

6 Conclusions

The merger situation

6.1. Under the reference dated 31 October 1989 (made under sections 64 and 69(2) of the Fair Trading Act 1973 'the Act') we are required to investigate and report whether a merger situation qualifying for investigation has been created in that enterprises carried on by or under the control of National Tyre Service Ltd (incorporated in the United Kingdom) have within the six months preceding the date of this reference ceased to be distinct from enterprises carried on by or under the control of Michelin Tyre PLC. For this purpose, the terms of reference refer to the test specified in paragraph (b) of section 64(1) of the Act (the assets test) without excluding the test in paragraph (a) of that section (the market share test). We are, however, required to exclude one of these tests if we find the other satisfied.

6.2. As was noted in paragraph 2.26, Michelin Tyre PLC (Michelin) acquired the whole of the share capital of National Tyre Service Ltd (NTS) from BTR PLC (BTR) on 23 June 1989. As is apparent in the note to Table 2 in Appendix 2.3, the value of the assets taken over exceeded £30 million, and the test specified in paragraph (b) of section 64(1) of the Act is therefore satisfied.

6.3. We accordingly conclude that a merger situation qualifying for investigation has been created. We have therefore to investigate and report whether the creation of that situation operates or may be expected to operate against the public interest. Since the merger was only completed in June 1989, and the two groups have been separately managed since that date, the consequences of the merger may not as yet have become apparent; in the public interest context therefore we are concerned with whether the merger may be expected to operate against the public interest.

The companies

6.4. The ultimate parent company of Michelin is Compagnie Générale des Établissements Michelin (CGE Michelin) based in Clermont Ferrand, France, which is beneficially interested in 92.75 per cent of Michelin shares. The Michelin Group operates world-wide as a supplier of tyres to the automotive industry. It is one of the largest tyre manufacturers in the world, with manufacturing plants in the European Community (France, Italy, Spain, and West Germany), North and South America, Africa and the Far East.

6.5. Michelin manufactures car, van and truck tyres under the Michelin brand in the United Kingdom for home sale and export, and also imports those and other categories of tyre from the Michelin Group's overseas plants for sale in the United Kingdom. All but a small percentage of replacement tyres are sold to distributors, including Michelin's wholly-owned subsidiary Associated Tyre Specialists Ltd (ATS).

6.6. ATS is the leading distributor of replacement tyres in the United Kingdom, its customers being both private individuals and commercial firms. It distributes both Michelin tyres and a wide range of tyres manufactured by other companies. Tyre sales account for about three-quarters of ATS's turnover; ATS also fits and supplies other automobile products such as exhausts, batteries, shock absorbers and wheels, and carries out MOT and vehicle safety checks at some of its outlets. The ATS tyre distribution business in the United Kingdom is carried on through 11 regional subsidiaries, and ATS also has a number of other subsidiary companies in the United Kingdom and Holland.

6.7. NTS was, before the merger with Michelin, the second largest distributor of replacement tyres in the United Kingdom. Tyre sales account for over 80 per cent of NTS turnover. NTS like ATS has broadened its range of car-related activities and sells and fits a wide range of parts including exhausts, batteries, brakes, clutches and shock absorbers as well as carrying out MOT tests. In March 1985 BTR acquired NTS from Dunlop, which had previously sold its tyre manufacturing business to Sumitomo Rubber Industries of Japan.

The acquisition

6.8. In 1989 BTR invited a number of interested companies, including some tyre manufacturers wishing to expand into distribution, to bid for NTS. Michelin told us that it made an initial bid in order to be placed on a short-list of bidders. Having been informed that it was on the short-list, Michelin then submitted a pre-emptive bid increasing its offer by £30 million to ensure both that it was successful and that competing bidders would not have access to NTS financial information.

6.9. The final price about £140 million including an advance of a sum of £25.8 million to NTS to repay indebtedness to the BTR group would appear high, given the previous profitability of NTS and the value of its assets. Michelin told us, however, that it had regarded the price as fully justified by the projected profitability of NTS. The latest estimates for 1989 and 1990 are for profits significantly lower than expected; but Michelin told us that it remains confident that adequate profits would be earned in later years to justify the cost of the acquisition.

6.10. We discussed with Michelin whether the price paid for NTS included any benefit that would result from enhancing Michelin's market power. Michelin denied this. Whatever Michelin's motives, however, one effect of the acquisition was to remove a main competitor in the distribution of tyres indeed the largest competing distributor and strengthen Michelin's position in this market.

6.11. Michelin told us that the main reason for the acquisition was to promote the development of autocentres, outlets providing 'fast-fit' servicing of cars and light vans, and in particular the sale of products and services other than tyres at these outlets. It also told us that, although it would determine the strategic development of ATS and NTS, NTS would as far as practicable be operated separately from ATS. However, the merger brings under common ownership of the major tyre manufacturer in the United Kingdom the two largest distributors by turnover of replacement tyres, and we have therefore to consider its impact on competition in the distribution of replacement tyres. Although, immediately before the merger, NTS had no direct involvement in the manufacture of tyres, we also have to take into consideration the vertical integration of the merged group with Michelin's activity as manufacturer of tyres, and importer of tyres from the Michelin Group's manufacturing outlets outside the United Kingdom.

The United Kingdom tyre market

6.12. The supply of tyres in the United Kingdom is a substantial and important economic activity. The value of new tyre sales (at manufacturers' prices) is estimated at almost £900 million in 1988, about one-quarter of which was supplied as original equipment (OE), for installation on new vehicles and the balance as replacement tyres. The price, the quality and the safety of the tyres supplied are all of considerable importance to the road user.

6.13. The largest category of tyre supplied accounting for 56 per cent of the value of tyre sales is that of car and light van tyres. Truck tyres account for a further 32 per cent of sales. Other categories of tyre supplied by ATS and NTS are earth-mover, agricultural and motorcycle tyres.

6.14. In considering the replacement tyre market, we have thought it appropriate in general to distinguish between categories of tyre car/light van tyres, truck tyres and other types of tyre although many of the ATS and NTS depots, and those of other distributors, supply all types of tyre. The majority of replacement car tyres are sold to individuals, and sale of car tyres can be regarded as

mainly consumer-oriented, more akin to a retail activity in which marketing and convenience of location play an important part.

6.15. The fitting of replacement truck tyres is technically more complex. Most tyres are fitted away from the distributor's depot, at the customer's own premises. A small proportion of tyre estimated at less than 10 per cent are fitted as a result of breakdowns. Rapid repair or replacement of tyres when breakdowns occur, to minimise the delay and inconvenience to the truck operators, is an important aspect of the service provided by distributors .

6.16. Even within the separate categories of car/light van and truck tyres, however, users' requirements vary widely. One estimate we have seen suggests that company fleet cars account for over 30 per cent of replacement car tyres supplied. Fleet owners may prefer to centralise arrangements for purchasing tyres. Within the truck tyre market, a significant proportion of tyre sales are to local hauliers, who mainly need to use local distributors; but larger fleets require national or extensive regional coverage. Even among the large fleet users, both car and truck, we found a wide variation in their perception of the number of suppliers able to meet their requirements, and of the effect of the merger.

The original equipment market

6.17. We understand that the bulk of tyres supplied as OE, for vehicles manufactured in the United Kingdom, are sold by the six producers with manufacturing facilities in the United Kingdom: Michelin, Goodyear, SP (Dunlop), Pirelli, Uniroyal and Avon, which are all members of the British Rubber Manufacturers Association (BRMA). There is a wider range of tyres fitted as OE on new vehicles imported into the United Kingdom.

6.18. Michelin is the largest supplier of OE tyres for vehicles manufactured in the United Kingdom, accounting by value for somewhat over one-third of OE car tyres and somewhat over one-half of OE truck tyres (and a similarly strong position in the supply of OE earth-mover tyres). Michelin also believes that it supplies tyres for a broadly similar proportion of vehicles imported into the United Kingdom.

6.19. Neither ATS nor NTS is involved in the supply of OE tyres, but the OE market does affect the supply of replacement tyres. The make of tyre fitted on a new car tends to be an important factor in the choice of at least the first replacement tyre on a car, and in replacing tyres on fleet cars. It was suggested to us that several manufacturers are prepared to supply OE tyres at relatively low prices, in order to obtain subsequent replacement tyre sales.

The replacement tyre market

6.20. The market for new replacement tyres is supplied by a wide range of manufacturers and importers. The six members of the BRMA themselves supply only about 60 per cent of replacement tyres in the United Kingdom (including tyres produced in the United Kingdom, and tyres imported by the members of the BRMA from their plants overseas). Imports have taken an increasing share of the replacement tyre market. As well as direct imports from about 30 other manufacturers, there is the 'grey' market. This means the purchase of branded tyres on the local market abroad for import into the United Kingdom when favourable opportunities arise mainly due to exchange rate movements or other factors.

6.21. Michelin is the leading supplier of replacement tyres in the United Kingdom, but its share of the replacement tyre market is considerably less than that of the OE market. In 1988 Michelin is estimated to have accounted for less than one-fifth (16 per cent) of the car tyre replacement market, and over one-quarter (26 per cent) of the truck tyre replacement market by volume, but higher shares of the value of sales (at manufacturers' prices): about one-fifth of car tyres and over one-third (about 35 per cent) of truck tyres.

6.22. As these figures suggest, the unit value of Michelin tyres tends to be greater than that of the market generally. Michelin tyres are marketed as of high quality, and Michelin does not attempt to compete with some of the lower-price imported tyres. Several users and distributors to whom we spoke confirmed that Michelin tyres were of high quality but were of the view that other major brands had now improved to narrow the differential.

6.23. In addition to new replacement tyres, retread or remould tyres are available for both truck and cars. Retread car tyres are substantially cheaper than equivalent new tyres, but have a limited role, not being suitable for all conditions. Retreads have a more significant role in the market for bus and truck tyres; Michelin truck tyres are regarded as particularly suitable for retreading because of their strength.

The distribution of replacement tyres

6.24. The bulk of tyres manufactured in the United Kingdom or imported into the United Kingdom are sold through distributors rather than direct to end users. The only Michelin sales direct to users are tyres sold under mileage contracts mainly to bus operators, and some sales to the public sector and utilities. Some tyres are also supplied to distributors through wholesalers.

6.25. The estimates we have seen suggest that there are as many as 5,000 specialist fitting centres which distribute car tyres, and somewhat over 2,000 outlets which distribute truck tyres. Car tyres are also available from a wide range of other outlets, such as some garages and vehicle distributorships, but these outlets account for less than 10 per cent of the market and may themselves buy from distributors.

6.26. Table 6.1 shows the number of outlets and estimated shares of the value of tyre sales (at final prices) of the leading tyre distributors by number of outlets. ATS and NTS together account for some 26 per cent of the value of sales of car tyres by distributors, and about 33 per cent of the value of truck tyre sales. Their combined share of volume of sales is somewhat less than this: some 21 per cent of car tyres and 30 per cent of truck tyres. ATS and NTS together additionally account for some 17 per cent of retread car tyres by volume, and 47 per cent of retread truck tyres (see paragraph 3.34). ATS and NTS together have more than double the number of outlets supplying car tyres than the nearest competitor, Kwik-Fit, and almost four times as many outlets supplying truck tyres than the next largest distributor. NTS alone has significantly more outlets than this distributor.

TABLE 6.1 **Leading distributors of new replacement tyres**

	<i>Number of outlets, end 1988</i>			<i>Market share, 1988 (by value)</i>	
	<i>Comprehensive (car and truck)</i>	<i>Car and light van only</i>	<i>Total</i>	<i>Car</i>	<i>Truck</i>
ATS	436	105	541	15	20
NTS	259*	149	408	11	13
Total ATS and NTS	695	254	949	26	33
Kwik-Fit**	-	349	349	8	-
Tyre Services GB	178	50	228	5	8
Standard	93	128	221	5	4
Motorway	167	20	187	5	7
Halfords**	-	111	111	***	-
Superdrive	-	104	104	2	-
Kennings	66	7	73	2	6
Charlie Brown	—	50	50	1	—
Total other leading distributors	504	819	1,323	28	25
Other	N/A	N/A	N/A	46	42

Source: MMC study.

*Includes 29 'Fleetserve' outlets which mainly supply tyres for truck fleets. NTS figures are as at June 1989.

**Kwik-Fit had over 400 outlets by the end of 1989, and Halfords 152 offering fast-fit service facilities.

***Less than 1 per cent.

6.27. Following the merger five of these chains are owned by tyre manufacturers: ATS and NTS by Michelin, Tyre Services GB by Goodyear, Central by Pirelli, and Motorway jointly owned by Avon and SP Tyres (owned by Sumitomo, the purchaser of Dunlop's tyre manufacturing business in 1984/85). Table 6.2 shows the share of these manufacturers and their distribution networks in both the supply and distribution of new replacement tyres. As shown in Table 6.2, these manufacturers account for about 64 per cent of the value of new replacement car tyres and 63 per cent of new replacement truck tyres (at manufacturers' prices). Their outlets ('equity' chains) account for some 41 per cent of the value of new replacement car tyres, and 52 per cent of the value of new replacement truck tyres distributed in the United Kingdom.

TABLE 6.2 **Manufacturers owning distribution outlets: estimated share of new replacement tyre markets, 1988**

Manufacturer	Distributor	Manufacturer's market share (by value)*		Distributor's market share (by value)**	
		Car	Truck	Car	Truck
Michelin	ATS	20	35	15	20
	NTS			<u>11</u>	<u>13</u>
				26	33
Goodyear	Tyre Services GB	}	}	}	}
Pirelli	Standard	}	}	}	}
Avon	}	} 44	} 28	} 15	} 19
SP Tyres***	} Motorway	}	}	}	}
Total		<u>64</u>	<u>63</u>	<u>41</u>	<u>52</u>

Source: MMC study.

*Share of supply of new replacement tyres by manufacturers and importers at manufacturers' prices.

**Share of distribution of new replacement tyres at final prices.

***SP Tyres acquired a majority interest in Motorway in 1989.

6.28. All of these equity chains distribute tyres of manufacturers other than their parent company; and conversely each of the manufacturers owning equity chains also supply other distributors. Ownership of distribution chains clearly, however, offers advantages to manufacturers. In particular the distributor is able to exert a degree of influence over his customers' choice of tyre. As shown in Table 3.15, all manufacturers with their own distribution outlets have a considerably higher share of sales in outlets they control than their share of the market generally.

6.29. Independent distributors are, however, important particularly in the distribution of car tyres. Of the large chains listed above, Kwik-Fit, Halfords (owned by Boots), Superdrive (a subsidiary of Shell) and Charlie Brown (owned by Kingfisher group) have all recently entered the market, or expanded rapidly, and several plan to expand further.

6.30. In contrast Kennings (a subsidiary of TKM) is the only independent distributor of truck tyres with more than 50 outlets. As shown in Table 3.8, we are aware of a number of regional distributors of truck tyres each with between 10 and 50 depots, but most independent operators have only one or two depots. Although these smaller distributors serve predominantly local markets, they are able to arrange breakdown cover outside their areas of operation through the National Tyre Distributors Association (NTDA), whose membership also includes the larger groups, and the Independent Tyre Distributors Network (ITDN), whose membership excludes these larger groups.

6.31. In order to assist in our understanding of the market, we conducted surveys of a sample of corporate customers, distributors, manufacturers, and importers. Somewhat over one-half of the customers who responded indicated that they regarded the distribution of tyres as very competitive on price, and fairly competitive on quality and range of products.

The distribution of Michelin tyres

6.32. About 40 per cent of Michelin sales of new replacement tyres of all types are to ATS; and a further 40 per cent to NTS and ten other national and regional groups which negotiate individual discounts for car or truck tyres with Michelin. The distribution of Michelin tyres is therefore relatively concentrated on larger distributors; the 12 distributors who account for some 80 per cent of Michelin sales account for only somewhat over 50 per cent of all tyres sold.

6.33. We received many criticisms that the Michelin discount structure penalised smaller distributors. As discussed in paragraph 3.59, Michelin publishes a scale of discounts from list prices which for car tyres in 1988 ranged from 39 to 44 per cent (including a guaranteed 4 per cent quarterly discount). Discounts to larger distributors are negotiated individually, the three largest customers (including ATS) receiving discounts of over [*] per cent. The purchase price to the largest distributors of car tyres in 1988 was therefore as much as [*] per cent below that to the smaller independents. One effect of this discount structure is that some smaller distributors find it cheaper to acquire tyres from ATS rather than direct from Michelin. Michelin's discount structure would therefore appear likely to inhibit smaller distributors in competing in the distribution of Michelin car tyres.

6.34. The evidence we have seen suggests that local distributors are at a lesser disadvantage in obtaining discounts on truck tyres than is the case with car tyres. For example, Michelin published discounts for the more popular sizes of heavy truck tyres range from 47 to 49.3 per cent, compared with discounts of over [*] per cent individually negotiated with some larger distributors. However, from the point of view of the small independent distributor, he pays a price of [*] per cent more for heavy truck tyres than the larger distributors (see Table 3.13).

6.35. A number of independent distributors felt that Michelin also gave preference to its own distribution outlets in other aspects of supply, for example in giving preference in supply to its own outlets, especially in periods of high demand. Michelin denied any such policy, and said that it dealt with orders on a strict chronological basis. Nevertheless, we have to consider whether as a result of the merger Michelin would be in a stronger position as both manufacturer and distributor to act to the detriment of its competitors, or users.

Michelin's plans for ATS and NTS

6.36. As shown in Table 6.1, at the time of our inquiry ATS had 541 depots, consisting of 436 comprehensive centres, and 105 car and light van service centres. The structure of the NTS network, and NTS's previous plan to develop that network, are shown in Table 6.3.

TABLE 6.3 **Number of NTS outlets**

	As at June 1989	As at January 1990	As planned by NTS*
Autocentres	43	47	}
Other car and light van	106	111	}
Comprehensive	230	211	130 approx
Fleetserve	29	34	60-70
Total	408	403	400+

Source: Michelin.

*Based on plans developed by NTS under BTR's ownership.

Before the merger, NTS was planning a reduction in the number of outlets supplying truck tyres from 259 as at June 1989, to about 200 (of which the number of outlets servicing mainly lorry fleets would be more than doubled to over 60); and an increase in the number of outlets servicing only cars and

* Figures omitted. See note on page iv.

light vans to 200 or more depending on site availability. Some 17 NTS depots (all but one of which was comprehensive) are at present being converted to autocentres.

6.37. As discussed in paragraph 6.11, Michelin told us that a main reason for the acquisition was to promote the development of autocentres, for which it believed many NTS depots were suitable for conversion. It presently envisaged that the ATS and NTS groups together would operate about 350 autocentres, and about 500 comprehensive depots, with disposal of about 100 surplus sites. The NTS concept of 'fleetserve' depots mainly servicing trucks would need to be reviewed. Michelin told us that this reduction in the number of comprehensive depots currently operated by ATS and NTS could be expected to lead to some loss of market share.

The effect on the public interest

6.38. We received many expressions of concern about the effect of the merger on competition in the distribution of tyres. About 60 per cent of distributors who responded to our questionnaire said that they thought the merger would affect competition, with the greatest concern among distributors of truck tyres. A similar proportion of users also said that the merger would adversely affect competition, with the greatest concern among larger users and those using truck tyres. There was, however, relatively little concern among those manufacturers which already owned a distribution network, or among the smaller importers which mainly supply independent distributors.

The effect of the ATS and NTS combined market share

6.39. In assessing the effect on the public interest, we have distinguished between car tyres, truck tyres and other forms of tyre. For convenience we separately consider in these categories the 'horizontal' effects of the merger, which result from the combined market share of ATS and NTS in the distribution of tyres, and the 'vertical' effects of the merger, which result from the ownership by Michelin as a tyre manufacturer of ATS and NTS, the main distributors of tyres. In practice we recognise that these issues will to some extent overlap.

Car tyres

6.40. The merged group with over 900 outlets is by far the largest distributor of car tyres, and double the size of its nearest competitor, Kwik-Fit. It at present accounts for some 26 per cent of the value of car tyre sales three times greater than that of Kwik-Fit and 21 per cent by volume.

6.41. In our view, the distribution of car tyres is a dynamic and competitive market, in which the merged group would have little scope to exercise market power. As shown in Table 6.1, there are several distributors with over 50 outlets who will continue to provide highly effective competition to the merged group, including a number independent of any manufacturer. Some of these groups supply a wide range of automotive products as well as tyres, and have shown their willingness to commit substantial resources to their development. There are also many smaller distributors. Competition is keen, with prices widely advertised and any variations in price soon apparent to users.

6.42. We considered whether smaller distributors were able to obtain tyres from manufacturers and importers at a sufficient discount to compete with the larger distributors. As we discussed in paragraph 6.33, Michelin's discount structure would appear likely to put smaller distributors at a disadvantage in competing in the distribution of Michelin car tyres. Nonetheless, local distributors would seem able to offer effective competition, in part by offering other ranges of tyre, including imported tyres. Michelin's discount structure by favouring the larger distributor may indeed be to its own disadvantage to some extent, and it told us that because of competition it was narrowing its range of discounts in car tyres in 1990.

6.43. A common concern of independent distributors was that the combined company would be in a position to secure still larger discounts, increasing the competitive disadvantage of the independents. Michelin told us that ATS and NTS were already receiving high discounts and that it

would not seek to aggregate the purchases of ATS and NTS in this way; indeed it doubted whether manufacturers (including Michelin itself) would be willing to grant higher discounts.

6.44. We would be surprised if ATS and NTS did not attempt to obtain advantage from the merger in this respect. However, we are doubtful whether the combined group would be in a position to secure significantly higher discounts from Michelin or other manufacturers than it does at present having regard to the volumes achieved by each of them separately, or inflict serious or lasting damage on its competitors to the detriment of the public interest. ATS and NTS would not, we believe, be in a position to drive their stronger competitors, who are also able to negotiate substantial discounts from manufacturers, from the market; and other tyre manufacturers would themselves have an interest in maintaining independent distributors. Even if some competitors were to withdraw because of the enhanced market power of ATS and NTS, Michelin would not in our view be able subsequently to raise prices significantly given the strength of the competition that would remain in the industry, and the likelihood of attracting further new entry into the industry.

6.45. We do not believe that there are significant barriers to entry into the car replacement tyre market. The acquisition and development of sites can be expensive: several companies have quoted costs to us of up to £0.5 million per site and in one case over £1 million. This would not, however, appear to have acted as a significant constraint on new entry, or the ability of existing firms to expand. The continued profitability of sales of car tyres coupled with the fact that distribution of car tyres can be combined with other services to motorists with higher profit margins has itself encouraged new competition. Recent entrants to the market include Halfords and Superdrive, each with over 100 outlets. Kwik-Fit has built up a network of over 400 depots in 15 years, mainly by acquisition but also partly by development of new sites, and plans to expand further. Several other companies such as Halfords have plans to develop substantial national chains over the next few years.

6.46. We considered whether the merger could have adverse effects in particular local areas. In almost all major towns there will continue to be a wide choice of distributor of car tyres, and indeed we are aware of few localities in the United Kingdom where the effect of the merger is to eliminate competition. In the few exceptional cases where the merger may significantly reduce local competition, any attempt by the combined group to abuse its position would, in our view, provide an opportunity for new entrants to these local markets. The threat of new entry may itself be a sufficient competitive discipline on the merged group.

6.47. Less than one-sixth of ATS sales of car tyres relate to national accounts car fleet operators who may require wide geographical coverage. Some car fleet operators expressed concern that there were few companies other than ATS and NTS able to offer an adequate geographical coverage, or facilities such as centralised invoicing, or nationally negotiated discounts. Other operators, however, were less concerned and believed there was sufficient competition from the other national and local distributors. In our view, provision of services to car fleet operators is likely to become an increasingly attractive activity to some of the larger distributors of car tyres and there would seem sufficient competition or potential competition to safeguard the interests of these users.

6.48. We have therefore concluded that the increase in market share as a result of the merger may not be expected to reduce competition in the distribution of car tyres.

The effect of vertical integration in supply of car tyres

6.49. A further concern, of distributors, customers and some manufacturers and importers, related to the vertical integration between Michelin as the leading supplier of tyres in the United Kingdom, and its ownership of ATS and NTS, the two leading distributors of tyres.

6.50. Many independent distributors feared that Michelin would cease to make its tyres available to them on reasonable terms. Some car fleet operators, whose choice of replacement tyre was determined by the make of tyre already fitted as OE, also feared that Michelin, as leading supplier of OE car tyres, would attempt to concentrate sales at its own distribution outlets, and reduce supplies to other distributors. Michelin denied that it would be in its interests as manufacturer or distributor to

pursue such a policy. It argued that, were it to cease to supply independent distributors, they would merely sell other makes of tyre instead.

6.51. In our view, Michelin's share of the supply of car tyres to distributors about one-fifth by value, less by volume would not seem sufficient to enable it seriously to damage the position of other distributors by withholding supply, or supplying on unfavourable terms. Were it to do so, we believe that there are sufficient alternative makes of car tyre which could as readily be sold by distributors. Michelin car tyres clearly have a strong brand image, reflecting their quality, Michelin's marketing, and Michelin's position as supplier of tyres as OE. This brand image is sufficient to support a price premium. If, however, Michelin car tyres are not available from independent distributors, or only available at even higher prices, we believe that the majority of car drivers would purchase alternatives of similar quality of other manufacturers. The damage would, we believe, be to Michelin, not to the independent distributor, the user, or the public interest.

6.52. Several users, manufacturers and importers were also concerned that ATS and NTS would reduce sales of other makes of tyre, or promote Michelin tyres at the expense of other makes. Michelin argued that, were it to do this, it would merely risk losing many of its customers to other distributors; and that to compete as a distributor it was necessary to sell all major brands of tyre.

6.53. Michelin tyres at present account for over 40 per cent of the volume of ATS sales of car tyres (see Table 3.17), considerably above Michelin's share of the market generally, and of its share of NTS sales. Michelin said that aside from occasional incentives to its sales force to promote Michelin tyres this did not reflect any deliberate policy on its part, but reflected ATS's own position in the market as a supplier of higher quality tyres such as those produced by Michelin.

6.54. Distributors would, however, appear to have influence over a user's choice of car tyre, particularly in circumstances where a user may be largely indifferent as to the brand he purchases. We would be surprised therefore if in due course Michelin car tyres would not be positively promoted at NTS. As shown in Table 3.17, were the share of Michelin sales at NTS outlets to be increased to that of ATS outlets, Michelin's share of the volume of car tyres supplied in the United Kingdom would be increased by about 2 per cent, to 18 per cent.

6.55. In our view, such increases in the share of the market for car tyres would not result in significant detriment to competitors or users. NTS was previously the largest independent tyre distributor; however, users would have considerable choice of alternative distributors if they were to be unable to obtain their preferred make of tyre at ATS or NTS outlets at a reasonable price. The market share of competing manufacturers or importers could be reduced, but they would still have the opportunity to supply the many independent distributors, accounting for more than one-half of car tyre outlets.

6.56. We do not therefore believe that as a result of the merger Michelin would be in any stronger position as both manufacturer and distributor to reduce or distort competition in the supply of car tyres. (We discuss the implications of vertical integration in the supply of truck tyres in paragraphs 6.70 to 6.76.)

Truck tyres

6.57. As was shown in Table 6.1, before the merger ATS with 436 outlets and NTS with 259 outlets were by some margin the largest distributors of truck tyres. The combined group at present has about 680 depots supplying truck tyres, almost four times larger than the next largest distributor, Tyre Services GB, owned by Goodyear, with 178 depots. Its market share at about 33 per cent of truck tyre sales by value, and 30 per cent by volume, is also about four times greater than that of its nearest competitor. As discussed in paragraph 6.36, Michelin intends ultimately to reduce the number of ATS and NTS depots supplying truck tyres to about 500, but this would still be about three times larger than any of its competitors. Michelin suggested that this rationalisation could itself cause some loss of market share, but this must in our view be uncertain. By rationalising depots in close proximity, Michelin should be able to retain most of the ATS and NTS customer base.

6.58. As discussed in paragraph 6.25, the number of outlets supplying truck tyres is significantly below that supplying car tyres, but still over 2,000 (most of which are comprehensive depots supplying both car and truck tyres), with over 350 companies in operation. The number of large chains is also lower, with only four companies including ATS and NTS having over 100 outlets and only six companies including ATS and NTS having over 50 depots distributing truck tyres. Of these six companies, NTS was, since its sale by Dunlop, the largest independent distributor. Only one of the six leading distributors, Kennings, with 66 outlets, is now independent.¹ The other five, with a total of some 1,120 outlets (of which ATS and NTS have 680), are now all owned by tyre manufacturers. ATS and NTS have one-third more outlets than the other four largest groups combined (including Kennings), and a market share by value one-third more than those groups combined. There are a number of smaller, regional chains, but most independent firms have only one or two outlets.

6.59. Unlike the car tyre market there has been little recent entry into distribution of truck tyres, other than recent acquisitions of outlets servicing both cars and trucks. The sale of truck tyres has been less profitable and has less scope to sell related products and services, and it would appear an unattractive market to enter, particularly on any national scale.

6.60. Most of the fitting of truck tyres is carried out at the customer's own premises; and distributors may be called on to change tyres at relatively little notice. Some customers may therefore require distributors' depots to be within 5 miles of their own premises, although others told us that a distance of up to 20 miles (depending on location) would be acceptable. To an extent, therefore, distribution of truck tyres can be regarded as a local market, in which local distributors play an important part.

6.61. The larger companies would, however, appear to have a number of advantages over the local distributors. They themselves receive higher discounts from manufacturers, allowing them in turn to offer higher discounts to larger tyre users. They are able to offer service to customers with depots in a number of locations, and also provide their own breakdown services over a wide area, whereas smaller distributors rely on the breakdown services provided outside their own area of operation by other companies through the NTDA and ITDN schemes.

6.62. The effect of the merger has been to remove the largest competitor to ATS. The disparity in size between the merged group and others in the industry would, in our view, put the merged group at a significant advantage over the other firms in the industry, a position in which we believe it could exert a degree of leadership over the prices to be charged.

6.63. In particular, the combined group would be in a strong position in offering services to companies requiring coverage nation-wide or beyond a local area. No statistics are available on the proportion of the total truck tyre market that can be regarded as national. `National accounts' accounts negotiated at head office represent about one-half of ATS truck tyre sales, of which ATS considered that `truly national accounts' represent somewhat less than one-half of truck tyre sales (see paragraph 3.48). Tyre costs of these users can be significant.

6.64. A number of larger users expressed concern that the merger would result in a significant reduction in competition between companies able to provide nation-wide coverage; some users indeed regarded ATS and NTS as the only distributors able to provide nation-wide coverage and believed that, as a result of the merger, they would lose their ability to get competitive tenders for their requirements. Others were less concerned.

¹[*Details omitted. See note on page iv.*]

6.65. Generally, these companies required service from a distributor's outlets close to their own depots, but preferred to have a contract with a national distributor rather than a number of local distributors to ensure a consistent tyre brand policy and to obtain discounts on a national basis and central invoicing. They also preferred to use the breakdown service of a national distributor, since they regarded their regular distributor as more likely to meet their requirements for use of particular tyres and able to offer a consistent service. Almost half of the local distributors who responded to our questionnaire generally themselves members of the NTDA and ITDN schemes also suggested that those schemes did not provide effective competition with the larger national chains.

6.66. In our view, the merger results in a significant reduction in the number of companies able to offer nation-wide coverage. ATS and NTS each have by some margin the largest national networks and together would be almost four times larger than their nearest competitor. Even were NTS to have reduced the number of its depots distributing truck tyres to 200, there would be only two competing networks of comparable size to NTS alone. Michelin argued that national cover could also be provided by Central and Kennings, each with between 50 and 100 outlets; but a number of users clearly did not regard networks of this size as adequate, and there would seem to be gaps in their coverage in several areas.

6.67. While those larger users requiring national coverage could, if dissatisfied with the prices charged or service offered by the merged company, divert all or part of their business to the smaller national distributors, or to the regional or local distributors, this would impose additional cost lower discounts or higher administrative costs upon them. We cannot therefore regard competition from these other sources as being as effective as the previous competition between ATS and NTS. Nor, unlike the car tyre market, do we believe that there is likely to be new entry into the distribution of truck tyres on a sufficient scale to provide an alternative source of nation-wide cover, or to provide effective competition to the merged group. Also, even smaller fleet owners on a more local basis may well prefer, for similar reasons, to deal with a group of distributors they know rather than separate distributors in several locations: the choice of distributor available for such users will also have been reduced by the merger.

6.68. We believe therefore that the merger will weaken competition in the distribution of truck tyres, particularly in supply to larger national users enabling the merged group ultimately to increase prices, or reduce standards of service, and believe in time that this may be expected to occur.

6.69. Although there is little noticeable concentration of ATS and NTS activities in particular geographical areas since they both have a strategic spread of outlets throughout the United Kingdom, the acquisition of NTS will also reduce competition to ATS in many local areas where the operation of the two groups previously overlapped. In most towns, there will still be a number of alternative distributors of truck tyres, but, as shown in Appendix 3.3, there are a number of locations where the merger has removed competition, or competition between national distributors. Unlike the car tyre market, we do not believe that new entry, or the prospect of new entry, would provide sufficient constraint on the merged group abusing its strong position in such local areas.

The effect of vertical integration in truck tyres

6.70. In paragraph 6.49, we referred to the concern of distributors, customers and some manufacturers and importers that arise from the vertical integration between Michelin as manufacturer and distributor of tyres.

6.71. We did not believe that Michelin's share of the supply of car tyres to distributors was sufficient to enable Michelin seriously to damage the position of other distributors by withholding supply or supplying on unfavourable terms. Michelin's share of the supply of truck tyres to distributors is, however, higher: over one-quarter (26 per cent) by volume and over one-third (about 35 per cent) by value. Some users of truck tyres specify the makes to be used, and some regard the Michelin tyre as of particularly high quality, and also particularly suitable for retreading.

6.72. We believe that, as a result of the merger, Michelin would be in a stronger position to favour its own distribution network in supplying Michelin truck tyres, either by price, or by giving priority to orders from its distribution network when there were shortages of supply and that, over time, it would increasingly do so. Given Michelin's importance as a supplier of truck tyres and the brand image of Michelin truck tyres as reflected in its premium price, such a policy would in our view be detrimental both to the competitiveness of other distributors, and to the choice of distributor available to users wishing to purchase Michelin tyres.

6.73. We also referred, in paragraph 6.52, to the concern of users, manufacturers and importers, that Michelin would reduce sales of other makes of tyres, or promote Michelin tyres at the expense of other makes. We did not believe that this would have a detrimental effect on competition in supply of car tyres.

6.74. Michelin argued that it was not possible to induce truck buyers to change their purchases, since these were sophisticated buyers who carefully assessed their tyre purchasing policy. The figures we have seen for the share of truck tyre sales at ATS and other equity chains would suggest that influence can be exerted over choice of truck tyres by some users. As shown in Table 3.17, were Michelin's share of the volume of truck tyres at NTS outlets to be increased to that at ATS outlets (about one-half), the effect would be somewhat greater than in the case of car tyres. Michelin's share of the volume of truck tyres supplied in the United Kingdom would be increased by about 2.8 per cent, to 28.8 per cent; and its share of the value of sales to as much as 38 per cent.

6.75. We believe the effect of any reduction in the market share of other manufacturers is potentially more serious in the case of truck tyres than of car tyres. Following the merger, equity chains control over 50 per cent of the market. This may be expected to reduce the ability of manufacturers without their own distribution network to compete, and inhibit the entry of new manufacturers to the market. If Michelin were to reduce the availability of other products, at NTS outlets, there could also be a reduction in the choice of tyre available for those users requiring nation-wide coverage, whose choice of distributor would have been reduced by the merger.

6.76. In our view the vertical integration between Michelin as the largest supplier of truck tyres in the United Kingdom and, by an even greater margin as a result of the merger, the largest distributor of truck tyres would put it in a position to exert considerable power in both these markets. It could use that power to enhance its share of the market as either distributor or manufacturer. Moreover, with a share of over one-third of the market as manufacturer, and almost one-third, by value, as distributor, competition is likely to be affected by the ambivalent attitude of the other firms in the industry. Competition from manufacturers and importers is likely to be constrained by their dependence on Michelin as a distributor of their products. Competition from distributors is likely to be constrained by their wish to distribute Michelin tyres, and in a market where truck tyre margins are low and better quality brands such as Michelin command a premium price, Michelin would be in a position to exert market leadership in price.

The effect on truck tyres: conclusion

6.77. We consider that the merger will reduce competition in the distribution of truck tyres in the United Kingdom, particularly reducing competition and choice for national and larger regional accounts, and competition in a number of local areas. Moreover, the vertical integration between Michelin as manufacturer and distributor of truck tyres will in the longer term strengthen Michelin's position further and may be expected to enable Michelin to reduce competition in both these markets. There is a real prospect in our view that the reduction of competition will, in due course, allow increases in the price of truck tyres to an extent that would not have been possible in the previous competitive conditions, and also reductions in the standards of service.

Other tyres

6.78. As a result of the merger, ATS and NTS are estimated to account for about 30 per cent of agricultural tyres distributed in the United Kingdom; a lesser proportion of earth-mover tyres (about 25 per cent by volume, 17 per cent by value); but less than 10 per cent of motorcycle tyres. Michelin is also estimated to supply about 25 per cent of earth-mover tyres, all imported from Michelin group plants overseas. We are not, however, aware of significant concerns about the impact of the merger in any of these other tyre categories.

6.79. As stated in paragraph 6.26, ATS and NTS have less than one-fifth of the market for retread car tyres but nearly one-half of the market for retread truck tyres by volume. A large proportion of retread car tyres sold by ATS are manufactured by the Michelin subsidiary, Langley Moor Remoulds Ltd. Michelin itself manufactures about one-half of ATS sales of retread truck tyres. Some manufacturers of retread tyres expressed concern that other makes of retread tyre would not be distributed by NTS, but Michelin told us that it did not have the capacity to increase its manufacture of retreads. Our views on the car retread market are similar to those on the car tyre market generally but any such concerns as regard truck tyres would be met by our recommendations below.

Conclusions and recommendations

6.80. We have therefore concluded that the merger may not be expected to reduce competition in the supply of replacement car tyres (paragraphs 6.48 and 6.56). We have on the other hand concluded that the merger may be expected to reduce competition in the supply and distribution of replacement truck tyres in consequence of Michelin's enlarged distribution activities and its vertical integration with the real prospect that this reduction in competition will allow an increase in the price of replacement truck tyres and reduction in standards of service offered by distributors (paragraph 6.77). We can see some benefits from Michelin's strategy of increasing the number of autocentres for fitting of car tyres and provision of other fast-fit services for motorists, but do not believe that the benefits outweigh those detriments to competition in the supply of truck tyres which result from the merger. We do not believe that the merger will produce any benefits in the distribution of truck tyres. We therefore conclude that the creation of the merger situation we have identified may be expected to operate against the public interest with the particular effects adverse to the public interest which we have identified in paragraph 6.77.

6.81. We are therefore required to consider what action (if any) should be taken for the purpose of remedying or preventing these adverse effects. Such action would need to be directed to rectifying the reduction of competition and other effects to which we refer. In our view the adverse effects arise only in the distribution of truck tyres. Divestment of all activities acquired from NTS, including those outlets only selling car tyres, would appear unnecessary, but divestment of those activities involved in the distribution of truck tyres would remedy these adverse effects. We would hope that this would also have the effect of maximising the competition that ATS would face in the distribution of truck tyres on a nationwide basis. This is not a case where we consider that there would be any enforceable behavioural undertakings for example, to operate NTS on an arm's length basis which would substitute for the loss of competition, or ensure that the merged group would not act in a way detrimental to competition.

6.82. We therefore recommend that Michelin be required to divest as a going concern those NTS outlets which are engaged in the distribution of replacement truck tyres at the date of this report excluding those outlets that, at the date of this report, NTS is currently converting into car-only outlets. This would require divestment in our view of the comprehensive outlets which distribute both car and truck tyres and the Fleetserve outlets which mainly distribute truck tyres as indicated in Table 6.3. It may be that this will involve the divestment of some outlets not principally relating to trucks but, if the adverse effects which we have identified are to be properly remedied, we see no alternative. We believe that this divestment should take place as soon as reasonably practicable and that the Office of Fair Trading should have discretion to implement this recommendation in a way which appears most likely to achieve the remedying of the adverse effects we have noted in this chapter. We further recommend that, pending completion of the divestment, the interim measures in force under which NTS is maintained as a separate enterprise should be maintained in force.

M S LIPWORTH (Chairman)

C C BAILLIEU

A FERRY

D G GOYDER

J D MONTGOMERY

Mr G C S Mather, being a member of the Group, dissents from the conclusions for the reasons set out in the note of dissent included in this report.

S N BURBRIDGE (Secretary)

30 January 1990