established relationship.
7. In considering the effects of the merger, we focused on three questions: whether Bucher was a competitive constraint in the UK on Johnston prior to the merger, either through directly competing with Johnston or as a potential credible supplier; whether Bucher would have imposed a competitive constraint on Johnston in the UK over the next few years in the absence of the merger; and whether the merger would weaken competition in the UK, for example through raising barriers to entry and to expansion, compared with the likely alternative to the merger.
8. Immediately prior to the merger Bucher did not have UK distribution arrangements. Its previous distribution agreement ended in November 2003, and since then Bucher achieved very limited sales and submitted only a few tenders to supply airport runway sweepers.

9. We looked at the barriers to entry and expansion in the market. The barriers to expansion for Bucher appeared to be higher than those for the main and middle-tier incumbents, and some of the recent entrants and smaller players. There were relatively long lead times needed to overcome these barriers. We therefore concluded that, prior to the merger, Bucher was not a direct competitive constraint on Johnston, and Bucher's possible relaunch in the UK was not exerting any significant competitive constraint on Johnston at the time of the merger.
10. We considered what might have happened to Johnston and Bucher if the merger had not happened. We concluded that Johnston would have been sold to one of the trade or non-trade purchasers that had already expressed interest during the original sale process. We also concluded that in the absence of the merger Bucher would have made significant efforts to relaunch itself in the UK.
11. We considered whether, in the absence of the merger and assuming Bucher relaunched in the UK, it would be expected to impose a significant competitive constraint on Johnston over the next few years, and did not find that it would. This was because of the considerable degree of uncertainty over whether Bucher would have achieved a significant presence in the UK in the face of competition from better-placed rivals already established in the market.
12. We considered whether the merger would weaken competition in the market, and concluded that it would not, as we found that any advantages enjoyed by the merged group were not enough materially to outweigh the effect of current and future market conditions. Accordingly we found that the market for sweepers in the UK would not be significantly less competitive than if the merger had not taken place.

13. For the reasons set out above, we do not find that the merger has resulted or may be expected to result in a substantial lessening of competition within any market or markets in the UK.

## **Provisional findings**

### **1. The reference**

1.1 On 6 April 2005 the OFT referred to the CC for investigation and report (under section 22(1) of the Act) the completed acquisition by Bucher of Johnston. We were asked to report by 20 September 2005. Our terms of reference are at Appendix A.

1.2 This document (together with its appendices) constitutes the provisional findings that we are required to publish under the CC's rules of procedure. Non-sensitive versions of main party and third party submissions are on our web site, along with a number of other documents relevant to this inquiry. We cross-refer to them where appropriate.

### **2. The sweeper industry and the companies involved in the merger**

2.1 Applications of street sweepers include litter collection from pedestrian areas and cleaning minor roads, major highways, road and building construction sites, airports and industrial sites.

2.2 Sweepers may be divided into the following categories: sub-compact, compact, mid-sized, truck-mounted and specialist truck-mounted. These categories of sweepers are discussed further at Appendix B.

2.3 Local authorities are the end-users for nearly all applications of street sweepers. Other end-users include airports and building and road construction sites. Around one-third of local authorities contract out their street-cleaning service to contractors; the remaining two-thirds of authorities with direct labour street-cleaning services may obtain some or all of their equipment from contract hire companies, as may street-cleaning contractors. Other end-users may also hire equipment.

- 2.4 Sweeper suppliers may thus sell direct to local authorities or other end-users, to cleaning contractors or to contract hire companies, creating a number of different routes through which sweepers reach their end-users.
- 2.5 Additionally, in the case of truck-mounted sweepers, suppliers normally receive a donor truck chassis, purchased separately by the customer (or by the sweeper manufacturer for the customer), and then mount the sweeping equipment on the chassis ready for dispatch to the customer. An alternative supply route is where a sweeper manufacturer sells the sweeping equipment to a truck chassis dealer and the equipment is mounted on the chassis for sale by the dealer.
- 2.6 Worldwide, export sales are most commonly made through a distributor in the country concerned. Export sales of truck-mounted sweepers often involve supplying the sweeping equipment to an overseas distributor, which then mounts it on a locally sourced chassis.

### ***Bucher***

- 2.7 Bucher is a publicly listed company with its headquarters in Niederweningen, Switzerland. Its turnover for the year ended 31 December 2004 was CHF 1,640.9 million (£721.6 million)<sup>1</sup>. The company operates in engineering and automotive industries worldwide, with five core areas, each a separate business division. One of these divisions is Bucher Municipal (called Bucher Automotive until 2005), which specializes in vehicles for clearing and cleansing traffic areas, and is the largest manufacturer of sweepers in Europe. Within Bucher Municipal there are two business units which are active in the sweeper sector: the German-based Bucher-Schörling GmbH (Bucher-Schörling) and the Swiss-based Bucher-Guyer AG (Bucher-Guyer). Bucher-Guyer also owns Bucher-Schörling Korea Limited and

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<sup>1</sup>£0.43975=CHF 1.0 (average exchange rate for calendar year 2004).

Bucher-Schörling Baltic SIA (Bucher-Schörling Baltic). Bucher has told us that, post-merger, Johnston would continue to operate as a separate company within Bucher Municipal.

2.8 Bucher-Schörling produces truck-mounted sweepers at its factory in Hanover. It was acquired by Bucher in 1994 and has approximately 200 employees. Its operations relate mainly to truck-mounted sweepers<sup>2</sup>. Bucher-Guyer's operations are not restricted to sweepers and include trading of tractors and other agricultural machinery, and fruit juice production plants. The sweeper-producing business of Bucher-Guyer is called Bucher-Guyer Municipal. Its operations are related mainly to sub-compact, compact and mid-size sweepers. Its 180 employees are based at Niederweningen. In autumn 2004 Bucher-Schörling Baltic opened a factory in Latvia which is a component assembly plant which currently has 16 employees.

2.9 In 2004, Bucher-Schörling generated an operating loss after tax and exceptional items of [X]<sup>3</sup>; Bucher-Guyer's sweeper business generated earnings before interest and tax (EBIT) of [X] and a profit before tax of [X].

### **Johnston**

2.10 Johnston is active in the production and sale of a range of outdoor cleansing equipment. Johnston used to be part of Johnston Group. Johnston Group had two distinct business divisions: the construction materials division, and the engineering business. The construction materials division was the driver for Ennstone's acquisition in November 2004 of Johnston Group, and Ennstone subsequently disposed of the companies in the engineering division.

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<sup>2</sup>It also distributes CityCat sweepers, winter equipment and airport sweepers.

<sup>3</sup>£0.6788=€1.0 (average exchange rate for calendar year 2004).

- 2.11 The engineering division comprised: Johnston; Saxon Specialist Vehicles Limited (a manufacturer of fire-fighting and rescue vehicles and airport support equipment, which ceased trading in March 2005); and two North American subsidiaries, Johnston Madvac Inc and Johnston Sweeper Company Inc, which were sold to the North American management team in May 2005.
- 2.12 Johnston has two overseas subsidiaries: MacDonald Johnston Engineering Company Pty Limited (Australia) and Johnston GmbH (Germany). Johnston's Australian subsidiary manufactures chassis-mounted regenerative sweepers (these recirculate exhausted air from the hopper) and refuse collection vehicles (as well as air hand-dryers and other washroom equipment). Johnston's German subsidiary used to distribute Johnston's products but has been non-trading since 2002.
- 2.13 Johnston also has a branch operation in Denmark (Johnston Beam)—it acquired this business unit in 1996. It fabricates specialist truck-mounted sweepers, and distributes sweepers into Scandinavia.
- 2.14 Johnston has four manufacturing facilities, three in the UK and one in Denmark (at its branch operation). The UK facilities are at Dorking (headquarters, sales and marketing, production of truck-mounted sweepers, fabrication of parts, including spare parts, for its whole sweeper range, and customer support), Ash Vale (fabrication plant for truck-mounted bodies) and Sittingbourne (production of compact sweepers). Johnston also has service facilities at five sites in the UK (Dorking, Sudbury, Livingston, Warwick and Bristol).
- 2.15 In the year ended 31 December 2003 Johnston generated operating profits of £2.09 million on turnover of £54.5 million. Johnston is the largest supplier of sweepers in the UK.

### **3. The transaction and the reasons for the merger**

#### ***The transaction***

- 3.1 Bucher announced on 18 February 2005 that it had acquired the European and Australian sweeper business of Johnston Group from Ennstone for a total of £20.5 million (on a debt-free basis), payable on completion partly in cash and partly by way of assumption of third-party and inter-company debt to be taken over by Bucher. The acquisition was completed on 31 March 2005. Further details of the events leading up to the Ennstone sale of Johnston and the handling of that sale process are given at Appendix C.
- 3.2 The terms of the transaction are set out in the sale and purchase agreement of 18 February 2005, between Johnston Management Holdings Limited, Ennstone and Bucher. It relates to the entire issued share capital of Johnston.

#### ***The reasons for the merger***

- 3.3 Ennstone told us that it bought Johnston Group because of Johnston Group's quarries business. Before the acquisition of Johnston Group was completed, Ennstone announced that it intended to sell off the engineering business.
- 3.4 Bucher told us that its reasons for the merger should be seen in the context of its municipal business failing to meet profitability targets. Bucher had been considering strategies for its municipal business, including: a stand-alone strategy; and a strategic acquisition to result in higher sales volumes and lower unit costs
- 3.5 Bucher told us that it had previously considered a number of other acquisitions in Europe.

- 3.6 One merger was examined in 2003, but rejected by the shareholders of the other company. Discussions were held about a second merger, but these terminated in the second half of 2004. Shortly thereafter, Bucher began pursuing the possible acquisition of Johnston. We understand that acquiring Johnston was a priority over this second acquisition, but we were also told that there were other reasons why the second possible acquisition did not proceed.
- 3.7 If the acquisition of Johnston had not occurred, Bucher would have had the option of pursuing alternative acquisitions which might also have brought benefits.
- 3.8 Bucher told us that the merger with Johnston was driven by the prospect of efficiency gains, and cited a number of areas where it saw scope for efficiencies. Its press release announcing the merger noted the prospect of efficiency gains, as well as the complementary nature of the two companies in product ranges and geographic market coverage. Bucher's reasons for the merger, therefore, go beyond the UK market.
- 3.9 Bucher's Merger Notice to the OFT stated that the principal reasons for the merger were to allow Bucher to establish a position in the UK market and achieve economies of scale within Bucher Municipal.
- 3.10 Further details on Bucher's reasons for the merger are given in Appendix C.

#### **4. Jurisdiction**

- 4.1 Under our terms of reference (see Appendix A), we are required to investigate and report on whether a relevant merger situation has been created. A relevant merger situation exists where two or more enterprises have ceased to be distinct and where the share of supply test or the turnover test specified in the Act is satisfied.

- 4.2 As a result of the transaction described in paragraphs 3.1 and 3.2 above, Bucher and Johnston have ceased to be distinct enterprises.
- 4.3 The share of supply test is satisfied if the merger creates or increases a share of at least one-quarter in the supply of goods or services of any description in the UK, or in a substantial part of the UK. Here, we look at the supply, over the course of the past few years, of truck-mounted sweepers in the UK, since Bucher's most recent sales have been of this type of sweeper.
- 4.4 The parties told us that their shares of the supply of truck-mounted sweepers in the years 2001 to 2004 were in excess of 50 per cent each year (Johnston) and between 1 and 10 per cent (Bucher). Adding Bucher's supply of truck-mounted sweepers to Johnston's results in a small increment to a greater than one-quarter share of supply in the UK. That is the case regardless of whether the calculation is done over a period of one, two or three years prior to the merger.
- 4.5 Since the share of supply test is satisfied we are not required to consider the turnover test.
- 4.6 We therefore find that the acquisition of Johnston by Bucher resulted in the creation of a relevant merger situation. The parties did not dispute that a relevant merger situation existed.

## **5. Market definition**

- 5.1. In order to assess the competitive impact of the merger, we need to consider the market or markets that will be relevant to that assessment. We looked first at the relevant product market and then the geographic market, each from both the demand and the supply sides. These considerations are set out in Appendix D. We

commissioned a survey of sweeper customers ('customer survey'), conducted by NOP World in May 2005. The survey had two components: first, 100 organizations that had purchased sweepers for their own business use within the past four years were asked to respond to a questionnaire; second, in-depth follow-up interviews were conducted with 22 of these respondents, covering their purchasing behaviour. A complete report on the results of the survey is published on our web site.

- 5.2. The evidence on whether the product market is narrower than all outdoor sweepers is inconclusive. There is some evidence of different categories of sweepers fulfilling similar end-use requirements, but customers do not appear very willing to switch between categories on the basis of price alone (see paragraphs 4 to 10 of Appendix D). On the supply side, there appear to be some overlaps between the ability of different suppliers to offer different categories of outdoor sweepers (see paragraphs 11 to 15 of Appendix D).
- 5.3. The key factor in relation to the geographic market appears to be the requirement of customers for a UK sales and after-sales presence. This restricted the geographic market to being no wider than the UK, and we received no evidence to indicate a geographic market narrower than the UK.

### ***Conclusions on market definition***

- 5.4. For the reasons set out in paragraphs 5.2 and 5.3, we conclude that the geographic market is limited to the UK. The product market comprises all outdoor sweepers, and our conclusions in section 8 are not affected by whether there may be more than one product market for outdoor sweepers, so we have not considered this further.

## **6. The counterfactual**

6.1 In order to assess the effect of the merger on competition in the relevant market, we need to identify what would have been likely to happen in the absence of the merger (the counterfactual). We therefore consider in turn what would have happened to Johnston, and what Bucher would have done.

### ***Johnston***

6.2 Prior to obtaining shareholder approval for the acquisition of Johnston Group, Ennstone announced, in October 2004, that it had concluded that it would seek to dispose of the Group's engineering business and had initiated talks with a number of parties with a view to achieving an accelerated disposal.

6.3 The sale of Johnston to Bucher was conducted through a competitive disposal process, which attracted indicative offers from a range of trade and non-trade buyers. Three final indicative offers were received, including from Bucher and the Rosewood Partnership (Rosewood). Rosewood is a small organization specializing in business recovery, which worked with members of Johnston's senior management to put forward a bid.

6.4 Whilst Rosewood had made a final indicative offer, Ennstone told us that it had serious concerns over the viability of Rosewood's funding and its ability to negotiate and conclude on mutually satisfactory terms. However, Rosewood told us that it had been confident that it would have been able to meet the timetable set by Ennstone, to negotiate and execute a sale and purchase agreement, and to raise sufficient funds.

6.5 The third bidder's final indicative offer was lower than Bucher and Rosewood's offers, and was not considered acceptable.

- 6.6 If the merger with Bucher had not gone ahead, Ennstone told us that it would have remarketed the business and approached interested parties.
- 6.7 We believe that, absent the acquisition by Bucher, Ennstone would have sought an alternative purchaser for Johnston. Ennstone had received a number of initial expressions of interest in acquiring Johnston, and we believe that they would have found a purchaser. We do not believe that Ennstone would have closed the business down, given its value and the interest from prospective buyers.
- 6.8 In the absence of the merger, we conclude that Johnston would have been sold to one of the trade or non-trade buyers which had already expressed an interest during the original sale process.

### ***Bucher***

- 6.9 In the absence of the merger Bucher would have had three main options in relation to the UK. These options were: (a) to exit the sweeper market altogether; (b) to continue without UK distribution arrangements (selling a small number of units into the UK); or (c) to establish comprehensive UK distribution arrangements. We consider Bucher's actions in relation to the UK from November 2002 to the merger, and then discuss each of these options.

### ***Bucher's actions from November 2002***

- 6.10 We asked Bucher about its plans for selling sweepers in the UK. It took us some time, and several exchanges with Bucher, to draw up a comprehensive picture of the nature and extent of Bucher's plans. For example, Bucher told us, amongst other things, that it was merely responding passively to approaches from UK customers, and was not in negotiations with potential UK distributors. We found that it was in fact investigating a relaunch in the UK through the establishment of a UK subsidiary. We

set out here our understanding of Bucher's actions from November 2002, when its UK distributor gave notice to terminate its distribution agreement.

6.11 In November 2002 AssetCo Ltd (AssetCo), Bucher's then UK distributor, gave notice to terminate its distribution arrangement with effect from November 2003. Work conducted by Bucher to establish a UK subsidiary to coincide with the termination of the distribution agreement included:

- a visit to the UK in May 2003, to discuss Bucher's future approach in the UK with parties interested in working with it as servicing agents;
- the production of several business plans for the establishment of a UK subsidiary: one was put to the Bucher Chief Executive Officer (CEO) in September 2003 but rejected. Work on a UK business plan was restarted within Bucher Municipal in October 2003; and
- giving assurances to AssetCo that a continued UK presence was planned: the then head of Bucher-Schörling wrote to it in September 2003 stating that Bucher intended to set up a UK subsidiary, with after-sales service and spare parts provided by a service partner.

6.12 Despite all this work, Bucher did not establish distribution arrangements to coincide with the termination of the AssetCo agreement. Bucher told us that it 'did not exit the market out of choice'. It also told us that it decided not to set up its own UK business at that time because of regulatory concerns, and because a viable strategy for a successful relaunch into the UK market was not in place.

6.13 Work focusing on establishing a permanent presence in the UK continued after the termination of Bucher's distribution agreement:

- The potential service provider that had been in discussions regarding working with Bucher terminated these discussions in December 2003 because of

regulatory concerns, and in February 2004 Bucher appointed Greenman (Municipal) Ltd (Greenman) as its after-sales service agent.

- Bucher appointed a UK salesman, who was employed through Greenman.
- Prospective Bucher UK staff, including a potential Managing Director, were interviewed in May 2004.
- In June 2004 the CEO of Bucher approved the preparation and implementation of the establishment of a Bucher-Schörling UK subsidiary in the last quarter of 2004. Bucher told us that approval was given by the CEO in light of the summary of Bucher's strategy and business plan 2005–2007.

6.14 In July 2004, during negotiations for the sale of a runway sweeper, Bucher-Schörling told a potential customer that Bucher had decided to establish a new partnership for after-sales service and, in the near future, its own UK subsidiary for sales and after-sales service. Bucher told us that this statement was made without the prior knowledge or approval of Bucher senior management. It told us that the statement reflected that the author of the letter believed that Bucher's plan was to establish a UK subsidiary.

6.15 As set out in Appendix C, Ennstone's interest in disposing of Johnston became clear during August 2004, when it announced that it had received enquiries from buyers for the business. As noted in paragraph 6.2, in October 2004 Ennstone announced that it had initiated talks with a number of parties.

6.16 Bucher told us that investigations into establishing a UK subsidiary were put on hold at Bucher Municipal level around September 2004, when Bucher was looking at opportunities to grow through acquisition. However, this decision was not communicated widely within the Bucher organization and some work on preparing for a UK relaunch continued.

### *Exiting the sweeper market*

6.17 Bucher told us that [REDACTED].

6.18 Aside from the possibility of other strategic acquisition opportunities, Bucher is a large sweeper manufacturer and has already implemented plans to reduce its cost base substantially through the establishment of a production facility in Latvia. It is not, therefore, clear that the merger with Johnston was critical to Bucher's ability to maintain a viable presence in the European sweeper market, or to meet its profitability targets. We saw no evidence of plans to exit the market, and do not believe this was a likely scenario.

### *Continuing without UK distribution arrangements*

6.19 Immediately before its acquisition of Johnston, Bucher was only selling a small number of units into the UK, without established UK distribution arrangements. As explained in paragraph 6.10, Bucher's UK distribution agreement for sweeper products ended at the end of November 2003.

6.20 Bucher told us that it had been investigating the possibility of a relaunch in the UK. The UK is Europe's largest market, and Bucher told us that it wanted to play an active role in the UK market but only if it could do so profitably. It also told us that to achieve sales in the UK it needed to establish distribution arrangements. From our study of its plans and what Bucher told us, we believe that Bucher was not planning to continue operating in the UK market without proper distribution arrangements.

### *Establishing a comprehensive distribution arrangement*

6.21 The third option we considered was that Bucher establish comprehensive UK distribution arrangements. This could be achieved either by setting up a UK

subsidiary to sell and distribute its products and provide after-sales service, or by appointing third parties to carry out these functions, or any combination of the two.

6.22 Bucher told us in its main submission (dated 28 April 2005) that, amongst other things:

- It had ‘little ability to enter the UK’, as it did not have access to a suitable distributor with national reach.
- It was ‘not a credible entrant’ into the UK sweeper market, and there were ‘other potential entrants who [were] much better placed than Bucher’.
- It had ‘developed no specific action plans for the UK beyond the aspirations set out in its 2004 three-year strategic review’, and ‘the 2004/5 budgeting process did not authorise or foresee any material new entry into the UK’.

6.23 Bucher subsequently told us that it had been investigating the possibility of establishing a UK subsidiary as a sales and after-sales organization (see paragraphs 6.10 to 6.15). It also told us that it had looked at contracting out after-sales services to a third party.

6.24 Bucher told us that [REDACTED]. We therefore considered [REDACTED].

6.25 [REDACTED].

6.26 We noted that Bucher had in train plans to reduce its cost base through the establishment of a plant in Latvia. Bucher told us that this would allow it to reduce its cost base. It could thus expect to reduce production costs. This would have allowed Bucher to increase margins on UK sales further.

6.27 In the absence of the merger we believe, therefore, that Bucher would have continued developing its plans for the UK, and would have made a significant effort to relaunch itself in the UK.

### ***Conclusions on the counterfactual***

6.28 We conclude that, in the absence of the merger:

- Johnston would have been sold to one of the trade or non-trade purchasers which had already expressed interest during the original sale process; and
- Bucher would have made a significant effort to relaunch itself in the UK.

## **7. Assessment of the competitive effects of the merger**

7.1 In order to assess the competitive effects of the merger, there were three key questions to address. The first related to the pre-merger situation; the second and third to the effects of the merger. The questions were:

- (i) Was Bucher a competitive constraint on Johnston in the UK prior to the merger, either through directly competing with Johnston or as a credible potential supplier?
- (ii) Would Bucher have imposed a competitive constraint on Johnston in the UK in the next few years in the absence of the merger?
- (iii) Had the merger weakened competition in the UK, or may it be expected to weaken competition in the UK, for example through raising barriers to entry and expansion, compared with the alternative?

7.2 In order to assess these questions, we considered first the nature of competition in the market for sweepers in the UK. Next, we assessed barriers to entry and expansion. We then considered whether, in the absence of the merger, Bucher was in a better or worse position than other suppliers to overcome these barriers, and compared this with the post-merger situation.

## ***The market for sweepers***

### *Customers*

7.3 As set out in paragraph 2.3, the majority of end-users of sweepers are local authorities. The two-thirds of UK councils that employ their own street-cleaning workforce only account for about a quarter of purchases of sweepers. Many of these local authorities hire sweepers from contract hire companies. The remaining three-quarters of sweeper sales consist largely of purchases by contract hire companies and street-cleaning contractors working for local authorities. In both of these cases, local authorities often influence the choice of sweepers used by specifying the type of products to be used.

### *Customer requirements*

7.4 There are a number of price and non-price factors which customers take into account when deciding on a sweeper purchase. The most important of these are set out below.

#### *Reliability*

7.5 In our customer survey, when asked what the single most important factor was in choosing a sweeper, the most frequently cited factor was reliability. This was borne out by other evidence we received. Several buyers told us that they would be prepared to select a higher-priced offering if it had better reliability. Providing reliable and rapid after-sales service, such as the supply of spare parts or response to a breakdown, was also an important factor, so that buyers could have confidence that their sweepers would function reliably throughout their working lives. We were told that sweepers were increasingly used in two or three shifts per day, and if a machine was off-road for any length of time the cost, both financial (mainly for contractors and hire companies) and in terms of public perception of the cleanliness of the streets (for local authorities), could be large.

### *Product performance*

- 7.6 The second most frequently cited single factor in choosing a sweeper was product performance. Buyers have clear (though sometimes differing) views on the best sweeper for a particular task. Their main criterion is to get the job done, which involves using sweepers that can perform the task to the standard required in the time available. Customers' experience of a sweeper and a supplier's reputation for performance (as well as reliability) are among the factors that our survey showed were important in a customer's decision as to whether a sweeper is likely to perform satisfactorily.

### *Price*

- 7.7 In our customer survey, the cost of a sweeper was only the third most frequently cited single factor quoted in choosing a sweeper. It was, however, the most frequently cited factor when buyers were asked to list all the factors they considered important. We received evidence that when some buyers know that two or more suppliers can meet their requirements, they often try to leverage one against the other to get the best price for a given level of quality.
- 7.8 Pricing in the sweeper industry is opaque. None of the suppliers we spoke to told us that they published price lists. One supplier also told us that Johnston had, on occasion, offered a sweeper at low or no cost when tendering to provide other types of sweepers. Products are highly differentiated because of the number and variety of add-on features demanded by customers. So even when the price paid in a particular contract is known, the information is not necessarily of great use to competitors or other buyers.

7.9 Because of the relative importance attached to the factors set out in paragraphs 7.5 to 7.8, we found that price was not the dominant consideration in the purchase of a sweeper.

### *Buying process*

7.10 The ways in which local authorities, street-cleaning contractors and contract hire companies purchase sweepers are discussed in Appendix F. Local authorities are required by statute to demonstrate that they are obtaining 'best value', which many achieve through open tendering. Large-value contracts are also covered by the EC Supplies Directive<sup>4</sup>, which requires public authorities to undertake a tendering process. Private sector organizations are not bound by these rules, and may therefore choose to negotiate directly with a supplier rather than operate a formal tender process. However, in order to win contracts for street-cleaning services, contractors must respond to local authorities' invitations to tender.

7.11 Our customer survey showed that, in their last purchase, customers approached on average three suppliers, and two of these provided competing bids. On average, there were another two or three suppliers which customers believed could have met their requirements. We noted, however, that there were more suppliers of some types of sweepers (generally the smaller ones) than others, so the survey responses may have reflected the purchase of some types of sweepers more than others.

7.12 We also heard evidence that some customers found benefits in purchasing all their sweepers of a particular type from one supplier. Although there are compatibilities in servicing and operator training that make such standardization helpful, several

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<sup>4</sup>Council Directive 93/36/EC of 14 June 1993 co-ordinating procedures for the award of public service contracts. OJ L199 (9 August 1993). Amended by Directive 97/52/EC.

customers to whom we spoke told us that it was not necessary to purchase all types of sweepers from the same supplier to achieve these efficiencies.

7.13 A supplier and a buyer suggested that the ability to offer a 'one-stop shop' for sweeper needs was of growing importance (see paragraphs 29 and 30 of Appendix G). However, several buyers told us that this was not a feature they considered important, and a number of buyers of large volumes of sweepers preferred to have multiple suppliers. Before the merger, Johnston was the only supplier able to offer products across the whole range of sweepers. Despite this, suppliers such as Applied Sweepers Ltd (Applied), Scarab Sweepers Ltd (Scarab), Schmidt UK Ltd (Schmidt) and Hako-Gruppe GmbH (Hako) were able to gain significant market shares for the particular types of sweepers they sold. We do not consider, therefore, that being able to offer a 'one-stop shop' is very important in the sweeper market.

7.14 Buyers of large numbers of sweepers told us that they were able to play competing suppliers off against each other to get the best price for a given level of quality. Although we saw no evidence of local authority buyers pooling their buying in order to achieve better terms, this may be because different local authority purchasers can have very different views on the mix and makes of sweepers needed in their fleet. However, we received evidence of local authorities working with contractors to use the contractor's purchasing power to obtain more favourable terms.

### *Suppliers of sweepers*

7.15 Currently, Johnston, Scarab and Schmidt are the largest suppliers in the UK market. Each sells over 100 units annually and offers a range of different types of sweepers. There is a middle tier of suppliers: Hako, Applied and Allianz Madvac (Madvac),<sup>5</sup> each of which sells between 50 and 60 units annually; these are concentrated on

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<sup>5</sup>Madvac was a subsidiary of Johnston until 2005. Its products are now distributed in the UK by Douglas.

smaller machines (none of them currently sells anything larger than a compact sweeper). Each of the remaining seven players (Bucher, Mathieu Yno SA (Mathieu Yno), Alfred Kärcher GmbH & Co (Kärcher), Tennant Company Inc (Tennant), Egholm Maskiner A/S (Egholm), Elgin Sweeper Company (Elgin)/Douglas Equipment Ltd (Douglas) and Dulevo International SpA (Dulevo)) sells up to 30 units annually. This group is made up mostly of recent entrants to the UK sweeper market.

- 7.16 In each product segment there are typically two or three major players (generally Johnston and at least one other) with large shares, and several suppliers with much lower sales. However, the market shares held by suppliers may not provide a true reflection of the competitive interaction between the suppliers. The key is for suppliers to establish themselves with customers so that they are seen as being credible in the sales process. A supplier's credibility is also important for customers who want to be able to use (or threaten to use) another supplier in their negotiations with suppliers (see also Appendix E, paragraphs 2 and 3).
- 7.17 There have been several entrants into the UK sweepers market in recent years. There are numerous examples of sweeper suppliers entering the UK, such as Elgin (which re-entered the market in June 2004 in partnership with the aviation support equipment supplier Douglas), Mathieu Yno and Schwarze Industries Inc (Schwarze). The majority of recent entrants have been suppliers of sub-compact and compact sweepers, and most of these have only achieved relatively small market shares (see Appendix E). In addition, existing UK sweeper suppliers have extended their product range—for example, Applied recently introduced a large sub-compact sweeper aimed at competing with some compact sweepers.
- 7.18 There is also a history of recent exits from supplying in the UK, such as Schwarze, which left the UK less than two years after it entered, and Elgin (prior to its recent re-

entry with Douglas). One supplier told us that it had decided not to introduce a new model in the UK as a direct consequence of the merger.

7.19 Our customer survey showed that at present most buyers were either very or fairly satisfied with the number of sweeper suppliers. Respondents also indicated that they generally considered bids to be very competitive. The degree of customer concern about this merger has been muted. There was more concern expressed by competitors. In general the concerns of competitors centred on the possible effects of the merged group as a larger, more powerful, supplier.

### ***Barriers to entry and expansion***

7.20 Details of our analysis on the barriers and their impact on different categories of supplier are set out in Appendix G. A detailed analysis of how the barriers specifically impact on different categories of existing and potential suppliers is in Appendix E.

7.21 We considered whether this market has significant barriers to entry and expansion. A precise product market definition as between all sweepers or particular types of sweeper is not required for this assessment. The only difference that would flow from separate product markets in the UK instead of our working definition of all sweepers in the UK is whether a manufacturer that extends its sweeper product range is characterized as entering into or expanding within a market.

7.22 In paragraph 7.16, we noted that it was important for suppliers to establish themselves with customers so that they were seen as being credible, judged by whether a supplier had crossed some threshold which signalled to customers a broad acceptance by the market of the reliability of their product and its support.

7.23 We considered the possible barriers to entry or expansion that had to be overcome to establish this credibility. We found these were of two types: marketing and support barriers, and production-related barriers.

7.24 The marketing and support barriers to entry and expansion we considered were:

- the ability to establish sales relationships with key customers;
- the cost and time to develop an effective distribution network;
- the ability to establish an effective after-sales service network;
- supplier reputation; and
- customer preferences.

7.25 The production-related barriers to entry and expansion we considered were:

- research and development (R&D) and engineering design skills;
- regulatory approval;
- production expertise; and
- the need for readily-available capacity.

7.26 We considered these possible barriers, in particular in the context of existing suppliers to the UK and other overseas sweeper suppliers, since these appeared to be the most likely suppliers to enter the market or expand their activities within it. We considered that all these likely suppliers with existing sweeper production would encounter few problems in meeting the R&D and engineering design skills, regulatory requirements and production expertise or capacity barriers. We did not consider these possible barriers further because they did not appear to be barriers to either entry or expansion for these types of suppliers (these barriers are assessed for potential entrants from related product areas in Appendix G). Each of the other barriers is considered in turn below (see paragraphs 5 to 37 of Appendix G for further details).

### *Establishing sales relationships with key customers*

7.27 We were told that the major sweeper suppliers in the UK had close relationships with their customers. Sales managers cultivated relationships to try and gain additional sales and to try to influence tender specifications. It took significant time and resources to develop these contacts, and we therefore concluded that the establishment of sales relationships constituted a barrier to entry or expansion for a supplier wanting to sell sweepers in the UK.

### *Developing an effective distribution network*

7.28 A credible sweeper supplier must have a distribution network—most customers told us that they would not consider buying brands supplied and distributed from outside the UK. These networks can be set up by the supplier (as a vertically integrated supply chain), but more commonly a supplier from outside the UK will find a UK distributor.

### *Establishing an effective after-sales service network*

7.29 An after-sales network is crucial. We were told that customers would not consider buying a sweeper that was not locally supported, even if it was offered at a substantial discount. The large private buyers we spoke to considered the ‘whole life’ cost of a sweeper, and factored into this the quality and availability of servicing and spare parts.

### *Supplier reputation*

7.30 As set out in paragraphs 7.5 to 7.8, buyers are, generally, reluctant to switch from tried and tested products. Suppliers need to build a reputation for product reliability, performance and service to persuade buyers to change their buying patterns; this constitutes a barrier to entry or expansion. We saw some evidence suggesting that the barrier to expansion enabling a supplier of one type of sweeper to supply another

type was lower than the barrier to entry, as buyers seem more willing to try a new product from an existing supplier than from a new one.

### *Customer preferences*

7.31 As set out in paragraph 7.12, some customers prefer to buy all their sweepers of a certain type or types from a single manufacturer, to simplify training or spare parts inventories. They may also achieve volume price discounts. Many customers, both in our customer survey and when we talked to them, indicated a preference for using their existing supplier for future purchases; reasons for this included familiarity and trust, servicing know-how, existing relationships, fleet consistency and convenience. We also heard about a preference on the part of some buyers for sweepers that were assembled in the UK. As customer preferences tended to favour existing suppliers, they represented a barrier to expansion and entry for suppliers wishing to sell to a customer to whom they had not previously sold.

### *Ability to overcome these barriers*

7.32 As set out in paragraph 7.15, the existing suppliers in the UK can be divided into three broad categories: the major suppliers (Johnston, Scarab, Schmidt); a middle tier of the suppliers with strong sales in one category of the outdoor sweeper market (Applied, Hako and Madvac); and the suppliers with a small presence in terms of units sold. There is also a category of potential entrants to the UK market. The barriers to entering and expanding for each of these groups is considered in detail in paragraphs 8 to 19 of Appendix E.

7.33 Expansion barriers for the first category are relatively low—they have in place the sales, distribution and after-sales networks, and have reputations as established, long-term players in the UK with established and successful products.

- 7.34 Similarly, expansion barriers appear to be relatively low for the middle tier of the market, although perhaps higher than for the main incumbents (see paragraphs 10 and 11 of Appendix E). Again, the middle-tier suppliers have the required sales, distribution and after-sales networks in place. They have successful products in the sub-compact range, and have recently introduced sweepers that are marketed as compact sweepers. Their established customer relationships and existing reputations should help them to expand their product range further should they choose to.
- 7.35 The remaining suppliers have limited sales and do not have significant market shares in any particular part of the outdoor sweepers market. Some are recent entrants, and lack the existing customer base or strong supplier reputation that more established incumbents can draw upon. Most have some form of existing distribution and after-sales arrangements, which can be built upon for further product expansion at some incremental cost. However, given their small level of recent UK sales, to expand they generally need further to develop customer relationships in the market. Some of the recent entrants in this group may be able to use their presence in the indoor sweepers market to help establish their credibility; others may be able to build upon their successes in other countries. But, generally, suppliers in this category face relatively higher barriers to expansion than the more established incumbents. We consider Bucher's ability to overcome these barriers in more detail in paragraphs 7.37 to 7.43.
- 7.36 Some suppliers not currently in the UK market could be at least as well placed to penetrate the UK market as some of the incumbents with small market shares. Like recent entrants, these potential entrants might be able to build upon any existing UK distribution and after-sales arrangements they might have for related products, any relevant UK customer relationships from related products, or any strong reputations for outdoor sweeper products from other geographic markets.

### ***Bucher and Johnston absent the merger***

7.37 We first consider Bucher's ability to overcome the barriers to expansion if the merger had not taken place. Bucher would have been larger than other suppliers in Europe. It would have had the financial resources of a large parent company behind it, and this would have given it some leeway to sustain losses whilst it relaunched in the UK. However, there would have been pressure on the UK business to achieve profitability quickly in order to help Bucher meet its profitability targets for sweepers. As noted in paragraphs 35 to 41 of Appendix E, there may have been timing issues relating to Bucher's possible relaunch, with several other suppliers having recently entered the UK market ahead of the possible relaunch.

7.38 Bucher lacked strong sales relationships with key customers in the UK. It had one salesman operating in the UK for most of 2004 and the start of 2005. Moreover, virtually all parties we spoke to expressed the view that it would have had to overcome damage to its reputation. This was caused by the failure to put in place a distribution and after-sales network when the distribution agreement with AssetCo ended (see paragraphs 6.11 and 6.12). As a result, for several months there was no UK after-sales agent to service Bucher sweepers or sell spare parts. However, a supplier and a customer both expressed the view that Bucher probably had sufficient financial resources to overcome this reputational barrier. We also heard evidence that some users had not had positive experiences with some Bucher sweepers in the past, suggesting that there may be a reputational barrier for Bucher to overcome with some potential customers, associated with past performance.

7.39 Bucher also lacked a distribution network. Its plans for a relaunch focused on establishing a UK subsidiary, rather than using a third party distributor. Although Bucher told us that it had not been able to develop a profitable business plan for establishing a vertically-integrated UK distribution network, we did not believe that

setting up a distribution network would necessarily have been an insuperable barrier to overcome given sufficient time and resources.

7.40 It is difficult to forecast reliably how long it would have taken for Bucher to overcome these barriers. As set out in Appendix G (paragraph 11), Bucher and Johnston commented upon this, and we received responses to our competitor questionnaire on how long it would take a new entrant to establish itself in the UK. On the basis of this evidence, we think that somewhere in the region of three to five years would be a reasonable time frame for Bucher to have established itself in the UK if the merger had not taken place.

7.41 Bucher had in place an after-sales service network, through Greenman. Bucher and a large customer told us that, whilst the existing network was sufficient to provide after-sales support to existing Bucher sweepers in the UK (and servicing the occasional new sale), it was unlikely to be sufficient back-up for a large-scale entry. Given the importance of the quality and speed of after-sales services, this is likely to have disadvantaged Bucher. We note that Bucher had been actively seeking an after-sales agent as part of its planning for a UK relaunch.

7.42 We have already described Bucher's damaged reputation in the UK (paragraph 7.38). We think that potential buyers may have been concerned that Bucher could leave them without support again, so Bucher was not well placed to overcome customer preferences and reputational barriers. As end-users typically expect their sweepers to last up to seven years, a long-term commitment to offer after-sales service is required.

7.43 In general, as set out in Appendix E, the barriers to expansion faced by Bucher appeared to be higher than for suppliers of sweepers with established sales,

distribution and after-sales networks already in the market. Bucher also faced reputation and customer preference issues at least as difficult to overcome as those faced by the other less established suppliers. The barriers for Bucher therefore appeared to be higher than the expansion barriers for the main and middle-tier incumbents, and some of the recent entrants and smaller players. However, we saw no evidence to suggest that the barriers were too high for Bucher to overcome given sufficient time and resources.

7.44 We believe that, in the absence of the merger, Johnston would have been sold to one of the trade or non-trade purchasers which had already expressed interest during the original sale process. Given Johnston's strengths prior to the merger, we have no doubt that Johnston would have been a strong and effective competitor, whoever acquired it. It would still have a strong sales, distribution and after-sales network, its existing reputation for reliability, and its large market share. It would also be able to offer the full range of sweepers, assuming it had been able to retain the rights to distribute Madvac products.

### ***The merged group***

7.45 The merged group would have the strongest sales capability and after-sales service in the market, as a result of acquiring Johnston's sales, distribution and after-sales service networks. It would also be able to build on Johnston's existing strong reputation with customers, and leverage that reputation on to Bucher products marketed under the Johnston brand.

7.46 The merged group would have at its disposal a broad and diverse range of products. It would be able to offer at least one product in each category of sweeper, from sub-compact through to specialist truck-mounted. Hence it could seek to market itself as a 'one-stop shop' for sweeper solutions.

- 7.47 It could seek to sell two complete ranges of products, but the potential advantages of this course of action would have to be weighed against the costs of producing similar products which may overlap and compete in their end-uses.
- 7.48 From Bucher the merged group would gain the backing of a parent company with large financial resources behind it. As at 31 December 2004, Bucher had market capitalization of CHF 534.6 million (£235.1 million), shareholders' equity of CHF 519.5 million (£228.5 million) and total assets of CHF 1,493.7 million (£656.9 million).
- 7.49 The merged group would also be able to benefit from scale economies in purchasing and production. Bucher estimated that the total cost savings would amount to [X] over the period 2005 to 2007. These would be achieved through joint sourcing of components, [X]. The merged group would also have the option of using any current spare capacity within Bucher or Johnston.
- 7.50 Bucher's Latvian assembly plant, opened in 2004, would allow the merged group to lower its cost base to the levels of other suppliers who have moved manufacturing out of western Europe.
- 7.51 The merged group would be the biggest-selling supplier in the UK, having inherited Johnston's products and infrastructure. The addition of Bucher products and know-how might further increase the merged group's market share to some extent.

### **Assessment**

#### *Was Bucher a competitive constraint on Johnston in the UK prior to the merger?*

- 7.52 Immediately prior to the merger, Bucher had only a small UK presence. From November 2003 onwards it had submitted only a few tenders to sell runway

sweepers, and had not tendered to sell integrated-chassis or truck-mounted sweepers. The evidence suggests to us that Bucher was not a direct competitive constraint on Johnston prior to the merger.

7.53 We saw a Johnston budgeting forecast which assumed that Bucher would relaunch in the UK. However, Johnston told us that this was simply an indication of seeing Bucher as a potential competitor, along with other companies listed in the document. Current and former Johnston staff told us that Bucher was not 'on the radar screen' as a competitor in the UK.

7.54 We concluded in paragraph 7.43 that the barriers to expansion for Bucher appeared to be higher than the expansion barriers for the main and middle-tier incumbents, and some of the recent entrants and smaller players. However, these barriers should not have been insuperable given sufficient time and resources.

7.55 In paragraph 7.40 we estimated that Bucher would have needed about three to five years to establish itself in the UK. There was little incentive for other suppliers to keep prices low when tendering just because of a possible relaunch of Bucher.

7.56 The evidence therefore leads us to the conclusion that Bucher's possible relaunch in the UK was not exerting a competitive constraint on Johnston at the time of the merger.

*Would Bucher have imposed a competitive constraint on Johnston in the UK over the next few years?*

7.57 There is a considerable degree of uncertainty over whether, if it relaunched, Bucher would have achieved a significant presence in the UK in the face of competition from better-placed rivals already established in the market. Given this uncertainty, we did

not find that Bucher would have imposed a significant competitive constraint on Johnston in the UK over the next few years had the merger not taken place.

*Has the merger weakened competition in the UK?*

7.58 We then considered whether the merger had weakened competition, or may be expected to weaken competition, in the UK, for example through raising barriers to entry and expansion, compared with the alternative. As set out in paragraph 7.51, the merged group would inherit Johnston's position as the market leader in outdoor sweepers, and be the leading supplier for all types of sweeper save for sub-compact sweepers. We expected the merged group to have a market share at least as large as that which Johnston would have had if the merger had not taken place, and maybe larger.

7.59 As shown in Appendix E, most of the competition in this market, certainly over the short to medium term, comes from suppliers already operating in the market. There are a large number of suppliers in this market; many of these are seen as credible suppliers when negotiating or tendering for sales. Many buyers try to leverage one supplier against another to get the best price for a given level of quality. These incentives on the customers will remain and they will be supported by the ease of finding alternative suppliers.

7.60 We compared the characteristics of the merged group with the likely characteristics of Johnston if the merger had not occurred (see paragraph 6.8). Through the merger Bucher would bring synergies, expertise, manufacturing capacity, R&D expertise and financial resources to Johnston. We did not believe that these advantages were enough materially to outweigh the effect of the market conditions set out in paragraph 7.59. Johnston was already strong in most of these areas. Customers seemed

satisfied that they were able to find enough suppliers for their needs pre-merger, and we did not expect this view to change appreciably as a result of the merger.

- 7.61 Concerns were put to us by competitors that the merged group would be able: (a) to raise prices; (b) to lower prices and drive competitors out of the market; and (c) to offer sweepers at low or no price as part of a package. Given what we concluded about the market and the merged group in paragraphs 7.59 and 7.60, we did not think that the merged group would be in a significantly better position to carry out any of these actions in the UK than Johnston would have been in the absence of the merger.
- 7.62 It was also put to us that, owing to its size, the merged group would discourage entry into the market, and would encourage exit from the market. One supplier (see paragraph 7.18) told us it had decided not to introduce a new model in the UK as a direct consequence of the merger. However, we did not consider that this would rule out the introduction of new models in the future.
- 7.63 We considered whether the merger would raise barriers to entry or expansion in this market. The major barriers for a company relate to that company's marketing and support arrangements, and how customers perceive the reliability, performance or cost of a sweeper. These barriers appear to be relatively insensitive to the changes in the market caused by the merger. We did not, therefore, expect barriers to rise as a result of the merger.
- 7.64 Overall, we thought that the merger would not lead to the market for sweepers in the UK being significantly less competitive than if the merger had not taken place.

## **8. Provisional conclusions**

- 8.1 We found that the acquisition of Johnston by Bucher resulted in the creation of a relevant merger situation.
- 8.2 Immediately before the merger Bucher had only a limited presence in the UK. We concluded that it did not exercise a significant competitive constraint on Johnston prior to the merger.
- 8.3 We did not find that, in the absence of the merger, Bucher would have imposed a significant competitive constraint on Johnston in the UK over the next few years, and we concluded that the merger would not lead to the market for sweepers in the UK being significantly less competitive than if the merger had not taken place.
- 8.4 In light of these conclusions we do not find that the merger has resulted or may be expected to result in a substantial lessening of competition within any market or markets in the UK.