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Decision No. 598

Determination pursuant to the Commerce Act 1986 in the matter of an Application for clearance of a business acquisition involving:

Elite Truck Rentals Limited

and

ORIX Truck Rental (a division of ORIX New Zealand Limited)

The Commission:	David Caygill Peter JM Taylor Donal Curtin
Summary of Application:	The acquisition by Elite Truck Rentals Limited of 100% assets of ORIX Truck Rental (a division of ORIX New Zealand Limited).
Determination:	Pursuant to section 66(3) (a) of the Commerce Act 1986, the Commission determines to give clearance to the proposed acquisition.
Date of Determination:	2 March 2007

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EXECUTIVE SUMMARY

1. A notice pursuant to s 66(1) of the Commerce Act 1986 (the Act) was registered on 6 December 2006. The notice sought clearance for the acquisition by Elite Truck Rentals Limited of 100% of the assets of ORIX Truck Rental division (a division of ORIX New Zealand Limited).
2. Elite has strong shareholding, management and familial relationships with TR Group Limited (TR Group). In the Application, the Applicant submitted that it accepted that the Application will be processed as if TR Group were the Applicant. The Commission has proceeded on the basis that Elite and TR Group should be viewed as one entity.
3. For the purposes of the acquisition, the Commission considers that the relevant markets are:
   - the national market for the provision of medium commercial vehicle rental services; and
   - the national market for the provision of heavy commercial vehicle rental services.
4. The Commission also considered whether or not there is a separate market for long-haul rental customers who prefer to enter into rental agreements with the rental firms that operate a nationwide network of branches providing heavy commercial vehicle rental services. While it appears that long-haul transport firms could potentially be captive to nationwide network rental companies, the Commission is of the view that the ability of these rental firms to separate out long-haul customers, and then price discriminate against them, seems to be limited. Accordingly, the Commission defines a broad market for all customers.
5. The Commission considers the likely counterfactual scenario to be:
   - ORIX continues to dispose of its assets and continues to trade until an appropriate buyer can be found for the downsized fleet.
6. In respect of the medium commercial vehicle rental services market the Commission is of the view that given the number of existing competitors in the market, the proposed acquisition is unlikely to result in a substantial lessening of competition in the factual scenario compared to the counterfactual scenario.
7. In the heavy commercial vehicle rental services market, in the counterfactual scenario, the Commission considers that ORIX would be likely to provide less of a constraint on the TR Group than it currently does. Even with ORIX as a declining competitor, it would still constrain TR Group in the counterfactual, but that constraint would be absent in the factual scenario. As the other existing competitors are not capable of providing nationwide coverage in terms of vehicle delivery and/or replacement, the Commission considers that without the possibility of nationwide expansion of existing competitors the difference between the factual and counterfactual scenarios would be likely to be significant.
8. The Commission considers that existing competitors, The Hire Company and Hirepool, would be able, easily and readily, to expand their businesses if the TR Group raised prices or lowered its service.
9. The Commission also considers that the threat of potential entry would be a competitive constraint in the factual scenario. The Commission considers that

firms could enter the market relatively easily and quickly and within two years. The Commission considers that the threat of this potential entry is likely to influence the behaviour of the TR Group post-acquisition.

10. Accordingly, the Commission is of view that in the factual scenario the TR Group would be constrained from exerting its market power through a combination of factors, including:

    - expansion from existing competitors; and
    - the threat of potential competition.

11. The Commission is therefore satisfied that the proposed acquisition will not have, nor would be likely to have, the effect of substantially lessening competition in any of the affected markets.

THE PROPOSAL

1. A notice pursuant to s 66(1) of the Commerce Act 1986 (the Act) was registered on 6 December 2006. The notice sought clearance for the acquisition by Elite Truck Rentals Limited of 100% of the assets of ORIX Truck Rental (a division of ORIX New Zealand Limited).

PROCEDURE

2. Section 66(3) of the Act requires the Commission either to clear or to decline to clear the acquisition referred to in a s 66(1) notice within 10 working days, unless the Commission and the person who gave notice agree to a longer period. An extension of time was agreed between the Commission and the Applicant. Accordingly, a decision on the Application was required by 2 March 2007.

3. The Commission's approach to analysing the proposed acquisition is based on principles set out in the Commission's *Mergers and Acquisitions Guidelines*.[1]

STATUTORY FRAMEWORK

4. Under s 66 of the Act, the Commission is required to consider whether the proposal is, or is likely to have the effect of substantially lessening competition in the market. If the Commission is satisfied that the proposal is not likely to substantially lessen competition then it is required to grant clearance to the Application. Conversely if the Commission is not satisfied it must decline. The standard of proof that the Commission must apply in making its determination is the civil standard of the balance of probabilities.[2]

5. The substantial lessening of competition test was considered in *Air New Zealand & Qantas v Commerce Commission*, where the Court held: [3]

> We accept that an absence of market power would suggest there had been no substantial lessening of competition in a market but do not see this as a reason to forsake an analysis of the counterfactual as well as the factual. A comparative judgement is implied by the statutory test which now focuses on a possible change along the spectrum of market power rather than on whether or not a particular position on that spectrum, i.e. dominance has been attained. We consider, therefore, that a study of likely outcomes, with and without the proposed Alliance, provides a more rigorous framework for the comparative analysis required and is likely to lead to a more informed assessment of competitive conditions than would be permitted if the inquiry were limited to the existence or otherwise of market power in the factual.

6. In determining whether there is a change along the spectrum which is significant the Commission must identify a real lessening of competition that is not minimal.[4] Competition must be lessened in a considerable and sustainable way. For the purposes of its analysis the Commission is of the view that a lessening of competition and the creation, enhancement or facilitation of the exercise of market power may be taken as being equivalent.

7. When the impact of market power is expected to be predominantly upon price, for the lessening, or likely lessening, of competition to be regarded as substantial, the anticipated price increase relative to what would otherwise have occurred in

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[1] Commerce Commission, *Mergers and Acquisitions Guidelines, January 2004*.
[2] Foodstuffs (Wellington) Cooperative Society Limited v Commerce Commission (1992) 4 TCLR 713-722.
[3] *Air New Zealand & Qantas Airways Ltd v Commerce Commission*, unreported HC Auckland, CIV 2003 404 6590, Hansen J and K M Vautier, Para 42.
[4] Fisher & Paykel Limited v Commerce Commission (1996) 2 NZLR 731, 758 and also Port Nelson Limited v Commerce Commission (1996) 3 NZLR 554.

the market has to be both material, and ordinarily able to be sustained for a period of at least two years or such other time frame as may be appropriate in any give case.

8. Similarly, when the impact of market power is felt in terms of the non-price dimensions of competition such as reduced services, quality or innovation, for there to be a substantial lessening, or likely substantial lessening of competition, these also have to be both material and ordinarily sustainable for at least two years or such other time frame as may be appropriate.

ANALYTICAL FRAMEWORK

9. The Commission applies a consistent analytical framework to all its clearance decisions. The first step the Commission takes is to determine the relevant market or markets. As acquisitions considered under s 66 are prospective, the Commission uses a forward-looking type of analysis to assess whether a lessening of competition is likely in the defined market(s). Hence, an important subsequent step is to establish the appropriate hypothetical future with and without scenarios, defined as the situations expected:

   - with the acquisition in question (the factual); and
   - in the absence of the acquisition (the counterfactual).

10. The impact of the acquisition on competition is then viewed as the prospective difference in the extent of competition in the market(s) between those two scenarios. The Commission analyses the extent of competition in each relevant market for both the factual and the counterfactual, in terms of:

    - existing competition;
    - potential competition; and
    - other competition factors, such as the countervailing market power of buyers or supplies.

THE PARTIES

ORIX New Zealand Limited (ORIX)

11. ORIX is a wholly-owned subsidiary of ORIX Australia Corporation Limited, which is in turn a wholly-owned subsidiary of the ORIX Corporation of Japan, a major international finance company.

12. In New Zealand, ORIX commenced business operations in 1994. ORIX currently provides fleet leasing services[5] for [ ] vehicles, including about [ ] heavy commercial vehicles, throughout New Zealand.

13. Currently, the ORIX rental[6] truck fleet consists of [ ] trucks and trailers. The rental division has management centres in Auckland, Palmerton North, Christchurch and Dunedin.

Elite Truck Rentals Limited (Elite)/ TR Group Limited (TR Group)

14. Elite is a privately owned company that has been recently created for the purpose of purchasing the ORIX truck rental division. The Applicant advised the Commission that it has never traded. Elite has strong shareholding,

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[5] See paragraph 68 for a description of the term ‘leasing’.
[6] See paragraph 69 for a description of the term ‘rental’.

management and familial relationships with TR Group Limited (TR Group). In the Application, the Applicant submitted that it accepts that the Application will be processed as if TR Group were the applicant.

15. In the context of the prohibition on a person acquiring assets of a business or shares if that acquisition would have, or would be likely to have, the effect of substantially lessening competition in a market, section 47(2) of the Act provides that a reference to a person includes two or more persons that are interconnected or associated. Section 47(3) clarifies that two or more corporate entities are associated if one, either directly or indirectly, is able to exert a substantial degree of influence over the activities of the other. The Commission is of the view that, in this context, a substantial degree of influence means being able to bring real pressure to bear on the decision-making process of the other.

16. In coming to a view on association, the Commission must consider each case on its particular facts.[7] Among the factors the Commission usually takes into account in determining association are the:

- nature and extent of ownership links between the companies;
- presence of overlapping directorships;
- rights of one company to appoint directors of another; and
- nature of other shareholder agreements and links between the companies concerned.

17. The Commission also considers the interaction between these various factors. For example, the Commission assesses the nature and extent of the communications between persons, and the apparent influence of one person on the key strategic decisions of the other.[8] The question for the Commission is whether two or more enterprises can, for the purposes of commerce and competition, be regarded as one.[9]

18. The TR Group advised the Commission that interests affiliated with Ron Carpenter own 85% of the ordinary shares of TR Group and interests affiliated with Andrew Carpenter own 15% of the ordinary shares of TR Group. Further, there are two directors of TR Group: Andrew Carpenter, and his father Ron Carpenter. Elite confirmed that Andrew Carpenter is the Managing Director of TR Group.

19. Andrew Carpenter advised the Commission that interests affiliated with himself own the majority of the shares in Elite and that Elite will be primarily controlled by himself.

20. In the Application, Elite considered that it was not legally interconnected or associated with TR Group, yet acknowledged that it will at the time of acquisition be affiliated with, and substantially influenced by, Andrew Carpenter. Elite and Andrew Carpenter have subsequently confirmed that Andrew Carpenter will have substantial influence over both Elite and TR Group by way of his affiliation with interests that own shares in both companies and his ability

[7] *Commerce Commission v New Zealand Bus Ltd* (2006) CIV 2006-485-585, para 212.
[8] Commission Decision No. 388: New Zealand Seafood Investments Ltd / Basuto Investments Ltd, para's 16 – 24.
[9] Commission Decision No. 278: Air New Zealand Ltd/Ansett Holdings Ltd/Bodas Pty Ltd, especially para's 180 – 182.

to control decision-making. This confirms close ownership links between the two companies and the presence of overlapping control by the same persons.

21. For the purposes of considering this Application, the Commission proceeds on the basis that Elite and TR Group should be viewed as one entity in determining whether the acquisition of ORIX by Elite would have, or would be likely to have, the effect of substantially lessoning competition in a market.

22. TR Group is a family-owned business that has been operating for 15 years and has 70 staff. TR Group leases and rents trucks and trailers. Its fleet consists of approximately [ ] trailers and [ ] trucks. TR Group has offices in Auckland, Whangarei, Wellington, Tauranga, Hamilton, Napier, Palmerston North, Christchurch and Dunedin.

OTHER PARTIES

Vehicle Rental Firms

Budget Rent a Car Limited (Budget)

23. Budget is wholly-owned by the AvisBudget Group. Budget is primarily a car rental firm, and operates 3,500 offices worldwide. Budget also provides rental vans and trucks in Australia, North America and New Zealand.

24. In New Zealand, some offices are part of the Budget Corporation, some are agencies, and some are franchises. Budget agencies manage the fleet from a depot for a percentage of the profits, but the assets are owned by Budget. Budget franchises own their fleets independently of the corporation, but use the Budget brand and infrastructure.

Hirepool (NZ) Limited (Hirepool)

25. Australian private equity firm Next Capital has an 80% stake in Hirepool, through Hirepool's parent company Rakino Group Limited. The remaining shares are owned by Hunter Powell Investments and senior Hirepool management.

26. Hirepool provides an equipment hire rental service through its 60 business units spread throughout New Zealand. It operates businesses that provide rental services in equipment ranging from home handyman to heavy construction equipment. It has recently acquired a number of rental businesses including: portable sanitation rental; portable energy generators rental; a party hire firm and rental vehicles.

27. In December 2006, Hirepool acquired Henderson Car Rentals Limited. Henderson operated a vehicle rental business of approximately 500 vehicles. It has vehicle depots in Henderson, Takapuna, Mount Wellington and Hamilton.

The Hire Company (The Hire Company)

28. The Hire Company is involved primarily in heavy equipment hire. It has six branches throughout New Zealand. Its equipment is used in gold mining, coal mining, roading and construction. The Hire Company also owns heavy commercial rental vehicles. Its annual turnover is approximately [ ].

Southern Equipment Centre Limited (Southern Equipment)

29. Southern Equipment is a privately-owned and operated transport and general engineering business, with branches in Invercargill, Dunedin and Christchurch.

Southern Equipment manufactures heavy equipment and trailers, as well as leasing and renting equipment and trailers. Southern Equipment has 20 staff and a [ ] turnover.

Other commercial vehicle rental firms

30. In addition to the firms listed above, there are a number of other providers of commercial vehicle rental services, including:

- Metropolitan Rentals Limited;
- North Harbour Rentals Limited;
- O'Neill Rentals Limited;
- Car and Commercial Rentals Limited;
- Commercial Refrigeration and Wholesale;
- Hanson Rentals Limited;
- Charter Trucks Limited; and
- Equipment and Transport Leasing Limited (ETL).

Vehicle Leasing Firms

Fleetpartners

31. Fleetpartners originated from the amalgamation of two vehicle leasing companies: Avis Lease and Truck Leasing Limited. Fleetpartners primarily provides fleet leasing services for [ ] cars and light commercial vehicles and [ ] heavy commercial vehicles throughout New Zealand, from its offices in Auckland, Wellington, Palmerston North and Christchurch.

Custom Fleet

32. Custom Fleet is the vehicle leasing division of GE Fleet New Zealand Limited, which is ultimately a wholly-owned subsidiary of the General Electric Company in the United States. The General Electric Company is listed on the New York Stock Exchange.

33. Custom Fleet's main business functions are the funding and management of vehicle fleets to corporate customers. In New Zealand, Custom Fleet has approximately [ ] lease vehicles, and provides management services for [ ] vehicles across New Zealand. Of those vehicles, approximately [ ] are commercial vehicles and [ ] are tractor units.

Vehicle leasing and rental customers

34. A sample of major commercial vehicle leasing and rental customers are the following:

Toll Tranz Link

35. Toll Tranz Link is a division of Toll NZ Limited, which is a wholly-owned subsidiary (via Toll Group (NZ) Limited) of Toll Holdings, an Australian-based transport and distribution company. Toll NZ is involved in rail freight operations and forwarding, and long-haul transport.

36. Toll Tranz Link operates a road transport division consisting of [ ] trucks. It owns [ ] transport vehicles and the remainder of its fleet consists of sub-contracted independent operators.

Halls Refrigerated Transport Limited (Halls)

37. Halls is a privately-owned freight transport company, specialising in refrigerated goods. Halls has a fleet of [ ] refrigerated trucks and trailers. Halls has nine distribution centres through out New Zealand.

Trans Otway Limited (Trans Otway)

38. Trans Otway is a privately-owned distribution and line haulage company, specialising in refrigerated goods. Trans Otway has a fleet of [ ] vehicles.

Linfox Logistics (N.Z.) Limited (Linfox)

39. Linfox is wholly-owned by Linfox Pty Limited, a privately-owned Australian logistics and transportation company. In New Zealand, Linfox has [ ] vehicles in its fleet.

Symons Transport Limited (Symons)

40. Symons is a privately-owned transport company, specialising in liquid goods, particularly milk. Symons has [ ] vehicles in its fleet.

Mainfreight Limited (Mainfreight)

41. Mainfreight is a logistics and transport firm. It operates a road transport fleet of [ ] vehicles, of which [ ]% are sub-contracted independent transport operators.

Dynes Transport (Tapanui) Limited (Dynes)

42. Dynes is part of a group of eight transport companies. It is a privately-owned firm, specialising in transporting stock, milk and logs. Dynes has [ ] vehicles in its fleet.

INDUSTRY BACKGROUND

43. Approximately 80% of all freight in New Zeeland is transported by road at some stage. The industry employs approximately 22,000 people and has an annual turnover of $4 billion.[10]

44. The road transport industry is made up of approximately 5,000 firms, largely locally-based, family-owned and run businesses. Most companies operate fewer than five trucks and the average fleet size is under nine vehicles.[11]

45. In the past 10 years, transport firms in New Zealand have increasingly become reliant on sub-contracting. Firms provide an umbrella parent company, win contracts and then sub-contract specific loads to small, independent firms. Examples of this type of firm include Mainfreight and Toll Tranzlink.

46. Vehicle renting and leasing providers service the road transport industry by providing vehicles, either on a temporary basis (through renting) or on a semi-permanent basis (through leasing).

PREVIOUS COMMISSION DECISIONS

47. The Applicant submitted that the Commission's previous decisions, Decision 584 and Decision 585, are highly relevant to the present Application. The

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[10] Statistics New Zeeland Transport Fact Sheets, see http://www.stats.govt.nz, last accessed 15 March 2007.

[11] Road Transport Forum New Zealand, see http://www.rtfnz.co.nz, last accessed 15 March 2007.

Commission also considers that Decision 478 is relevant to the present Application.

Decision 478: Custom Fleet (NZ) Limited/ Hertz Fleetlease Limited (31 October 2002)

48. On 16 October 2002, the Commission received an Application for clearance for Custom Fleet (NZ) Limited to acquire the whole of the issued share capital of Hertz Fleetlease Limited from Ford Motor Credit Company.

49. The Commission considered that the relevant markets were the markets for:

- the provision in New Zealand for fleet leasing services; and
- the provision in New Zealand for fleet management services.

50. The Commission granted clearance for the acquisition on the basis that the combined entity would be constrained, within both the fleet leasing and fleet management markets, by existing competition within these markets.

51. In relation to the fleet leasing market, the Commission considered that the combined entity would face additional constraints from:

- potential competitors, given that there are no significant barriers to entry; and
- its customers, in the form of countervailing power, where customers have the ability to switch easily between lease providers, or even to self-fund vehicles.

Decision 584: GE Fleet New Zealand/Custom Fleet (NZ) Limited (5 July 2006)

52. On 7 June 2006, the Commission received an Application for clearance for GE Fleet New Zealand Limited to acquire the business of Custom Fleet (NZ) Limited.

53. The Commission considered that the relevant markets were the national markets for:

- the provision of fleet leasing services; and
- the provision of fleet management services.

54. In the national fleet leasing market, the Commission considered that the combined entity would face constraints from the presence of several major competitors, and from competition from small lease companies and finance companies. Accordingly, the Commission considered that there would be little difference between the factual and the counterfactual.

55. In the leasing market, GE Fleet did not provide a comprehensive fleet management service and, in addition, there was significant existing competition. Accordingly, the Commission considered that there would be little difference between the factual and counterfactual scenarios.

Decision 585: ORIX New Zealand Limited/Truck Leasing Limited (20 July 2006)

56. On 7 July 2006, the Commission received an Application for clearance for ORIX New Zealand Limited to acquire 100% of the shares of Truck Leasing Limited, trading as Esanda Fleetpartners. Esanda Fleetpartners was then owned by UDC Finance Limited, a subsidiary of the Australia and New Zealand Banking Group Limited.

57. The Commission considered that the relevant markets were the national markets for:

- the provision of fleet leasing services; and
- the provision of fleet management services.

58. In the national fleet leasing market, the Commission considered that the combined entity would face constraints from the presence of several major competitors, and from competition from small lease companies and finance companies. Accordingly, the Commission considered that there would be little difference between the factual and the counterfactual.

59. In the national fleet management market the Commission considered that there would be little difference between the factual and the counterfactual, on the basis that neither ORIX nor Esanda operated in this market to any notable extent.

MARKET DEFINITION

60. The Act defines a market as: [12]

> "… a market in New Zealand for goods or services as well as other goods or services that, as a matter of fact and commercial common sense, are substitutable for them."

61. For the purpose of competition analysis, the internationally accepted approach is to assume the relevant market is the smallest space within which a hypothetical, profit-maximising, sole supplier of a good or service, not constrained by the threat of entry, would be able to impose at least a small yet significant and non-transitory increase in price, assuming all other terms of sale remain constant (the SSNIP test). The smallest space in which such market power may be exercised is defined in terms of the dimensions of the market discussed below. The Commission generally considers a SSNIP to involve a five to ten percent increase in price that is sustained for a period of one year.

62. The Applicant submits that the relevant market for the proposed acquisition is:

- the national market for the supply of vehicle rental services.

63. The Applicant considers that this is consistent with the market definitions used by the Commission in Decisions 585 and 584.

Product Dimension

64. The greater the extent to which one good or service is substitutable for another, on either the demand-side or supply-side, the greater the likelihood that they are bought and supplied in the same market.

65. Close substitute products on the demand-side are those between which at least a significant proportion of buyers would switch when given an incentive to do so by a small change in their relative prices.

66. Close substitute products on the supply-side are those between which suppliers can easily shift production, using largely unchanged production facilities and little or no additional investment in sunk costs, when they are given a profit incentive to do so by a small change to their relative prices.

67. In defining the relevant product market, the Commission has assessed the degree of demand- and supply-side substitution of the following:

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[12] S 3(1) of the Commerce Act 1986.

- leasing and renting vehicles;
- passenger vehicles and goods vehicles;
- different types of commercial vehicles, including light, medium and heavy; and
- different types of customers.

Leasing and renting vehicles

68. The Commission uses the term 'leasing' in this instance to describe the type of arrangement whereby a leasing firm purchases a specific vehicle at a customer's request and leases the vehicle to the customer for up to 75% of the vehicle's economic life.[13]

69. The Commission uses the term 'renting' in this instance to describe the activity whereby a rental firm purchases a range of vehicles that are likely to meet the demand of a customer requiring a vehicle on a daily/weekly/monthly basis, or a customer is unsure about the length of time for which it requires the vehicle.

70. Customers informed the Commission that they rent vehicles for breakdowns/maintenance and for peak season. Toll Tranzlink said that rental is for seasonal fluctuations and daily spikes. Likewise, Trans Otway, Dynes, Coca-Cola Amatil, and Linfox all advised the Commission that they use rental vehicles for breakdowns/maintenance and to cover additional work in their peak seasons.

71. Leasing customers advised the Commission that they lease vehicles to have semi-permanent vehicles in their fleets. Fleetpartners said that leased trucks are custom built and sourced for a specific use. Leased vehicles are built to customer specifications, from the make/model of the vehicle down to the CD player preference. Leasing firms also informed the Commission that leased vehicles will often be painted with the customer's name, logo, branding or signage, in the case of leased goods vehicles.

72. For instance, Custom Fleet advised the Commission that customers choose between buying outright and leasing vehicles. Custom Fleet stated that a customer approaches them and asks for a deal on a particular truck. From there, Custom Fleet builds a quote and, if the customer wishes to proceed, Custom Fleet then sources the truck.

73. The Commission has found that rental prices are usually determined on a daily, weekly or monthly basis, but are always higher than leasing prices. Leasing prices are generally determined on a monthly and kilometre basis.

74. Industry participants also distinguished leasing and renting on the grounds of availability. Renting, especially for breakdowns, is time sensitive. Mainfreight advised the Commission that freight is time critical, especially fast moving consumer goods. Therefore, renting firms need to be able to deliver a vehicle quickly. Mainfreight stated that the rental firms it uses can usually have a vehicle to a breakdown site within an hour.

75. On the other hand, customers requiring a leased vehicle place an order and, depending on the specifications, wait for between 6-12 weeks. In some cases, it

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[13] The length of time of an operating lease is determined by Inland Revenue Department's depreciation rules, which state the maximum lease period, for which depreciation may be claimed, is 75% of the vehicle's useful life.

can take a lot longer; for instance, Custom Fleet stated that it had one specialist vehicle that took six months to be delivered from when it initially placed the order.

76. From a supply-side perspective, leasing and renting vehicles are different types of businesses. In essence, leasing primarily involves the provision of a financial arrangement, whereas renting involves maximising the utilisation of a stock of assets (e.g. trucks) over a period of time.

77. Industry participants, including Custom Fleet, The Hire Company and Budget, confirmed that renting and leasing are totally different businesses, and that rentals are almost the exact opposite of leasing. Industry participants considered that the aim of a lease business is to dispose of the asset to a customer straight away, while renting is about owning and utilising the asset over a period of time.

78. There are also different financial risks associated with leasing and renting vehicles. The financial risk for rental firms is associated with the non-utilisation of the assets, i.e. vehicles sitting in the rental yard not being used. Custom Fleet stated that there is a high risk in the rental industry due to the need to predict demand, whereas for leases, specific orders are placed with the truck suppliers to meet the customer's requirements. The financial risks in leasing are associated mainly with the difference between the residual value of the vehicle once it has been returned from lease and its market value.

79. Industry participants informed the Commission that providers of vehicle leasing would not be likely to switch quickly, within one year, to renting in response to a SSNIP. [ ] stated that in the face of a SSNIP, leasing firms would not be likely to enter due to the high capital cost needed (even though this would not be sunk), and because the existing rental firms could just put their prices back down and it would be a big investment for a temporary return.

80. The Commission considers that the both lack of demand-side and supply-side substitutability means that there are likely to be separate markets for the provision of rental vehicle services and leasing vehicle services.

81. As there is no aggregation in the provision of vehicle leasing, the Commission has not considered this market further.

Provision of vehicle rental services

82. Industry participants informed the Commission that in some cases there may be a degree of overlap in substitutability between different types of vehicles, for instance light commercial vehicles such as cargo vans or utility cars may be used to transport both goods and passengers. The fact that light commercial vehicles can have a secondary field of application, for instance the transport of people, does not imply that there would be any significant substitutability between light commercial vehicles and passenger vehicles. The Commission considers that passenger rental vehicles tend not to be substitutable for commercial rental vehicles.

83. From the supply-side, if a supplier of passenger rental vehicles wished to expand into the commercial vehicle rental market, it would need to consider buying a range of vehicles and significantly altering its customer base.

84. The Commission considers that the both lack of demand-side and supply-side substitutability means that there are likely to be separate markets for passenger rental vehicles and commercial rental vehicles.[14]

85. As there is no aggregation in the provision of passenger rental vehicles, the Commission has not considered this matter further.

Provision of commercial vehicle rental services

86. Commercial vehicles used for transporting goods range from light weight units requiring a car licence[15] (e.g. a 2,000 kilogram furniture truck), to heavy weight vehicles used to transport considerable weights on regional and long distance routes requiring specialist training and a heavy vehicle licence (e.g. a 10-ton curtainside truck). Land Transport New Zealand defines licence categories that drivers need in order to be able to drive vehicles with different total weight ranges, as outlined in Table 1.

Table 1: New Zealand Licence Categories

Licence type	Gross Laden Weight (GLW) or Gross Combined Weight (GCW)[16]	Examples of vehicles	Example of use
Class 1	a vehicle that has a GLW of 4,500 kg or less	Passenger car, passenger van, cargo van, utility car (ute), 2,000 kilogram tip truck, 2,000 kilogram furniture truck	Private use
Class 2	any rigid vehicle with a GLW of more than 4,500 kg but less than 18,000 kg	3,000 kilogram furniture truck, 5-ton furniture truck, 7-ton tip truck	Metropolitan deliveries, furniture moving
Class 3	any combination vehicle with a GCW of more than 12,000 kg but	Refrigerated rigid truck with a 6x2 axle, 2 axle simple transport trailer, 2	Metropolitan bulk deliveries with trailers e.g. Coca-Cola uses a lot of

[14] This is consistent with decisions made by the Australian Competition and Consumer Commission and the Office of Fair Trading. See: *Avis Renta A Car System/Budget Car Rental*, 22 August 2002, ANZSIC 7741, and *Aerial Consolitated Transport Pty/Southern Cross Chauffeured Limousines and Canberra Hire Cars Limited*, 28 February 2006, C2006/284

[15] A car licence is a Class 1 licence.

[16] Land Transport New Zealand, Factsheet 11 available at http://www.landtransport.govt.nz/factsheets/ last accessed 17/2/07, defines vehicle weights as:

Gross laden weight (GLW) is the greatest of the following:

- any weight specified (following the latest modification, if applicable) as a vehicle's gross laden weight by the vehicle's manufacturer
- any weight specified as the gross laden weight of a particular vehicle (or a vehicle of its kind) by the Director of Land Transport
- the weight of a vehicle together with any load it is carrying, including any equipment and accessories.

Gross combined weight (GCW) is the sum of the gross laden weights of the vehicles that make up a combination vehicle.

	less than 25,000 kg	axle curtainside pull	this type of truck
Class 4	any rigid vehicle with a GLW of more than 18,000 kg	10-ton curtainside truck, Tractor units, Alloy tippers	Construction companies use alloy tippers to transport gravel
Class 5	any combination vehicle with a GCW of more than 25,000 kg	Tractor unit towing a trailer, Alloy tipper towing a trailer	Tractor units towing trailers are used for transporting goods over long distances e.g. groceries

87. The European Commission, in several merger decisions namely Renault/Volvo, Iveco/Fraikin and Volvo/Scania decisions[17], identified three market segments according to the gross vehicle weight of trucks. These product markets were:

- light trucks up to 7 tonnes;[18]
- medium trucks between 7-16 tonnes; and
- heavy-duty trucks >16 tonnes.

88. This decision to separate trucks into three different product markets was based on the truck manufacturing industry standards, which defined technical differences of the trucks and, accordingly, their production lines. The EC particularly paid attention to the technical differences between medium and heavy segments of the market. Furthermore, the EC concluded that the technical boundary between these two product groups corresponded to a commercial distinction, which made it possible to differentiate between two groups of customers.

89. It appears that the truck manufacturing industry and transport regulation authorities clearly distinguish between three groups of commercial vehicles according to their gross laden weight, thus suggesting that there are likely to be three separate groups of customers using different groups of products.

90. The Commission, therefore, considers that such distinction is relevant to the commercial vehicle rental market and further differentiates between light, medium and heavy commercial vehicles.

<u>Light commercial vehicles</u>

91. In New Zealand, a Class 1 licence (commonly called a ‘car licence’) can be used to drive any vehicle up to 4,500kg of gross laden weight (GLW). The Commission uses the term ‘light commercial’ to refer to commercial vehicles less than 4,500kg GLW.

92. On the demand-side, industry participants considered that this separation of licences means that customers are divided into the general public and commercial operator drivers. Industry participants informed the Commission that commercial vehicles less than 4,500 kg are marketed to the general public,

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[17] Case No IV/M.004, RENAULT/VOLVO, 07/11/1990; Case No. COMP/M.1739, IVECO/FRAIKIN, 3/12/1999; Case No COMP/M.1672, VOLVO/SCANIA, 15/03/2000.

[18] In RENAULT/VOLVO, this product market was limited to trucks below 5 tonnes gross vehicle weight.

while commercial vehicles over 4,500kg are marketed to commercial firms. Since the driving requirements as well as the vehicle specifications are different for medium and heavy commercial vehicles, it is unlikely that the general public will switch to using such vehicles as a substitute for light commercial vehicles.

93. From the supply-side, if a supplier of commercial rental vehicles up to 4,500kg wished to expand into medium or heavy commercial vehicles, it would not be able to do so without incurring significant capital costs in acquiring a sufficient range of rental vehicles, though not all of these costs would be sunk. Nevertheless, the decision to invest a significant expenditure into rental vehicles over 4,500kg will be heavily influenced by the supplier's ability to target commercial firms rather than general public.

94. The Commission, therefore, considers that light commercial vehicles are likely to fall into a separate product market from that for the provision of medium or heavy commercial rental vehicles.

95. As there is no aggregation in light commercial vehicles area, the Commission has not explored this area further.

<u>Medium and heavy commercial vehicles</u>

96. The classes of licences for these type of transport vehicles are:

- Class 2 – any rigid vehicle with a GLW of 4,500kg to 18,000 kg.
- Class 4 – any rigid vehicle with a GLW of more than 18,000kg.

97. Class 3 and Class 5 enable a driver to tow trailers with Class 2 and Class 4 vehicles respectively. The Commission uses the term 'medium commercial' to refer to commercial vehicles with a GLW of 4,500kg to 18,000 kg, and the term 'heavy commercial' to refer to commercial vehicles with a GLW of more than 18,000kg.

98. The Commission considers that the characteristics of heavy commercial vehicles include:

- driven by professional drivers with class 4 or 5 licences;
- mainly used by transport firms and/or construction firms;
- capable of transporting considerable weight on short (e.g. tippers) and long (e.g. tractor and trailer units) distances;
- provide driver comfort, including sleeping compartments, for transport of goods on long distances.

99. These characteristics differentiate heavy trucks from other commercial vehicles.

100. From a demand-side perspective, there is a lack of substitutability between different types of trucks. Industry participants have informed the Commission that trucks are hired for specific purposes. A refrigerator truck cannot be substituted for an alloy tipper truck and vice versa. However, there is some substitutability at the margins between different sizes of vehicles. For instance, a furniture remover may require a 7 tonne truck (Class 2) but only be able to rent a 10 tonne truck (Class 4) due to availability. In this case the vehicles would be substitutable, providing the rental customer holds a Class 4 licence.

101. There appear to be various categories of medium and heavy commercial vehicles. On one side, certain medium and heavy commercial vehicles are used for the

purposes of rapid delivery of goods, usually within metropolitan areas, for instance furniture trucks. On the other side, there is a demand for specific vehicles to carry goods long distances and/or heavy loads, for instance tractor units and trailers.

102. For the reasons given above, different customer needs seem to be clearly defined for medium rental vehicles on one side, and heavy commercial rental vehicles on the other side. While the Commission acknowledges that there might be some overlap in demand-side substitutability between the different sizes of the same type of truck, the Commission considers that there is unlikely to be any significant substitutability between the different types of medium and heavy commercial vehicles.

103. In general, the Commission takes a pragmatic approach and considers that any vehicle between 4,500kg to 18,000kg GLW would fall into medium commercial vehicle category, considering that a separate licence is required for vehicles over 18,000 kg, therefore suggesting that distinctive groups of customers use heavy commercial vehicles.

104. From a supply-side perspective, if a supplier of medium commercial rental vehicles wished to expand into the heavy commercial vehicles rental market, it would require significant capital investment. Industry participants have told the Commission that rental vehicles need to be fairly new, as they need to be reliable and in excellent condition. The capital costs to acquire a new heavy commercial vehicle range between $160,000 and $450,000, while those for a medium commercial vehicle vary between $60,000 and $100,000, but again not all of these costs are sunk as there is an active second-hand truck market in New Zealand. Nevertheless, the decision to invest a significant expenditure into the heavy commercial rental vehicles will be heavily influenced by the supplier's ability to target heavy commercial vehicle rental customers.

105. Acquiring ten units of various commercial vehicles for the purpose of rental services is expected to cost more than $1.5million. It is unlikely that a small change in relative rental prices for heavy commercial vehicles would give enough profit incentive to encourage near competitors to commit such high additional investment, even when these capital costs are not sunk.

106. Overall, both demand- and supply-side characteristics of the heavy commercial vehicles rental market suggest that there are likely to be separate markets for medium commercial vehicles and heavy commercial vehicles.

107. Accordingly, the Commission considers that separate product markets should be defined for:

- medium commercial vehicles (between 4,500kg and 18,000 GLW and requiring Class 2 and/or Class 3 licence); and
- heavy commercial vehicles (over 18,000kg GLW and requiring Class 4 and/or Class 5 licence)

Conclusion on Product Dimension

108. The Commission concludes that for the purpose of assessing the competitive effect of the proposed acquisition, the relevant product markets are:

- the provision of rental services for medium commercial vehicles; and
- the provision of rental services for heavy commercial vehicles.

Functional Dimension

109. Functional level differentiation is more relevant for goods markets than for service markets. Services can be provided to all functional levels but, in themselves, services generally operate on a retail basis, with occasional circumstances where services are provided at the wholesale level.[19]

110. In the markets for the provision of rental services for medium and heavy commercial vehicles, firms provide services directly to business customers. These customers use medium and/or heavy commercial vehicle rental services as input into their own production or service. The scope of the acquisition is, therefore, at the wholesale level, where the rental vehicle firms manage a direct relationship with businesses requiring medium and/or heavy commercial vehicle rental services.

111. The Commission concludes that the appropriate functional level is the provision of wholesale rental services for medium and heavy commercial vehicles to businesses.

Geographic Dimension

112. The Commission defines the geographic dimension of a market to include all of the relevant, spatially dispersed sources of supply to which buyers would turn should the prices of local sources of supply be raised.

113. The Applicant considered that the geographic market is a national one.

Medium commercial rental vehicles

114. From the demand-side perspective, customers tend to request the rental service from the provider in their local area or region. For some types of specialty vehicles, customers will pay for the vehicle to be delivered to the region or will send a driver to pick up the vehicle. However, the majority of firms the Commission interviewed stated that customers would generally not go outside their region, even in the face of a SSNIP in their region. In addition, industry participants stated that moving rental vehicles between the North and South Island was particularly costly as transportation of commercial vehicles across the Cook Strait costs $1,200-1,300. Accordingly, customers in one island are unlikely to source a commercial vehicle from the other.

115. On the supply-side, providers of medium commercial vehicle rental services tend to operate on a local and regional basis. The Commission tested whether a SSNIP would induce firms to switch into nearby geographic regions.

116. For a rental firm to switch from its existing geographic region to the next nearest region, it would need to lease yard space and progressively increase its fleet. While such expansion would require an additional investment, these capital costs would not all be sunk, due to the ability to resell the assets. Industry participants advised the Commission that finding new yard space was relatively easy, as yard space did not have to be centrally located.

117. Henderson Rental Cars Limited (recently acquired by Hirepool) started in West Auckland, moved to South Auckland and then into Hamilton. Likewise, Southern Equipment Centre started its rental business in Invercargill, and then established depots in Dunedin and Christchurch, and now services the entire South Island. These cases demonstrate the relative ease with which firms are

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[19] Mergers and Acquisitions Guidelines, page 20.

able to enter into neighbouring regions. In addition, those rental companies that operate in two or more regions do not differentiate on prices for the same product between regions.

118. On balance, the ability of firms to expand into neighbouring regions to supply the same product under same terms and conditions suggests that the boundaries are likely to be drawn in a broader area than that suggested by the demand-side consideration.

119. The Commission is, therefore, of view that the geographic dimension of the market for medium commercial vehicle rental services is national.

Heavy commercial rental vehicles

120. From the demand-side perspective, customers tend to rent heavy commercial vehicles for longer periods than medium commercial vehicles. Some customers also ‘roll over’ their rental contracts for significant periods of time, and are therefore more prepared to bear the cost of hiring vehicles from other regions.

121. In regard to breakdowns, rental customers informed the Commission that price is not the first consideration; timeliness of getting a vehicle to the scene is. This is weighed against the price of the contract and the relationship between the transport company and the contractor of services. Rental customers stated that they would rather “take a hit” on a single breakdown than lose the overall contract. Accordingly, paying to have a vehicle delivered from another region would not make a significant difference to the customer.

122. On the supply-side, the same characteristics apply as for medium commercial rental vehicles, though an additional investment is required to expand into other regions and involves higher capital costs for heavy commercial rental vehicles.

123. Accordingly, the Commission considers that the there is likely to be a national market for heavy commercial rental vehicles.

Conclusion on Geographic Dimension

124. The Commission concludes that for the purpose of assessing the competitive effect of the proposed acquisition, the relevant geographic markets are:

- the national market for the provision of rental services for medium commercial vehicles; and
- the national market for the provision of rental services for heavy commercial vehicles.

Customer Dimension

125. Industry participants informed the Commission that some customers prefer to enter into rental agreements with the rental firms that operate a nationwide network of branches providing heavy commercial vehicles rental services. TR Group and ORIX seem to be the only firms that operate such a nationwide distribution network. This network enables the customers to secure the rapid supply of required rental vehicles in any place in New Zealand.

126. A nationwide distribution network seems to be relatively important for those customers who typically transport goods on long distance routes. For this customer group a risk of vehicle breakdown in any part of a long distance route, with associated loss of profit in the case of non-delivery of the goods to the point

of destination, can be reduced if the rental company can secure a prompt replacement of the broken-down vehicle wherever the accident might happen.

127. A consequence of the merger between the TR Group and ORIX, as the only suppliers able to operate nationwide, is that they would no longer compete to provide the national service. Those transport companies using this service could potentially be exposed to higher prices from the merged entity. However, this would depend upon the ability of the merged entity to price discriminate between its customers, such that the 'national' customers were charged higher prices than the rest.

128. These customers generally are those who use tractor units and trailers or very large rigid trucks and trailers. Such customers are likely to be firms providing long-haul transport services, and include Linfox, Freightlines, Mainfreight, Symons Transport, Trans Otway and Toll Tranzlink.

129. While long-haul transport services are often one part of larger transport firms' operations, these firms often provide metropolitan deliveries as well, thus suggesting that they could equally be defined as short-haul customers. For instance, Mainfreight is a long-haul customer of the TR Group, and it also operates a metropolitan delivery service that rents medium commercial vehicles from the TR Group. Mainfreight could be categorised as both a long-haul and short-haul customer. A consequence is that it would be difficult for the merged entity to separate Mainfreight's (and other customers') long-haul requirements from their short-haul requirements, in order to price discriminate.

130. In addition, other types of firms also fall into the long-haul category, in that they need on occasion to undertake a long delivery of goods between two distant regions. For instance, Surplus Brokers Limited is an auction house that moves furniture between regions, and Smith City Limited is a furniture retailer that uses large commercial trucks to deliver its goods throughout the South Island. While these firms transport goods long distances, they prefer medium size trucks for ease of use in metropolitan areas. These firms use the same trucks for long-haul trips as for their metropolitan deliveries. While these types of firms do transport goods long-haul, the nature of the firms suggests that the bulk of their operations are short-haul.

131. The Commission considers that while it appears that long-haul transport firms could potentially be captive to nationwide network rental companies, the Commission is of the view that the ability of these rental firms to separate out long-haul customers, and hence to price discriminate against them, seems to be limited. Therefore, for the purposes of the present Application, the Commission defines a broad market for all customers.

Conclusion on Market Definition

132. On the basis of the above analysis, the Commission considers that the relevant markets in this proposed acquisition are:

- the national market for provision of medium commercial vehicle rental services; and
- the national market for provision of heavy commercial vehicle rental services.

COUNTERFACTUAL AND FACTUAL

133. In reaching a conclusion about whether an acquisition is likely to lead to a substantial lessening of competition, the Commission makes a comparative judgement considering the likely outcomes between two hypothetical situations, one with the acquisition (the factual) and one without (counterfactual).[20] The difference in competition between these two scenarios is then able to be attributed to the impact of the acquisition.

Factual

134. In the factual scenario, TR Group would acquire the truck rental division of ORIX.

Counterfactual

135. ORIX advised the Commission that if the acquisition did not proceed, [ ]. It said that its truck rental division [ ]. ORIX informed the Commission that the division is currently [ ].

136. ORIX considered that it had [ ].

137. ORIX informed the Commission that renting vehicles was not part of its core business, and that it needed to now concentrate on its core business. [ ], it would still be a distraction from its core business.

138. ORIX has undertaken several strategies [ ].

139. In July 2006, ORIX also started an extensive print marketing campaign to try to increase sales of existing rental trucks.

140. In October 2006, the ORIX board decided to sell the business and exit the vehicle rental services market. ORIX stated that the truck rental division [ ]

141. [ ].

142. [ ].

143. ORIX's analysis showed that the [

[20] Air New Zealand & Qantas Airways Ltd v Commerce Commission (No.6), unreported HC Auckland, CIV 2003 404 6590, Hansen J and KM Vautier, Para 42.

]. The Commission considers that ORIX has limited ability [ ]

144. The Commission has analysed [ ]

145. The Commission accepts [ ].

146. While the Commission considers that absent the acquisition, it is possible that [ ] The Commission considers that if ORIX were to continue to trade in the market, then it is likely it would be on a significantly smaller scale than is currently the situation.

147. For these reasons, the Commission considers the likely counterfactual scenario would be:

- ORIX continues to dispose of its assets and continues to trade until an appropriate buyer can be found for the downsized fleet.

148. In both the factual and counterfactual scenarios, ORIX would continue to trade for the purposes of the Commission's timeframe for its competition analysis. However, the Commission considers that in the likely counterfactual scenario, ORIX would continue to downsize its fleet and therefore be a weaker competitor than it is presently.

COMPETITION ANALYSIS

Medium Commercial Vehicle Rental Services

Existing Competition

149. Existing competition occurs between those businesses in the market that already supply the product, and those that could readily do so by adjusting their product-mix (near competitors).

150. An examination of concentration in a market can provide a useful indication of the competitive constraints that market participants may place upon each other, providing there is not significant product differentiation. Moreover, the increase in seller concentration caused by a reduction in the number of competitors in a market by an acquisition is an indicator of the extent to which competition in the market may be lessened.

151. A business acquisition is unlikely to substantially lessen competition in a market where, after the proposed acquisition, either of the following situations exist:

- The three-firm concentration ratio (with individual firms' market shares including any interconnected or associated persons) in the relevant market is below 70%, the combined entity (including any interconnected persons or associated persons) has less than in order of 40% share; or
- The three-firm concentration ratio (with individual firms' market shares including any interconnected or associated persons) in the relevant market is above 70%, the market share of the combined entity is less than in the order of 20%.

152. There are number of firms already established in the market for the provision of medium commercial vehicle rental services in New Zealand. Table 2 shows the market shares, measured by the number of vehicles operated by each of the major main competitors in February 2007.

Table 2: Estimated number of vehicles in medium commercial vehicle rental services market

Truck Rental firm	**Number of vehicles**	**% market**
TR Group	**[ ]**	**[ ]%**
ORIX	**[ ]**	**[ ]%**
Combined firm	*[ ]*	*[ ]%*
Budget	[ ]	[ ]%
The Hire Company	[ ]	[ ]%
Hirepool	[ ]	[ ]%
Charter Trucks	[ ]	[ ]%

Truck Rental firm	Number of vehicles	% market
Metropolitan	[ ]	[ ]%
North Harbour Rentals	[ ]	[ ]%
Car and Commercial	[ ]	[ ]%
O'Neill Rentals	[ ]	[ ]%
Commercial Refrigeration	[ ]	[ ]%
Hanson Rental Trucks	[ ]	[ ]%
Total	[ ]	100.00%

153. Post-acquisition, the combined entity would have a market share of [ ]% and the three-firm concentration ratio would be [ ]%. This is inside the Commission's safe harbours. The aggregation is small.

154. In the factual scenario, there would continue to be a number of local/regional operators that provide medium commercial vehicle rental services and would continue to compete with the TR Group. In addition, Budget has a national presence in this market, and its fleet size is larger than the TR Group's. There would be five firms with a market share over [ ]%, and several smaller firms as well.

155. Due to the low level of aggregation and the existing competition in the factual scenario, the Commission considers that the proposed acquisition would not result, nor would be likely to result, in a substantial lessening of competition in the market for the national provision of medium commercial vehicle rental services. Accordingly, the Commission has not considered this market further.

Heavy Commercial Vehicle Rental Services

Existing competition

156. There are number of firms already established in the market for the provision of heavy commercial vehicle rental services in New Zealand. Table 3 shows market shares by number of vehicles operated by each of the competitors in February 2007.

Table 3: Estimated number of vehicles in heavy commercial vehicle rental services market

Truck rental firm	Number of vehicles	% market
TR Group	[ ]	[ ]%
ORIX	[ ]	[ ]%
Combined firm	*[ ]*	*[ ]%*
ETL	[ ]	[ ]%
City Trucks	[ ]	[ ]%
North Harbour	[ ]	[ ]%
Southern Equipment Centre	[ ]	[ ]%

Truck rental firm	Number of vehicles	% market
Hirepool	[ ]	[ ]%
Charter Trucks	[ ]	[ ]%
The Hire Company	[ ]	[ ]%
O'Neill Rentals	[ ]	[ ]%
Hanson Rental Trucks	[ ]	[ ]%
Total	**[ ]**	100.00%

157. Post-acquisition, the combined entity would have a market share of [ ]%, and the three-firm concentration ratio would be [ ]%. These ratios are outside the Commission's safe harbours.

ORIX declining

158. Industry participants informed the Commission that it was not surprising that ORIX is determined to exit the market, as they believe that ORIX has made some major mistakes in the heavy commercial vehicle rental market. Vehicle rental firm Car and Commercial rentals suggested that ORIX is a finance company and, therefore, has little experience with and knowledge about the truck industry. Likewise, O'Neill Rentals considered that ORIX is not suited to the truck market.

159. Industry participants advised the Commission that ORIX had been struggling in the market for a while. Henderson's said that ORIX had been doing "crazy deals" to try to attract business, and that it had basically "dropped out of the market". Budget considered that ORIX's exit was not surprising as ORIX had had a lot of management changes in recent years.

160. Southern Equipment Centre stated that if the transaction did not go through ORIX would just slowly exit the market. It was also unsure as to why the TR Group was purchasing ORIX, because it considered that the TR Group could just wait until ORIX exits the market. Southern Equipment Centre concluded that the TR Group must be purchasing ORIX's customer list, and that the goodwill could not be that significant.

161. Despite these views, other operators considered that ORIX was the only firm currently competing with the TR Group on a nationwide basis. This would mean that, in the factual scenario, there would be no other firm competing directly with the TR Group in the provision of nationwide coverage, in terms of vehicle delivery and/or replacement.

162. Henderson's stated that the TR Group and ORIX are the only market players who compete for the "big trucks", and that if a customer wanted a heavy vehicle their first calls would be to the TR Group and ORIX. Budget also advised the Commission that the TR Group and ORIX are the only ones that supply the big trucks.

163. In the factual scenario, the Commission considers that while some market players like City Trucks, ETL and Hirepool would provide constraint on the TR Group in the provision of regional coverage in terms of vehicle delivery and/or replacement, they would not constrain the TR Group in terms of nationwide coverage.

164. In the counterfactual scenario, as noted above, ORIX would continue to trade over the timeframe used by the Commission for its competition analysis and so would continue to provide some constraint on the TR Group, including with regard to nationwide rental customers. However, the Commission considers that ORIX would be likely to provide less of a constraint on the TR Group than it currently does.

165. In short, even as a declining competitor, ORIX would still constrain TR Group in the counterfactual, but that constraint would be absent in the factual scenario. As the other existing competitors are not capable of providing nationwide coverage in terms of vehicle delivery and/or replacement, the Commission considers that without the possibility of nationwide expansion of existing competitors the difference between the factual and counterfactual scenarios would be likely to be significant. It is, therefore, necessary to consider the ability of existing competitors to expand to cover the whole country.

Nationwide expansion of existing competitors

166. The Commission considers that in order to expand in the market on a nationwide basis, other operators, like City Trucks or ETL, would need to develop a nationwide network of branches, offices and yards capable of providing delivery and replacement of heavy commercial rental vehicles.

167. Expansion of regional operators would be far more likely to happen by successive expansions into the adjacent regions, rather than immediately developing a nationwide network. When Henderson Car Rentals (now Hirepool) expanded its operation geographically, it did so from Auckland to Hamilton. Likewise, Southern Equipment Centre expanded its operation from Invercargill to Dunedin and Christchurch, and now services the entire South Island.

168. The Commission has considered whether this kind of geographic expansion would be likely to have a significant impact on competition in the factual scenario for the provision of nationwide coverage.

169. In December 2006, Hirepool purchased Henderson Rental Cars Limited, an Auckland based rental vehicle provider. Hirepool has depots (for its equipment rental business) in most metropolitan centres throughout New Zealand. [ ].

170. Hirepool has been acquiring businesses in other rental markets in the last year, including port-a-loos, portable energy generators and a party hire firm. Hirepool has also grown significantly organically in the past three years, especially after being acquired by Australian private equity investor Next Capital in 2006.

171. Hirepool has also approached other vehicle and equipment rental firms with the intention of acquiring them, including [ ]. [ ].

172. [ ] informed the Commission that Hirepool had told it that it considered ORIX to be a weak competitor, and that Hirepool's goal was to take ORIX out of the market. In addition, [ ] stated that Hirepool knew that ORIX was struggling, and that there was no point in buying it, as it was going to exit anyway.

173. [ ], as this is where the customer synergies are with its current customer base. However,

Hirepool stated that, even though it was not primarily focussed on the heavy commercial vehicle rental market, if the demand was there, it would fill that demand.

174. The Commission considers that Hirepool has an aggressive growth strategy, both through acquisitions and organic growth. The Commission considers that with Hirepool developing a nationwide network of branches, servicing the demand for additional nationwide service for heavy commercial vehicles would be within Hirepool's capability.

175. While the Commission acknowledges that heavy commercial vehicle customers are not Hirepool's target customer group, the Commission considers that it is likely that if in the factual scenario the TR Group raised prices or lowered its service for these rental customers, Hirepool would expand into this area.

176. Given Hirepool's [ ] and its own general strategic direction, the Commission considers that if Hirepool were to expand in the heavy commercial vehicle rental market, it would be likely to be nationwide.

177. The Hire Company has a presence in this market with [ ] heavy commercial vehicles. It has six strategically placed branch offices across the South Island and North Island. However, The Hire Company's customers tend to be construction firms, and thus do not require nationwide coverage in terms of vehicle delivery and/or replacement.

178. The Hire Company considers that there is a big opportunity in the heavy end of the vehicle market, especially in the factual scenario with ORIX exiting the market. In 2000,
[
]

179. The Hire Company also informed the Commission,
[
].

180. The Commission considers that in the factual scenario, if the TR Group raised prices or attempted to use market power, then The Hire Company would be very likely to expand into providing nationwide rental services.

Conclusion on Existing Competition

181. The Commission is of view that there are plausible signs of nationwide expansion of existing competitors that would be likely to create some constraint on the ability of the combined entity to exert its market power.

Potential Competition

182. An acquisition is unlikely to result in a substantial lessening of competition in a market if the businesses in that market continue to be subject to real constraints from the threat of market entry. The Commission's focus is on whether businesses would be able to enter the market and thereafter expand should they be given an incentive to do so, and the extent of any impediments they might encounter should they try.

Barriers to Entry

183. The likely effectiveness of the threat of new entry in preventing a substantial lessening of competition in a market following an acquisition is determined by the nature and effect of market conditions that impede entry.

184. The Commission identified a number of entry conditions to the heavy commercial vehicles rental market in New Zealand. These are:

- a rental services licence;[21]
- capital of at least $5 million;
- a depot for vehicles.

185. Industry participants advised the Commission that a rental services licence is easy to get and takes about six weeks. City Trucks, which entered the heavy commercial vehicles rental market in Auckland in mid-2006, advised the Commission that obtaining a licence had been straightforward.

186. Raising the appropriate amount of capital could potentially be a barrier to new entry. However, the Commission considers that such capital expenditure will not present sunk costs for the potential entrant, since exit is unlikely to involve a significant loss in terms of residual value of the rental fleet, except possibly for specialised or large volume vehicles.

187. Vehicle rental firms advised the Commission that obtaining a suitable depot was not a significant problem.

188. The Commission has not found any significant barriers to prevent new entry. The Commission considers that the TR Group is likely to be subject to the threat of market entry in the factual scenario. The Commission has therefore gone on to assess the likelihood, extent and timeliness of such entry, to act as a sufficient constraint on the combined entity.

The "LET" Test

189. In order for market entry to be a sufficient constraint, entry of new participants in response to a price increase or other manifestation of market power must be:

- Likely in commercial terms;
- Sufficient in Extent to cause market participants to react in a significant manner; and
- Timely, i.e. feasible within two years from the point at which market power is first exercised.

<u>Likelihood of Entry</u>

190. The history of past market entry can be used as an indicator of the likelihood of new entry in the market. There are a number of examples of entry into this market. ORIX entered the relevant market relatively recently (1999), and expanded rapidly to a nationwide business operation with an extended network of branch offices covering both the South and North Islands.

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[21] Land Transport New Zealand requires that a rental service license be obtained by anyone who rents out vehicles and charges for the use of that vehicle. See http://www.ltsa.govt.nz/commercial/rsl.html last sourced 14 March 2007.

191. The recent acquisition of Henderson Rental Cars Limited by Hirepool also demonstrates that entry by acquisitions by players who provide other rental products such as equipment hire, is also likely to happen.

192. City Trucks entered the market in Auckland in mid-2006. City Trucks is primarily a second-hand tractor unit and trailer dealer. It decided to enter the heavy commercial vehicle rental market after leasing and renting firms had entered the second-hand vehicle market. The Commission considers that this demonstrated that new entry by firms who operate in other markets related to heavy commercial vehicles is also likely to happen.

193. Southern Equipment Centre entered the heavy commercial vehicle rental market through its other business, trailer manufacturing. It informed the Commission that customers asked it to rent out trailers and that renting tractor units was the next logical step. The Commission considers that this demonstrated the likelihood of new entry by trailer manufacturers.

194. Budget is currently operating in the medium commercial vehicle rental market, and has a nationwide network of branch offices. Budget appointed a commercial manager in mid-2006 to develop the commercial side of its business and build the division into a “critical mass”. Budget informed the Commission that [ ]

195. [ ]

196. The Commission is of view that various possible entrants are likely to consider market entry under favourable commercial terms in the national market for the provision of heavy commercial vehicle rental services, and that they are likely to offer a nationwide service.

<u>Extent of Entry</u>

197. The Commission considers that for entry, or the threat of entry, to provide a competitive constraint on the TR Group in the factual scenario, the entry would need to be of significant scale. Specifically, the Commission considers that entry would need to be nationwide or, alternatively, regionally but with clear intention to expand on a nationwide basis within a reasonable time to be able to compete with the TR Group.

198. [ ] Other potential entrants are most likely to undertake a small-scale entry into the relevant market and would have to grow to the level necessary to constrain the combined entity.

199. Any de novo entry of sufficient extent to constrain is likely to involve a significant capital investment. Under favourable commercial conditions, raising such capital is not likely to present difficulty for the potential entrants identified. [ ]

200. In addition, the Commission considers that such capital expenditure is unlikely to give rise to significant sunk costs for the potential entrant, since exit from the market is unlikely to involve a significant loss in terms of residual value of the rental fleet.

Timeliness of Entry

201. Industry participants informed the Commission that it would take within a period of six weeks to six months to build a fleet of heavy commercial rental vehicles, once sufficient capital investment had been secured. City Trucks advised the Commission that it took them approximately 12 months from inception to be able to start providing rental services. The Commission considers that entry into the market would be feasible within two years.

Conclusion on Potential Competition

202. The Commission considers that the threat of potential entry would be a competitive constraint in the factual scenario. The Commission considers that the ability of firms to enter the market relatively easily and quickly, within two years, is likely to influence the behaviour of the TR Group post-acquisition.

OVERALL CONCLUSION

203. The Commission has considered the probable nature and extent of competition that would exist, subsequent to the proposed acquisition, in the following markets:

- the national provision of medium commercial vehicle rental services; and
- the national provision of heavy commercial vehicle rental services.

204. The Commission considers the likely counterfactual scenario to be:

- ORIX continues to dispose of its assets and continues to trade until an appropriate buyer can be found for the downsized fleet.

205. In respect of the medium commercial vehicle rental services market the Commission is of the view that given the number of existing competitors in the market, the proposed acquisition is unlikely to result in a substantial lessening of competition in the factual scenario compared to the counterfactual scenario.

206. In the heavy commercial vehicle rental services market, the Commission is of the view that in the factual scenario the TR Group would be constrained from exerting its market power through a combination of factors, including:

- expansion from existing competitors; and
- the threat of potential competition.

207. The Commission is therefore satisfied that the proposed acquisition will not have, nor would be likely to have, the effect of substantially lessening competition in any of the relevant markets.

DETERMINATION ON NOTICE OF CLEARANCE

208. Pursuant to section 66(3)(a) of the Commerce Act 1986, the Commission determines to give clearance for the proposed acquisition by Elite Truck Rentals Limited of 100% of the assets of ORIX Truck Rental (a division of ORIX New Zealand Limited).

Dated this 2 March 2007

David Caygill
Deputy Chair
Commerce Commission