

# 7 Views of other parties

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## Introduction

7.1. In this chapter we summarize the evidence put to us by third parties in written and oral submissions.

## GUS plc

7.2. GUS told us that it had been concerned about the performance of its home shopping businesses since 1997, and that its shareholders had been contrasting their relatively poor returns—and the declining demand for AMO—with the much more attractive returns and growth prospects for GUS's other activities. GUS had employed £700 million of its shareholders' capital on average throughout this period and had failed to make an adequate return on home shopping since 1998. This concern was illustrated by a growth, in the years 1996 to 2002, of 32 per cent in total spending on non-food retailing, and by 29 per cent in home shopping, whilst in AMO, the area where the bulk of GUS's customers were, sales fell by 22 per cent.

7.3. GUS's initial response had been to seek to develop home shopping in a number of ways. It bought Argos in April 1998 for £1.7 billion following a contested bid. Argos had defended itself by proposing a joint venture link with Littlewoods, but that was not seen by investors in Argos as such a valuable alternative as that offered by GUS. GUS told us that it had seen Argos as a good business in its own right. But, in addition, it provided an opportunity to use some of the GUS infrastructure and expertise to improve the trading fortunes of Argos. Given the unique position Argos enjoyed in the UK—some 60 to 70 per cent of all households in the UK had an *Argos* catalogue—GUS saw an opportunity to sell clothing to the Argos customer base. GUS added that Argos was now a multi-channel retailer. It had stores and took a good deal of its business over the Internet, and around 20 per cent of Argos sales were deliveries direct to the home. GUS had been very pleased with the acquisition of Argos. It had realized some synergies; it also launched Argos Additions (a clothing catalogue), which grew relatively well.

7.4. During 1999, the decline of the AMO business accelerated, causing GUS in December 1999 to issue a profits warning.

7.5. Subsequently, a complete review of the GUS business portfolio was undertaken and a new strategy for the GUS group was outlined in May 2000. This review covered three options for GUS home shopping: (a) fix/right size it; (b) sell it; and (c) wind it down. At that time, option (a) was chosen since no approaches to buy the GUS home shopping business were forthcoming and because the wind-down option then was not seen as the best means to maximize the present value of the future cash flows from the business at that time. However, the wind-down option was always seen as a fall-back plan if option (a) failed.

7.6. A new strategy for GUS home shopping was therefore devised. This involved stabilizing the GUS home shopping business; leveraging core competencies to support Argos and to develop other new business opportunities, for example in logistics; and launching new and potentially more profitable DMO catalogues over time. The strategic plan for GUS home shopping in April 2000 stated, 'The base expectation was for a low growth, low investment business which provided a platform for entry into more exciting markets such as third party services or financial services'. The profitability of GUS home shopping had been hit by two major factors. First, it experienced a significant, unforeseen decline in sales due to a continuing structural shift of customers away from AMO home shopping; and second, it experienced a significant increase in costs as a percentage of sales due to the decline of the business, which was driven by the high fixed-cost base. The business therefore needed to cut its costs significantly, to develop third party demand for its infrastructure, and to create the right customer proposition to compete in the new more competitive market environment.

7.7. GUS described its strategy for Reality, which was intended to deal with the problem of the high cost base. GUS said that during 1998 to 2000, the interest of UK businesses in remote selling grew significantly. Internet-based selling enabled 'bricks and mortar' retailers to offer their products directly to customers at competitive levels of cost. This was because the Internet did not require a printed catalogue and was flexible enough to accommodate frequent range and price changes. This meant that retailers such as Tesco and Dixons Stores group could sell directly to customers via the web as well as through

their stores. In addition, because of the ‘dot.com’ boom, UK retailers felt compelled to invest ahead of the curve to establish web sales and home delivery in order to be competitive with the emerging Internet businesses and to satisfy investors that they had a ‘dot.com’ strategy.

7.8. As a result, there was potentially a big market for third party services to support Internet selling, in particular home delivery and customer order management. GUS believed there was a significant opportunity for GUS home shopping to provide these services. Doing this would in turn drive incremental profit and provide volume to help to ‘right size’ the cost structure of the business supporting the in-house home shopping business. To enable GUS home shopping to provide a full service to third parties, GUS bought the Reality web design business in May 2000.

7.9. Given the significant management challenges within GUS home shopping of fixing the existing catalogue proposition, reducing costs, attracting third party business and providing an efficient infrastructure, it was decided that GUS home shopping should be split into two businesses. One would be a customer-facing home shopping business and the other would be a service infrastructure business consisting of logistics, customer contact management and web enablement services. The latter was branded Reality.

7.10. In the end, this move was not successful for a number of reasons. The focus on selling to third parties and servicing that business adversely affected costs and distracted management from providing an adequate service level to GUS home shopping. This in turn impacted adversely on the sales of the home shopping business. Third party sales never reached the scale envisaged and therefore cost ratios were higher than planned. The amount that Reality could charge third party customers was significantly undermined by competition, particularly the competitive pricing by Parcelforce which made large losses, subsidized by the public purse. The collapse in 2001 of the ‘dot.com’ boom also significantly reduced expectations of future sales. In early 2002, therefore, GUS took the decision to refocus Reality. It was merged into the rest of ARG and run primarily as a service provider to GUS home shopping and Argos.

7.11. GUS gave us details of how it had set about creating a competitive customer proposition. It said that over the last three years, it had invested significant capital, management time and resource in attempting to reposition the home shopping business. The key problem was that the traditional AMO home shopping business was in long-term decline. The decline was well documented and was, GUS believed, a function both of changing customer circumstances—more women working, improved disposable incomes, improved ability to access credit through means other than an agency account—and a dramatic change in the UK competitive retail landscape. This last change had been very significant in changing customer perception of the ‘value for money’ represented by the bundled agency proposition.

7.12. The UK retail competitive landscape had changed fundamentally over the last ten years. Businesses such as Matalan, Primark and New Look had grown substantially by selling low-priced fashionable clothing. In addition, supermarket groups, such as Asda and Tesco, had gained substantial share of the UK clothing market. These two developments had given budget-conscious customers access to a wide range of inexpensive clothing for themselves and their families. Buying clothing in the UK had never been cheaper or easier.

7.13. The household goods market had also seen the rapid development of everyday low-pricing retailers such as B&Q and Argos. In addition, many retailers such as DFS began to offer long-term interest-free credit to consumers on big-ticket items, with direct delivery to the home. Since 1997, there had been an unprecedented development by major retailers across many sectors offering multi-channel-based service to their customers.

7.14. All the above had eroded the benefits that AMO home shopping operators were able to offer to their customers—choice, convenience and credit. GUS home shopping’s strategy to address these competitive pressures was to use its purchasing, logistics, marketing and customer database management skills to develop new DMO home shopping propositions to replace the volume being lost in the AMO business.

7.15. The DMO home shopping catalogue brands contained ‘unbundled’ offers to customers. During the years 1999 to 2002, GUS home shopping successfully launched or built up its DMO offerings, including: expansion of the *Marshall Ward* portfolio of DMO home shopping brands; launch of the

*Argos Additions* DMO catalogue in conjunction with Argos; launch of the *abound* catalogue targeting fashion-conscious women; and the development of several niche catalogues including *McCord*, for home furnishings, and *Innovations*, which had both been purchased from the Burton Group in late 1997.

7.16. GUS home shopping was successful with this strategy. DMO sales grew from £96 million in the year ended March 1999 to £323 million in the year ended March 2003. However, this was not good enough for several reasons. GUS home shopping's AMO sales in the UK declined from £1.5 billion in the year ended March 1999 to £1.2 billion in the year ended March 2002. Thus, the investment in developing a number of DMO catalogues was not enough to replace the sales lost in the AMO business. Customer acquisition and retention costs in DMO businesses, except in the case of Argos Additions, were very high. Aside from these costs, in the era of UK multi-channel retailing, pure DMO home shopping propositions began to suffer from a lack of fashionability compared with high street operators and a less convenient offering. There were significant costs and inefficiencies created in trying to run a multi-brand, DMO operation using a system which was built to support an AMO big-book operation. Finally, it became clear that without a complete infrastructure and IT system transformation estimated to cost at least £100 million, the sales of AMO and DMO could not be expected to become profitable in the near to medium term.

7.17. While this process was under way, GUS also had conversations with Littlewoods—then still owned by the Moores family—and with a Continental mail-order business to explore options for co-operation in various aspects of the business and/or selling or sharing assets, but, in the event, nothing came of any of these discussions. In the middle of 2002, GUS had discussions with a potential buyer who was [redacted]; there were discussions about the possibility of a joint venture with certain assets from Littlewoods, but those discussions came to an end when the Barclay brothers acquired Littlewoods in October 2002.

7.18. By the summer of 2002, the central management of GUS was reaching the view that the time had come to get out of home shopping, either by selling its operations to someone else, or by running them down. GUS had wound down another of its businesses, GEF, a few years before, so was confident that it could put together a programme to manage the process. At that time its best estimate was that the likely proceeds of a rundown would be of the order of £685 million to £780 million and that it would take some two to three years fully to realize them. There were, however, three clear downsides with closure: the job losses would be considerable; the loyal customers who had stayed with the business despite the overall decline would lose their catalogues; and there was always the risk that something unforeseen could emerge to reduce the estimated proceeds. So, in the autumn of 2002, GUS also began exploring the option of finding a buyer. It told us that if a sale had not been agreed by the middle of 2003, then the board would have announced that the home shopping business would be run down. GUS said that it would still have considered selling to a buyer even after the run-down had begun, but that, in practice, once the process had been under way for more than a few months, and the most attractive assets had started to be sold off, the prospects of a successful sale going ahead would become increasingly unlikely.

7.19. In the event, two potential trade buyers emerged: the Barclay brothers, who by then had acquired Littlewoods, and [redacted], along with a number of venture capitalists. After several months of negotiations, largely with the trade buyers, the best offer which GUS received, and the only one that stood comparison with the likely proceeds of running the business down, came from the Barclays.

7.20. On 27 May 2003, GUS and March entered into a sale and purchase agreement under which March acquired all of the issued share capital of a number of GUS's subsidiaries. The agreement is described in Chapter 3.

7.21. We asked GUS for its view of what might have happened had the acquisition by March not taken place. GUS told us that whilst it believed that a wind-down was a viable and potentially effective solution, it did involve risks to its continuing business and had unwelcome consequences for both staff and customers, which a sale would avoid. For GUS, the issue came down to price. If the businesses could be sold for a sum that came close to what it might expect to realize from a wind-down, then a sale was the better option. But if the potential bidders were willing to pay only prices that were well below the wind-down value, then a wind-down was the better choice. Either way, it was clear that a continuing future for these businesses as part of GUS was not a realistic option.

7.22. We put it to GUS that there was evidence to suggest that there was still a possibility that it would have continued to run the home shopping and delivery business, had it not been sold to March in

May 2003. GUS did not accept that there was any evidence to suggest this. GUS said it believed that to have continued in the business, it would have needed to commit at least another £100 million, as referred to earlier. However, it did not believe the sales and margin estimates underpinning the investment plan, and therefore felt that this would not have been a sensible investment. This investment plan, which was prepared by Accenture for the GUS home shopping business, never got to the formal stage of approval by GUS senior management and was never presented to the GUS board.

7.23. GUS said that the wind-down option involved a controlled shutting of the business with the value being realized through the collection of the debtor book and the sale of some of the assets of the business. Embarking on a wind-down plan would have immediately foreclosed the option of sale of the whole business as a going concern to a third party for a price that was more attractive than winding down the business. In the absence of a deal at the level March was prepared to pay, winding down the business was a far more attractive financial option than a sale to any other third party.

## **Mail-order companies**

### **Agency mail-order companies**

#### ***Otto UK***

7.24. Otto is an amalgamation of the businesses of Grattan and Freemans. Its parent company is Otto (GmbH & Co KG) of Germany. It consists of a home shopping division and a parcel delivery division. Otto commented on the OXERA survey (see Appendix 7.1). It believed that the merger would lead to a monopoly situation. It had concerns about the potential impact on its competitive position in the marketplace and the effect on consumers. There was therefore a public interest dimension. The merger had the potential to affect some of the most vulnerable people in society—the financially excluded. For them, choice would be severely limited by a concentration of the AMO method of trading, and giving one business around 70 per cent of the market. Otto said that the barriers to entry into the AMO market were insurmountable, and there was no realistic prospect of new players entering the market.

#### *The AMO market and its customers*

7.25. Otto estimated that the AMO market was still very significant and it accounted for approximately £2.8 billion of business a year. The distinct AMO market was characterized in three ways, which differentiated it from DMO and the high street: first, the breadth and depth of the offer—catalogues offered a very extensive range and choice of goods; second, the terms of trade, particularly the availability of interest-free credit, on which most business was conducted—10 per cent commission on all payments made by the agent, free delivery and returns; third, by the type of customer—agents shopped on behalf of themselves and others within their network. Customers of agents were predominantly from the vulnerable, financially excluded, segments of society. A high proportion of customers of agents would not be able, or would find it very difficult, to obtain mainstream credit in their own name as they were seen individually as unacceptable lending risks. Otto drew attention to the analysis by London Economics in the 1997 MMC report which stressed the importance of mail-order credit to consumers in SEGs C2, D and E, and it believed that that analysis remained valid today. Otto also pointed out that the Government had expressed particular concerns about the terms and availability of affordable credit for this group.

#### *Parcel home delivery service*

7.26. Otto has its own distribution network, Parcelnet. This was created in 2000 from the separate distribution networks of Freemans' Speedlink and Grattan's Direct Line. Parcelnet utilizes a network of self-employed couriers primarily using their own household private car who deliver to the homes of individual customers. It also operates a van service in the London area. Otto utilizes its own network to make deliveries wherever possible, as this is the most cost-effective solution. Other deliveries are undertaken by specialist carriers or by companies with the requisite geographical access to deliver to areas not covered by Parcelnet. It has a contract with Reality (the parcel delivery of GUS home shopping,

now owned by March) for home delivery services; Reality also competes with Parcelnet in the budget B2C parcel delivery market.

7.27. Otto believed that the merger would see a reduction in choice of B2C parcel delivery options. Such restrictions were likely to lead to an increase in costs and limited competition, which would be detrimental to Otto, other businesses which relied on B2C distribution and to customers. The merged operation would be approximately three times the size of Parcelnet. Otto said that distribution was a capital-intensive industry with very few industry leaders in the B2C market. A monopoly situation within the B2C distribution market would create an unfair competitive advantage. The scale of the combined operation might lead to predatory pricing against Parcelnet in order to secure its third party customers. There could also be damage to its third party business, where Reality was currently used to supplement Parcelnet's capabilities. This would have the effect of making its ability to offer a one-stop-shop delivery solution less attractive. It could also be the case that Otto would receive differentiated service and pricing compared with the merged group, and so putting its home shopping businesses at a further disadvantage. It would also be possible for the merged group to decline to renew the contract on terms commercially acceptable to Parcelnet.

7.28. With regard to the possibility of B2B carriers entering the B2C market, Otto said that it had not seen anyone successfully enter the value end of the market. It thought that B2B carriers might touch at the premium end of the market (ie the high-value product where they could pass on a distribution charge of maybe up to £10 to the customer). However, their infrastructures tended to be different from those of B2B carriers: they distributed to business addresses, which were in different districts and premises from domestic addresses; they were invariably attended deliveries; their IT infrastructure was generally very expensive because of the market's track-and-trace requirements; and they offered a 24-hour minimum delivery service, often with additional tighter requirements such as overnight or delivery within a 2-hour time band. They were expensive because they had built their networks in order to provide that level of service. It would be difficult to spread the infrastructure over a low-cost, comparatively low-service operation.

#### *Price competition*

7.29. Otto said that price competition within AMO had been strong prior to the merger. There were clear examples of where competitors had changed the price of items in their main catalogues so as to compete more effectively.

#### *Possible remedies*

7.30. Otto did not believe that there were any safeguards, except divestment, that could be applied that would effectively address the competition and potential consumer detriment issues in respect of distance-selling aspects. As regards the distribution businesses, it believed that it might be possible to formulate a set of safeguards controlling prices, security of services and appropriate penalties for failure to comply. Any such safeguards would need to have regard to the long term as well as the short term. However, it would be important to ensure that these behavioural remedies could be properly monitored and enforced, and that they addressed the fundamental issues of increased competitive strength of the combined businesses and the lack of alternative providers.

#### *Comments on statement of hypothetical remedies*

7.31. Otto, in commenting on the CC's statement of hypothetical remedies, said that any of the proposed remedies would result in a better position for competing businesses and for consumers than would be the case if the merger were allowed to proceed.

7.32. The divestment of all of the GUS businesses acquired by March would be highly effective, as it could result in a restoration of the pre-merger market balance and competitive structure. The divestment of the entire GUS operation to a single controlling entity would be most practicable, due to the complex and interrelated nature of the businesses. However, there should also be scope for the sale of different elements to different businesses.

7.33. Otto said that the options described by the CC for partial divestment were: (a) divestment of GUS Agency Home Shopping business alone; (b) divestment of GUS Home Shopping businesses (AMO and DMO); and (c) divestment of particular assets, for example catalogue titles. Any of these could be effective to a greater or lesser extent, if they were to result in the restoration of the pre-merger market balance. It would be possible to dispose of the door-to-door collected credit business Morses separately. The key determinant was the extent to which the elements of the business were capable of separation such that they remained viable in isolation, or when conjoined with assets of the purchasing business.

7.34. Otto said that the total divestment of Business Express or Reality would be effective. This view was dependent upon the divested home delivery business securing a long-term distribution arrangement for the existing associated home shopping company parcel volumes. Volume was a critical success factor in this market and the parent companies provided the majority of the distribution business volume. In Otto's opinion, a national budget B2C distribution business, operating with the current market cost and service proposition, would not be viable without parcel volumes of this magnitude. Otto said that the maintenance of the independence and integrity of the two companies' client portfolios and critical data was essential as was the companies' continuing provision of complementary services to other competitors in the budget B2C parcel delivery market who did not have 100 per cent national coverage.

7.35. Otto said that it did not consider the partial divestment of particular assets of Business Express or Reality as an effective remedy. Partial divestment of infrastructure/physical assets would not enable a new entrant to compete effectively or act as a constraint to the merged entity. High volume and national coverage were the critical success factors in this market.

### ***Redcats (UK) plc***

7.36. Redcats is one of the two remaining competing operators to the parties to the present merger in the AMO sector. It was formerly known as Empire Stores Group plc. Its parent company is Redcats SA (being part of the group of Pinault-Printemps-Redoute SA of France). Redcats supplied comments prepared by NERA on the recent Verdict report dated October 2003, and also research by Alchemy on its top customers. It also commented on the OXERA survey (see Appendix 7.2).

### ***Agency mail order***

7.37. Redcats submitted that AMO was an important, distinct market which was not in decline, and which would continue to meet clear and distinctive needs for a significant body of consumers in purchasing comprehensive ranges of household goods and clothing on interest-free instalment credit for which there was no equivalent under any other mail-order or retailing arrangement.

7.38. The historical background of the 'clubs', from which the modern concept of AMO derived, demonstrated clearly that AMO was a unique and distinct concept which was not comparable or interchangeable with DMO or any other retailing concept. This was now reflected in the fact that the regulatory treatment was distinct in various respects in relation to AMO as compared with other types of credit and credit agreements; that is to say, AMO companies were permitted to describe their offering as 'interest free' (see paragraph 7.39(d)).

7.39. Redcats explained that various further factors indicated strongly that AMO was a distinct market now, just as it was at the time of the 1997 MMC report, taking into account the following considerations:

- (a) There was a distinct and substantial body of consumers in the lower SEGs who were dependent on the instalment credit (without apparent indebtedness) under AMO, for whom other forms of credit would not be substitutable. Indeed, the evidence shows that a significant proportion of AMO customers did not have a credit card, and there had been little change in this position since 1997.
- (b) The costs of entry into the AMO sector were enormous, as indicated clearly by the OFT in its advice to the Secretary of State in this case, and indeed, as the OFT observed, there had been no new entrants into the AMO market in the last 35 years. Further, there was no substitutability of supply from DMO into the AMO business.

- (c) Electronic and online shopping had not affected the basic market as defined by the MMC in 1997.
- (d) The regulatory treatment of AMO under the Consumer Credit Act 1974 was distinct in various respects from the treatment of DMO and other credit arrangements. In particular, AMO suppliers were permitted to promote the credit aspects of AMO as 'interest free', because the 'cash price' was the same as the credit price for the basic weekly instalment facility, and indeed compound interest did not apply in instalment credit under AMO, unlike the position with most other retailing credit arrangements, including DMO.

7.40. The importance of instalment credit to the majority of AMO agents and customers was so strong that, Redcats believed, an increase in overall price levels of AMO retailers, even of a magnitude of, say, 10 per cent, would be unlikely to cause a sufficiently high transfer of demand to DMO or other retailing channels to make the price rise unprofitable for AMO as a whole. This was because a very large proportion of AMO agents and customers were in the lower SEGs and did not have the available cash for necessary purchases and would, in many cases, not be eligible for mainstream credit (or did not wish to undergo the cost and/or risks associated with mainstream credit).

7.41. Accordingly, if a customer was observed spending £40 on DMO and £40 on AMO, it was reasonable to assume (on the basis that AMO prices were higher than DMO prices) that the £40 spent on DMO effectively exhausted the consumer's access to cash or credit (other than AMO instalment credit). If, at this point, the price of AMO increased, the consumer could not shift expenditure from AMO to DMO sales because the customer did not have access to cash or credit. Therefore, under the 'hypothetical monopolist' test AMO was a distinct market.

7.42. To the extent that there might be some competitive constraints from outside the AMO markets, it should be noted that those constraints would be significantly weakened by the fact that, according to the Verdict 2000 report, the combined group would also control more than 34 per cent of the mail-order sector generally, and more than 38 per cent of the mail-order sector excluding door-to-door selling.

7.43. Redcats submitted that there had been no change in the position since 1997 that would justify a departure from the MMC's conclusions in the 1997 report that AMO was a distinct market. It was clear that online selling and purchasing (including Internet retailing and interactive television) did not affect the position because these retailing channels generally concerned very specific product types only and because the Internet was, to the extent that it mattered at all in relation to DMO, predominantly used as an additional means of placing orders rather than constituting a distinct type of supply arrangement.

7.44. Redcats said that evidence showed, most importantly, that AMO continued to meet the needs of the lower SEGs, including in particular those residing in neighbourhood renewal areas. Moreover, there had been no significant change in the overall levels of use of instalment credit in AMO which continued to be high, being used by almost nine out of ten customers, compared with only three out of ten DMO customers purchasing on credit.

7.45. Redcats stated that the distinct nature of AMO as a market activity was emphasized by the fact that there was an asymmetry of competition for users between AMO and DMO, in that DMO customers might find satisfactory alternatives in AMO catalogues, but the reverse would not apply. This was because DMO catalogues were generally far more focused and specific in terms of product ranges than AMO catalogues and because instalment credit facilities were not available in DMO. Further, there was no substitutability of supply on the part of DMO operators wishing to diversify into AMO, due to the limited product ranges normally carried by DMO catalogues compared with the 'department store' type of catalogues which were characteristic of the AMO sector.

7.46. The DMO catalogues which were as comprehensive as AMO catalogues in the product range covered were generally those which had been launched by AMO catalogues. The reverse never occurred, ie no AMO catalogue version of a DMO catalogue had ever been launched.

7.47. The consequences of the merger would be seriously anti-competitive in that it would result in a substantial lessening of competition in the AMO sector. The merger involved the common ownership and control of the two largest operators in the AMO sector, giving the combined group a market share of 71 per cent in this sector, with only two other competitors, Otto and Redcats. This was against the

background of a market which was already more concentrated now than in 1997 as a result of the merger of Grattan and Freemans pursuant to EC merger control clearance in 1999.

7.48. Redcats drew attention to the CC's conclusions in the recent Safeway merger report<sup>1</sup> stating that, in the same way as for such acquisitions of Safeway, the merger of March and GUS—being a merger of the two largest operators in the AMO sector—represented a reduction from four to three of the players in the market. It would also represent an unacceptable and significant loss of sources of innovation and diversity, and a significant loss of rivalry and future competition between retailers in the relevant AMO market. Redcats also drew attention to the NERA report prepared for Redcats, which concluded that any decline that might be occurring in the AMO market was likely to exacerbate the competition policy concerns arising from the merger.

#### *Parcel home delivery services*

7.49. In addition, the merger would result in the only low-cost parcel home delivery service operators, which fulfilled the needs of the AMO sector, being brought under common ownership and control. There was a real possibility, indeed probability, that full implementation of the merger would result in significant competitive disadvantages for competing AMO companies such as Redcats which was reliant on the services of Business Express and/or Reality. There was a real possibility that the combined ownership and control of these two businesses would be manipulated, directly or indirectly, to reduce the price competitiveness of AMO product ranges of suppliers competing with the merged entity (ie Littlewoods/ShopDirect). Therefore, the vertical integration of the only suitable parcel home delivery service providers into the merged entity would further contribute to distortions of competition in the AMO market and also in the wider mail-order sector. To the extent that price rises for delivery services might occur irrespective of the merger, Redcats commented that it had been able to play Reality and Business Express off against one another, and that even allowing for any price increases that would take place in the absence of the merger, the merger would be likely to lead to significantly greater price rises.

7.50. Redcats did not think that its volumes of business would be sufficient to create the right economies to attract existing transport companies into the B2C delivery business, even if the price per parcel were, say, 10 per cent higher. It was difficult to estimate how high the price would have to be in order to attract entry. There were significant infrastructure costs in building the sort of network that would be needed, with many distribution depots around the UK and numerous vehicles. There would also be costs involved in setting up the complicated systems, and providing the skills, that were needed to maximize efficiencies in delivering from the depots to all the individual consumer addresses. Barriers to entry were, therefore, quite significant.

7.51. Redcats said it was also an issue that if the merger went ahead in its entirety, any entrant to the delivery market would not get the volume of the vertically integrated merged entity, which would account for some 70 per cent of the AMO mass. This would impair the ability of other players, such as Redcats, to bring in new entrants to service them if they were squeezed on distribution by the merged entity.

#### *Overall conclusion on the merger*

7.52. Redcats considered that the threats to competition in the AMO sector, and also in relation to low-cost B2C parcel delivery services, were so great that the CC should recommend a prohibition of the merger and divestment by March of the GUS home shopping and the home delivery services businesses.

#### *Conclusion on possible remedies*

7.53. Redcats said that the overriding concern under the Act was to achieve a full and effective remedy of the adverse public interest consequences resulting from the present merger. Since the adverse public interest consequences in this case affect the structure of the market, structural remedies, ie

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<sup>1</sup>*Safeway plc and Asda Group Limited (owned by Wall-Mart Stores Inc); Wm Morrison Supermarkets PLC; J Sainsbury plc; and Tesco plc: a report on the mergers in contemplation*, The Stationery Office, Cm 5950, September 2003.

divestment of all or a substantial part of the acquired businesses, were appropriate. Alternatively, divestment could be required of the Littlewoods mail-order businesses and either the GUS or Littlewoods home delivery businesses. Behavioural remedies were not appropriate except by way of supplementary and ancillary remedies in relation to divestment requirements.

7.54. It was possible that such divestment requirements would result in financial losses and costs to the parties by reference to the price paid by March to acquire the GUS businesses. However, irrespective of the amount of the loss involved, such remedy would not involve any ‘punishment’ of the parties. Rather, such losses would be the inevitable consequence of the proper implementation of the public law remedies of a merger situation which was entirely and in every respect of the parties’ own making. Given that the costs to society from unscrambling were likely to be minimal, it would be all the more contrary to the objectives and requirements of the Act to give any protection to the parties against their losses that would result from a divestment requirement in so far as an inflated price or premium was paid by March to eliminate its main competitor from the market.

7.55. Redcats stated that since the parties would not receive any financial protection from a downturn in market conditions, or the consequences of an unsatisfactory bargain resulting in the acquirer having overpaid for the acquired businesses, all the more so they did not merit leniency or protection in relation to the losses they would incur in implementing the requirements of the Secretary of State (and recommendations of the CC) under the Act in relation to the acquired businesses.

7.56. Any arguments concerning the impracticality of finding a purchaser for the businesses to be divested would be misplaced. By reference to its own profitability, Redcats believed that GUS home shopping, which had a much greater market share, should be a viable going concern even if there were no alternative purchaser. In any event, there was likely to be a willing purchaser or purchasers, provided that the price was set at the appropriate level by reference to market conditions, the value of the relevant assets and the projected future earnings under competitive conditions. If the GUS businesses were in financial difficulties and the value of such businesses (or the corresponding Littlewoods businesses) was accordingly significantly reduced for the purposes of a divestment sale, then the parties should still be required to divest such businesses irrespective of the achievable price, provided that the CC and the Secretary of State concluded that such divestment was the necessary and appropriate remedy for the adverse effects on the public interest.

#### *Comments on statement of hypothetical remedies*

7.57. Commenting on the CC’s statement of hypothetical remedies, Redcats said that as the present merger affected the structure of the AMO and wider mail-order markets, structural remedies were needed. It believed that such structural remedies must be either full divestment of the acquired GUS businesses or, as an alternative, divestment of the whole of the Littlewoods mail-order business (AMO and DMO) together with one of the merged home delivery businesses.

7.58. Complete divestment of the whole of the GUS or Littlewoods mail-order businesses (AMO and DMO) was necessary in order to ensure the transfer of a stand-alone business. The individual AMO catalogue businesses of GUS or of Littlewoods could not be separated into individual going-concern businesses. Divestment of one of the two home delivery businesses would only be an appropriate remedy if it were accompanied by divestment of the mail-order business of either GUS or Littlewoods. If this were not the case, then behavioural remedies would be required in order to ensure that the divested business had sufficient critical mass to constitute a realistic source of competition to the home delivery business retained by GUS/Littlewoods. For these reasons, Redcats believed that such behavioural remedies would not be a satisfactory solution.

7.59. Redcats did not accept that there could be no willing purchaser of the acquired GUS businesses, provided that they were offered at an appropriate price. It also reiterated that, when considering appropriate remedies, any question of possible loss to the parties was not relevant. The parties had entered into and completed this merger voluntarily and with their eyes open, and they had every opportunity to assess the risks and possible consequences of it being referred to the CC. They must accept such consequences of this decision in the same way as they must accept responsibility for their own business decisions.

## **Catalogue retailers**

### **Argos Ltd**

7.60. Argos, which remains part of GUS, said that with regard to the CC's statement of hypothetical remedies, it wished to comment on the proposal to divest the Reality or Business Express operations in part or in whole.

7.61. As a customer of Reality one-man delivery services (see Appendix 3.3), Argos saw the merger of Reality and Business Express, combined with the scale volumes provided by the merged home shopping businesses, as providing the opportunity for investment in the creation of a modern, efficient service which would ultimately improve the service that Argos could offer to its customers. Historically, it had generally been difficult for third party parcel delivery businesses to operate profitably in the UK as charges to customers generally did not cover the cost of providing the home delivery service. These businesses were therefore often attached to a large-volume business, such as AMO home shopping, which could subsidize the delivery businesses. In this situation, it had been difficult for businesses like Reality to invest in upgrading its service (for example, timed delivery, Saturday/Sunday delivery, next-day delivery, order tracking etc).

7.62. Argos, therefore, supported the merger of the Reality and Business Express operations as an important step towards the development of a long-term sustainable third party supplier. From a customer viewpoint, it believed that the combined entity should be able to provide a modern, efficient service. Although, in the short term, in order to fund the investment, it was possible that costs might rise, Argos believed that in the longer term this could be mitigated. First, the combination of the infrastructure should allow March UK to reduce costs. Second, the investment should enable the delivery features to be more flexible and enable Argos to offer its consumers enhanced service on a chargeable basis.

7.63. With regard to the suggested separation of the Reality/Business Express operation from the home shopping operations, Argos saw this as being an obstacle to investment in the infrastructure. The success of both parts of the business were inherently linked. The home shopping proposition could not become competitive in the wider UK retail market without significant improvement in the customer service and delivery infrastructure and the customer service and delivery infrastructure could not invest without the financial support of the home shopping business.

7.64. Separating the delivery businesses (Reality or Business Express or the combined service entity) from the catalogue operations, ShopDirect (that is, what was formerly GUS home shopping) and Littlewoods would, Argos believed, result in a worst case scenario from a third party customer and end-consumer point of view. A separation reduced the incentive on the catalogue operators to protect and develop the delivery business, the volumes then declined more rapidly, there was no ongoing investment in the infrastructure and therefore the service levels decline further. If all this were to happen, Argos, as customer, would face rising costs and declining service levels. In order to continue to provide the service to its customers, it might have to seek alternative suppliers, but the costs would be higher. Argos's customers would then be faced with a choice of having the service at a higher price or forgoing the convenience of home delivery for certain products.

## **Direct mail-order companies**

### **N Brown Group plc**

7.65. N Brown is a DMO company which also has direct response and direct selling activities. It commented on the NOP survey (see Appendix 7.3) and the OXERA survey (see Appendix 7.4). N Brown had a number of serious concerns about the merger, both as regards home shopping and as regards parcel delivery.

## ***The market for home shopping***

7.66. In N Brown's view, there remained a number of characteristics which clearly defined AMO as a distinct market. Credit availability continued to be the fundamental ingredient of the selling proposition in the AMO model. AMO customers were drawn from the C2 and DE SEGs, and were typically unable to gain access to other forms of direct credit and were therefore dependent on AMO. Furthermore, AMO operators had increasingly focused on the credit needy, leaving a core of customers more than ever dependent on AMO. AMO operators covered a wide range of products while DMO catalogues typically focused on a smaller range of products or a particular niche market. AMO prices were up to 20 per cent higher than high street prices due to the bundled nature of the pricing. The cost of credit, delivery and return, and the agent's commission, were factored in to determine the final price.

## ***Customer base***

7.67. N Brown gave us information about trends in the use of credit in AMO on the one hand and DMO on the other. Whilst the number of agents had decreased from 5.3 million to 4.4 million over six years from 1996, the use of credit by agents and their customers had remained stable above the 95 per cent mark. In addition, AMO operators were lowering the monetary thresholds above which longer interest-free terms became available for individual purchases, thereby offering increasingly longer credit terms by extending the length of interest-free windows to a wider selection of products, and intensifying 'buy now, pay later' campaigns. In contrast, during the same period, the use of credit within the DMO market had declined from 50 per cent to about 30 per cent. This showed the stark difference in the role that credit played between the AMO and the DMO market.

7.68. AMO customers were typically from the C2 and DE SEGs. In contrast, DMO customers were more likely to be from the A, B and C1 groups. The percentage of agents who bought for people other than in their own household was relatively stable with a decline from 34 per cent in 1997 to 30 per cent in 2003. In contrast, the spend per agent had not declined and had actually increased from £244 to £280 in the five years from 1997 to 2003. The AMO market was smaller than it had been in 1997 because the number of new customers entering the market had fallen below the number of customers exiting the market. In addition, increasing affluence among the population, combined with the fall in the cost of fashion, meant that there was a decreasing immediate demand for credit which was the driver for AMO sales. As the overall SEG profile of customers who were attracted to AMO moved downmarket, the remaining credit-constrained AMO customers were increasingly captive and more vulnerable to exploitation of market power.

## ***The effects of the merger on home shopping***

7.69. N Brown said that as a result of the merger, the merged entity would be by far the largest player in the AMO market with a market share in excess of 70 per cent. The other competitors in the AMO sector, Otto and Redcats, would have a 29 per cent market share and would not pose a credible competitive constraint on the merged entity.

7.70. The merger would reduce the choice available to customers and give the merged entity the ability to load prices considerably by exploiting further the inability of credit-constrained customers to access other forms of credit. The merged entity would also be able to exploit its market power by imposing more burdensome terms of trade in areas such as delivery and returns as well as the length of interest-free periods. N Brown expected that the competitive initiatives in which the parties currently competed head-to-head would be phased out (for example, the 'buy now, pay later' and other credit terms). These strategies would produce more disguised but equally detrimental effects on consumer welfare.

7.71. In N Brown's view, DMO operators did not act as a competitive constraint on AMO operators. The DMO companies operated with different target audiences and different offers.

7.72. N Brown was also concerned that the merged entity would be able to exploit the supply-side links between AMO and DMO to behave anti-competitively. The same suppliers served both the AMO

and DMO markets. The merged entity would have the ability to attract its suppliers to exclusive agreements, which would directly affect N Brown.

7.73. In addition, N Brown was concerned that in so far as the merged entity did not enter into exclusive supply terms, suppliers were likely to agree better price terms with the more powerful merged entity. The same mechanism might apply in relation to other procurement areas such as marketing and advertising.

### ***Parcel delivery***

7.74. N Brown submitted that the merger would bring together two suppliers of B2C ‘budget’ home delivery services, with a market share of some 60 per cent. The competition which had previously existed between Business Express and Reality would disappear and the merged entity would be able to increase prices to third parties for parcel delivery. Although prices had recently been increased, N Brown was nevertheless concerned that the merger would give scope for further increases that would otherwise not have happened. N Brown was concerned that the merger would leave N Brown with only one third party alternative to the merged entity for its parcel delivery needs, and that that third party was itself partly reliant on the merged entity. In N Brown’s view, B2B operators would be unlikely to enter the B2C market.

7.75. Commenting on the possibility of new entry to the delivery market if the merger went ahead and prices started to rise, N Brown said that the trunking aspects were the easy part—warehouses, vehicles and computer systems were readily available. What differentiated B2C from B2B was the ability to carry a parcel up a drive and then deliver it. That was the most expensive and complex part of an otherwise simple process and would perhaps dissuade entry. With sufficient volumes, it could become an attractive proposition, but in order for a potential entrant to determine whether it would get sufficient volumes it would have to predict how the incumbent would react to entry. If there was concern that, through the scale of its operation, it could take predatory action, then the potential entrant might decide that it was not worth making the up-front investment.

7.76. N Brown commented that entry was difficult because home shopping was nationwide. Companies could not choose where their customers came from and so they had to be able to distribute their products across the country. It was not feasible for a new entrant to open a depot to cover just one or two areas, with the intention of extending coverage when it had built up capacity, because home shopping companies would not choose to use different delivery companies in different regions. It was also important to remember that, for some of the smaller home shopping companies, delivery was a significant proportion of the selling price. Most of them charged an amount for postage and packing in order to recover some of the cost, but increases in this could affect whether or not it was profitable for them to continue in business.

### ***Comments on statement of hypothetical remedies***

7.77. N Brown commented on the CC’s statement of hypothetical remedies. It believed that the only effective remedy that would ensure that there was no lessening of competition, and that no detrimental effects arose in the markets affected by the merger, was a divestment of all the GUS businesses acquired by March.

7.78. This was largely due to the highly integrated nature of GUS’s AMO and DMO mail businesses. As a consequence of the high level of integration, any divestment of a part or parts of either of those businesses would be unlikely to form a viable or attractive option to a potential purchaser. Similarly, with regard to the delivery business, both Business Express and Reality were highly integrated with, respectively, Littlewoods’ and GUS’s home shopping activities. A divestment of the delivery business alone would therefore not be viable unless the business was transferred together with a long-term contract with the merged entity to deliver its products. Even in those circumstances, there would be serious doubts as to the viability of the delivery business going forward following the expiry of the contract with the merged entity.

7.79. N Brown said that the dynamics of the home shopping business and its dependence on access to a delivery network with sufficient capabilities in terms of density meant that it would be very difficult

to separate out parts for divestment. It believed therefore that the only effective remedy to address the anti-competitive effects that were likely to arise as a result of the merger was a divestment of the GUS businesses.

## **Next plc**

7.80. Next told us that it had acquired Grattan in the 1980s and later sold Grattan on to Otto. Next's catalogue, *Next Directory*, had been produced in 1987 as a result of the combination of the mail-order skills of Grattan and the retail skills of Next. *Next Directory* was produced twice a year and was significantly different from AMO offerings. The fashion products in the *Next Directory* book could be found in the Next high street stores. Next sold its own branded products. The products were also offered online, and the price of the products was the same, regardless of the channel through which they were bought. Next also had a growing home furnishings business. *Next Directory* customers were subject to a credit-scoring process. Next regarded its cost of credit as competitive in the industry.

7.81. With regard to parcel delivery, Next told us that its products were mostly delivered by Parcelnet, the courier service operated by Grattans. Next had a preference for courier services as these could offer a more personal service to customers.

### ***The market for home shopping***

7.82. Next said that it did not differentiate between a retail market and a home shopping market. It believed that there were several shopping channels, and these channels were for shopping in a high street store or shopping from home. As for competition, the biggest competitor to *Next Directory* was the Next retail operation, and vice versa. Other competitors were Marks & Spencer and Gap. In Next's view, AMO shopping and DMO shopping had been converging for some time.

7.83. The AMO business had historically been based on providing credit and access to the consumer goods market for its customers. However, the growth of DMO catalogues, the greater availability of credit and the growth of other channels, such as retail discount clubs and the Internet, meant that the AMO business was no longer unique in catering for these customers and therefore was no longer a separate market.

### ***The effect of the merger on the home shopping market***

7.84. Next did not have any concerns about the merger. It considered that all businesses, whether in the home shopping or in the retail sector, needed to work to maintain the quality and price competitiveness of their products in order to maintain their competitive position.

### ***The effect of the merger on parcel delivery***

7.85. Next did not have concerns as regards parcel delivery. It thought that the distribution industry was highly competitive, although it noted that Parcelforce was withdrawing from the delivery of large business items.

## **Retailers**

### **British Retail Consortium**

7.86. The British Retail Consortium (BRC) is the lead trade association representing a wide range of retailers. It believed that home shopping should be viewed in the context of retail as a whole, as it was one way in which consumers could choose to shop, and it competed for business with high street

retailers, out-of-town stores, and e-commerce. The merger and its effects on competition should not, therefore, be seen only in the context of home shopping.

7.87. Retailers operated in a highly competitive environment and that was the main reason that during the last decade the price of shop goods rose by one percentage point less than the overall level of inflation. Home shopping operated within this context, and the evidence was that to some extent home shopping consumers were turning towards e-commerce and television shopping instead of mail order. One of its advantages had been seen as interest-free shopping—but even this was under threat from high street retailers and from the lower interest rates currently available in general.

7.88. The BRC observed that industry reports had stated that mail-order sales, as a share of overall retail sales, had declined from over 4 per cent in the early 1990s to around 3.5 per cent in 2001 and 2002, though the actual value of sales had grown to about £8.5 billion in 2001. It had also been reported, in July 2003, that during the first half of 2003 alone online spending had doubled from the previous year to £4.75 billion with 12 million people shopping online, and the prediction was that sales would be in the order of £15 billion for 2003. This would exceed the amount spent on home shopping sales in 2001.

7.89. The BRC said that against this background of growth, in what must be regarded as its closest rival form of shopping, it was probably almost inevitable that there would be some sort of consolidation in the home shopping sector if companies were to be able to continue to offer home shopping at competitive rates and enjoy the economies of scale necessary to compete in the modern world.

### **J R Retail Consultants**

7.90. J R Retail Consultants (JR), independent retail consultants, said that the traditional advantages of catalogue shopping (credit and convenience) had become questionable and mail order could no longer be considered as a separate entity from the rest of the retail trade. The availability of ‘free’ credit, at a time when credit was not available to much of the population and social attitudes towards debt were different from today, set home shopping apart from the rest of the retail trade.

7.91. The inescapable conclusion had to be that traditional home shopping as characterized by GUS and Littlewoods was in terminal decline because it could no longer be viewed as a discrete segment of the retail trade. Today, all retailers had a multi-strategy approach to their customers embracing stores, catalogues, credit and online facilities. Successful retailing meant giving customers what they wanted and today’s consumer no longer made a distinction between catalogue (DMO) and store-based retailing.

7.92. In order to survive, GUS home shopping and Littlewoods had to compete not with themselves or the remaining smaller home shopping companies but with every retailer. Preventing this merger would achieve nothing for the public interest—the merged entity would still be a peripheral weak player in the context of UK retailing—but was likely to hasten the demise of both operations with consequent job losses and reduced consumer choice. Such were today’s retail realities where both businesses had already passed their sell-by date. The combination of the two could provide one last chance not just to slow the decline but to use the greater strength to justify the investment required for change.

### **Matalan Retail Limited**

7.93. Matalan said that it had no objection to the merger, and it did not wish to seek any safeguards.

### **Multi-channel retailer**

7.94. A multi-channel retailer said that it was concerned at the implications for the home parcel market resulting from the merger. Reality carried about 40 million parcels a year for companies outside the GUS group, and Littlewoods operated Business Express, which delivered about 25 million parcels for non-Littlewoods customers. Reality and Business Express had, in the past, competed vigorously in the marketplace for this business. However, following the withdrawal of Parcelforce from the volume parcel delivery service, both companies had dominated the market.

7.95. At the time of Parcelforce's withdrawal, the retailer said that, in common with a number of other mail-order companies, it had had its prices unilaterally increased by 30 per cent by its existing carrier, Business Express. As such, it was concerned that a merger between Reality and Business Express would lead to further price increases for this essential service.

7.96. Most e-commerce and catalogue mail-order businesses were dependent on these services, and the rates charged were an extremely sensitive parameter in their businesses. DMO companies generally passed the cost of carriage on to the consumer in the form of a 'post and packing' charge. The multi-channel retailer felt that the amount charged was a real inhibitor to demand, and to the further development of e-commerce and mail-order retailing.

## **Shopping channels**

### **QVC**

7.97. QVC is an electronic home shopping channel which operates via a broadcast service on Freeview cable and satellite television platforms.

7.98. QVC gave us information about its business and expressed concerns about the effect of the merger on parcel delivery.

### ***The market for parcel delivery***

7.99. QVC considered that there existed a distinct market for budget B2C delivery services, consisting of high-volume deliveries of low-value items, over the weight of 1 kg. This could be distinguished from delivery of high-value items, such as PCs and mobile phones, for which consumers were willing to pay higher prices.

7.100. QVC stated that Business Express and Reality had been its two main options when seeking tenders for business, and that, since the exit of Parcelforce from the high-volume sector to focus on a two-day service and premium delivery options, Business Express and Reality were the only two low-cost services with national coverage. QVC had not found that other carriers aspiring to serve the budget B2C market had been able to offer tenders that would meet its needs. In the view of QVC, regional carriers were not in the same market and did not represent a competitive force to Reality and Business Express, because regional carriers could not offer a national service at reasonable cost.

7.101. QVC said that given the commercial requirements of speed and reliability, it would prefer to spread its risk over at least two undertakings, and not to increase the number of parcels subject to that risk.

### ***The effect of the merger on parcel delivery***

7.102. QVC was very concerned about the suggestion that had been made by Littlewoods that delivery prices for budget B2C goods would rise from their current rate to the rates applied by B2B carriers. Such rises could significantly damage QVC's business. QVC thought it extremely unlikely that, in the absence of the merger, Business Express prices would have risen to the level of B2B services. It was unlikely that consumers would accept this increase. QVC added that it did not have its own internal delivery network. QVC also doubted if efficiency gains as a result of the merger would be passed on to customers.

7.103. QVC said that before the merger, the existence of Business Express as a separate entity exerted sufficient competitive pressure to force Reality to offer a differentiated budget service, in order to attract higher volumes. Post-merger, the range of delivery options was likely to become narrower. As a result, e-commerce sales and other home shopping companies would find it more difficult to compete with traditional retail outlets. The merger might further result in a loss of innovation in developing new

delivery options, for example pre-booking delivery slots with the customer, or use of reception boxes outside a customer's home.

### ***Comments on CC statement of hypothetical remedies***

7.104. Commenting on the statement of hypothetical remedies, QVC did not consider that the following remedies would satisfy concerns relating to a substantial lessening of competition in the market for budget B2C home delivery services: (a) divestment of the GUS AMO home shopping business alone; (b) divestment of GUS home shopping business (AMO and DMO); or (c) divestment of particular assets of the GUS home shopping business. In particular, none of these remedies would ensure that there was effective competition in the market for budget B2C home delivery of parcels, because Business Express and Reality would continue to be controlled by one home shopping business.

7.105. QVC considered that the divestment of all the GUS businesses acquired by March could satisfy the competition concerns, provided that the purchaser was one that had an incentive to continue to operate Reality as a separate competitor to Business Express in the supply of budget B2C home delivery services. In particular, QVC considered that so long as the prospective purchaser of the GUS businesses were to continue to operate the home shopping part of the GUS businesses, it would also continue to operate a B2C home delivery service, and to offer budget B2C home delivery of parcels to third parties.

7.106. As regards the possible remedy relating to divestment of the Business Express or Reality parcel delivery services, QVC considered that if either one of these businesses were to be divested, it would be necessary, in order to avoid a substantial lessening of competition, for March to provide the divested business with a contract for the purchase by March of parcel delivery services from the divested business. This contract would have to be of sufficient volume and sufficient duration to enable the divested business to establish itself as an independent entity offering budget B2C home delivery services on a nationwide basis. A minimum of five years should be provided for in respect of duration. QVC said that before the approval of such a remedy, customers of Business Express and Reality, such as QVC, should be allowed to review the provisions of the relevant supply agreement (where necessary without specific confidential business information) in order to ensure that it met all the relevant requirements. It would also be appropriate at the same time to place obligations on the home delivery business retained by March to offer B2C parcel delivery services on to third parties in a non-discriminatory manner on the same basis that such services are provided within March to March's home shopping businesses.

7.107. Regarding the hypothetical remedy relating to the divestment of particular assets of Business Express or Reality, QVC was particularly concerned that there could be a tendency for March to divest the least attractive assets, rendering the divested entity an insufficiently effective competitor in the budget B2C parcels delivery market. In addition, without the transfer of an existing, cohesive business, including the trade names and marks as well as all existing operations, the divested business or its acquirer would inevitably incur increased costs in establishing a new business. Further, QVC considered that it would be considerably more difficult for third parties or the competition authorities to judge whether the assets divested were sufficient to enable the same degree of competition as existed before the merger. Consequently, QVC did not consider that this remedy would be appropriate.

7.108. QVC said that another remedy which would be acceptable was the divestiture by March of both Business Express and Reality to separate, and appropriate, third party purchasers. If this were to occur, QVC considered that it would not be necessary for March to enter into a supply agreement such as that referred to earlier with either divested business.

### **sit-up Ltd**

7.109. sit-up Ltd (sit-up) is the parent company of: (a) bid-up.tv, which is a live, interactive shopping auction channel; (b) price-drop.tv, a recently-launched falling price auction channel; and (c) Screenshop, an 'infomercial-based' 24-hour shopping channel. sit-up said that the company had been highly successful since inception in 2000. bid-up.tv and price-drop.tv broadcast for 17 hours a day, with approximately ten auctions an hour. Products offered are general merchandise, household products, electrical goods, toys, jewellery and some clothing.

7.110. sit-up said that its logistics requirements were driven by the auction and shopping schedules of its channels and by the delivery promises to its customers. Once an auction or sale had been completed, goods must be picked and delivered to customers on time and without damage. This required a high-quality nationwide delivery operation that could respond to fluctuations in volume; such a requirement was particularly important in the run-up to the Christmas period.

7.111. sit-up told us that over 1 million units were shipped to its customers during 2002, the vast majority of which were single-item deliveries. Volumes were growing significantly this year, and by the end of the year sit-up expected to have shipped in excess of 3.5 million units. Given the continued expansion of digital television in the UK, and the increasing popularity of sit-up's customer proposition, sit-up expected that substantial growth would continue in 2004 and beyond. The relatively low sales value of each parcel meant that the rate charged for delivery was an extremely critical part of the business model.

7.112. sit-up used Business Express for 99 per cent of its deliveries. Its decision to use Business Express was influenced by Business Express's willingness to trade with a new business; an ability to deliver B2C parcels nationwide; and an acceptable cost for the service provided.

7.113. sit-up said that other carriers tended to specialize in B2B delivery. With the exception of Reality, the few companies that did offer home delivery services tended to provide national coverage at premium prices, for a faster speed of delivery; however, that did not fit with sit-up's commercial requirements. Some carriers such as Parcelnet offered a courier-based service that was designed to deliver cost-effectively a core range of relatively small parcels containing, for example, items of clothing. However, sit-up's parcels tended to be boxes and cartons of slightly larger dimensions that Parcelnet did not wish to carry in significant numbers. The only other carrier was Parcelforce, which would be likely to charge significantly more for this service due to the nature of its infrastructure.

7.114. sit-up was therefore extremely concerned that a merger between Reality and Business Express would lead to significant price increases for this essential service. It considered that a merger of these two delivery operations would be against the public interest.

7.115. With regard to the possibility of safeguards, sit-up suggested that it would be extremely difficult to construct adequate safeguards. However, it might be possible to construct something based on the following: the merged delivery operation entity could be subjected to a cap on the profits that it could earn in relation to its turnover and capital employed; and could be required to be run as a separate business; and could be required to offer services to third parties at the same price for a given service level to all customers, including GUS home shopping and Littlewoods; and could be subject to audit by a different firm from that employed by GUS home shopping and Littlewoods; and the auditors could be required to confirm to customers that those safeguards had been observed in the spirit as well as in the letter of the restrictions.

## **Suppliers**

### **Andromeda Entertainment Plc**

7.116. Andromeda Entertainment Plc (Andromeda) is a major supplier of both video games consoles and video games to mail-order companies. It said that whilst in the past catalogues had been competing with each other for a market share of this business, in the last three years they had also had to fight high street retailers and e-commerce enterprises. The traditional added value of home shopping—namely interest-free credit, unrestricted returns and free home delivery—had compensated consumers for the higher prices of goods in the past.

7.117. However, this had all changed and the consumer could now obtain credit on the high street at more advantageous terms, buy goods at cheaper prices and in many instances take advantage of free delivery. Similarly, the e-commerce business model focused on an aggressive pricing strategy.

7.118. Andromeda said it was obvious that home shopping had to reinvent itself by becoming more competitive, and this was only achievable by rationalizing its own logistics, offering better services,

cheaper prices and more choice. This could only be achieved by the amalgamation of mail-order companies. It believed that the merger could only benefit the consumer as it would reinstate the traditional benefits of home shopping, thus enabling mail-order companies to compete more effectively in the marketplace. Andromeda therefore fully endorsed the merger.

### **DAL Consumer Electronics Ltd**

7.119. DAL Consumer Electronics Ltd said that it was a supplier of consumer electronics to the UK, acting as an agent for a Japanese group which had a substantial manufacturing facility in South Wales. It believed that the merger was in the public interest.

7.120. It also believed that the merger would improve the merged entity's ability to compete with the high street and supermarkets, which in its view were polarizing the channels to which the public could go for consumer electronics. There were increasingly fewer options for the consumer, and the merger would create a strong brand, which the consumer could trust and turn to as an alternative.

### **Get Clothing Co Ltd**

7.121. Get Clothing Co Ltd believed that the merger was good news for the consumer as it would offer more competitive prices. The merger of both companies would ensure full utilization of resources with the benefits being passed on to the consumer. As a supplier, it would be in a position to offer more competitive prices to the merged company. It felt that without this merger the home shopping industry would not be able to compete effectively with the high street.

### **KD Products Ltd**

7.122. KD Products Ltd said that it supported the merger, when taking into account the vastly expanding mail-order industry as a whole, and the highly varied marketing techniques employed. A larger, stronger organization might have greater competitive capability against the bigger European competitors such as Quelle and Otto, the latter being already well established in the UK.

### **Playtex UK**

7.123. Playtex UK, a division of Sarah Lee Branded Apparel, said that for a number of years the trade had seen a decline in the mail-order sector against the high street and value sectors. It observed that in the calendar year to June 2003, the total mail-order sector had fallen from 12 to 10.3 per cent in overall lingerie terms. In Playtex UK's opinion, the acquisition would therefore benefit the mail-order business by strengthening this class of trade.

### **Puma United Kingdom Ltd**

7.124. Puma United Kingdom Ltd (Puma) said that it was a supplier of branded products to the sport trade and to all the mail-order houses, including GUS home shopping and Littlewoods. Its product range included sports and sports fashion footwear, clothing etc.

7.125. Puma understood that March would maintain two separate businesses with separate buying teams, albeit with a common warehouse/distribution facility. As such, Puma would continue to have two opportunities to present its future ranges for selection, and it did not believe that this would restrict the marketplace. The additional financial security of March behind the existing GUS home shopping operation would also increase competition as both independent teams could effectively compete with one another.

7.126. Puma said that it had no concerns about the common warehouse facility. It would, however, be concerned if the proposal was simply a facade to merge the buying teams in the near future, as this would restrict Puma's ability to get product into catalogues and in front of consumers.

## **Graham Technology plc**

7.127. Graham Technology plc said that it provided customer-facing processes to both GUS home shopping and Argos, and had supplied both companies for some years. It believed that the merger was in the best interests of all parties and would provide a more competitive and efficient service to home shopping catalogue customers.

## **MGN Limited**

7.128. MGN Limited (MGN), a publisher of magazines and supplier of advertising space, said that GUS home shopping, and its post-acquisition equivalent, ShopDirect, was both an advertiser and commercial partner of MGN Limited, a division of Trinity Mirror plc. MGN published the *Daily Mirror*, *Sunday Mirror* and *The People* plus associated magazine titles. GUS home shopping/ShopDirect had used, and continued to use, MGN titles to promote its own catalogue brands such as *Marshall Ward*, *abound* and *Love It* to readers of MGN titles. It did this through branded display advertising usually for selected fashion merchandise. They also inserted free-standing branded catalogues into MGN titles using MGN inserting capability. For these activities it bought space/inserted slots as with any advertiser. As a commercial partner, it prepared, printed and provided to MGN for inserting a range of fashion and household goods catalogues under the *Daily* and *Sunday Mirror* and *People* brands. This was based on a shared risk commission-on-sales approach.

7.129. MGN said that it was generally in favour of the acquisition for the following reasons. There was a risk that, should this acquisition be deemed to be unacceptable on competition grounds, ShopDirect might be wound down or closed completely. The mail-order business was highly specialized and process-driven involving massive stock commitments, highly complex logistical capability and advanced database expertise. The mail-order market generally was also under tremendous pressure with trade comment indicating much greater competition chasing declining business. Should ShopDirect come back on to the market (if March were ordered to divest itself of ShopDirect), it was difficult to imagine who would buy such a complex business in a difficult and overcrowded market unless they were already involved and were looking for customer acquisition or cost economies of scale. Such candidates would, however, be likely to encounter the same competition issues. It would be surprising if an approach were to come from a non-catalogue or retail business. In such a context, the ShopDirect business could be lost, the degree of consumer choice reduced and a large number of jobs lost including many highly experienced people.

7.130. The central consideration in this review related to whether the consumer interest was being compromised. Given MGN's view relating to current levels of development activity within ShopDirect and the forward commitments for 2004, and the fact that it was ostensibly being run completely independently of the Littlewoods operation, MGN considered that consumer choice was not being eroded. The business was now being more tightly run and focused, which should be to the benefit of customers.

7.131. The other aspect under consideration was whether the new combined company would have a share of the market that would allow it to act against the public interest. This related specifically to price control and the access to credit for that part of the market that used this form of shopping. If the review focused solely on the 'big-book' sector of the market—Littlewoods, GUS/ShopDirect, Redcats, N Brown, Grattan/Freemans (Otto)—the removal of one of the principal players could be construed as a narrowing of choice and therefore providing the potential for increased market control by the reduced number of operators. However, MGN believed that this would be a false premise as the catalogue market was more widely based and, far from the major catalogue operators competing among themselves, they existed within the much broader retail market.

7.132. Should the decision be to allow the merger, then MGN would suggest that a condition be applied that ShopDirect and Littlewoods continued to operate as separate marketing entities with their own discrete customer database to ensure the maintenance of choice. This would still allow backroom efficiencies to be achieved through a streamlined warehouse and distribution system across the Littlewoods and ShopDirect operations with potential benefits to customers.

## **Servis UK Ltd**

7.133. Servis UK Ltd said that during the last 12 months it had seen the position of mail order weaken in the domestic appliance market. It was concerned that without the merger the future of mail order might disappear against the strong competition from multiple high street retailers and mass merchandisers.

## **Silentnight Holdings PLC**

7.134. Silentnight Holdings PLC was fully supportive of the merger. It said that the home shopping market had been in decline for several years, reflecting various factors including socio-economic trends, the ready availability of consumer credit and increased competition from traditional retailers. It believed that home shopping provided a very useful service to the UK market and, as such, was keen to see it preserved and strengthened. It also believed that the merger would help to sustain mail order and so enable it to compete with the rest of the market.

## **Stuart Peters Ltd**

7.135. Stuart Peters Ltd said that, as a supplier to both GUS and Littlewoods, it had seen a dramatic loss in business during the last few years. It felt that the home shopping industry would not be in a position to compete effectively with the high street unless the merger was allowed to proceed. It did not therefore believe that the merger would operate against the public interest.

## **Supplier A**

7.136. A supplier said that it supplied both GUS and Littlewoods. It believed that the merger would help its continued business within the home shopping market. The market was reducing in size on a yearly basis, and the supplier believed that its survival lay in offering an alternative to the high street by way of the major players consolidating and joining forces.

## **Supplier B**

7.137. A supplier said that both Littlewoods and ShopDirect (formerly GUS) were run by Mr Aidan Barclay and his executive team. It was impossible to imagine 'Chinese walls' in this situation and the new organizational structures were identical in both companies.

7.138. The Barclay Brothers were reported as having said they had been told by GUS that if March had not bought GUS home shopping then its parent company would have closed it down and collected the customer debt. As a result, GUS had the support of the unions and others concerned about job losses. Large job losses were inevitable as a result of this merger. Only the Barclay Brothers had the means to pay the price they did for GUS home shopping given the synergy benefits of a merger with Littlewoods Home Shopping.

7.139. This supplier did not accept the figures given to the unions that only 500 jobs would be lost if Littlewoods and GUS home shopping merged. The number would be at least 5,000; there would be little point to the merger if only 500 jobs were removed.

7.140. The supplier said that both Littlewoods and GUS had recently changed agreed terms of trade by altering settlement discount, adding 'listing fees', delaying payments etc. These changes were made at a high level and did not involve the buyer who had negotiated the supply contract. This supplier believed that the situation would worsen if the merger were allowed.

7.141. The merged entity could abuse its near-monopoly position with its customers who needed short-term, low-value credit and whose alternative way to obtain this would be via 'loan sharks'. It could also increase the cost to the consumer of credit by increasing the APR from 29.9 to 39.9 per cent and dropping the much-used interest-free 40 weeks credit option as GUS had done this autumn. This supplier

said that it did not expect Empire (Redcats) or the failed merger of Grattan and Freemans (Otto) to be players in this credit market for much longer. They were both subsidiaries of European companies which did not understand the credit business in the UK.

7.142. This supplier reported rumours that if the merger were not allowed, March would close GUS and collect the debt. March could also send the *Littlewoods* catalogue to former GUS customers as it would still have the mailing list. In the supplier's opinion, if the merger were not allowed then March should be forced to sell GUS and give up the mailing list.

7.143. There had been other potential buyers for GUS's mail-order interests. The supplier believed that the business could have been turned around, as most of the major problems related to product, catalogue and marketing—areas about which the Barclay Brothers knew little but which other potential buyers could have put right. Consumers would be better served by having a choice between the *Littlewoods* catalogue and ShopDirect.

7.144. As regards delivery services, the supplier said that former employees of GUS had created an onerous contract that gave Redcats a delivery service standard and price that were below market rates, and which were not available to others. The real concern was that new mail-order companies would not be attractive to this delivery giant and their growth would be stunted, thus further damaging the recovery of UK mail order.

7.145. The supplier said that the merger should not be allowed to stand. As regards possible remedies, it believed that March should be required to sell the entire business. Unless the business was put back to how it was and allowed to be bought by people with experience and interest in the sector, it would soon cease to exist. Any other of the hypothetical remedies would require a degree of trust in March that was unlikely to be found, and would at best allow other existing players to acquire mailing lists and close the business down.

## **Supplier C**

7.146. A major UK consumer electronics manufacturer said that it supplied both GUS and Littlewoods, and that it had observed the marketplace for the home shopping business in the UK electricals sector for many years. The changing nature of the supply of electrical products was obvious. New, emerging mass merchandiser channels, and increasingly acute competition on the high street and retail parks, combined with easy access to affordable credit, had meant that the traditional home shopping/mail-order model had been under increasing pressure for some years.

7.147. This supplier believed that the analogy between the decline of the traditional television rental business, where the major players were eventually allowed to consolidate to maintain consumers' choice, and the inevitable consolidation required in the home shopping sector was apparent. A strong home shopping operation was clearly required to maintain diversity and choice for the consumer, and it believed that the merger would achieve this.

## **Vanguard Textiles Limited**

7.148. Vanguard Textiles Limited is a manufacturer and distributor of household textiles, namely bedlinen, towels and coordinating accessories. It said that it had been a major supplier to both GUS and Littlewoods home shopping businesses for over 25 years. During that time it had witnessed the decline in market share of AMO which had been lost to various high street businesses. Vanguard believed that, individually, both GUS home shopping and Littlewoods would continue to decline along with the remainder of the mail-order industry. However, one strong home shopping business, rather than a fragmented industry, would be able to compete more effectively with the high street. As well as maintaining a choice of shopping channel for the consumer, a strong home shopping business would also safeguard many thousands of jobs which might otherwise be lost.

## **Wyvern Furniture Ltd**

7.149. Wyvern Furniture Ltd said that it had made representations to the OFT, because it had been concerned about the possibility of a merger of the products offered by way of furniture by Littlewoods and GUS home shopping. It said that these concerns had been removed by both parties during the course of normal trading relationships.

## **Credit providers**

### **BrightHouse**

7.150. BrightHouse gave us information about its business. It stated that it did not have a view about the merits or demerits of the merger.

### **Provident Financial plc**

7.151. Provident Financial plc (Provident Financial) is a financial services group whose principal activities involve the provision of credit products suited to the needs of lower-than-average-income consumers. Its principal home credit activities are carried on by the subsidiaries, Provident Personal Credit and Greenwoods Personal Credit, which currently had more than 12,000 agents (over 75 per cent of whom were women) and about 1.6 million customers (up from about 1.3 million in 1997). Its agents made weekly calls on customers both to issue loans, normally in the form of cash or vouchers that were accepted by a range of shops, and also to collect repayments. Provident Financial said that cash advances in the home credit sector were usually in the order of £150 to £300. Repayment periods varied from 14 weeks to three years, but in most cases ranged from six to twelve months. Once a loan had been advanced, the borrower would normally expect to repay it, and the interest it attracted, in regular weekly amounts (collected by the agents).

7.152. Provident Financial said that its cash advances allowed for an unlimited choice of stores for customers. Indeed, this ability to shop around enabled customers to offset the charges on its loans by paying cheaper prices for goods. By contrast, a customer who, needing credit to buy goods, had to use AMO would have to pay a price which reflected the 'bundled' cost of credit. It was possible for that 'bundled' price to be as much as the cost of the same goods in a high street store plus Provident Financial's charges on a loan to buy them.

7.153. Provident Financial submitted that the increased competition that had developed in the supply of credit to lower-income consumers meant that there would be few (if any) consumers who would regard AMO as their only available source of credit. Faced with an increasing range of products competing for the supply of credit to lower-income consumers, the established players were having to look to ways to improve efficiencies and/or broaden their product ranges. It was understandable, therefore, that Littlewoods and GUS were seeking to merge their activities. Integrating the two businesses was likely to bring significant cost savings.

7.154. It remained to be seen how the two businesses would be integrated if the merger proceeded, including how GUS's Morses home credit business would be developed, within the group's wider catalogue credit business. In general terms, however, Provident Financial expected the merged group to remain a strong competitor in the supply of credit to lower-income consumers, active across a range of products from AMO (eg GUS) to home (retail) credit (eg Morses) to personal loans (eg the HBOS venture).

7.155. The merged business would be the very clear leader in the AMO sector—a considerable way ahead of Otto and Redcats. However, the increased competition and range of different credit products now available to lower-income consumers meant that even such a significant consolidation within the sector ought no longer to be a cause of concern for the competition authorities.

7.156. Provident Financial expected to be able to respond to these continuing developments in the market (including the Littlewoods/GUS home shopping merger) by further developing its range of products to ensure that they remained competitive and attractive to UK consumers.

## **Trade unions**

### **Transport and General Workers' Union**

7.157. The Transport and General Workers' Union (T&G) believed that there was a strong public interest case in favour of approving the proposed acquisition of the GUS home shopping business by March UK.

7.158. T&G said that there were clear benefits from the merger for those, including many of its members, who used home shopping. It had been clear for some time that AMO home shopping was in severe decline. The merger was the best chance of ensuring the survival of this service and preserving choice for consumers.

7.159. First, it would allow March UK to establish a modern and competitive home shopping business that could compete against the rapid rise in direct mail, e-commerce and direct competition from the high street. The latter source of competition remained the greatest challenge to the home shopping business. High street retailers, and particularly those in the value sector, provided very strong competition to home shopping businesses in general. The merger would help strengthen catalogue shopping; it would help it reverse its current steady decline, and enable it to compete effectively with high street stores.

7.160. Second, the merger would ensure that the existing service currently enjoyed by the customers of GUS home shopping was preserved. Having spoken to its members and the other unions involved, and having listened to the case put by the GUS management, the T&G was clear that the acquisition by March offered the only realistic alternative to secure the future of the GUS home shopping business. Without the acquisition, the GUS management would have closed the business. The fact that sales had declined by 20 per cent in 2003 alone made this proposition harder still to refute. There were roughly 19,000 jobs at stake in the GUS business, and their loss would have a very significant impact on the local economies and would have a social impact on the local communities in which they were located. The T&G strongly supported the merger as the best way of preserving those jobs and the service that they provided to GUS customers.

7.161. The T&G was convinced that the parcel services of both Littlewoods and GUS home shopping had been operating on an unsustainable basis with a pricing structure that had been well below true costs, both for internal distribution and for deliveries for third parties. The merger provided March and GUS with the opportunity to create a modern and viable parcels business that was sustainable in the long term and that could provide an efficient and competitive service to third parties. In particular, the T&G felt that it would be clearly against the public interest for the merger to be jeopardized due to concerns arising from the parcels delivery businesses, which formed such a small part of the two home shopping businesses.

7.162. The T&G strongly believed that there was a sufficient case for allowing the merger to stand without the need for further remedies.

### **Union of Shop, Distributive and Allied Workers**

7.163. The Union of Shop, Distributive and Allied Workers (USDAW) said that it was its strongly-held belief that the further existence of the GUS home shopping business could only be preserved through an association with Littlewoods as the only possible alternative both to protect the employment base and to provide the commercial foundation on which both Littlewoods and GUS home shopping could continue and prosper. USDAW did not believe that the merger represented a monopolistic position either in catalogue retailing or in home delivery services.

7.164. USDAW said that any closure of sites and laying off of staff would have a devastating effect upon the old mill towns in Greater Manchester, Lancashire and areas of Yorkshire. Furthermore, over the last few years the mail-order sector had changed dramatically so that the old definitions of home shopping had become blurred with retailing generally. The result was a more varied and multi-channel retailing scene in the UK. Littlewoods and GUS home shopping were just one of a number of companies that had home shopping in their operations.

7.165. In USDAW's view, it had become increasingly irrelevant to describe the former mail-order sector in a narrow fashion. Remote ordering, whether via catalogues, the Internet, or interactive television, was where the future of retailing was to be found. The GUS home shopping business did not just compete with Redcats and Littlewoods or Next but also with Asda or Tesco or Matalan.

7.166. The merger had not been a typical case of one company increasing market strength through acquisition in an expanding sector, but rather of two companies seeking merger for mutual survival. USDAW was relieved that Littlewoods wished to strengthen both companies through merger. Had March not intervened, the GUS home shopping business would have faced the very real prospect of closure. With sales declining and an urgent need for cash to sustain its balance sheet and make the investments necessary for a long-term future, the GUS home shopping business could not go on for very much longer.

7.167. As to parcel delivery services, for a number of years Business Express and Reality had carried parcels, both for themselves and for some third parties, at rates that were well below economic cost. Other home shopping companies, whilst carrying most of their own parcels themselves, had used Business Express and Reality to deliver the parcels they did not want to carry to take advantage of this uneconomic pricing.

7.168. USDAW believed that Littlewoods and GUS home shopping should be given a chance to rationalize their operations and create a more efficient, viable parcels service, that would ensure the sustainability of their own businesses and provide a truly competitive player in the UK parcels market. USDAW also believed that it would be disproportionate to allow any concerns over such a small and ancillary part of these two businesses to jeopardize the future of the GUS home shopping business. USDAW submitted a survey carried out by OXERA which is summarized in Appendix 4.2.

## **Parcel delivery services**

### **Famac Network Limited**

7.169. Famac, which is based in Northern Ireland, said that it had provided a delivery service there for GUS and Littlewoods, as well as for other mail-order companies, for a considerable number of years.

7.170. Famac said that during the last five years it had experienced a continual decline in mail-order business, initially affecting the smaller mail-order companies, but now also affecting GUS and Littlewoods, both of which had seen their parcel volumes decline. The main reasons put forward for this were: stiffer competition from the high street; store-card credit facilities being more accessible, especially to lower earners; and low inflation and interest rates leaving the consumer with more disposable cash, and therefore not requiring lengthy credit terms.

7.171. Famac felt that if mail order were to survive, it would require an even flow of product to sell, including fashion, footwear, household goods and furniture. In recent years mail-order companies, with the exception of Next, had struggled and it believed that GUS and Littlewoods would not be able to counteract this trend without the merger. What was needed was a redesigned offer to the consumer that had an appeal which, at least, matched the high street retailers; this could best be achieved in a joint business.

7.172. Whilst mail order equated to a small percentage of the total retail market, it was still a very important part of the British way of life. Famac believed that the merger would be good for the business in general and would protect both employment and its standing in the marketplace.

## **G&M Distribution**

7.173. G&M Distribution said that it had provided delivery services for both GUS and Littlewoods home delivery services for many years. It believed that the merger could only have a positive impact on the home shopping market.

## **Parcelforce Worldwide**

7.174. Parcelforce Worldwide, the express and international parcels arm of Royal Mail Group plc, said that B2C parcel delivery services could potentially be segmented in various different ways.

7.175. In terms of the substitutability of the two types of offering made by the parties, Parcelforce said that it was not possible to make a straightforward differentiation between the services on the basis of the type of products being dispatched, or their intrinsic value in each case. Reality/Business Express's customers' requirements might vary considerably.

7.176. However, based on Parcelforce's own historical experience in the provision of three-day-plus delivery services, there was a correlation between low-value goods being dispatched by delivery service providers and the 'budget' business parcel delivery service offered by the merging parties.

7.177. B2C and B2B services constituted a highly differentiated market, with degrees of substitutability on both supply and demand sides between budget B2C services and B2C mainstream services, and also between B2C mainstream services and B2B services. Indeed it would appear that there was potential substitutability between all services and not simply between services whose specification was only slightly different.

7.178. Whilst it was clearly accepted that each of Business Express's and Reality's prices for B2C parcel delivery services would have to rise even in the absence of the merger in order to cover costs of providing the service, Parcelforce Worldwide still pointed to the fact that the existing small number of carriers which focused on B2C parcel delivery services would be reduced by the merger, such that the two largest players (accounting, in Parcelforce Worldwide's view, for a total of at least 165 million parcels a year) would be subsumed into one operation. Depending on the CC's view of market segmentation and on the possibility that B2B service prices would act as an effective potential competitive constraint on prices, it was possible that the merger would result in price rises occurring sooner than they would have done in the absence of the merger. Prices would probably need to rise substantially for a B2B price constraint to actually become a factor in limiting price rises.

7.179. In terms of market response to any price rise caused by (a) either the necessary price increases in order to cover costs described above or (b) any increased or hastened price increases as a result of the merger, it was possible that choice for smaller mail-order companies would diminish, forcing them to pay prices for distribution which they could not recover. An example of this effect could be charity mail-order companies that might be unable to sustain sales of their low-value merchandise via their own mail-order catalogues as a result of the increase in distribution costs, and therefore lose one of their existing routes to market.

7.180. The opportunity provided to the merged entity, if the transaction was cleared, was for consolidation of two national networks (and therefore potential efficiency gains) and increased capability in providing highly profitable services such as a Saturday service, offering a nationwide network of consumer drop-off points and a comprehensive track-and-trace system, which monitored product movement from collection to picking and packing, depot, delivery van and front-door delivery. As a result, it was expected that the merged entity would have a broader range of B2C services. Accordingly, even if prices rose as a result, they might be considered by clients to be fair, considering the increase in quality of service provided, which would accordingly strengthen the offering. Parcelforce Worldwide also said that price increases, coinciding with a marked improvement in quality of service, would reduce the overall differences currently perceived by the market between the specifications and features of B2C services versus B2B services.

7.181. Aside from the strengthening of the parcel delivery offering by the likely increase in quality of service, it was also worth noting that such price rises may be potentially damaging to the budget end of B2C services where the priority was on low-cost conveyance, rather than on providing add-on features

such as track-and-trace technology, and delivery to be guaranteed or time certain. With regard to budget end-customers and potential other sources of supply, Parcelforce Worldwide said that it was unlikely that Royal Mail's current product portfolio could be considered a major alternative, given that Royal Mail was currently providing mainly a next-day guaranteed (Special Delivery) service at above the budget B2C price, essentially limited to items under 2 kg, and its non-guaranteed Packet Post product, essentially with the same weight restriction.

7.182. However, Parcelforce Worldwide said that it did not discount the possibility of potential entry at the budget B2C end of the market by 'no-frills' entrants, or relationships being formed between express carriers and other mail-order companies (for example, N Brown with Securicor Omega Express). A third option might be that small mail-order companies could form their own alliances to support a collaborative delivery network simply for their captive home shopping customers.

7.183. [Details omitted. See note on page iv.] In the medium to long term, it was likely that consumer shopping volumes via television, the Internet and other channels would compensate for the decline in AMO volumes, leading to resumption in market growth. With increased consumer confidence as to each of these new medium's security and convenience, so would the expectation of the consumer for flexibility and convenience (time of delivery, delivery point, notification of impending delivery, etc) and speed extend into the distribution of their goods. Accordingly, Parcelforce Worldwide expected that demand for reliable, guaranteed, insured express services with technological 'add-ons' such as high-specification track-and-trace, signature, and evening deliveries would increase.

7.184. Smaller mail-order operators might take their distribution in-house or ally with others to build their own delivery infrastructure, to counter price increases. The main barrier to entry would be to achieve nationwide coverage, but then they could still achieve good regional coverage, and outsource their requirements for remoter areas. New technology, such as online distribution exchanges which allowed vans and trucks to be filled both on outward and return journeys, made distribution alliances increasingly feasible.

7.185. Niche start-ups might also appear, particularly on a local or regional basis. Indeed 'man-and-van' operators were constantly appearing serving local areas. A good example of an existing regional player was Famac, which had cornered the market for mail-order delivery in Northern Ireland. There were hundreds of smaller, same-day couriers, and regional logistics operators that had been established for many years in various local regional/metropolitan markets, surviving by adjusting to the opportunities (B2B to B2C) in their regions. Regional couriers like [Details omitted. See note on page iv.] had shown interest in the B2C market ([§]), and some of these could form into networks offering UK coverage. Next-day courier NCN was formed around 13 years ago as a cooperative network, from around 100 regional same-day carriers. The National Courier Association was a similar cooperative network of around 100 carriers for same-day transit, and again around 13 years old. Many couriers were registered on web-site exchanges, for example Courier Exchange. Networks could also be grown by a franchise model (in the same way that many B2B parcel carriers have grown in the UK).

7.186. Parcelforce Worldwide had made losses continually for the past decade and was faced with the need for drastic restructuring. Given that Parcelforce Worldwide essentially had a high-cost, high-added-value network, it was necessary for the business to shed its highly unprofitable three-day-plus traffic. The alternative would have been total closure of the business with the loss of more than 10,000 jobs. However, Royal Mail still had a USO requirement to provide a three-day-plus service to the public, so Standard Parcels was moved from Parcelforce Worldwide to Royal Mail. Additionally contract business customers were no longer given the option to use the service.

### **SameDayNet Postvan Ltd**

7.187. SameDayNet Postvan Ltd (Postvan) said that it operated a national parcel company. It was concerned at the possible effects the merger might have on pricing, and it believed that Business Express and Reality might already be coordinating their activities in the market. It was aware of only one other company in the market, Parcelnet, which was small and possibly unable to compete with the merged company. Postvan believed that either Business Express or Reality should be divested to prevent a monopoly within the UK home parcel delivery market.

7.188. Postvan was of the view that the home parcel delivery market was separate from the traditional next-day UK parcels market, differing in pricing structure and service offerings. The traditional B2B home UK parcels market comprised Parcelforce, Business Post, Interlink and Amtrak. These companies did not compete with Business Express or Reality as they offered different services in their own markets. For example, Business Express and Reality offered economy 48-hour deliveries based on pricing the quantity dispatched per day, whereas Parcelforce and Business Post charged per parcel for any quantity of parcels dispatched.

## **Postal Services Regulator**

### **Postal Services Commission**

7.189. It was the Postal Services Commission's (Postcomm's) understanding that presently most parcel operators were involved in both B2B and B2C deliveries. To the extent that mail delivered to businesses was located in high-density delivery areas, certain operators might seek to limit the scale of their operations to those areas. However, this was not always the case and the majority of parcel operators were in addition likely to deliver to households. Indeed, mail delivered to households accounted for approximately 58 per cent of the market. Recent evidence suggested that in the parcels and express market<sup>1</sup> the core operators included Parcelforce, Securicor Omega Express and TNT. The market shares for each respectively were 20 per cent, 16 per cent and 13 per cent.

7.190. Where operators did not seek to establish their own delivery networks, Postcomm said that entry to the more costly delivery areas could nonetheless be further facilitated as liberalization of the postal service gained pace, including via access to the postal supply chain, which should lead to an increasing proportion of letter delivery becoming contestable by commercial operators. It was open to operators to negotiate access terms with Royal Mail, including for parcel deliveries, and failing this to apply to Postcomm for a determination.

## **Consumer groups**

### **Consumers' Association**

7.191. The Consumers' Association (CA) was of the view that whilst there had been significant developments in the home shopping market over the last few years, it was concerned that the accrual of market power that this merger signified could lead to considerable loss of benefit for a group of consumers that were least able to take advantage of the recent change in the high street and catalogue market. If no divestments were offered, it believed that the merger should be blocked. CA was not convinced that the closure of GUS home shopping would lead to a greater loss of consumer welfare as the break-up of assets would most likely lead to a more equitable redistribution of market share than this merger would deliver.

7.192. In its submission, CA commented on the analysis by the OFT. It believed that, for the purposes of this reference, the OFT analysis to date had been entirely correct. The position of the AMO market was distinct from the wider market. However, what was important was not so much that a sub-market either existed or was separate from the wider market. The more important issue was what the mechanisms were by which the firms in that market were constrained.

7.193. CA noted that the merged parties viewed each other as close competitors; indeed this appeared to be one of the key drivers for the deal. This raised the issue of price competition between catalogues and the competitive constraints that currently existed in the market, and were likely to exist post-merger.

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<sup>1</sup>Express refers to services for items that require speed and reliability in the collection and delivery of items. These are typically items such as document exchange services or document delivery services, which may require delivery for a specific time (ie next-day guaranteed delivery) and/or proof of delivery.

7.194. CA said that it saw little prospect of significant post-merger market entry in the AMO market. This aspect of the OFT analysis did rather point to the existence of a separate market for AMO. As a rule of thumb, one must always ask of the hypothetical monopolist which market it was that it sought to dominate. In this case the merger only made sense if scale could be achieved in a number of markets, the anchor market being the AMO market. This would tend to point to the AMO market remaining a separate market, albeit a declining one.

7.195. CA agreed with the OFT analysis that the market was extremely concentrated and had significant barriers to entry. On its own, this increase in concentration would normally be sufficient to lead CA to argue that the merger should be prohibited. However, it believed that this was a market with significant countervailing factors on which further focus was needed. CA said that its reading of the trends in the catalogue sector pointed to a number of conclusions about trends within the sector:

- (a) The market had seen significant growth in DMO catalogues.
- (b) Much of this growth had been in catalogues offered by existing AMO catalogue suppliers.
- (c) The market had seen significant shifts in consumer behaviour.
- (d) This shift had occurred both within the sector, through the growth of DMO catalogues and decline of AMO-only customers, and from outside the sector through the growth of non-traditional clothing retailers.
- (e) Overall agency numbers had been bolstered by a switch by a number of AMO customers to mixed AMO/DMO consumption.

7.196. CA said that, on balance, its concerns lay with the potential for market power to be abused among those least able to shop around. At the very least, this merger would limit the ability of the credit-reliant to switch catalogues. Its fear in this regard would be that the decline of AMO catalogue shopping had created an incentive to protect margins. In certain areas of the business this ability was severely constrained by the wider catalogue market and by the high street. However, in other areas of the AMO catalogue market the constraint appeared to be less strong (evidenced by differential catalogue/high street margins). It was precisely in these markets that the poorer, most credit-reliant consumers shopped. If the constraint in this segment of the market was less than in the area where the more mobile consumers shopped, then CA's fears would be threefold. First, the inability to maintain margins in one segment created an incentive to increase them in another—that is, the inability to raise prices in clothing created an incentive to increase them in brown/white goods. Second, the current market structure did not allow any individual firm to do this without suffering competitor response. The natural desire to raise margins (by pricing or limiting credit terms) among credit-reliant consumers had been held in check by factors within the AMO market as much as by factors outside. Indeed, the external factors (differential impact of the high street) had in many ways pulled the sector into building a case for a greater cross-subsidy from the credit-reliant. Third, any significant accretion of market power could remove the internal AMO market constraint and allow the differential impact of the external market (the high street) and incentivize the dominant firm to use the more captive credit-reliant sector as a means of boosting margin.

7.197. CA would be concerned if the merger led to a market position that allowed the merged company to launch effectively 'fighting brand' catalogues to target the smaller players. It would also be concerned if the enhanced market power led to a break-up of the big-book catalogues that allowed the cross-subsidy process to become more explicit. The break-up of the big-book catalogues might be a trend that was likely to feed through the market over the coming years. However, if it was done as a conscious attempt by a dominant player to maximize returns, rather than a response to competition within the market, then CA feared that the gains that might accrue to highly mobile switchers would come at the expense of significant losses to the less mobile credit-reliant consumers. If this were the case, CA could see many of the advantages offered to poorer consumers from the big-book catalogues whittled away. The possible detriment from displacing consumers from the AMO catalogue market to other credit markets would be significant.

7.198. CA said that the argument made regarding the departure from the market of GUS home shopping was a real one, but it was mindful of the OFT analysis in this regard. Whilst the departure of GUS home shopping might well be a possibility, CA was neither convinced that it was imminent nor that it was necessarily the only option available. The current deal with Littlewoods might be the optimal deal

as far as GUS was concerned, but it was unlikely to be the only one available to it over the coming years (assuming a long wind-down operation).

7.199. Given the three catalogues that comprised the GUS stable (*GU*, *Choice* and *Kays*) and their respective market shares (18, 6 and 18 per cent) it was difficult to see how anything other than almost a three-way split between the remaining three players in the market (Littlewoods, Otto and Redcats) could maintain the market in its current equilibrium. Such a break-up was also likely to be the result if indeed GUS ceased trading and sold its assets. CA could not, however, rule out other divestment routes. However, if such divestments were not offered in this merger, CA saw no solution other than recommending that it be blocked.

## Research organization

### Professor Elaine Kempson

7.200. Professor Elaine Kempson, Director and Professorial Research Fellow at the Personal Finance Research Centre, University of Bristol, gave us details about two large-scale national surveys which the PFRC had conducted in 1989 and 2002, which were respectively published by the Policy Studies Institute in 1992 and the DTI in 2002. She also referred to qualitative studies that she had undertaken with smaller sets of people over a number of years.

7.201. Professor Kempson indicated main trends in the availability of credit. Since 1989, access to credit facilities had increased markedly. However, the proportion of households actually owing money on consumer credit had not increased. Since 1989, the use of credit cards had increased whilst credit purchases from mail-order catalogues and hire purchase had declined. In 1989, 23 per cent of households were currently repaying money owed to a mail-order catalogue; this had declined to 17 per cent in 2002.

7.202. Over that time, there were indications that use of AMO catalogues had become even more concentrated in poorer households. The proportion of mail-order customers who were lone parents had doubled from 7 to 14 per cent. The proportion of working age people who were not in work had increased from 14 to 26 per cent, with a commensurate fall in the proportion who were in employment from 76 to 61 per cent.

7.203. Mail-order catalogue users now had access to a larger number of credit facilities, with the average number increasing from 3.21 in 1989 to 4.16 in 2002. There had been a shift in the types of credit on which mail-order catalogue users owed money. Compared with 1989, fewer mail-order users had a hire-purchase agreement but more owed money on a credit card.

7.204. In 1989, 40 per cent of households had a credit card compared with 52 per cent in 2002. However, the increase in card holding had not been spread evenly across all types of household. There had been an increase in the proportion of card holders who were pensioners and who owned their home outright. There had been a widening of access to credit cards, with a number of new entrant providers in the sub- and near-prime markets. On the whole, however, they seemed to have targeted people with impaired credit histories rather than people who lived on low incomes in the long term. Companies which offered credit on less favourable terms than mail-order companies were sale and buy-back and rental purchase companies.

7.205. Professor Kempson provided some statistics on people who owed money on either a GUS or a Littlewoods catalogue. 60 per cent of these customers had gross annual incomes of less than £15,000, compared with 49 per cent of all households and 41 per cent of credit-card users. 34 per cent of customers of Littlewoods and GUS home shopping were of working age but not in employment. 33 per cent were social tenants. 24 per cent were currently in arrears with one or more of their household commitments. Mail order remained the first choice of credit for many low-income households, particularly those with children who wanted designer clothes and footwear. Most people interviewed used mail order through choice, although many had constrained access to high street credit, particularly in-store credit.

7.206. Mail order was attractive because it was a good way of spreading costs, and was convenient for people who could not get to shopping centres. Mail order was also accessible to people who might otherwise find it difficult to get access to lower-cost credit, and attractive to Muslims because the interest-free provisions complied with Islamic teaching.

7.207. Some people chose not to use mail-order catalogues because of the cost of the goods and the fear of overcommitment.

7.208. Professor Kempson concluded that while there had been a widening of access to credit in recent years, low-income households had not benefited from it. So although use of mail order as a source of credit had declined, it seemed to have become more concentrated among low-income households. It was undoubtedly a source of credit that was greatly valued by people on low incomes, especially by families with children, and pensioners. Any reduction in choice could, potentially, be to the detriment of the six in ten customers of Littlewoods and GUS home shopping who had gross annual incomes of less than £15,000.

## **Local investment agency**

### **Manchester Investment & Development Agency Service**

7.209. Manchester Investment & Development Agency Service (MIDAS) is the inward investment agency for the Manchester conurbation, but it works also with the indigenous companies to assist where possible with their retention within its area.

7.210. It said that the home shopping business was a declining sector, given changes in shopping habits, including the growth of Internet shopping. Therefore, whilst GUS had been a long-standing and major employer in the area—and MIDAS had valued its presence—the level of employment had decreased over the past few years and it had been concerned about the long-term future of the home shopping business, as there had been little sign of significant investment compared with other parts of GUS, for example Argos and Homebase.

7.211. Given this background, its concern was that the maximum level of jobs was retained in the Manchester area, within a viable business. MIDAS was not aware that there were any other bidders for the GUS home shopping business and therefore ownership by March was the best option for long-term survival. Certainly it was evident that the acquisition of Littlewoods Home Shopping resulted in investment in Liverpool (a new head office), and March had indicated to MIDAS that it would pursue the same strategy in this case—retention of separate brands, a separate head office—with GUS home shopping being run as a distinct business unit. This, in MIDAS's view, would help to maximize continued operations and employment in the area.

7.212. MIDAS had no doubt that some economies would result. The question was, would this be less than it would have been if GUS had retained the business, and its considered view, based on its contact with the business pre- and post-acquisition, was that new ownership brought vitality to the business that was lacking previously. A run-down or closed-down business would not provide effective competition in the marketplace. Therefore, subject to guarantees concerning the transparent separation of the two business functions, MIDAS supported the merger.

### **Northwest Development Agency**

7.213. The Northwest Development Agency (NWDA) said that it was responsible for leading the economic development of the North-West region. It wished to register its concern in favour of the merger, which could have a dramatic effect on employment in the North-West. The NWDA understood that if the merger had not taken place, then GUS would have been forced to close its home shopping and delivery businesses with the loss of some 19,000 jobs nationwide—a significant number of which would be within the North-West. Moreover, given the nature of many of these jobs, they would not be easily transferable outside the current travel-to-work areas where they were located—a factor which the NWDA believed would diminish the future employment prospects of any of those who were to be made

redundant, thus having a disproportionately concentrated effect on certain areas such as Halton and Oldham. This would be a serious blow to the region's economy, and would be avoided if the merger were allowed to stand.

## **Local authorities**

### **Liverpool City Council**

7.214. Liverpool City Council said that Littlewoods Home Shopping had been an institution, not just in Liverpool but throughout the North-West, for over 70 years and it continued to be a principal investor within the city. The recent decision to invest over £20 million in the Speke Estuary Commerce Park was further evidence of Littlewoods' long-term commitment to the region.

7.215. The City Council believed that the acquisition of GUS Home Shopping created an exciting opportunity to reposition the home shopping industry to compete in an ever more difficult retail environment, and to meet the changing requirements of the electronic era. AMO was a uniquely British institution, but it had been in decline for many years. This decline had been accelerated rapidly over recent years. Littlewoods had a proven long-term commitment to the sector. Applying the same techniques that it had already used in its own business, the combined company would be better placed to compete more effectively with the rest of the retail sector, and be able to sustain the availability of the AMO catalogue model.

7.216. The merger would significantly enhance the home shopping industry, not just consolidating the position of Littlewoods in this sector, but providing the platform for further growth of both the North-West and the UK as a whole in the global market.

7.217. The City Council said that it had urged the OFT to consider the merger in terms of the whole UK non-food market, in which the combined operation would have only a 3 per cent share.

### **Manchester City Council**

7.218. Manchester City Council said that in its view the merger would strengthen the competitive position of businesses based in Manchester and elsewhere in the North-West. GUS was a major employer in the Manchester area and had been a very significant generator of employment within the city itself. The new owner, March, had reassured the City Council that it had a strong commitment to maintaining and expanding activity in Manchester and had expressed an intent to invest in the industry in order to support these objectives. The City Council was clearly very anxious to ensure that the employment base within Manchester was protected and, if possible, enhanced, and it looked forward to working with the new owner of GUS home shopping in order to ensure that these objectives were realized.

### **Wigan Council**

7.219. Wigan Council was fully supportive of the merger. It felt that the merger would provide greater financial stability to the companies involved in their future trading activities, and would assist in guaranteeing the substantial employment that GUS currently had in the borough.

## **Home delivery customers**

### **Direct Wines Limited**

7.220. Direct Wines Limited (Direct Wines) told us that it was the UK's largest home delivery wine company. Its sales in the year to June 2003 were in excess of £200 million, made up of 4.2 million cases

of wine delivered almost exclusively to consumers. Direct Wines did not have its own delivery network. The majority of its deliveries were handled by Reality, and the bulk of the remainder were handled by ANC, in addition to Homeserve and Concord handling some deliveries in the South-East.

7.221. Direct Wines was concerned that, despite the recent lack of direct competition between Reality and Business Express, the merger of these two businesses would potentially significantly reduce competition in the B2C delivery market.

7.222. Direct Wines said that following Parcelforce's exit from the market, Business Express and Reality would effectively have more than 50 per cent of the B2C market, and would have a near monopoly of B2C parcels greater than 10 kg with national coverage. It was very significant that Reality did offer national coverage. Regional delivery services did not offer a satisfactory solution, due to the sheer complexity of dealing with a large number of small carriers.

7.223. Business Express and Reality had competed strongly in the past and Direct Wines had used both in the last five years. More recently, Business Express had been unwilling to carry wine. However, the combination of Business Express and Reality would remove the possibility of an alternative to Reality, should Business Express change its attitude to wine delivery in the future.

7.224. Direct Wines was concerned at the possibility that prices were likely to increase. For over 12 years, Direct Wines had used Reality as its principal carrier, at rates which had been consistent, in that they had risen to take account of increases in underlying costs, offset by reductions due to efficiency gains as volumes increased from an initial 0.4 million cases a year to 4.2 million cases a year. The probability was that price increases would be greater if the merger were allowed to proceed. Since the acquisition of Reality by Business Express, Direct Wines faced proposed increases in rates substantially in excess of underlying cost increases and greater than could be justified by fully costing the service. Delivery to the consumer formed a significant part of the cost of home delivery wine and increases in delivery rates would inevitably make home delivery wine more expensive and less competitive compared with the major supermarkets.

7.225. Direct Wines said that there were only five significant players in the B2C market with national coverage capable of handling volumes relevant to Direct Wines. These were Reality, Business Express, ANC, Securicor Omega Express and Parcelnet. However, Parcelnet's operation, which consisted of couriers using private cars, was not practicable for wine delivery. Therefore the combination of Reality and Business Express represented a serious reduction in potential competition.

7.226. Furthermore, the barriers to entry were significant, due to the very high cost of creating the infrastructure, and it was unlikely that there would be new entrants in the foreseeable future. It was very unlikely that B2B carriers would want to enter the market for budget B2C deliveries to any significant extent, as the service offer was substantially different, being focused exclusively on next-day delivery, and B2B rates were inevitably higher than B2C rates, except in London. B2B carriers had no infrastructure for high volumes of B2C parcels, and there was no evidence that any were prepared to make the investment.

7.227. The structure of the carriers was also a significant issue for Direct Wines. In its experience, the day-to-day management of a uniform, national, quality delivery service and the interface with Direct Wines' customers was less easy to achieve with franchise structures. Business Express and Reality had been before the merger the two principal wholly-owned carrier businesses.

7.228. With regard to efficiencies, Direct Wines believed there might be considerable efficiencies from the combination of Business Express and Reality at depot and driver round level. The benefits of these efficiencies should be available to the consumer and not lost as a result of the reduction in competition.

7.229. Direct Wines concluded that [*Details omitted. See note on page iv.*]. In the event of a catastrophic failure at Reality, the possibility of using Business Express would be removed by the merger.

7.230. Direct Wines submitted that the merger would have an effect on the competitive position of the home delivery wine business. If the profitability of home delivery wine business were eroded by above-inflation increases in delivery costs, that would mean that sales of non-supermarket home delivery

wines would reduce as some marginal sales activities were eliminated. The result would be that the hold of the large supermarkets on the wine sector would be increased and competition in selling wine would be reduced.

7.231. Direct Wines concluded that the merger of Business Express and Reality was not in the public interest because it was not in the long-term best interests of the individual consumer. The merger would lead to increased costs and/or a further concentration of the retail wine market in the hands of the large supermarkets. This would lead over time to increased prices and reduced choice. In addition, service standards might fall.

## **The Wine and Spirit Association**

7.232. The Wine and Spirit Association said it was concerned that the merger would significantly reduce competition in the delivery to the home market for all products, but in particular, wine. There was already limited competition as many carriers did not have appropriate infrastructures for product with fragile characteristics; this was particularly true in the less expensive, non-time-sensitive end of the marketplace, where traditionally Business Express and Reality had been the only two players.

7.233. Whilst Business Express had withdrawn from wine delivery in recent times, the Association believed that was due to the lower prices offered by its main competitor, Reality. The Association was concerned that in the absence of a competitor there would be no strong reason for Reality to continue to offer good-value pricing. Several members of the Association had informed it that its fears were not unfounded as their latest rate reviews saw increases substantially higher than the rate of inflation and no constraints on increases in the longer term. These cost increases would inevitably have to be passed on to the consumer in terms of higher prices or delivery charges.

7.234. The Association considered that there would be an effective monopoly at the lower end of the home delivery market with no realistic possibility of a new entrant until prices had risen sharply, or even the prospect of the total removal of service, which would then only be provided by specialist carriers at more than double the current delivery cost. These costs would, again, have to be passed to the consumer, and might affect the overall viability of the provision of wines by distant selling, particularly at the lower end of the market.

7.235. If the merger were to be allowed to stand, the Association considered that the only effective remedy to protect consumers' interests would be the divestment of one of the delivery networks of the combined entity. However, it believed that the most effective protection would be achieved by divestment of all the acquired businesses.

## **Members of Parliament**

### **Ms Anne Begg MP**

7.236. Anne Begg, MP for Aberdeen South, said that there was a branch of White Arrow Express in her constituency, and therefore she had an interest in the acquisition of GUS home shopping by March. She believed that the public interest would be served by this merger in relation to improved consumer services and employment. Indeed, without the merger, GUS home shopping, where sales had declined by 20 per cent in 2003, would face closure with the loss of 19,000 jobs throughout the UK. Ms Begg was extremely concerned by the employment implications of failure to allow the merger to go ahead. The implication of major job losses were profound, both in employment and the knock-on effects for the local community.

### **Mr Frank Cook MP**

7.237. Frank Cook, MP for Stockton North, said that 91 of his constituents were employed by GUS home shopping, and the continued existence of their jobs now depended on the outcome of this inquiry.

7.238. Home shopping faced intensifying competition, not least from Internet shopping and from high street retailers launching their own catalogues. March and GUS home shopping hoped to merge in order to become as efficient as possible, and to continue to compete effectively and protect the thousands of jobs that were at stake.

7.239. Mr Cook said he was dismayed that the OFT had decided to make this referral, and he would be very concerned if the CC were to block the merger. To deliberately render the business less efficient in the medium to long term—which was what such a decision would effectively mean—could have a highly deleterious effect on the communities which depended on the survival of some 19,000 jobs nationwide within home shopping. Unless there was some genuinely compelling reason, of which Mr Cook was currently unaware, for blocking this merger, he had no hesitation in supporting USDAW in calling for it to be approved.

### **Mr David Crausby MP**

7.240. David Crausby, MP for Bolton North East, said that he was deeply concerned at the potential loss of valuable jobs if the merger between GUS home shopping and March was not allowed to proceed.

7.241. The merger would offer improved consumer services and much-needed employment. GUS home shopping had seen sales decline by 20 per cent in 2003, and without the merger, the company had an uncertain future and could face closure with the loss of 19,000 jobs, many of which were based in his constituency.

7.242. He understood that one of the main issues raised by the OFT concerned the merger of the two parcel delivery businesses, and a concern that the merger would lead to rising costs. As with the main AMO shopping operations, he believed that Littlewoods and GUS should be given the opportunity to create a more efficient, viable parcels business that would ensure the provision, in the long term, of a truly competitive service to their customers.

7.243. Mr Crausby said he realized that the CC must balance the public interest against its duty to ensure fair and effective competition.

### **Ms Louise Ellman MP and Mr Tony Lloyd MP**

7.244. Louise Ellman MP and Tony Lloyd MP wrote on behalf of a group of 30 MPs (see Appendix 7.5). Seven of the group—Colin Challen MP, Janet Dean MP, Michael Foster MP, Dr Brian Iddon MP, David Stewart MP (see also paragraph 7.266), Derek Twigg (see also paragraph 7.267) and Robert Wareing MP—also wrote separately along the same lines. The MPs said that the public interest would be served by this merger in relation to improved consumer services and employment. Without the merger, GUS home shopping, where sales had declined by 20 per cent in 2003, would face closure with the loss of 19,000 jobs, many in their constituencies. The MPs anticipated that the merger would improve competition with high street retailers, with cost savings from the merger passed on in lower prices. They were extremely concerned by the employment implications of failure to allow the merger to go ahead. The implications of major job losses in some of the poorest constituencies were profound both in terms of unemployment and the knock-on effects for local communities.

7.245. The MPs commented that in referring the merger to the CC they understood that the OFT expressed the view that closure of the GUS business might be better for competition than to merge with Littlewoods. They believed this failed to recognize that home shopping customers were more likely to be lost to high street retailers such as Matalan and Primark than to other catalogue retailers. Closure of the GUS home shopping business would give no appreciable benefit either to consumers or other catalogue retailers.

7.246. They also understood that one of the main issues raised by the OFT was the merger of the two parcel delivery businesses and a concern that the merger would lead to rising costs. As with the main AMO shopping operations, they believed that Littlewoods and GUS should be given the opportunity to create a more efficient, viable parcels business that would ensure they could provide in the long term a truly competitive service to their customers.

7.247. It would be disproportionate to allow any concerns over such a small part of these two businesses to jeopardize the future of the GUS home shopping business with all its consequences. Their constituents would find it very difficult to understand a decision not to approve the merger on grounds related to the parcels business alone, which was only a peripheral part of the two home shopping businesses.

7.248. The MPs believed that the public interest case for approving the merger was compelling, and they urged that the merger should be allowed to proceed.

### **Mr Lindsay Hoyle MP**

7.249. Lindsay Hoyle, MP for Chorley, said that he had received representation from a number of his constituents regarding the sale of GUS home shopping. If the merger with March was not allowed to go ahead, there would be little future for GUS home shopping, and the 19,000 people employed within the industry would face job losses and cut-backs. Given the need for a strong home shopping business in the UK, and in the interests of those employed within it, the merger should be allowed to proceed. Mr Hoyle added that the merger had the support of USDAW and other trade unions within GUS home shopping.

### **Rt Hon Alun Michael MP**

7.250. Alun Michael, MP for Cardiff South and Penarth, said it had been represented to him that the public interest would be served by this merger in relation to improved consumer services and employment. He understood that without the merger, GUS home shopping, where sales had declined by 20 per cent in 2003, would face closure with the loss of 19,000 jobs, of which 147 were in his constituency. He anticipated that the merger would improve competition with high street retailers, with cost savings from the merger passed on in lower prices. Mr Michael was extremely concerned by the employment implications of failure to allow the merger to go ahead. The implications of major job losses in some of the poorest constituencies were profound, both in terms of unemployment and the knock-on effects for local communities.

7.251. Mr Michael commented that in referring the merger to the CC he understood that the OFT expressed the view that closure of the GUS business might be better for competition than to merge with Littlewoods. This appeared not to recognize that home shopping customers were more likely to be lost to high street retailers such as Matalan and Primark than to other catalogue retailers. Closure of the GUS home shopping business would give no appreciable benefit either to consumers or other catalogue retailers.

7.252. He also understood that one of the main issues raised by the OFT was the merger of the two parcel delivery businesses and a concern that the merger would lead to rising costs. As with the main AMO shopping operations, he believed that Littlewoods and GUS should be given the opportunity to create a more efficient, viable parcels business that would ensure they could provide in the long term a truly competitive service to their customers.

7.253. It would be viewed as disproportionate to allow any concerns over such a small part of these two businesses to jeopardize the future of the GUS home shopping business with all its consequences. His constituents would find it very difficult to understand a decision not to approve the merger on grounds related to the parcels business alone, which was only a peripheral part of the two home shopping businesses.

7.254. Mr Michael said he realized that the CC must balance the public interest against its duty to ensure fair and effective competition. He believed that the public interest case for approving the merger was compelling.

## **Mr Terry Rooney MP**

7.255. Terry Rooney, MP for Bradford North, stressed the effect that the merger might have on people who were excluded from the wider credit market, usually the more disadvantaged members of society. He was concerned that the merger might lead to a streamlining in the credit system, resulting in a possible restriction in credit terms that might tempt some catalogue shoppers into the unregulated credit market which, in many cases, had criminal and anti-social elements attached to it. He believed that a major part of what might be a sizeable 'at risk' group was likely to be dependent on the credit terms offered by reputable catalogue shopping firms. Mr Rooney added that the potential effect on the policies to reduce social exclusion being pursued by the Government could be extremely serious.

## **Ms Christine Russell MP**

7.256. Christine Russell, MP for the City of Chester, said that the public interest would be served by the merger in relation to improved consumer services and employment. Without the merger, GUS home shopping, where sales had declined by 20 per cent in 2003, would face closure with the loss of 19,000 jobs, many in her constituency. She anticipated that the merger would improve competition with high street retailers, with cost savings from the merger passed on in lower prices. Ms Russell was extremely concerned by the employment implications of failure to allow the merger to go ahead. The implications of major job losses in some of the poorest constituencies were profound, both in terms of unemployment and the knock-on effects for local communities.

7.257. Ms Russell commented that in referring the merger to the CC she understood that the OFT expressed the view that closure of the GUS business might be better for competition than to merge with Littlewoods. She believed this failed to recognize that home shopping customers were more likely to be lost to high street retailers such as Matalan and Primark than to other catalogue retailers. Closure of the GUS home shopping business would give no appreciable benefit either to consumers or other catalogue retailers.

7.258. She also understood that one of the main issues raised by the OFT was the merger of the two parcel delivery businesses and a concern that the merger would lead to rising costs. As with the main AMO shopping operations, she believed that Littlewoods and GUS should be given the opportunity to create a more efficient, viable parcels business that would ensure they could provide, in the long term, a truly competitive service to their customers.

7.259. It would be disproportionate to allow any concerns over such a small part of these two businesses to jeopardize the future of the GUS home shopping business with all its consequences. Her constituents would find it very difficult to understand a decision not to approve the merger on grounds related to the parcels business alone, which was only a peripheral part of the two home shopping businesses.

7.260. Ms Russell said she realized that the CC must balance the public interest against its duty to ensure fair and effective competition. She believed that the public interest case for approving the merger was compelling and she urged that the merger should be allowed to go ahead.

## **Ms Helen Southworth MP**

7.261. Helen Southworth, MP for Warrington South, said that the public interest would be served by this merger in relation to improved consumer services and employment. Without the merger, GUS home shopping, where sales had declined by 20 per cent in 2003, would face closure with the loss of 19,000 jobs, many in her constituency. She anticipated that the merger would improve competition with high street retailers, with cost savings from the merger passed on in lower prices. Ms Southworth was extremely concerned by the employment implications of failure to allow the merger to go ahead. The implications of major job losses in some of the poorest constituencies were profound, both in terms of unemployment and the knock-on effects for local communities.

7.262. Ms Southworth commented that in referring the merger to the CC, she understood that the OFT expressed the view that closure of the GUS business might be better for competition than to merge

with Littlewoods. She believed this failed to recognize that home shopping customers were more likely to be lost to high street retailers such as Matalan and Primark than to other catalogue retailers. Closure of the GUS home shopping business would give no appreciable benefit either to consumers or other catalogue retailers.

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7.265. Ms Southworth said she realized that the CC must balance the public interest against its duty to ensure fair and effective competition. She believed that the public interest case for approving the merger was compelling and she urged that the merger should be allowed to go ahead.

### **Mr David Stewart MP**

7.266. David Stewart, MP for Inverness East, Nairn & Lochaber, said that following representations from USDAW he had concerns that, in the longer term, Highland jobs in Business Express could be threatened should the merger not be allowed to proceed. The Business Express depot in Inverness employed about five people dealing mainly with Littlewoods Home Shopping business. However, the depot was serviced by a number of van owner/drivers who got work through this operation. Although the employment situation in Inverness was not as difficult as some of the other Littlewoods sites, Mr Stewart was concerned about the threat to workers and their families' jobs, and about the threat to other businesses that relied on these operations.

### **Mr Derek Twigg MP**

7.267. Derek Twigg, MP for Halton, said that he had been approached by a significant number of his constituents regarding the merger. He believed that the public interest would be served by this merger in relation to improved consumer services and employment, and he was extremely concerned by the employment implications of failure to allow it to go ahead. Without the merger, GUS home shopping would face closure with the loss of 19,000 jobs within the industry, many of which were in his constituency.

## **Individuals**

### **Investment banker**

7.268. An investment banker, commenting on the statement of issues, said that the trends of the last few years suggested that AMO was a form of retailing that was not only open to competition from players in the more broadly defined retail market, but also appeared to be one where the effect of competition appeared to be threatening its survival. A merger between the GUS and Littlewoods AMO businesses would help to create a significant and viable competitor, whilst without a transaction it was difficult to see the long-run future for at least one of these businesses.

7.269. Analysts following the sector had written at length about the progressive demise of AMO. For GUS in particular, as a quoted company, this had been a problematic issue. From a profit base of just below £150 million in the year to March 1996, the GUS home shopping operations had become only marginally profitable by March 2000. The key factor behind this decline was the consistent decline in

sales in AMO. Whilst GUS was able to stabilize profits at relatively low levels through cost cutting, revenues had continued to decline.

7.270. In the equity market the causes of this long-run decline had been analysed for many years. The view generally held was that whereas home shopping, and AMO home shopping in particular, were historically seen as a distinctive retail channel, the barriers that enabled this sector to avoid competition from the rest of the high street had been progressively eliminated. The main agency players now faced a very different competitive landscape, and arguably one in which they were ill-equipped to compete effectively.

7.271. The development in retailing that had probably most damaged the AMO sector had been the growth of 'value' clothing retailers such as Matalan, Primark and Peacocks, on the one hand, and the clothing retail activities of the supermarket operators, particularly Asda and to a lesser extent Tesco, on the other. All of these operators had achieved strong revenue growth in recent years and collectively had shifted price points in the UK clothing market sharply downwards. Clothing had traditionally been the most important product market for the AMO players and the downward shift in pricing from the store-based retailers had had a severe effect on demand in the sector. The AMO operators had found it extremely difficult to match the pricing offered by these competitors as the costs of home delivery, catalogue production, agents' commission, customer recruitment and bad debts were difficult to recover when entry-level price points were as low as they now were. From the customers' perspective, the sharp downward shift in clothing prices in the value segment had made it less attractive to buy these products from the AMO players. At the same time, there had been substantial growth in the availability of credit, including to the near-prime segment of the market which historically may have had limited alternatives to AMO home shopping as a source of credit. This had meant that the availability of credit, which had historically been one of the AMO sector's key selling points, was no longer so important to customers' purchasing decisions.

7.272. The investment banker said that the low-cost store-based retailers had used their scale economies to reduce further the prices offered to consumers. This created a 'virtuous circle' in which market share gains translated into improved store productivity and purchasing efficiencies, with the gains in profitability reinvested into lower prices, which in turn generate further market share gains. For the AMO sector the reverse had been happening. The loss of market share across the industry in recent years had generated cost and purchasing scale disadvantages, making it progressively harder to match the values and prices offered by the store-based competition. The cost disadvantages of the AMO players were therefore worsened over time as they lost market share to store-based operators.

7.273. For a number of years the equity market appeared to have valued the GUS AMO business on a wind-down basis—that is, equity analysts had broadly accepted that the business was worth no more than the cash that could be generated by closing the business down and collecting in the receivables after meeting the closure costs including a possibly increased level of bad debts that would be incurred.

7.274. The investment banker said that the fact that GUS eventually decided to sell this business for a value that was broadly equivalent to the receivables book was in itself a powerful statement about the prospects for AMO. Despite having a clear market leadership position, GUS was prepared to sell the business for a price broadly equivalent to its wind-down value, suggesting that management did not see a plausible cash-positive scenario beyond this level. This implied that management saw little prospect of reviving the business and that it believed the deal offered a more straightforward way of realizing the cash than would otherwise have been generated from a wind-down. This appeared to be clear evidence that AMO was not a distinctive channel but instead a form of retailing that was being competed away by more competitively advantaged rivals. In this light, viewing AMO as a distinct channel where consolidation was regarded as anti-competitive did not appear to be a sensible conclusion.

## **Employees of GUS home shopping**

7.275. We received signed petitions on behalf of eight employees of GUS home shopping which they sent to their MPs urging them to support the merger.

## **A further employee of GUS home shopping**

7.276. An employee of GUS home shopping wrote to the Secretary of State in support of the merger and asked that the letter be passed on to the CC.

P J FREEMAN (*Chairman*)

A GREGORY

B LYONS

R TURGOOSE

A M YOUNG

R FOSTER (*Chief Executive and Secretary*)

23 December 2003