# 5 The views of the main parties

## Views of Gillette

### *Background to the transaction*

5.1. Gillette told us that it saw the press announcement of the sale by Stora of the CP Division in June 1989. Gillette said that its corporate strategy was that whenever a company which was engaged in any of its core businesses became available it tried to acquire it if possible, and Wilkinson Sword was no exception. It was therefore interested in the possibility of acquiring the Wilkinson Sword wet-shaving business.

5.2. Gillette was not interested in the matches and lighters businesses but, in view of Stora's insistence on selling the whole CP Division as a package, came to the conclusion that if it was to acquire as much of the Wilkinson Sword business as it could it would have to find someone interested in the other businesses.

5.3. Although it would have preferred to take the whole world-wide Wilkinson Sword shaving products business, Gillette recognised that any acquisition of the Wilkinson Sword business in the EC was liable to be a subject of concern on the part of the European Commission and also of the national competition authorities, including those in the United Kingdom and West Germany. Nevertheless, Gillette believed that the Wilkinson Sword shaving products business in markets outside the EC was capable of substantial expansion, was potentially valuable to it and would fit in well with its own shaving products business. This was particularly so because of Gillette's long-established corporate policy of not licensing its principal existing trade marks (notably the Gillette name) to third parties which were not wholly-owned subsidiaries. In particular, an acquisition of the Wilkinson Sword business outside the EC would allow Gillette to:

*(a)* acquire trade mark rights which had a good potential for Gillette in certain markets outside the EC (eg India, Pakistan, China, Egypt, Kenya, Morocco and the Soviet Union, as well as in Eastern Europe);

*(b)* increase its critical mass in certain non-EC markets (eg Australia, New Zealand, Japan and some other Far East markets) where it would acquire marketing and distribution facilities (as well as trade mark rights); and

*(c)* acquire blade manufacturing facilities in the Manaus region of Brazil (allowing it to rationalise its manufacturing facilities there and its Latin American distribution activities) and in Zimbabwe.

5.4. Gillette said that, driven by the need to protect its position in the world shaving market, its key objectives in relation to the proposed sale by Stora were as given in the paper to its Board in August 1989:

- to acquire and retain as high a proportion of the shaving business as is permissible by the relevant anti-trust authorities;

- to acquire such shaving interests without prior notification and approval from the anti-trust authorities; and

- not to own the match or disposable lighters business for anything other than a temporary period and only with guaranteed and contracted disposals.

It appointed Lazards to act on its behalf. Lazards then approached MSI which was conducting the sale on behalf of Stora.

### *Involvement in the consortium*

5.5. Gillette told us that, in conjunction with its financial and legal advisers, it set about considering how, without infringing competition regulations, it could be involved in a tender offer acceptable to Stora which would ensure that it acquired the Wilkinson Sword business in the markets where there would not be competition law objections. Gillette was aware that the senior management of the CP Division were interested in the possibility of a leveraged management buy-out, and with the help of its merchant bankers, Lazards, it learnt that Procuritas (a Swedish company specialising in financing management buy-outs) and a number of other Scandinavian investors were interested in participating. Lazards brought the parties together and discussions commenced about the possibility of a leveraged management buy-out of the CP Division. Lazards was also instrumental in arranging the financing and brought in Morgan. In discussing proposals, Gillette and the other parties were anxious to ensure that any arrangements should prove acceptable to the various competition authorities which would have jurisdiction to investigate them.

5.6. Gillette stated that there was no possibility of it going ahead with a simple purchase of the non-EC wet-shaving business because the Scandinavian partners did not have sufficient finance themselves to purchase the whole CP Division from Stora which was insisting on a single sale of the whole business preferably to a trade buyer. Gillette said it would have been happy to buy the non-EC wet-shaving businesses and to have no further involvement had this been an option but Stora had made it clear that it would only sell the CP Division as a whole.

5.7. Gillette said that the plan which developed involved the establishment of a buy-out vehicle incorporated under Netherlands law (ie Eemland which subsequently changed its name to Swedish Match NV) which would put in an offer for the whole of the Stora CP Division. Agreements between the parties would provide for the sale of the non-EC shaving products businesses by Swedish Match NV to Gillette and the phased sale by Swedish Match NV of the matches and lighters businesses over a two-year period to third parties, following which Swedish Match NV would remain as the owner of the Wilkinson Sword shaving products business within the EC. Commitments in principle were obtained from investors and banking institutions prepared to back the buy-out plan and to provide equity and loan finance.

5.8. Gillette said that it was the joint architect of the buy-out vehicle and was the prime mover in the establishment of Swedish Match NV as a viable vehicle capable of successfully bidding for the Stora CP Division. Also, its involvement may well have given enhanced credibility to the management in their opinions as to the future profitability of Wilkinson Sword.

5.9. In answer to the question as to why it required a shareholding in Swedish Match NV, Gillette repeated that its objective was to acquire as much of the Wilkinson Sword wet-shaving business world-wide as it could and that to do that it was advised by Lazards that the best way was to participate in a leveraged buy-out. It was further advised that it would have to be a fairly substantial investor to make the deal work and that it should participate both in the equity and in the loan finance.

5.10. According to Gillette, it had to play a prominent part in the consortium because Stora wanted to have a major trade buyer involved. But in Gillette's view the deal might have gone ahead if it had declined to participate and it thought that Procuritas might have been able to find some other trade buyer who was interested in the shaving part; there could have been other combinations.

## *Gillette's view of the transaction*

5.11. Gillette told us that it had never previously had any experience of a leveraged buy-out, as normally it made its acquisitions outright. The whole financing operation as far as Gillette was concerned was left to Lazards to deal with.

5.12. Gillette told us that it had not previously made any significant investments in, or provided significant loans to, any non-associated company and there was certainly no group policy with regard to arrangements of this type (which would be considered on a case-by-case basis).

5.13. Gillette said that Wilkinson Sword's non-EC/US business was making only a small profit and would not have been as attractive a proposition to a prospective purchaser outside the wet-shaving business as it was to Gillette. Because of Gillette's infrastructure around the world it felt it could realise the potential of the valuable Wilkinson Sword name in many countries where Wilkinson Sword had not done so, Gillette considered therefore that it was able to put a higher value than others on the non-EC/US assets.

5.14. The desire to achieve its objectives as outlined above, together with the fact that it would receive commercial rates of interest, persuaded Gillette to participate in the mezzanine debt as well as the equity financing of Swedish Match NV provided the necessary restrictions were in place to satisfy the requirements of competition law.

5.15. Gillette told us that by early December 1989 the details of the financing had still to be finalised. Difficult negotiations were continuing against the background of time constraints being imposed by Stora. In addition, leveraged buy-outs were then being viewed with increased caution by banking institutions and, as it was the year end, many potential lenders had already closed their books. Thus, in order to keep the deal going, Gillette had to participate in the debt financing of Swedish Match NV to a greater extent than it would have liked.

5.16. Gillette further explained that it was in order to save the transaction that it agreed at a late hour to cede 2 per cent of the equity to ICG which was threatening to pull out of the transaction on the grounds of unacceptable returns on its proposed investment in the mezzanine finance. This had the effect of reducing Gillette's share of the total equity in Swedish Match NV from just under 24 per cent to just under 22 per cent. Also it agreed to pay Stora up to US $11 million over the period up to 1997 to reflect the fact that the loan note issued to Stora to cover the shortfall of SEK 300 million (US $48 million) in institutional funding carried no interest. Stora had accepted the subordinated interest-free loan because it preferred this arrangement to a reduction in the selling price. Gillette said that its Board felt able to offer compensation to Stora in lieu of interest on the loan note after a three-year period because those concerned were confident that it would be paid off within that period and because the high rate of interest on Gillette's mezzanine loan would cover any such payments if they did become due.

5.17. Gillette told us that the new company was set up in the Netherlands for tax reasons. Since Netherlands company law does not permit non-voting shares, Gillette's contribution to the equity funding had to be in the form of convertible loan stock. Tax reasons were also the explanation for the funds for Gillette's mezzanine loan being sourced from its German subsidiaries although made available through Gillette's United Kingdom subsidiary, Lustrasilk.

5.18. Gillette confirmed that the price it paid Swedish Match NV (then Eemland) for the non-EC businesses of Wilkinson Sword was somewhat higher than originally contemplated. It decided to add to the value it originally placed on the intellectual property to compensate in part for the reduced amount the finance houses were prepared to subscribe. On the other hand, Gillette said, the amount it put into the mezzanine finance was rather less than expected so that overall its investment was still within its Board-approved limit of US $154 million. Whilst Gillette was the beneficial owner of the non-EC businesses, Wilkinson Sword was still running many of them on Gillette's behalf pending completion of transfer arrangements.

5.19. Gillette gave us the following account of the events of 20 and 21 December 1989 when the various agreements giving effect to the transaction were signed in a manner which had been pre-planned. It said that representatives of the parties which were to be equityholders (ie holders of ordinary shares or equity loan stock) in Swedish Match NV and/or creditors of Swedish Match NV, together with

representatives of Stora, gathered together in London on 20 December to agree the final form of all the various agreements. During the course of 20 December, sums representing the shareholder and creditor monies were transferred to MGTC by all the members of the bidding group including Gillette. Gillette also transferred sums representing amounts payable for the non-EC intellectual property and assets. MGTC was to hold the monies until the agreements were signed. By late that evening all the agreements had been considered and their final form agreed. The parties then signed most of the agreements, including the Equityholders' Agreement, the Voting and Management Agreement (pursuant to which officers and directors of Swedish Match NV were appointed), the Purchase Agreement with Stora (as part of which, the first closing took place on 20 December) and the non-EC shaving assets transfer agreement. In connection with these arrangements, a shareholders' general meeting of Eemland was held. Gillette said that the parties reassembled on 21 December when the Senior and Mezzanine Loan Agreements were signed. Also on 21 December, MGTC released the various sums to Swedish Match NV and paid to Stora the amounts due under the first closing. The IP Agreement was signed on 2 January 1990, pursuant to an undertaking signed on behalf of Swedish Match on 20 December 1989. The Loan Stock Instruments were issued later as required by the Voting and Management Agreement (on 30 March 1990). Further events took place during 1990, including the second closing (on 30 March) and third closing (on 19 October).

5.20. Gillette said that the term `equityholder' (as opposed to shareholder) was used because of the two separate types of equity capital in Swedish Match NV, ie ordinary shares and equity loan stock. It stressed that the ordinary shares were the only equity which carried voting rights.

### *Gillette's views on the wet-shaving market*

5.21. Gillette maintained that the United Kingdom wet-shaving products market was very competitive. It said that in trying to influence customers to change from disposables to systems it had experienced competition from Wilkinson Sword in particular.

5.22. It suggested that consumers in the United Kingdom razors market were looking for added value and Gillette's response was to concentrate on technological and product innovation supported by heavy advertising so that `the imagery and motivation of the consumer are driven in that way', whereas Wilkinson Sword and Bic tended to compete more on a price basis.

5.23. Gillette said that its current aim was to gain market share for its systems products at the expense of disposables and of own-label. It agreed that the own-label market was largely supplied by Wilkinson Sword. It felt that Wilkinson Sword would also concentrate on systems in order to improve margins.

5.24. Gillette told us that it used both volume and value measurements in assessing the wet-shaving market and that it had confidence in the various surveys that had been made by market survey organisations.

5.25. Gillette confirmed that it was the price leader in the United Kingdom market. Its explanation for the substantial price rises in real terms in recent years was that they were due to high increases in television advertising costs which fed through to the price to the consumer, and to attempts to move the price of disposable razors closer to those for systems products to make them an `easier jumping off point' for the consumer.

5.26. Gillette's view was that the disposables market share was topping out at around the 65 per cent (by volume) level and that double edge consumers seeking to change might now transfer to systems rather than disposables. It considered that in the United Kingdom the relatively high proportion of disposables sold was significantly influenced by female purchasers. In value terms the disposables share had been falling.

5.27. Gillette said that it did not publish a price list primarily because smaller retailers purchased products from wholesalers, and because each major retailer attempted to negotiate its own terms, conditions and prices.

5.28. After Bic and Swedish Match NV the most significant competitor in Gillette's view was likely to be Warner-Lambert with its Schick products although it had not achieved a major presence in the United Kingdom so far. American Safety Razor was a relatively new entrant on the scene and had achieved some success with own-label sales but not with its branded goods. Gillette observed that neither company had taken steps to implement a comprehensive marketing strategy for branded products in the United Kingdom, which would include expenditure on advertising and promotion as well as building up channels of distribution for their products. Gillette referred to Bic as an example of a manufacturer which had entered the United Kingdom market and quickly built up a sizeable share, not through specialised technology but rather because it applied its successful marketing strategies to the wet-shaving market.

## *The agreements and the safeguards they include*

5.29. In agreeing to being involved in assisting the financing of the leveraged management buy-out, Gillette had been anxious, for reasons of competition law in the United Kingdom and elsewhere, to ensure that it would not acquire influence over the buy-out company or the businesses which that company was to operate. Gillette said that great care had been taken when negotiating the arrangements to ensure that the detailed terms of the agreements would include proper safeguards to achieve this objective. In this regard Gillette sought and obtained legal advice from leading anti-trust lawyers in all relevant jurisdictions including the United Kingdom.

5.30. Gillette pointed out that despite having become a sizeable equityholder in Swedish Match NV, it had acquired none of the rights associated with the ordinary shares since all its equity was in the form of non-voting convertible loan stock.

5.31. Gillette said that it had foreseen that competition rules would be likely to restrict its ability to exercise its pre-emption rights under the Equityholders' Agreement. The arrangements made, as described in Chapter 3, reflect its intention to structure the deal so that the options granted to it under the Equityholders' Agreement as amended by the relevant side letters did not enable it to exercise material influence within the meaning of the Fair Trading Act 1973 (the Act). In addition Gillette stressed, firstly, that it was expressly provided in the Voting and Management Agreement that it would never be entitled to nominate any director, and secondly, that it had covenanted with Swedish Match NV, the management and the Scandinavian investors that it would not exert or attempt to exert any influence over the Board or any members of the Board.

5.32. Gillette emphasised to us that the terms of the convertible equity loan stock gave it no voting rights, no representation on the Board of Swedish Match NV and no access to internal Swedish Match NV information. It could convert its non-voting equity loan stock into ordinary shares only if any of the three conversion events were to occur, but it had no influence or control over whether such events would in fact occur. If a conversion were to occur, Gillette's non-voting equity loan stock would convert into ordinary shares equivalent to 22 per cent of Swedish Match NV's total equity excluding any ordinary shares held by the management pursuant to the bonus plan. As to the three potential conversion events Gillette commented as follows:

*(a)* It could see no legitimate objection to its having some say, albeit limited, in the event of winding up.

*(b)* It would be inappropriate for it to be confined to being a non-voting equityholder if Swedish Match NV had a share listing. If a listing was sought, Gillette's position (including the question of whether it would remain as an equityholder of Swedish Match NV) would need to be reviewed.

*(c)* Gillette had no desire to be a sizeable equityholder without influence in a company which, the majority of the equity having been sold, had come under different ownership and, possibly, different management. Conversion of its non-voting equityholding into ordinary shares with voting

rights would give it the opportunity to maximise the return on its investment in these circumstances.

5.33. Gillette added that, even on a conversion in any of these three circumstances, it would not acquire the usual rights of an ordinary shareholder nor the opportunities for influence which those rights would otherwise confer, as it would still have no right to Swedish Match NV information or Board representation, and would remain bound by its covenant not to exert or attempt to exert any influence over the Board or its members.

5.34. Concerning the debt facility arrangements, Gillette was not involved in any way with the senior debt but had made available US $69 million of mezzanine finance through its subsidiary Lustrasilk. It stated that the agreement did not confer on Gillette any right to be represented on any Board, committee or other body constituted by creditors of Swedish Match NV nor was it entitled to financial or other information provided to the institutional mezzanine debt financiers. Also, whereas Gillette had no right to accelerate repayment of its mezzanine loan, Swedish Match NV could repay all or part of the debt at any time before the 14 years due date without needing Gillette's consent.

## *Effect of the sale of non-EC assets and the IP Agreement*

5.35. Gillette stated that these agreements did not give it any right or interest in the Wilkinson Sword wet-shaving business in the United Kingdom, especially since it had undertaken not to use the trade marks in any EC member country or the USA.

5.36. In respect of a possible conflict between the provisions of the IP Agreement and the requirements of section 85 of the Treaty of Rome, Gillette stated that the trade mark and intellectual property provisions of this agreement merely reinforced and clarified the separation of ownership of the intellectual property rights inside and outside the EC and USA. It had acquired no rights in the trade marks and other intellectual property in any EC member state and submitted that the contractual provisions did not infringe Article 85(1) of the Treaty of Rome and that therefore they were enforceable (and Article 85(2) was not applicable). Furthermore, even if Gillette were to consider itself not bound by the provisions on the grounds that they might infringe Article 85(1), it would be open to Swedish Match NV to bring proceedings against Gillette in the English courts under Clause 6 of the IP Agreement, and Swedish Match NV could also bring trade mark infringement or passing-off proceedings against Gillette in the United Kingdom.

5.37. In the situation where an EC country borders on a non-EC country where the same or related marketers are operating in both countries, eg Germany and Austria, Gillette said that it would be open to Swedish Match NV to bring proceedings against it if there were any transgressions by mutual customers attempting to benefit from cross-border price differentials, but that also Clause 16 of the IP Agreement provided that the parties would seek to resolve such problems in good faith. Gillette felt that this was not an issue regarding customers in the United Kingdom. Gillette drew our attention to its discussions with the German Bundeskartellamt on this subject and noted that one possible outcome of these discussions may be the sale of the Wilkinson Sword business in Austria (and possibly the other EFTA countries) back to Swedish Match NV.

5.38. In the case of an EFTA or other country joining the EC, Gillette said that the agreement provided for the business to be offered back to Wilkinson Sword at a price to be agreed or set by independent arbitration. In the case of the removal of customs barriers by a country without its necessarily joining the EC, the situation was less clear. Gillette was convinced that the current agreement would prevent it from doing anything or knowingly allowing anything to be done which would result in its product coming into an EC country from a non-EC country. Furthermore, Gillette believed that as a matter of law, parallel imports from non-EC countries could not pose a problem for Wilkinson Sword since it could rely on its trade mark rights to exclude such imports.

5.39. Whereas Gillette intended to make full use of the Wilkinson Sword brand name in all areas where it could, it did not feel that this would be to the disadvantage of Wilkinson Sword's own business in the EC and USA even if it became known that Gillette was manufacturing and supplying Wilkinson Sword

branded products outside the EC and USA. The way in which Gillette would use the Wilkinson Sword brand outside the EC and USA would probably vary from market to market.

5.40. Gillette did not feel that there was anything in the Wilkinson Sword technology it had acquired as a result of the IP Agreement which it could or would wish to use in products manufactured or sold in the EC or USA. However, Gillette explained that it expected to continue marketing Wilkinson Sword branded products incorporating this technology outside the EC/USA (both products supplied to it under the Supply Agreement in place until the end of 1991 and products of its own manufacture). Gillette informed us that its knowledge of Wilkinson Sword's technology was based on its examination of Wilkinson Sword's products in the market-place and on inspection of public patent and other filings; it had not had access to any of Wilkinson Sword's R&D facilities either during or since the negotiation of the transaction.

## *Undertakings given to the US Department of Justice*

5.41. Gillette said that the restrictions placed on it as part of the settlement of the US anti-trust proceedings were not only intended to ensure that it could not acquire the US Wilkinson Sword business but also to assure the US authorities that it would not be able to use its position as a Swedish Match NV equityholder and creditor, or its position as a marketer of Wilkinson Sword products outside the USA, to influence Swedish Match NV in the conduct of its business. Gillette pointed out that the US authorities had stated that the Final Judgment would substantially eliminate those competitive risks by restraining Gillette's ability to influence Swedish Match NV. It maintained that the safeguards which had been put in place under the agreement were such that its position as an equityholder and creditor of Swedish Match NV, and its position as a marketer of Wilkinson Sword products outside the EC and US, did not give it the ability to influence Swedish Match NV's policy. In consequence of the undertakings it had given, it considered that the US Department of Justice had accepted that Gillette now had no ability materially to influence Swedish Match NV.

## *The benefits and advantages for Gillette*

5.42. Gillette said that by participating in the transaction it was able to acquire the non-EC Wilkinson Sword businesses. It considered that the price it was required to pay for those businesses-not only the direct purchase price of $72.3 million for the non-EC businesses and intellectual property (of which some $6.4 million plus interest will eventually be repaid to Gillette as consideration for the transfer back of the US business) but also the sums it was required to commit to the transaction through equity and debt finance-was attractive in view of the commercial potential those non-EC businesses would have in its hands.

5.43. Gillette told us that it would have preferred to have participated in a transaction whereby it could have acquired the non-EC businesses without having to participate in the financing of the buy-out vehicle. Such an alternative was, as previously noted, not available because of the circumstances in which Stora was proposing to sell its CP Division and because of financing constraints. In agreeing to participate in the financing of Swedish Match NV, Gillette took the view that the matches and lighters businesses were readily saleable such that its mezzanine debt was likely to be repaid. Furthermore it saw its equity interest as a sound investment, a view clearly shared by the Scandinavian investors, together with the banks and other financial institutions which provided senior and mezzanine finance.

5.44. The non-EC businesses held real attractions for Gillette, notwithstanding the previous lack of success the Wilkinson Sword businesses had shown outside the EC. Gillette said it was aware that it had not bought a strong and viable business operation; it would be more accurate to say that it had bought various businesses and assets outside the EC and USA which had considerable potential when brought under the ownership of Gillette, a group which already had a significant presence in most of the non-EC/USA markets concerned. Neither Stora nor Allegheny, the previous owners of the Wilkinson Sword businesses, had realised their potential outside the EC and USA, essentially because they did not have the critical mass, synergies and investment opportunities which Gillette believed it could bring to the businesses.

## *Effects of the transaction*

5.45. Gillette did not think that its rights of pre-emption in certain circumstances and its potential ability to force a sale to a nominated third party would conflict with the objectives of the management and other shareholders. It stated that all it had was the right over a short period of time to find another buyer for the wet-shaving business to match an existing offer and that since the terms had to be identical, the shareholders could be getting exactly the same return. In the event of Swedish Match NV contemplating a joint venture, Gillette thought that if there were particular advantages in its joining with a specific company Gillette would be unlikely to be able to match them and the deal would go ahead.

5.46. In Gillette's view its pre-emption rights existed to protect its interests in a situation where a proposal had been made to sell off the business at a price which it considered would offer insufficient return on its investment and it wanted to seek or make a better offer. It pointed out that the Scandinavian investors had sought similar pre-emption rights on the matches and lighters businesses.

5.47. Gillette agreed that the remaining business of Swedish Match NV after the sale of the matches and lighters businesses would be of interest to actual or potential competitors in the wet-shaving market if the opportunity came for them to buy a stake in the Wilkinson Sword businesses.

5.48. Gillette said that if other shareholders or the management wanted to sell the business it would make a strictly financial judgment in deciding whether to look for an alternative buyer in the short period of time available. It pointed out that, to be able to exercise its option, it would have to find someone who would be prepared to pay the same price on the same terms to achieve the same objectives which the shareholders or management would have. Gillette said that it would be highly unlikely that it would be able to do that in any case where the other shareholders or management were seeking to involve a competitor or a specific type of buyer who was going to offer specific benefits to the business.

5.49. Gillette agreed that the waivers in the side letters to the Equityholders' Agreement gave it exclusive options in relation to the wet-shaving business which the other shareholders did not enjoy. It pointed out that the Scandinavian shareholders had rights covering the matches and lighters businesses which Gillette did not enjoy and that overall the parties which retained specific rights were those which were interested in having them. The reason for arranging the waivers by means of side letters to the agreements was, Gillette said, because it was simpler and quicker than amending the agreement.

5.50. Gillette said that its pre-emption rights in relation to the wet-shaving business and assets were of interest to it if the opportunity lawfully to execute them arose in the future, but that the pre-emption rights as far as the shares were concerned were primarily to protect its investment as a non-voting equityholder and a substantial holder of mezzanine debt.

5.51. In Gillette's opinion Wilkinson Sword's loss of all its trade marks outside the EC and US as a result of the transactions did not deprive it of the critical mass essential for it to develop the EC business. Gillette felt that the EC and US markets Wilkinson now had would constitute a viable, competitive and profitable business. In addition Gillette said that Wilkinson Sword would be able to sell products outside the EC and US under new brand names or to retailers looking for supplies of own-label products.

5.52. Gillette agreed that the effects of its pre-emption rights could stop someone it perceived as a competitor from taking over the Swedish Match NV business or acquiring an interest in it but this was not its primary aim when these rights were agreed. Gillette said that by participating in the leveraged buy-out it had not deprived a competitor of the right to bid for the Wilkinson Sword businesses.

5.53. Gillette did not think it had any ability to intervene in any rights issues or in any way influence a management decision on recapitalisation by Swedish Match NV, particularly in view of the undertakings it had given the US Government.

5.54. Gillette told us that Swedish Match NV could pay off its mezzanine loan at any time before maturity at par plus accrued interest, and that Swedish Match NV did not have to reimburse any payments in lieu of interest that Gillette might have to make in respect of the Stora loan note.

## *Future developments*

5.55. Gillette told us that it intended to manufacture its own supply of Wilkinson Sword products and was already planning to make them in some of its factories for marketing after the end of the two-year Supply Agreement with Swedish Match NV. It confirmed that the agreement would be limited to the two years from 1 January 1990.

5.56. Gillette advised us that there was no overall policy as to how it was going to use the Wilkinson Sword name: decisions would be made by the respective managers responsible for the various markets.

5.57. Gillette believed that the EC Wilkinson Sword business as an ongoing entity would generate value and that it would get its money back and a good return through its equityholding. Its assessment was based on the premise that the matches and lighters businesses would realise enough to allow the mezzanine debt to be refinanced within two to three years.

5.58. In Gillette's view there was plenty of scope for improvements in the margins on Wilkinson Sword products which were well below Gillette's margins on equivalent products in the EC.

5.59. Gillette said that a listing or a sale of Wilkinson Sword were definite possibilities after the initial three-year period since certain parties would probably then want to exit and take their profit. It thought a winding up would be highly unlikely.

5.60. In regard to a possible future disposal of its equity in Swedish Match NV to a non-associated purchaser, Gillette said that it would be happy to consider any realistic offer after the end of the obligation to retain it until 1 January 1993 but it would resist strongly any requirement for a forced sale and would look to cover its full investment plus whatever margin could be obtained. The same view was expressed in relation to the mezzanine debt.

## *Gillette's views on the monopoly situation*

5.61. Gillette agreed that a monopoly situation as defined in the Act existed in its favour in respect of wet-shaving products in the United Kingdom. It also accepted that its main competitor over the whole range of wet-shaving products was Wilkinson Sword, both as a supplier of branded products and as an own-label supplier, whether by volume or value. However, it stressed that it viewed Bic (which supplied only disposable razors) as a significant competitor in the United Kingdom market; also, it pointed out that Warner-Lambert (although small in the United Kingdom) was a significant competitor over the whole range in many markets.

5.62. Gillette's view was that the sale of the Wilkinson Sword business by Stora had not affected or changed the monopoly position in wet-shaving products in the United Kingdom. Gillette originally said that it had not assessed the impact of the transaction on the United Kingdom market or its effect on Wilkinson Sword's share but later advised us that it had considered that the transaction would not have any impact.

5.63. Gillette felt that despite the unusual situation in which, as a monopolist, it had a significant involvement in its main competitor in the United Kingdom market, it had managed to avoid having any influence on the management as a result of the transaction.

5.64. It was suggested by Gillette that the Swedish Match NV management, encouraged by their incentives, would be motivated to compete very strongly against those whom they saw as their competitors and would not be influenced in their running of the business by the fact that a major competitor had a large shareholding and creditor position.

5.65. Gillette maintained that the transaction would make no difference to the way in which its own managers would compete with Wilkinson Sword in the EC and USA: it had a five-year plan for its business and it would stay with that plan. Furthermore, Gillette suggested that its monopoly position did not detract from the presence of vigorous competition, and potential new entry, from Wilkinson Sword, Bic, Schick and own-label suppliers.

5.66. The provision of finance by Gillette to Swedish Match NV could not in Gillette's view be shown to be operating against the public interest since it held that Wilkinson Sword's financial viability would not be affected. It also stated that its whole business philosophy and objectives were contrary to striking a less aggressive competitive attitude than previously.

## *Gillette's views on its ability to influence Swedish Match NV*

5.67. Gillette said that whilst it played a prominent part in the discussions leading up to the transaction on 20 December 1989 and accepted that it had influenced the structure of the deal that evolved, it nevertheless did not have the ability to influence Swedish Match NV's (Eemland's) policy either then or at any time. For reasons of applicable competition rules, Gillette said that it had insisted that its involvement in the transaction be structured so as to preclude any possibility for it to exert any active or passive influence over the buy-out company or the businesses it would operate or for it to have access to any of Swedish Match NV's internal information once it commenced operating.

5.68. If further funding was required Gillette considered it would not have any voice or influence or be able to participate unless it was with US Governmental consent or EC approval although this could be requested if appropriate.

5.69. Gillette maintained that the agreement covering the terms of the loan excluded it from having any rights to say how the business would be run irrespective of its position as a creditor. In its view, the IP Agreement did not give it an ability to influence Swedish Match NV.

5.70. Gillette said that the covenants restricting its ability to influence Swedish Match NV could be modified or removed provided unanimous agreement of the other parties was obtained. In that event the competition requirements of various governments would still restrict its ability materially to influence Swedish Match NV.

5.71. Gillette maintained that the individual rights and agreements, whether taken singly or in total, did not give it an ability to influence the policy of Swedish Match NV. It said that it had taken great care during the negotiations to ensure that the terms of the agreements would include proper safeguards against influence over Eemland or the businesses which Eemland was to acquire.

5.72. Gillette said that the possibility of being able to exercise its pre-emption rights was remote. Again Gillette felt that the undertakings given in the US Final Judgment limited its ability to exercise these rights.

5.73. Gillette maintained that the short-term Supply Agreement did not give it any ability to influence Swedish Match NV. It added that there was no question of this agreement being continued beyond 1 January 1992.

5.74. With regard to its position as an important creditor, Gillette submitted that its mezzanine loan did not confer any ability to influence the policy of Swedish Match NV since it had no power to require repayment before 2003 whereas Swedish Match NV could repay the loan when it wished.

## *Gillette's views on possible remedies*

5.75. In the course of our inquiry, we put to Gillette, on a hypothetical basis, possible remedies to adverse effects and invited it to comment on the likely effects of these possible remedies.

5.76. Gillette reiterated that undertakings had been given in the USA and that there was no objection to those undertakings being given again for the United Kingdom, as detailed in paragraph 5.85.

5.77. Gillette stated that it had no long-term interest in being an equityholder or a creditor of Wilkinson Sword: the importance in the short term was to safeguard itself financially in relation to the investment and the loans. There was therefore no objection to selling off the equity on the open market but there would be an objection to a forced sale because this would be likely to result in a substantial loss to Gillette.

5.78. In regard to disposal of the equity, Gillette would have no objection in principle to disposing of this after 1 January 1993 but it considered it would be inappropriate and disproportionate to order immediate divestment.

5.79. If the equityholders in Swedish Match NV wished to dispose of the company whilst its debts to Gillette were still outstanding, Gillette would be most concerned to retain the right to find a financially viable concern to take over the business in order to ensure that repayment of its debt was not jeopardised. There was no problem from Gillette's point of view in the company being sold when its outstanding loans were not at risk and in that case the pre-emption rights could be very substantially modified or dropped.

5.80. Gillette considered that an order to divest the loans would be equivalent or close to writing off substantial debts and submitted that this was not a realistic option which would be disproportionate in the light of all the other safeguards. As far as creditor rights were concerned, Gillette understood that its only right was the repayment of the debt.

5.81. Gillette submitted that a requirement to divest Wilkinson Sword in the United Kingdom would be draconian and inappropriate as a remedy and it could only have the effect of weakening Wilkinson Sword and the whole financing structure of its business.

5.82. Remedies requiring Gillette not to act as an agent and not to obtain additional interest in Swedish Match NV would in its view be covered by giving undertakings in the United Kingdom similar to those given for the USA, as would matters of contact between the companies and the requirement not to nominate Board members.

5.83. Gillette stressed that the Wilkinson Sword trade mark rights outside the EC and USA were valuable rights which it had paid for and it saw no basis for any remedy restricting their use, although Gillette proposed possible undertakings intended to remove any possibility that its ownership of the trade mark rights outside the EC and USA might give rise to problems for Swedish Match NV.

5.84. Control or restraint on the margins and pricing of Gillette wet-shaving products in the United Kingdom would be wholly inappropriate in its view.

5.85. Gillette did say, however, that it was willing to give certain undertakings in respect of possible public interest issues. These were:

*(a)* to waive the pre-emption rights under Clause 6.8 of the Equityholders' Agreement (ie on a listing) absolutely and irrevocably;

*(b)* to waive the pre-emption rights under Clause 6.9 (ie sale of equity to third party) absolutely and irrevocably where either:

(i) Gillette's loans to Swedish Match NV together with accrued interest and the Stora loan note have been repaid; or

(ii) the sale of equity to the third party is conditional upon repayment of Gillette's loans to Swedish Match NV (together with accrued interest) and of the Stora loan note;

*(c)* to waive the pre-emption rights under Clause 7 (ie as a business sale) absolutely and irrevocably where either:

(i) Gillette's loans to Swedish Match NV (together with accrued interest) and the Stora loan note have been repaid; or

(ii) the sale of the business or assets to the third party is conditional upon repayment of Gillette's loans to Swedish Match NV (together with accrued interest) and of the Stora loan note;

*(d)* to undertake that it will not acquire directly or indirectly any additional interest in any ordinary shares, equity, loan stock, loan notes or other securities in Swedish Match NV with the exception of accrued interest on the debt;

*(e)* to provide a proxy to Swedish Match NV to cast all votes it might acquire as an equityholder;

*(f)* to undertake that it will not act as an agent for Swedish Match NV in the production, marketing, distribution or sale of wet-shaving products in the United Kingdom;

*(g)* to undertake that it will not use any Wilkinson Sword trade marks in the United Kingdom and to use all reasonable endeavours to procure that persons to whom it sells goods under these trade marks outside the EC/US do not sell them into the United Kingdom;

*(h)* to undertake not to have any contact, direct or indirect, with Swedish Match NV management except as may be necessary for the operation of the Supply Agreement up to the end of 1991 and not to have any contact with any of the other Swedish Match NV equityholders which would directly or indirectly have the same object or effect; and

*(i)* to undertake not to participate directly or indirectly in the management of Swedish Match NV and not to suggest or nominate any candidate for election to the Board of directors of that company.

## Views of Swedish Match NV

### *Background to the transaction*

5.86. An outline of the history and structure of Swedish Match AB and Wilkinson Sword is given in Chapter 2. That chapter also explains the involvement of certain employees of Swedish Match AB, including a senior manager of Wilkinson Sword, in the consortium which arranged the leveraged buy-out of Stora's CP Division. The acquisition was agreed on 20 December 1989 and completed over the next three months. Details of the new company, Eemland, which subsequently changed its name to Swedish Match NV, and of the transaction are given in Chapter 3.

5.87. As explained in Chapter 3, agreement was reached during the course of our inquiry on the sale of the matches and lighters businesses by Swedish Match NV leaving the EC and US Wilkinson Sword operation as the company's only business of any significance.

## The involvement of Gillette in the consortium

5.88. Swedish Match NV believed that Gillette wanted a shareholding in the new company because of its decision to concentrate on its core business and to take every opportunity to invest in it. Gillette's intention was to invest in Wilkinson Sword to the full extent permitted by current legislation. Swedish Match NV understood that Gillette would have been interested in acquiring the entire wet-shaving business of Wilkinson Sword particularly as it had a high regard for its technical and commercial capabilities. However, having regard to its position in the European wet-shaving market, Gillette recognised that such an acquisition would have been unacceptable to the EC Commission and to certain national competition authorities, notably those in the United Kingdom and West Germany. Although it therefore ruled out the

possibility of acquiring the entire Wilkinson Sword business it wanted to invest in the business to the full extent permitted by the current legislation. It appeared to Swedish Match NV that Gillette believed also that it would be able to acquire certain non-EC parts of the business without objections being raised. Swedish Match NV said that it believed Gillette considered that this part of the business was capable of substantial expansion, both because of Gillette's greater capacity to exploit the Wilkinson Sword brand in markets where it was already established and because it could use the Wilkinson Sword trade marks in countries in which, for policy reasons, Gillette did not use its own trade mark, eg in India, China and the Soviet Union.

5.89. Swedish Match NV said that Gillette sought to devise, together with a group of potential investors from Sweden, a structure that would achieve its objectives and which would be compatible with applicable competition laws. Swedish Match AB's management were to be invited to participate in the buy-out to ensure continuity in the management of the businesses. The structure ultimately devised was for a leveraged buy-out as follows:

*(a)* the establishment of Swedish Match NV as the vehicle for the acquisition of the entire Stora CP Division, in which certain senior members of that division's existing management were to have a small stake;

*(b)* the sale by Swedish Match NV of the non-EC businesses of Wilkinson Sword to Gillette; and

*(c)* the eventual sale by Swedish Match NV of the matches and disposable lighters businesses to third parties.

## *The involvement of Swedish Match NV management in the consortium*

5.90. Swedish Match NV said that its executives were initially involved in the sale of the CP Division as the Stora employees who in conjunction with MSI put together information for the sale documentation which Stora provided to potential investors. This was mainly a description of the businesses and forecasts of their operation. After joining the consortium they also updated and reworked the information for inclusion in documentation used in connection with the financing of the acquisition. Mr M Rossi was Chief Executive of the CP Division of Stora and subsequently Chief Executive of Swedish Match NV. He stated that neither he nor the other members of the buy-out team had played any part in negotiating the price or in the purchase and sale agreement, as required by Stora. Their co-operation with the prospective purchasers was given only when Stora advised that the consortium of the Swedish investor group, Gillette and Morgan headed the short list, at which time the management concerned effectively became part of the buying group.

5.91. Swedish Match NV said that when the management became actively involved in October/November 1989, the core of the shareholder group had already been formed and this group introduced the lenders to the management. Management had lengthy discussions with the potential shareholders and lenders to explain the businesses to them.

5.92. Swedish Match NV said that, in effect, the headquarters staff of the CP Division based in Nyon, together with Mr K Gruber of Wilkinson Sword in Germany, became the Swedish Match NV management team. The headquarters of the new company remained at Nyon whilst the headquarters of the Wilkinson Sword business was transferred from High Wycombe to Solingen.

## *The transaction*

5.93. Swedish Match NV said that Stora was anxious to ensure a visible Swedish involvement in any consortium seeking to acquire its CP Division in view of the historical importance of Swedish Match AB as a long-established national company. Swedish Match NV told us that MSI felt that the individual businesses of the CP Division could have been sold more profitably if they had been sold separately. However, Stora refused to consider this since it had decided that the division was to be sold as one entity and the purchaser was to be responsible for any further disposals. Thus it was left to the buy-out consortium to dispose of the matches and lighters businesses.

5.94. Swedish Match NV understood that the shareholder group was formed through contacts between Gillette, Lazards, Morgan and, at a later date, Procuritas. This group had already been formed when the management became involved in the buy-out consortium. The lenders for the new company were then being sought by Lazards and Slaughter and May, Gillette's financial advisers and solicitors respectively. The management group provided information to enable potential shareholders and lenders to decide whether to invest or lend to the new company. The group was not involved in the choice of shareholders or lenders, although Mr Rossi suggested Procuritas when the need for Swedish involvement was mooted. The only negotiations in which the management group was involved as regards the buy-out from Stora concerned the basis of its equity participation in the new company and the terms of the incentive schemes.

5.95. Swedish Match NV acknowledged that, as in any leveraged buy-out, its investors tended not to have quite the same horizons as long-term institutional investors. Swedish Match NV said that it wished to move as rapidly as it could towards a stronger position in terms of margins and profitability, so that it could seek a flotation or sale of the business or otherwise reduce its debt. Since, when this was done, its shareholders would be able to realise their investment, the sooner this was achieved the greater would be the shareholders' return on their investment.

5.96. Swedish Match NV said that the relatively expensive nature of the Gillette mezzanine debt (LIBOR plus 6 per cent) was offset by the Stora loan note (no interest payable by Swedish Match NV) such that the overall cost of the two was reasonable. Moreover, interest on the Gillette debt was capitalised which had cash flow advantages. Swedish Match NV could in any case repay the Gillette interest if it chose to. Also, it could repay all the institutional mezzanine loan and part of the Gillette mezzanine loan without having to repay Stora. However, it had no plans for repayment at present.

5.97. Initially Gillette purchased all the Wilkinson Sword assets outside the EC. Subsequently Swedish Match NV bought back the business in the US. The principal features of Gillette's purchase of the assets of Wilkinson Sword outside the EC and US were listed by Swedish Match NV as follows:

*(a)* Gillette acquired the Wilkinson Sword trade marks and certain know-how and other intellectual property subsisting outside the EC and US at 20 December 1989.

*(b)* Wilkinson Sword was no longer able to supply wet-shaving products and related toiletries outside the EC and US under its own trade marks. It remained free to supply shaving products and toiletries outside the EC and US as own-label products or under new brands.

*(c)* Gillette granted to Wilkinson Sword a non-exclusive, royalty free, perpetual licence to use all the patents and other intellectual property it had purchased from Wilkinson Sword (excluding trade marks).

*(d)* A Supply Agreement whereby Wilkinson Sword would supply Wilkinson Sword branded products to Gillette for marketing outside the EC and US. This was originally envisaged as a transitional arrangement for a minimum two-year period, after which the agreement would be terminable by either party on six months' notice. In the event the parties concluded a fixed two-year agreement that expires on 31 December 1991.

## *Repayment of debts*

5.98. When asked for realistic expectations of when it would repay the senior and mezzanine loans, Swedish Match NV told us that its plan was that the asset acquisition facility of the senior debt would be repaid by mid-1991 from funds generated by the sale of the matches and lighters businesses. The revolving credit facility of the senior debt would be repaid by the end of 1993 from deferred proceeds of the sale of the matches and lighters businesses and some additional cash flow from the Wilkinson Sword business. Repayment of the institutional mezzanine debt would commence in 1993 and was forecast to be completed by 1995. However, Swedish Match NV told us that this debt was more likely than not to have been replaced.

5.99. Swedish Match NV said that if it repaid the Gillette mezzanine PIK loan in full it was required to repay the Stora loan note whereas it could repay the senior mezzanine debt without affecting the Stora loan note. It told us that the Stora loan was repayable by 31 December 1995 at the latest. Swedish Match NV considered that part of the Gillette PIK loan could be repaid without triggering repayment of the Stora loan, but there was an option to pay the interest on the Gillette loan in the interim period.

### *Opportunities to buy back Wilkinson Sword businesses*

5.100. Swedish Match NV told us that although Gillette had acquired rights to the non-EC/US Wilkinson Sword businesses in December 1989, Swedish Match NV was still running them. Discussions about the process of transferring the businesses were continuing.

5.101. Swedish Match NV said that it had the right to buy back the Wilkinson Sword business in any country which joined the EC in future and the right to go to arbitration if it could not agree a price with Gillette. It would give serious consideration to buying back the businesses in other EFTA countries and would also consider buying back the business in any other country offered to it by Gillette. However, Swedish Match NV did not have an obligation to purchase everything available as offered and the decision would depend on its perception of the importance of the business offered as well as its financial position at the time and the attitude of its bankers.

5.102. We were told by Swedish Match NV that, of all the businesses Gillette might offer to sell back, it would regard it as most important to buy back the Wilkinson Sword Austrian business, because of its proximity to the German market and to prevent it falling into the hands of somebody who would act differently from Gillette and who might not have the same ethical standards as Gillette. Similarly following the repurchase of the US Wilkinson Sword business, the relationship between USA and Canada was important, and it would therefore be interested in reacquiring the Canadian business.

5.103. Swedish Match NV understood that if Gillette wished to sell a Wilkinson Sword business, Gillette had no obligation to offer it to Swedish Match NV first unless it operated in a country which was joining the EC. Nevertheless Swedish Match NV was confident that commercial considerations would cause Gillette to approach it in the event that Gillette wished, or was obliged, to sell a non-EC/US Wilkinson Sword business. Moreover as a result of an exchange of views between the lawyers of Gillette and Swedish Match NV, it seemed not unlikely that Gillette might be required to sell back the business in Austria as a result of action by, for example, the EC competition authority.

5.104. If Swedish Match NV declined to buy, or Gillette did not offer, a particular Wilkinson Sword business, Swedish Match NV considered that Gillette would be free to pass the rights and technology to any third party, including a competitor. Swedish Match NV said that this could be a matter of concern to it in certain circumstances.

5.105. Swedish Match NV advised us that at the present time the transaction is under consideration by the regulatory authorities in France, Germany, Canada, Australia, New Zealand and Brazil as well as by the MMC and the European Commission. It had also been considered by authorities in the US and Ireland.

### *The market*

5.106. Swedish Match NV said that it was unlikely that a new entrant to the wet-shaving market would be able to produce blades to the quality standards achieved by Wilkinson Sword, Gillette and other established manufacturers and which were demanded by United Kingdom customers. Another major obstacle was the high cost of adequate promotion and advertising needed to change purchasing preferences in this market; according to Swedish Match NV Warner-Lambert's failure to make this investment had hindered its attempts to expand its currently very small percentage of United Kingdom sales. Attempts by Malhotra and American Safety Razor to introduce their branded products (Supermax and Personna) had likewise achieved very limited success. A major area for competition between the suppliers was for shelf space at retail outlets where competitors sought to persuade multiples such as Sainsbury and Boots to devote adequate shelf space to their products.

5.107. In Swedish Match NV's view the most likely route into the United Kingdom market for a new entrant was as an own-label supplier; own-label products accounted for some 10 per cent by volume of this market. It noted that American Safety Razor had managed to pick up about 40 per cent of the United Kingdom own-label business in four years. Wilkinson Sword estimated that its own-label products accounted for most of the remaining 60 per cent of such sales, which amounted to 18 per cent by value (24 per cent by volume) of its total United Kingdom sales of razor blades.

5.108. Swedish Match NV believed that the European market for wet shaving would expand due to a recent trend for younger customers to prefer this method to dry shaving. There was a higher level of dry shavers in Germany and Scandinavia (60 per cent of the total shaving market) than in the United Kingdom (30 per cent) but Swedish Match NV considered that the trend to wet shaving would cause the high levels of dry shaving in Germany and Scandinavia to fall over time. Swedish Match NV expected that any expansion of the European wet-shaving market would be mainly in the systems segment and that the demand for double edge blades would further decline.

## *Effects on competition*

5.109. Swedish Match NV told us that Wilkinson Sword intended to compete no less aggressively with Gillette than it had done in the past. It was confident that it would be able to service its debt without adversely affecting Wilkinson Sword's ability to compete. It could not conceive of any alteration in Wilkinson Sword's position in the market because of Gillette's equityholding or its provision of finance, given the limitations on Gillette's voting and creditor rights.

5.110. Swedish Match NV's policy was to promote branded products whilst defending market share with own-label sales. All brands and trade marks used by Wilkinson Sword for its EC products were owned by Wilkinson Sword Ltd. Swedish Match NV stated that this situation had not been changed as a result of the transaction. It told us that Wilkinson Sword was still able to supply shaving products and toiletries outside the EC/US area as own-label products or under new brands but not to supply them there under the Wilkinson Sword trade marks.

5.111. Swedish Match NV said that the supply of Wilkinson Sword branded products to Gillette under the two-year Supply Agreement was intended to allow Wilkinson Sword time to make any necessary adjustment to its production arrangements and to allow Gillette time to establish manufacturing capability for the Wilkinson Sword product range outside the EC and US as it existed at December 1989. As stated in paragraph 5.97, the arrangements could be terminated at any time after December 1991 by either party on six months' notice but Swedish Match NV advised that the parties had now concluded a fixed two-year contract expiring at the end of 1991.

5.112. Swedish Match NV stated that of the 1989 production at Cramlington about 40 per cent by volume (a smaller amount by value) was for markets outside the EC and US. Gillette had purchased the Wilkinson Sword branded business in these markets and the transitional supply arrangements for 1990 and 1991 enabled Gillette to source its requirements of Wilkinson Sword branded products from Swedish Match NV. However, the restructuring of the Wilkinson Sword business since the acquisition (eg the closure of the plant at Irun, Spain, and the relocation of production) meant that the Cramlington plant was far less reliant on production for the non-EC/US markets than the 1989 figures tended to suggest. It added that both Cramlington and Solingen plants were essential to meet Wilkinson Sword's market requirements and there was no intention of closing either at present. Although the workforce at Cramlington had been reduced by 90, this had been done as part of the restructuring to improve productivity at the plant.

5.113. By 1992 Wilkinson Sword expected to have increased its sales in the EC and US to compensate for any loss in production attributable to the Supply Agreement with Gillette coming to an end. It was particularly confident of increasing its share in the United Kingdom and the USA (where it expected to achieve a break-even result within 12 months).

5.114. Swedish Match NV stressed that it was important to recognise that Gillette was a `minority passive investor' without Board representation or voting powers or the right to receive information provided to other investors. Its rights were essentially limited to certain pre-emption rights on the disposal of the investors' shares and/or the disposal of Wilkinson Sword assets. Details of these rights are given in

Chapter 3. Swedish Match NV said that whilst Gillette's pre-emption rights in the agreement did not influence the present conduct of the business, they could be an inhibiting factor on a future sale or flotation.

5.115. In Swedish Match NV's view, the very existence of the pre-emption rights could discourage some potential buyers from making an offer, particularly in those circumstances where Gillette could match a third-party offer. Also there was a class of buyer to which Gillette might not wish the business to be sold and would therefore seek to find a nominee of its own, even though the other shareholders would be prepared to sell to that buyer. Swedish Match NV said that, taking the two factors together, the pre-emption rights certainly could damage its chances of obtaining the best price for the business and of interesting a wide range of prospective purchasers in a sale.

5.116. As regards the rights contained in the Equityholders' Agreement, Swedish Match NV speculated that Gillette might wish to ensure that if and when the business were to be sold, it would be sold into hands that were not inimical to its interests.

5.117. Swedish Match NV acknowledged that in the event of a sale of the business and assets, or of the majority of the equity, or a merger, it would be open to Gillette, even without its pre-emption rights, to put in an offer that matched or beat an offer on the table. However, the pre-emption rights safeguarded Gillette's position in the event of a rapid deal being struck, to which it might not otherwise have been alerted.

5.118. Swedish Match NV stated that, in its opinion, Gillette's rights as an equity participant and creditor would not of themselves adversely affect competition in the United Kingdom wet-shaving market because the transaction had been structured to ensure that Gillette was not able to influence either the policy or the conduct of the Wilkinson Sword business.

5.119. In Swedish Match NV's opinion, Gillette would learn very little that it did not already know about Wilkinson Sword's business and technology as a result of the transaction. Also, whilst Morgan had access to sensitive information by virtue of its attendance at Board meetings, Swedish Match NV was convinced that this would not be passed to Gillette, particularly as there was a specific undertaking by Morgan and the other investors not to do so. Swedish Match NV said that it had sold to Gillette only technical know-how which existed outside the EC and US. It defined this as primarily know-how in connection with its former factories in Brazil and Zimbabwe relating to double edge blades and disposables.

5.120. Swedish Match NV acknowledged that if the transaction had not been a leveraged buy-out and if it had not involved Gillette, Wilkinson Sword might have retained the businesses outside the EC and USA. However, Swedish Match NV said that it did not expect the sale of these businesses to affect Wilkinson Sword's ability to compete in the United Kingdom wet-shaving market, nor did it believe that their sale would seriously affect the cost structure of the new company. In its view the loss of the non-EC (and non-US) markets was more than compensated for by the ability to concentrate management and finance in the areas that remained.

5.121. Swedish Match NV gave the following reasons for its expectation that the wet-shaving market would become more competitive rather than less competitive:

*(a)* the return of Wilkinson Sword to being a separate corporate entity rather than a division of a conglomerate, enabling management to focus on the wet-shaving business;

*(b)* the concentration of Wilkinson Sword's effort on the EC and US markets, thus avoiding dissipation of management effort and finance on trying to develop world-wide activities;

*(c)* the streamlining of Wilkinson Sword's product range and manufacturing facilities and the reduction of its head office overheads; and

*(d)* the financial arrangements providing an incentive to management to ensure that the Wilkinson Sword business was successful.

5.122. Swedish Match NV told us that it was confident of its ability to achieve a major increase in margins without increasing prices unduly. It intended that such increases in margins, which were already taking place, would be obtained:

*(a)* by its `production restructuring programme';

*(b)* as a consequence of having eliminated lower margin non-EC/US markets from its network;

*(c)* by profiting from the trend towards higher margin systems blades;

*(d)* by harmonisation of price differences between European markets; and

*(e)* by rationalisation of its product range and packaging.

5.123. It did not expect an aggressive competitive response on price to result from this strategy, because most of the improvements in margins would come from lower costs and the product was not particularly price sensitive, at least in the systems end of the business. Swedish Match NV observed that Gillette was a strong, confident market leader with high margins resulting from that strength in the market and the wide spread of its overheads due to the scale of its operations and therefore felt that Gillette would have no interest in predatory pricing and generally would be a stable competitor.

5.124. Swedish Match NV said that it intended to continue to compete in all three market segments: systems, disposables and double edge. Over the last 15 years its United Kingdom market share by volume had decreased from 50 per cent to 23 per cent, largely owing to competition from Bic, but it intended to rebuild and regain market share both from Bic and Gillette making full use of the high Wilkinson Sword brand awareness.

5.125. Swedish Match NV considered that it was well placed with a full range of competitive products in all market segments both to wrest market share from the major competition and to benefit from the overall increase in market size. It expected its own-label sales to remain at the current level with Wilkinson Sword continuing to supply the largest share of this sub-market in the United Kingdom. It understood that Gillette was not involved in this sub-market.

5.126. Swedish Match NV drew our attention to the IP Agreement under which it was not allowed to sell Wilkinson Sword branded products in Gillette's territories, Gillette was not allowed to sell Wilkinson Sword branded products from outside the EC or US to customers inside the EC or US, and neither party was allowed to sell such products to customers whom it knew would export them into the other's territories. It regarded these provisions as a contractual restatement of the rights that flowed from the respective trade marks of the two parties.

5.127. Swedish Match NV did not expect Gillette to use the Wilkinson Sword trade marks to establish a lower price alternative to Gillette's main product lines outside the EC and USA. It thought that they would mainly be used where Gillette could not own 100 per cent of the business, eg the Soviet Union and China.

5.128. As noted in paragraph 5.102, Swedish Match NV told us that it regarded Austria as an important market because of its proximity to the German market and because certain trading and wholesaling companies operated in both countries. It acknowledged that when the same products were supplied by different companies, ie Wilkinson Sword in Germany and Gillette in Austria, price differences could develop in the two countries and then customers in these countries would tend to buy where it was cheaper. While it could in theory prevent imports into Germany from Austrian wholesalers by virtue of its trade mark rights, there remained a risk of undercutting by such imports since in practice the enforcement of trade mark rights could involve taking action against its own major customers in Germany, which was not practicable.

5.129. Swedish Match NV told us that the Wilkinson Sword business was by no means mature and had scope for further growth. Its value to the shareholders would depend on its market value when it came to a flotation or sale rather than its capacity to reduce its debt out of its cash flow. The guiding principle behind the management and funding of Wilkinson Sword would be to enhance the profitability and value of the business.

### *Swedish Match NV's view on the monopoly situation*

5.130. Swedish Match NV said that the fact that Gillette had entered into the agreements, which included pre-emption and other rights, did amount to relevant acts or omissions within the terms of the reference. However, the act on Gillette's part of setting up Eemland made it less likely that Wilkinson Sword would end up in the hands of another company in the wet-shaving business. In Swedish Match NV's view the transaction had resulted in Wilkinson Sword remaining a free and independent agent in the British market and, as a result, in there being less concentration and more competition than if it had passed into the ownership of another wet-shaving company. It did not accept that the equity rights, even if taken as a whole and inclusive of the pre-emption rights, made any difference to the present state of competition, and hence of monopoly, in the United Kingdom market even though they could have some effect by inhibiting the sale of Wilkinson Sword to a trade buyer.

### *Gillette's ability to influence Swedish Match NV*

5.131. Swedish Match NV said that Gillette's interest in the equity of Swedish Match NV was limited to non-voting loan stock. Gillette was not entitled to Board representation. Nor was it entitled to receive from Swedish Match NV information that the other investors received under the Equityholders' Agreement; for their part, those investors had undertaken not to disclose such information to Gillette. Accordingly, Swedish Match NV submitted that Gillette's equity participation did not of itself give it any influence over the policy of Swedish Match NV. Gillette's loan stock was convertible into share capital in limited circumstances, namely on the sale of all the equity in Swedish Match NV to a third party; on the winding up of Swedish Match NV; or on the listing of all ordinary shares in Swedish Match NV. In its view only if Gillette's loan stock were to be converted in the last of these situations would it be realistic even to contemplate the conversion giving rise to any consequences for competition. However, the fact that Gillette's exercise of rights in future could possibly have consequences for competition did not signify that the existence of those rights gave Gillette the ability at present to influence the policy of Swedish Match NV.

5.132. Turning to Gillette's rights as a creditor, Swedish Match NV said that Gillette's contribution of $69 million was provided through the Mezzanine Facility Agreement. Gillette's rights under the agreement were subordinated to those of the senior debt and other mezzanine lenders. The Gillette debt had a final maturity of 14 years. The Facility Agreement contained covenants and default provisions commonly found in loan agreements of this kind, but Gillette was bound by decisions of the facility agents syndicating the loans (MGTC for senior, ICG for mezzanine loan) and other lenders as to such matters as enforcement of covenants and events of default. If Gillette were to remain a lender to Swedish Match NV after the senior debt and institutional mezzanine debt had been fully repaid, the only covenants that Gillette could enforce would be those regarding repayment of capital and interest since, according to Swedish Match NV, the other covenants were given only for the benefit of the other lenders. None of the rights that Gillette had under the Mezzanine Facility Agreement would, in Swedish Match NV's view, enable it to influence its policy.

5.133. Swedish Match NV acknowledged that Gillette (and other investors) had certain pre-emption rights if a shareholder wished to transfer its shares in Swedish Match NV, or if the latter wished to sell `the whole or any substantial part of its business or assets'. The essential point about these pre-emption rights was that if Gillette were to exercise them at some later date this might (depending on the circumstances) have consequences for competition. However, Swedish Match NV submitted that this did not signify that at present the existence of these rights gave Gillette the ability to influence the policy of Swedish Match NV. It accepted that the existence of these rights would be likely to inhibit a future sale or flotation.

### *Swedish Match NV's views on possible remedies*

5.134. In the course of our inquiry, we put to Swedish Match NV, on a hypothetical basis, certain possible remedies to counter any adverse effects we might find and invited it to comment on them.

5.135. Swedish Match NV submitted that any possible remedy should be proportionate, in the sense that it should be no more than was necessary to remedy the adverse effects identified by the MMC; and it should also strike an appropriate balance between the perceived seriousness (or otherwise) of the adverse effects and the consequences of the remedy for the parties concerned.

5.136. Concerning the disposal of Gillette's equityholding to a non-associated company, ie the shares and loan stock, Swedish Match NV said that the impact would be neutral. So far as it was concerned, Gillette's rights as an equityholder were so limited that it could see no reason why Gillette should be required to divest.

5.137. In regard to the pre-emption rights on the disposal of shares, on a listing or on a sale of assets, Swedish Match NV acknowledged that it would clearly be advantageous for the rights to be removed, but it did not seek to have this done. In terms of practicability it saw no reason why it could not be done. However, if the equity, together with the pre-emption rights, was transferred to a third party this could be damaging and in such circumstances Swedish Match NV would prefer the rights to remain with Gillette, a company that it at least knew.

5.138. Swedish Match NV said that there would be no particular advantage to it if Lustrasilk was required to dispose of its interests as a creditor; again, the effect as far as it was concerned would be neutral. However, it would find a requirement to repay the debt in order to remove Gillette as a major creditor `extraordinarily unattractive'.

5.139. Swedish Match NV considered that a requirement on Gillette not to acquire any additional interest in Swedish Match NV securities or stock (other than accruing interest on the existing debt) was already covered by the US undertakings although it accepted that these had been given only to the US authorities. Generally, it would be against Gillette, or any other shareholder, being able to acquire more shares which could give it control.

5.140. Concerning the use of the Wilkinson Sword trade marks outside the EC and USA, Swedish Match NV said that Gillette was contractually bound not to damage the value of these trade marks and Gillette would be unlikely to have any interest in breaking that undertaking. However, Swedish Match NV would be concerned if Gillette decided or was forced to divest the trade marks and they found their way into other hands. Swedish Match NV said that whilst it would expect commercial considerations to cause Gillette to offer them first to Swedish Match NV in any event, it would be an added comfort if Gillette were legally obliged to do this.

5.141. Swedish Match NV said that it would be disastrous if it were required to divest the Wilkinson Sword business at this stage because its entire economic plan was predicated on management having a reasonable period of time in which to improve the volume and profitability of the Wilkinson Sword business so as to enhance its value. It emphasised that if it were forced to sell the business within a much shorter time-scale, this would be likely to cause its shareholders to incur substantial financial losses, particularly as the matches and lighters businesses had now been sold. In its view such a possible remedy would lack proportionality.

5.142. A requirement that Gillette should not act as agent for Swedish Match NV in the United Kingdom in any respect would not concern Swedish Match NV one way or the other: Swedish Match NV could not think of any circumstances in which it would want to appoint Gillette as its agent in the United Kingdom.

5.143. Swedish Match NV said that it would not wish to see any form of restraint on margins and pricing of Gillette's products. It considered that the history of regulatory price controls showed that they were best avoided. In this particular case, any capping of Gillette's margins or prices was likely to be far more damaging to Wilkinson Sword and the other competitors than to Gillette. Moreover, Swedish Match NV regarded it as most unlikely that Gillette would engage in predatory pricing since it stood to lose far

more from such action than Wilkinson Sword. In any event predatory pricing could be dealt with under applicable competition laws.

5.144. Swedish Match NV said that Gillette had no right to attend Board meetings or to nominate members of the Board, and that there was no question as to its having any management role in the company. Swedish Match NV considered that a requirement on Gillette not to have direct or indirect contact with any person who attended Board meetings of Swedish Match NV would be unnecessary. The nature of arrangements with Gillette was such that, apart from the area of sorting out the contract for supply and the handover of the non-EC businesses, it was extremely unlikely that Swedish Match NV would have anything other than the most tenuous social contacts with Gillette.

## Views of Stora

### *Background*

5.145. Stora told us that its rationale for the purchase of Swedish Match AB in 1988 was that it felt the combination of the two businesses at different ends of the forestry and paper industry would give rise to significant advantages. In addition it was felt that Stora would benefit from the knowledge of the many geographical markets and forest holdings which Swedish Match AB had acquired, resulting in a combined group with a strong international profile operating within several product areas and geographical markets.

5.146. Stora stated that the acquisition of Wilkinson Sword as part of Swedish Match AB was incidental to its main purpose in the transaction and that it was clear from the outset that certain of Swedish Match AB's consumer products businesses such as Wilkinson Sword were not within its core business. Accordingly, Wilkinson Sword and the matches and disposable lighters businesses were operated together as a stand-alone division (CP Division) by its existing management as Swedish Match AB. It was Stora's intention to absorb the majority of the other activities of the company as purchased into different divisions or subsidiaries of Stora.

### *Arrangements for the auction*

5.147. Following a corporate review (in early 1989), Stora decided to sell its CP Division as a single package because, it said, of its similar product distribution networks, its operation as a single business and, in the case of matches, a declining demand in developed countries.

5.148. Stora said that with the advice of its financial adviser, MSI, it determined that the most effective way to sell its CP Division was by way of a competitive controlled auction. The auction process involved potential bidders being required to satisfy Stora and its advisers of the structure of their bids, the way in which they would be financed, their plans for employees and of all relevant regulatory matters. Also Stora was anxious to have a visible Swedish involvement in view of the national historical associations of the match business.

5.149. Stora said that it chose to have the sale of its CP Division conducted by an external organisation because it felt it did not have the natural contacts with potential buyers that it normally had in its core business areas. Stora having appointed MSI for this purpose, MSI took the lead in this matter in consultation with Stora. The management of the CP Division also became involved in making presentations and assisting in the sale, and had related incentives.

5.150. Stora said that MSI's brief was to obtain the highest price possible for the CP Division consistent with Stora's hopes of having an industrial buyer and the involvement of Swedish purchasers. However, it emphasised that MSI did not act to put together any bidding group or assist in the organisation of Eemland and its financing.

### *Conduct of the sale*

5.151. Stora was disappointed that there had been only a small number of firm bids. The bid from the consortium which included Gillette was accepted because it was considerably higher than the others and also because it included Swedish investors which Stora considered important for political and public relations reasons.

5.152. Stora was informed by Gillette of its interest as a potential buyer at the end of September 1989. As far as Stora could see it appeared that Gillette was instrumental in drawing up the plans for the new company, Eemland.

5.153. Stora told us that for tax reasons it was very important for it to close the deal in 1989. So as to enable the transaction to proceed it reluctantly agreed to Lazards' request for the loan note of SEK 300 million to meet the shortfall in funds raised to meet the agreed price.

5.154. According to Stora, Eemland first became an active party in the negotiations after it had received the bid in November although participation was mainly through Slaughter and May and Lazards.

5.155. Stora stated that the CP Division management had no participation as such in the negotiation of bids but were consulted extensively in connection with the preparation of the Stock Purchase Agreement in relation to the businesses being sold. It also said that management were not involved in the actual negotiations between Stora and Eemland either on behalf of Stora or on behalf of Eemland. But Mr Rossi and other members of management did meet with potential bidders principally to give management presentations.

### *Gillette's influence on Swedish Match NV*

5.156. Stora said that it would not have contemplated bids for the individual businesses and rejected some bids on that account although it would have accepted complementary bids resulting in disposal of the whole division.

5.157. Stora said that it was told when the deal was negotiated that Gillette would have no influence on Swedish Match NV (Eemland) in Europe (ie the wet-shaving operation in the EC) although it would have an interest in the business. It was Stora's guess that if there had been no competition restrictions Gillette would have wanted to buy the world-wide wet-shaving business of Wilkinson Sword.

5.158. Stora felt unable to comment further on whether the new structure gave Gillette the ability materially to influence Swedish Match NV in any way.