

6 Conclusions

The merger situation

6.1. Under the reference, dated 14 December 1989 (Appendix 1.1), we are required to consider whether arrangements are in contemplation which, if carried into effect, would result in the creation of a merger situation qualifying for investigation as defined in section 64(8) of the Fair Trading Act 1973 ('the Act') in that enterprises carried on by Trailerent Ltd (Trailerent) would cease to be distinct from enterprises carried on by or under the control of Tiphook plc (Tiphook), and that (section 64(1)(b) of the Act) the assets which would be taken over exceed £30 million. The assets of Trailerent exceed £30 million (Appendix 2.3) and the condition set out in section 64(1)(b) of the Act is therefore satisfied.

6.2. The acquisition of Trailerent was approved by Tiphook's Board on 13 December 1989 and a conditional contract to purchase Trailerent was entered into.

6.3. We consider, therefore, that arrangements are in contemplation by Tiphook which, if carried into effect, would result in the creation of a merger situation qualifying for investigation.

6.4. Consequently, we have to determine whether the creation of the merger situation which we have identified may be expected to operate against the public interest (section 69(1)(b) of the Act).

The events leading up to the merger

Trailerent

6.5. Trailerent is a subsidiary of Mercantile Group Plc (Mercantile) which, in turn, is wholly owned by Barclays Bank PLC (Barclays). Trailerent is solely a trailer rental company and carries on its business entirely in the United Kingdom. Following a review within Barclays, Mercantile decided early in 1989 to dispose of its non-financial activities. As part of this process, Mercantile invited offers for Trailerent. Five indicative bids were received; the highest, at £10.1 million, was from Tiphook, and it was accepted.

Tiphook

6.6. Tiphook's principal businesses are container rental, trailer rental and rail wagon rental. It entered the trailer rental market in 1982 when it acquired Central Trailer Rental. In November 1988 it acquired another trailer rental company, Rentco International. Its trailer rental division was then renamed Central Trailer Rentco (CTR). This division carries on business in the United Kingdom and nine other European countries. The proposed acquisition of Trailerent accords with Tiphook's intention to continue to expand its trailer rental fleet in the United Kingdom.

6.7. In response to our request, Tiphook provided us with copies of certain of its Board minutes and related papers, which presented the rationale for the Trailerent deal. These papers include a financial justification for the bid and refer to advantages Tiphook would obtain from various synergistic benefits and from being able to offer the most comprehensive range of trailers to the largest customer base. They also indicate a defensive element in Tiphook's motivation: avoiding

Trailerent being acquired by another party. We questioned Tiphook closely about this last reason. We concluded that the primary reason for the merger was to enhance Tiphook's ability to provide the best pan-European service, a legitimate competitive objective.

The trailer rental market

6.8. A little over 10 per cent of the goods moved by road in the United Kingdom (the wider road transport market) is carried in rented trailers. We estimate that in 1990 the trailer rental fleet was around 42,000 and accounted for about a fifth of the total United Kingdom trailer parc.

6.9. The customers of trailer rental companies fall into two categories: 'hire-and-reward' hauliers and 'own-account' manufacturers, wholesalers and retailers with their own transport fleets. Some trailers are used for supplementary storage, for example by retail chains. On the demand side, rental can broadly be split between transient (hire for periods of less than a year) and contract (hire for periods of a year or more). There is a degree of overlap between the two segments but three-quarters of transient rental is for periods of three months or less. The same trailers are used for both segments.

6.10. Trailer rental customers have the choice of outright purchase, hire purchase, finance leasing, transient or contract rental, and hire of hauliers. Operating leases are offered by rental companies and to a limited extent by others and are virtually indistinguishable from contract rental; the latter is more likely to have various additional services associated with it such as breakdown cover, servicing and maintenance, and tyre replacement. The longer the rental period, the more viable the purchase and finance lease options become. They are unlikely to be attractive at the short end of the transient segment which accounts for roughly half of trailer rental supply and where the flexibility of rental is of paramount importance to cope with seasonal and other fluctuations in demand. Here subcontracting is an alternative to meet short-term needs but in the hire-and-reward sector has the material disadvantage of requiring the haulier or distributor to share his profit margin with the subcontractor. More generally, trailer rental has become much more attractive than ownership in recent years because of tax and balance sheet advantages, and the greater flexibility of rental. Hence the strong trend towards rental which Tiphook expects to continue, although demand for trailers is presently subdued as a result of a slowdown in growth in the economy. This view is broadly shared by the present market leader, TIP, and by Trailerent. We have concluded that there is a separate trailer rental market which operates within the wider road transport market, where some alternatives are available to trailer rental customers. We return to this matter in our consideration of the public interest.

6.11. There are many different types of trailers which may be grouped in five main categories (see paragraph 3.4). Types range from basic chassis for carriage of containers to relatively sophisticated vehicles such as reefers, which are refrigerated trailers for temperature-controlled transport. There are about 20 manufacturers of trailers in the United Kingdom, mainly small firms. Two of the largest, York Trailers and Craven Tasker, also rent out trailers, trading as United Rentals and Eurofleet respectively.

6.12. The trailer rental industry is relatively new in the United Kingdom, where the first trailer rental operator (TRO) started trading in 1969. Our survey of TROs showed that the majority of them started renting out trailers in the late 1970s or in the 1980s. Before specialist rental companies became established some hauliers with surplus trailers rented them out, and a number of hauliers continue to do so. Within the wider road transport market, some tractor and truck rental companies supply trailers with their tractors, and they may also include drivers as part of the contract.

6.13. There are at least seven TROs with national networks of depots. We refer to them as national companies; apart from CTR and Trailerent, they include TIP, whose main activity is trailer rental, and haulage and contract distribution firms with trailer rental as part of their activities such as BRS Trailer Rental (BRS) and Dawson (paragraph 3.30). We estimate that TIP, the current market leader, has a share of about 31 per cent. Tiphook and Trailerent are the second and third largest operators, with around 23 per cent and 11 per cent respectively.

The public interest issues

6.14. The main public interest issue arising in this inquiry is the effect of the proposed merger on competition. There has been an increase in concentration in the trailer rental market in recent years. Tiphook took over Rentco in 1988 and TIP acquired CSL in 1989. The main parties estimate that the market share of the top five companies was 60 per cent in 1985 and 68 per cent in 1989. We estimate that the top five companies, following the proposed merger, would have nearly 80 per cent of the market. Tiphook would have around 34 per cent and TIP 31 per cent giving the top two companies about 65 per cent of the market. They would have over 70 per cent of reefers available for rental. The third ranking firm would be BRS with some 8 per cent of the trailer rental market. BRS is primarily a haulier and contract distributor and for the present seems to be concentrating on specialist trailers. The next largest firm is United Rentals, which rents out only trailers manufactured by its parent company. The remainder of the market is satisfied by a host of smaller firms.

6.15. Because of the substantial share of the market which the top two companies, Tiphook and TIP, would have following the proposed merger, the degree to which their behaviour would be constrained by the presence of a large number of smaller TROs and by competition in the wider transport market is the major issue of the inquiry. Before dealing with this in our discussion of competition, we turn to the effect of the proposed merger on manufacturers of trailers and on employment, and consider whether there would be any benefits from the merger.

6.16. The Commercial Trailer Association, representing 18 trailer manufacturers, was strongly opposed to the proposed merger on the ground that it would place excessive purchasing power in the hands of one customer. TIP and CTR are, however, already large customers for trailers and we do not believe that CTR's acquisition of Trailerent would make any significant difference, particularly as trailers purchased for rental are only part of the wider market for trailers. We also note that there is countervailing power in the concentration amongst the trailer manufacturers themselves; the top three have an estimated two-thirds of United Kingdom market for trailers (paragraph 3.6).

6.17. Although its plans have not been finalised, Tiphook's current expectation is that, following a merger, CTR and Trailerent would be run entirely separately. In due course, however, it expects to bring about some rationalisation. We accept its view that the effect on employment is unlikely to be substantial. It told us that lessons had been learned from the Rentco acquisition; the ensuing weeding out of depots had resulted in some deterioration in service and a consequent loss of business. If the acquisition of Trailerent went ahead, care would be taken to ensure continuity of service to customers.

6.18. We can see no significant benefits to the public interest from the proposed merger. Any savings from rationalisation are likely to be small.

Competition

6.19. The main parties argued in their joint submission that the merger would not reduce competition. The great majority of rental customers required only a small number of trailers which could generally be met by one or other of the TROs operating in their particular area. It followed that local and regional TROs with small-scale operations were a considerable competitive force. Further small-scale entry into a growing market was facilitated by the ready availability of finance for the purchase of trailers, which were regarded as good security. Entry on a larger scale was also possible, particularly by those who were already active in related transport markets and were ideally placed to enter the trailer rental market.

6.20. The main parties also considered that the alternatives to rental in the wider transport market (paragraph 6.27) constrained the behaviour of all TROs. Developments in this wider market such as the lifting of restrictions on cabotage within the European Community (EC), development of a unified EC rail network and the continued development of inter-modal road/rail systems would serve to enhance that constraint.

6.21. Our surveys of competitors and of CTR's and Trailerent's customers revealed that for the most part competitors were not concerned about the merger. The views of customers were mixed. 43 per cent of respondents, including a high proportion of Trailerent's customers and reefer operators, saw adverse effects, believing that there would be an opportunity for CTR to exploit its market position after the acquisition of Trailerent (see, for example, Transfrigoroute's evidence at paragraph 5.34). 38 per cent were unconcerned and 15 per cent believed that there would be beneficial effects such as lower prices, increased choice, improved services. The remaining 4 per cent saw both adverse effects and benefits. The Freight Transport Association found little concern about the merger amongst its members; there was a very low response to its enquiries from its broad membership (paragraph 5.30).

6.22. The Department of Transport did not believe that the high level of competition in the trailer rental market would be damaged by the merger. If the rental sector of the wider transport market became uncompetitive there would be a movement back into ownership and this could happen quite quickly because second-hand trailers were readily available. It also felt that recent EC decisions, particularly the progressive relaxation of cabotage restrictions, would be likely to introduce a whole new competitive edge in the European road haulage market.

6.23. We were conscious of the fact that our survey of the trailer rental market took place in the low season when rental business normally declined and that this normal reduction in business had been exacerbated by a downturn in retailing, a sector which generates a large demand for trailers. Nevertheless we are satisfied that the vigorous price competition that was described to us by many in the industry, notably in transient rental, is not a temporary phenomenon. The evidence on prices emerging from our own survey was mixed but it was clear that some customers were able to negotiate prices down during periods of low demand. Our survey showed that the prices of national TROs were sometimes higher than those of local TROs and in other cases lower. Additionally, we have no doubt that prices in the contract rental segment of the market are constrained by the leasing/purchasing options for customers. Tesco's contract with Hill Samuel for the leasing of trailers is a good illustration of this (paragraphs 4.19 and 5.27).

6.24. It emerged from our survey of customers that their three most important considerations when renting trailers were availability, reliability and price. We have seen no indications that the national TROs have any particular advantages in respect of reliability or price, but, although competition is essentially on a local basis, the national TROs generally have an advantage as regards availability of the wide variety of trailers required by customers. We understand that in practice there is little substitution between types of trailer. We found that the average size of fleet per depot of CTR and TIP, excluding trailers on contract, was over 250 and for Trailerent it was 150. Some of the other larger companies had similar sizes. Excluding the largest nine firms the average size was 35 per depot. It follows that customers are more likely conveniently to obtain the types of trailers they need, in the required numbers, from one of the large, usually national, TROs. We also found that large national haulage companies which rent trailers both on contract and for transient use prefer to negotiate with one or more national companies for all their needs, and so obtain a more competitive price. It is not surprising, in these circumstances, that our survey showed that 62 per cent of customers of CTR and Trailerent did not use local or regional firms, 30 per cent used them only occasionally and 8 per cent used them as a principal source. However, the evidence also points to a knowledgeable group of customers who are industry professionals used to shopping around for the best price, so stimulating competition.

6.25. We recognise that if the merger proceeded there would be a new situation. CTR would overtake TIP and become the market leader with around 34 per cent of the trailer rental market, followed by TIP with about 31 per cent. The concern, particularly in the transient rental segment, is that the merger would leave two strong specialist TROs with approaching a two-thirds share of the market. There is always a danger in such circumstances that neither party would see vigorous price

competition as being in its best interests. While TIP's evidence indicated that it did not consider that it competed primarily on price, clearly TIP had found it necessary to respond to price competition. In this industry, competition will continue to come from the smaller TROs, particularly in the transient rental market, and, if prices drift upwards, is also likely to come from new entry encouraged by those better prices and the relative ease of market entry (paragraph 6.29).

6.26. The merged companies and TIP would together have over 70 per cent of the supply of reefers for rental, which reefer customers generally found disturbing (paragraphs 5.24 and 5.34). Reefers are at the expensive end of the trailer rental market; for example, they represented only 8 per cent of the total rental fleet but were likely to generate at least twice that proportion of the turnover of TROs. It is a segment which is particularly likely to continue to grow vigorously in line with the expected further increase in demand for temperature-controlled haulage. We should therefore expect reefer rental to provide an attractive niche for existing TROs and possible new entrants. In this connection we note that some of the larger TROs such as BRS, United Rentals and Dawson have a strong interest in specialist trailers, particularly reefers (see paragraphs 3.33 and 5.11). No doubt members of Transfrigoroute would be very ready to use alternative sources to CTR and TIP if there were any signs that they were ceasing to be competitive.

6.27. We concur with the main parties' argument that the proposed merger could not isolate the enlarged CTR from the more general pressures to which all TROs are subject in the wider transport market (paragraph 4.27). Although some users have a preference for rental for reasons of flexibility, accounting and taxation, we believe that the options available in the wider market are a real constraint on the behaviour of TROs. As we have already indicated, this is most obvious in the contract rental segment and the longer end of the transient segment where purchase and finance leasing are likely to be acceptable options for some customers. Even at the shorter end of the transient segment there is the option of subcontracting (paragraph 6.10). We also believe that this pressure from the wider market is likely to increase as road hauliers respond to changes in the EC such as the development of a unified EC rail network, including the Channel rail tunnel, and the recent start on the process of relaxing restrictions on cabotage (paragraph 3.7).

6.28. We note, finally, that in every area where CTR and Trailerent both have depots, at least one of the other top five national TROs is present (paragraph 3.39). We consider, therefore, that the proposed merger raises no particular concerns as regards regional competition.

New entry

6.29. We accept the view of the main parties and others who gave evidence to us that barriers to entry into the trailer rental market are low. Finance is readily available on the security of the trailers, and we have seen no evidence of significant economies of scale which would be likely to deter such entry on a small scale in a growing market. There are no technical barriers to entry nor does it appear to be difficult for companies to obtain appropriate sites. This view is supported by the existence of a large number of small rental companies successfully competing in their localities. Entry on a more extensive basis is clearly possible, particularly for a company with an existing network of sites.

Conclusions on competition

6.30. While there will be a significant increase in concentration as a result of the proposed merger, the trailer rental market will continue to be competitive. The principal factors leading to this conclusion are:

- (a) there is vigorous price competition in the industry and, stimulated by a knowledgeable group of customers who are industry professionals used to shopping around for the best prices, it may be expected to continue (paragraphs 6.23 and 6.24);

- (b) prices in the contract rental segment of the market are constrained by the leasing/ purchasing options for customers (paragraph 6.23);
- (c) as to the transient rental segment of the market, competition will continue to come from the smaller TROs with the additional constraint of the customer's option to subcontract in the wider road transport market (paragraphs 6.25 and 6.27);
- (d) we expect reefer rental to provide an attractive niche for existing TROs and possible new entrants (paragraph 6.26);
- (e) no particular concerns arise regarding regional competition (paragraph 6.28); and
- (f) barriers to entry into the growing market are low (paragraph 6.29).

Conclusions on the public interest

6.31. The only significant public interest issue arising out of the proposed merger is its effect on competition in the trailer rental market. Despite the increased concentration caused by the combination of the second and third largest operators, we believe that the trailer rental market will continue to be competitive. We conclude, therefore, that the merger may be expected not to operate against the public interest.

P H DEAN (Chairman)

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2 April 1990