

***Case No IV/M.1527 -
OTTO VERSAND /
FREEMANS***

Only the English text is available and authentic.

**REGULATION (EEC) No 4064/89
MERGER PROCEDURE**

Article 6(1)(b) NON-OPPOSITION
Date: 16/06/1999

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COMMISSION OF THE EUROPEAN COMMUNITIES

Brussels, 16-06-1999

In the published version of this decision, some information has been omitted pursuant to Article 17(2) of Council Regulation (EEC) No 4064/89 concerning non-disclosure of business secrets and other confidential information. The omissions are shown thus [...]. Where possible the information omitted has been replaced by ranges of figures or a general description.

PUBLIC VERSION

MERGER PROCEDURE
ARTICLE 6(1)(b) DECISION

To the notifying party

Dear Sirs,

Subject: Case No IV/M.1527 – OTTO VERSAND/FREEMANS

Notification of 10.05.99 pursuant to Article 4 of Council Regulation No 4064/89

1. On 10 May 1999, the Commission received a notification of a proposed concentration pursuant to Article 4 of Council Regulation (EEC) No 4064/89 (“the Merger Regulation”) by which OTTO Versand GmbH and Co (“OTTO”) would acquire sole control, within the meaning of Article 3 (1) (b) of the Merger Regulation, of Freemans plc (“Freemans”).
2. After examination of the notification, the Commission has concluded that the notified operation falls within the scope of the Merger Regulation and does not raise serious doubts as to its compatibility with the common market and with the functioning of the EEA Agreement.

I. THE PARTIES

3. OTTO is active in the non-food home shopping business in a number of different countries, either directly or through its subsidiaries: it is active in all the EU member states, with just over two thirds of its Community-wide turnover being in Germany; in Norway, Iceland, Switzerland and Liechtenstein; in the USA (through its links with the Spiegel group) and the Far East. In the United Kingdom, OTTO operates through its subsidiary, Grattan plc (“Grattan”) which it acquired in 1991. Grattan has a number of different divisions and brands in the UK, which include both agency mail order and direct mail order.

4. Freemans, a subsidiary of Sears plc is active in the non-food home shopping business, and whilst it has a subsidiary in the Netherlands its activities are substantially in the UK. Freemans brands include both agency mail order and direct mail order.

II. THE OPERATION

5. The notified operation involves an agreement signed by the parties whereby OTTO will purchase the entire share capital of Freemans from the present owner, Sears plc.

III. CONCENTRATION

6. The notified operation constitutes a concentration within the meaning of Article 3 (1) (b) of the Merger Regulation.

IV. COMMUNITY DIMENSION

7. OTTO and Freemans have a combined aggregate world-wide turnover in excess of EUR 5,000 million [...]. Each of them has a Community-wide turnover in excess of EUR 250 million [...]. The parties do not achieve more than two-thirds of their aggregate Community-wide turnover within one and the same Member State.
8. The notified operation therefore has a Community dimension.

V. COMPETITIVE ASSESSMENT

A. Relevant Product Market

9. The parties put forward three different market definitions, although in their opinion the widest, that of all non-food retail, is the correct one.

a) Non-food retail

10. This market definition would entail all non-food high street stores being part of the same product market definition as home shopping. The parties argue this should be the case as all retailers, whether via stores or catalogues, compete with each other, and that the high street store prices have a constraining effect on the catalogue prices.
11. OTTO/ Grattan provided evidence (from Taylor Nelson Sofres Fashion Trak) that, for 1998, those customers of theirs who bought womenswear bought only about 20% of their purchases from Grattan catalogues and the rest from elsewhere.
12. Also, a number of high street retailers are now active in direct mail order; in the last two years, four such companies have launched catalogues: Marks & Spencer, Tesco, Arcadia and Debenhams. Tesco have a joint venture with Grattan, OTTO's subsidiary, and Debenhams with Freemans.

b) Home shopping

13. This market definition excludes high street stores, but includes all home shopping, ie catalogues sold through agents, directly sold catalogues, and other forms of home shopping (TV, internet, etc), the latter representing very much a minority although growing.

14. Home shopping, be it a market or not, appears to be evolving – as stated above, a number of new entrants from the high street are starting to produce direct mail order catalogues. Furthermore, all the five existing UK agency companies have also launched new direct catalogues in recent years, eg: Empire launched Vert Baudet and Daxon in 1997; GUS launched Disney, Sports Elite, Thomas Burberry, Style Plus in 1997 and Select (Choice Direct) in 1998; Littlewoods launched Index Extra in 1996 and Arcadia brands in 1997/98 (a joint venture with Arcadia, a high street company); Freemans launched The Book in 1998 and have announced the launch of Debenhams Direct (a joint venture with Debenhams) in 1999/2000; Grattan are launching a joint venture with Tesco. Grattan also already have a direct order catalogue, Kaleidoscope, which they developed in the 1990s and in 1996/97 they changed it to a “wrap-around” catalogue, ie, completely identical catalogue to their agency one apart from the cover, with all products and prices identical.
15. High street brands, such as Marks & Spencer, Debenhams, and Next, appear to be using direct mail order as a way of reinforcing customer loyalty and establishing a “seamless interface” between customer and brand.

c) Agency mail order

16. This market definition includes only those home shopping catalogues which are sold through agents. These agents are not employees of the company which produces the catalogue, but receive a commission from them in respect of the goods they order, both for themselves and on behalf of other people. The parties state that the way in which agents are credit checked by agency companies is no less stringent than other credit checks for store cards, credit cards, etc. Traditionally, agency catalogue prices were “bundled”, ie, they included in the price of goods the cost of commission to the agent, delivery, credit, etc (hence agency prices have traditionally been higher than prices for comparable goods in direct mail order catalogues – see below).
17. The previous Commission Decisions in the home shopping area (Case No IV/ M 070 Otto/ Grattan and Case No Iv/ M 080 La Redoute/ Empire, both 1991 cases) defined the market as home shopping as a whole. In 1997, however, the then UK Monopolies and Mergers Commission (“MMC”), in its Report into the proposed merger between Littlewoods and Freemans, determined that there was a distinct market for agency mail order. The MMC came to this conclusion because they found that direct mail order differed markedly from agency shopping in that direct mail order did not use agents; the prices for direct mail order were similar to high street prices whereas with agency mail order the prices were 15 to 20% higher; usually with direct mail order there was no possibility of interest free credit whereas this was a crucial aspect of agency mail order; the range of goods in each direct mail order catalogue was usually narrower than with agency; and many direct mail catalogues were more up-market than agency ones.
18. The views of third parties on the issue of market definition were mixed, reflecting the contrary views put forward to the MMC at the time. Responses from agency players were unanimous in stating that agency was not a distinct market, whereas responses of direct catalogue companies were more divided on this issue.
19. The parties have argued that the MMC conclusion is not the correct market definition because they believe that the market for non-food retail has further developed and that

in this changing business environment the availability of credit and the system of agents in agency mail order loses its importance vis-à-vis price competition.

20. The parties point out that a number of changes have occurred to the home shopping business in the last two years. In particular, reference is made to the number of high street retailers that have entered this business (see above). In addition, there has also been a blurring of the division between agency and direct mail order. Some agency companies, for example, produce identical “wrap-around” catalogues for agency and direct, others produce catalogues where a percentage of goods (and quoted prices) are identical. The September 1998 survey “Verdict on Home Shopping: an analysis of the home shopping market by sector”, by Verdict Research Ltd, suggests that this leads to a certain amount of “cannibalisation” (existing agency customers buying from the direct catalogue of the same company).
21. Furthermore, the parties point out that where there is a difference in the prices quoted for identical products in agency and direct catalogues, all agents receive a commission in the region of 10% to 12.5%, which is equivalent to a price reduction which, together with the other “bundled” elements of the mail order price, results in the prices which the agents pay being approximately the same as the prices customers of direct mail order catalogues pay.
22. The parties suggest that the number of “true agents” (with more than 2 customers outside the home) has been declining. The GfK Home Shopping Survey (conducted by GfK Marketing Services Ltd) in October 1998 stated that Grattan’s true agents account for [...] of its customer base; excluding agents own purchases, the parties estimate that this amounts to [...] of Grattan’s total agency sales and around [...] of Freemans’ total agency sales. There is nothing to suggest that many of these customers would not have access to alternative forms of credit. The September 1998 Verdict survey states that “agency’s USP [unique selling point] of credit has been undermined by readily available credit elsewhere”.
23. There may remain a group of people who may be unable to obtain credit other than through agents. However, given the size of this customer group relative to the overall customer base, it is unlikely that agency mail order companies would be able to price discriminate against this specific group.
24. It appears therefore that the home shopping market has been changing rapidly in recent years, such that there is a blurring between direct and agency and even between home shopping and the high street. In any event, however, even on the most narrowly defined market, there would not be the creation or strengthening of a dominant position as the result of the concentration (see below). The product market definition can therefore be left open in this instance.

B. Relevant Geographic Market

25. The parties have stated that the relevant geographic market is the United Kingdom. This was also the conclusion of the MMC report in 1997 and was confirmed by third party views.

C. Competitive Assessment

26. On the broadest product market, that for all non-food retail, market shares for the parties and hence the post-concentration entity are not significant.
27. If the relevant product market was for home shopping as a whole, then the market shares of the parties would be as follows (for 1997, figures provided by OTTO):

Company	Market share
GUS (Great Universal Stores)	24%
Littlewoods	16%
<i>Grattan</i>	8%
<i>Freemans</i>	7%
Empire	5%
N. Brown	4%
Next	4%
Others	32%

28. On the narrowest market definition, that of agency mail order, the proposed concentration would result in the post-concentration entity having a market share of approximately 23%.

Company	Market share
GUS	43.9%
Littlewoods	25.6%
<i>Freemans</i>	12.2%
<i>Grattan</i>	10.5%
Empire	7.8%

a) Horizontal aspects

29. As can be seen from the tables, in either an agency mail order market or a home shopping market, the combined entity would become stronger, either just overtaking or

remaining behind the current second largest player, Littlewoods, with GUS the market leader.

30. Given the market position of the merged entity vis-à-vis these other large and established players, it can be concluded that the operation would not lead to the creation or strengthening of a single dominant position.
31. It has been pointed out that, on the basis of the narrowest possible product market, that is the agency market, the operation would result in three players holding more than 92% of the market. However, while the merged entity would move much closer to the current second player, Littlewoods, there would remain almost a 20% differential in market share between this second player and the market leader, GUS. In addition, factors mentioned in the paragraphs above indicate that the pricing policy of these agency players is constrained to some degree by direct home shopping and/ or high street retail. Given this market structure the proposed operation would not substantially increase the likelihood of coordinated behaviour such as to create a position of oligopolistic dominance between these three players.

b) Vertical aspects

32. In order to examine the vertical aspects of the concentration, in particular with regard to the possibility of increase in purchasing power of the merged entity vis-à-vis its suppliers, the distinction between mail order and other retail distribution channels is not relevant since there is no reason to presume that suppliers would have to adapt their production specifically for mail order companies.
33. It is therefore appropriate to consider total retail sales in each product group as an adequate framework within which to assess the vertical aspects of the proposed concentration. Taking into account all retail activities of the OTTO group, market shares in OTTO's domestic market of Germany for 1998 were as follows: womenswear: [...%]; menswear: [...%]; childrenswear: [...%]; household textiles: [...%]; furniture: [...%]; other household products: : [...%]; sportswear/ products: [...%]; total textile: [...%]. Market shares for OTTO's subsidiary, Grattan, in the UK in 1997 were: womenswear; [...%]; menswear: [...%]; childrenswear: [...%]; household textiles: [...%]; furniture: [...%]; other household (excluding electric): [...%]. Market shares for Freemans in 1998 in the UK are as follows: womenswear: [...%]; menswear: [...%]; childrenswear: [...%]; sportswear: [...%]; sports equipment: [...%]; household textiles: [...%]; furniture: [...%]; other household products: [...%] It follows from this that the vertical implications of the proposed concentration in terms of market shares will be minor.

VI. CONCLUSION

34. For the above reasons, the Commission has decided not to oppose the notified operation and to declare it compatible with the common market and with the EEA Agreement. This decision is adopted in application of Article 6 (1) (b) of Council Regulation (EEC)

For the Commission,