

6 Conclusions

The merger situation

6.1. This reference concerns the proposed acquisition by The Gillette Company (Gillette) of Parker Pen Holdings Limited (Parker), a company incorporated in the UK.

6.2. The reference was made on 5 October 1992 under the Fair Trading Act 1973 (the Act) (see Appendix 1.1). Under it we are required to investigate and report whether arrangements are in progress or in contemplation which, if carried into effect, would result in a merger situation qualifying for investigation as defined in section 64(8) of the Act, in that enterprises carried on by or under the control of Gillette would cease to be distinct from enterprises carried on by or under the control of Parker. For this purpose the reference prescribes the test in section 64(1)(b) of the Act (the assets test) and provides that, if we find this test or the alternative test in section 64(1)(a) (the market share test) satisfied, we shall exclude the other from our consideration.

6.3. As described more fully in paragraph 2.25, the offer made by Gillette and accepted by Parker, subject to clearance by the regulatory authorities, valued Parker at £285 million. The gross value of Parker's world-wide assets as at the time of its last balance sheet in February 1992 amounted to £115 million. Apart from a loan repayment of £12 million due in March 1992 we know of no significant change that would materially reduce that value.

6.4. We therefore conclude that the assets test is satisfied and that, if the arrangements referred to in paragraph 6.2 are implemented, a merger situation qualifying for investigation will be created. As the merger has not been implemented, the second question in the terms of reference relating to the actual creation of a merger situation (Appendix 1.1) does not require an answer. We have therefore to consider whether the creation of this merger situation may be expected to operate against the public interest.

The companies

6.5. Gillette is a multinational company based in the US. Its core product lines are razors and razor blades but it also sells a range of other consumer goods. Its well-known brands, besides Gillette, include Braun (electrical goods), Oral-B (dental care products) and Liquid Paper (correction fluids).

6.6. Gillette entered the writing instruments business by acquiring Paper Mate in 1955. Paper Mate products are manufactured in California and in a number of developing countries and by sub-contractors in Europe and Japan. In 1987 Gillette acquired Waterman SA (Waterman), the leading French pen manufacturer, which has two manufacturing centres, at Nantes and Chamonix. Neither Paper Mate nor Waterman manufactures or assembles writing instruments in the UK.

6.7. The Parker Pen Company was established in the 1880s in the US and 'Parker' has been a leading world brand in the writing instruments market for many years. Parker products are manufactured in Wisconsin (the original site), Newhaven in the UK and Meru in France.

The proposed merger

6.8. In 1976 The Parker Pen Company acquired a majority interest in Manpower Inc (Manpower), a company providing temporary staff to a wide range of organizations. Manpower grew rapidly and in the early 1980s became the predominant part of the Parker business. In 1986 the writing instruments business of The Parker Pen Company, which had been performing poorly, was acquired by a consortium of management and other investors primarily based in the UK and became a UK company, Parker Pen Holdings Limited. During 1987 and 1988 proposals for the sale or market flotation of the company were considered but stock market conditions were not propitious and these were not pursued. In 1989 certain investors wished to realize their investment in Parker; the company was refinanced and it was agreed that in 1992 shareholders would be provided with an opportunity to realize their investment. In January 1992 offers for Parker were invited and after negotiation a conditional offer of £285 million made by Gillette was accepted and an Agreement on the sale announced on 10 September 1992.

6.9. For Parker the proposed merger provides the promised opportunity for certain institutional shareholders to realize their investment. Gillette told us that the merger provided a unique opportunity to expand its international interests in the writing instruments sector by broadening its range, particularly in mid-range refillable instruments. It would also give it a significant market presence in a number of countries where its distribution arrangements and market shares were relatively weak.

The market for writing instruments

The size of the market

6.10. The term writing instruments covers a wide range of products, including both disposable and refillable types, ranging from standard wooden pencils, felt-tip pens, specialist drawing and marking instruments and mechanical pencils to the various types of ink-filled instruments: ball point pens, roller ball pens and fountain pens.

6.11. The writing instruments market in the UK, whether taking disposable and refillable instruments together or separately, is one for which few statistics are collected and such as exist are not comprehensive. We have built up our picture of the market from official statistics, information from the parties and other pen suppliers, wholesalers and retailers and from independent market surveys. Parker provided us with a survey which it had commissioned in 1991 from a market research company, Market Measures, which concentrated mainly on the sector of the market retailing at £2.50 or above. We have found this survey helpful in looking at the market for refillables. Its estimates, which are broadly consistent with other independent market research estimates, suggest a total UK market for writing instruments as a whole (defined to exclude wooden pencils and crayons) of £226 million at retail prices, split almost equally by value between refillables and disposables, although, given relative prices, far larger numbers of disposables are sold.

The product

6.12. All the main types of writing instrument come in both disposable and refillable forms. The two are usually built round the same type of mechanism and will be to some extent in competition (see paragraph 6.18). By far the greater number of sales of writing instruments are of pencils and cheap disposable ball point pens. Within the pens sector the roller ball (which uses a ball point type mechanism with liquid ink) has gained market share since its introduction in the early 1970s, and fountain pens have staged a revival over the last ten years.

6.13. Apart from the introduction of the roller ball, there have been no major technical advances in recent years in writing instruments. The main features of present day fountain pens, for example, go back many years. Current research appears to be towards improving mechanisms and ink quality and delivery. Products at all price levels appear to be efficient and reliable. The production processes are comparatively simple. Parker's high-volume lines, the Jotter and the Vector, are produced by a continuous process; their

other refillables, mainly more expensive models, are all hand-assembled. Machinery and components are readily available.

6.14. Prices for writing instruments range from a matter of pence for pencils and disposable ball point pens to about £200 for a top-of-the range fountain pen (setting aside a handful of sales of yet more highly-priced prestigious gold and silver pens and mechanical pencils). The cheapest pens, both disposable and refillable, are functional, although style and appearance play some part. At higher levels a range of fountain pen, roller ball, ball point and mechanical pencil is often offered in matching finishes. There is much emphasis on style and the range of finishes, for example enamels, lacquers, and gold plating. We regard all these different types of writing instrument as forming part of one market.

The suppliers of writing instruments

6.15. There are a large number of suppliers to the UK market, a number of which are described more fully in paragraph 3.31. There is a wide range of choice at all price levels but no one at present covers the whole range of disposables and refillables. In disposables the main names in the UK are Bic and Staedtler, with Paper Mate, Pentel, Pilot and Berol as other significant suppliers. In refillables Parker, Waterman and Sheaffer have models covering the whole price range. At the lower end of the price range Paper Mate is also represented while in the higher-priced sector there are a number of other well-known brands, including Cross, with a full range of models at all price levels. Recent entrants include Elysée, Diplomat and L'Plume, while an older brand, Montblanc, has established a considerable presence at the higher-priced end of the pen market. Dunhill and other well-known names like Cartier and Yves Saint Laurent have used a brand already well-known in other areas to establish themselves in the prestige end of the market. A few brands like Tombow have established a niche for fashion or novelty pens. Some manufacturers which have a strong position in their home markets, such as Pelikan in Germany, also have a presence here. Some multiples, notably W H Smith (Retail) Ltd (W H Smith) with its Signature and Messenger pens, have established own-label brands in the lower- to medium-price bands, which are currently also supplied from overseas.

6.16. Parker does not manufacture disposables but produces a comprehensive range of refillable pens—ball point, roller ball and fountain pens—from a recommended retail price of about £3 upwards and a range of mechanical pencils, some of which are sold in sets with pens. It is strong in the lower end of the refillable market with its Jotter and Vector ranges. Of Gillette's two brands, Waterman also produces a full range of refillable instruments but its sales in the UK are relatively more concentrated at the higher end of the market. Paper Mate is an important supplier of disposable pens mainly for business use; 70 per cent of its sales revenue comes from disposables. It also sells a decreasing range of refillables at the lower end of the refillable price range, currently up to about £10 retail price.

The market for refillables

6.17. As Parker produces no disposables, in examining the proposed acquisition we are primarily concerned with the potential effects on the market for refillable writing instruments. We looked first at how far refillables can be seen as a separate market from disposables and whether the refillable market itself should be divided into several distinct sectors.

6.18. The cheapest refillable pens can be bought for little more than £1; at this price they are in competition with disposables and many may be treated as disposables by their users. There is no clear price point beyond which consumers distinguish refillables as a distinct product; evidence from various sources during the inquiry suggested that it would lie between £2 and £5. However, many of the disposables and cheap refillables below this level are efficient, well-designed and attractive. They provide competition for the lower-priced models in the more distinct refillables market supplied by Parker and others. Following the approach in market research carried out for Parker referred to in paragraph 6.11 we have broadly equated this refillables market with the market for writing instruments priced at £2.50 or above.

6.19. In discussion with us suppliers tended to divide the refillables market into low, medium and higher-priced segments, but these divisions are not clear-cut and are not defined by distinct price points nor by any clear differences in appearance. There is no great difference in technology as one moves up the range of pens, but more expensive pens have better quality nibs, better finishes and better mechanisms. This is perhaps most important for fountain pens, which often have a gold nib. On the other hand there is no difference between the refills supplied for cheap and expensive instruments in a brand range; for example, all Parker roller ball pens use the same refill and ink supply mechanisms, as do all their ball point models.

6.20. There is, however, an important distinction in the retail sector, based on selling methods. The more expensive refillable pens are kept and displayed under glass and sold by counter staff, while the lower-priced models are on open display, usually presented for self-service on racking in blister packs, which sometimes incorporate presentation boxes. The price point from which pens are kept under glass varies according to the outlet. It may start at £10 or at a somewhat higher level. In most outlets instruments costing £20 or more are displayed in this way.

6.21. All the main suppliers provide refills for their own brands of refillables. In some cases a refill can be used in other brands and a number of suppliers use and supply a ball point refill interchangeable with Parker's. In addition, Parker sales are sufficiently large to make it worthwhile for some multiple retailers to stock as alternatives cheaper own-brand refills. Parker also told us that its roller ball refill is technically different from others. For fountain pens each supplier again provides its own cartridges but an international cartridge is available that will fit a number of brands, including Parker. Whether alternatives are available or not, most customers looking for a refill for a branded pen will ask for a refill of the same brand and sales tend to reflect market shares for pens. It seems sensible therefore to regard the refills market as directly related to the pen market.

The market by trade channel

6.22. Writing instruments are sold into three main channels:

- (a) Largest by value is the retail market with most sales for personal use by the purchaser or as a gift; it is estimated that almost three-quarters by value of sales of pens with a recommended retail price of £2.50 or above are through the retail market.
- (b) Secondly, there is the business gifts market, supplied either direct or through business gift houses; here there are substantial purchases of disposables or cheaper refillables overprinted with the buyer's logo or slogan, for advertising or promotional purposes. More expensive pens are also bought as personal incentives or gifts, and then compete not only with one another but with a range of other gift items. Overall this sector is thought to take by value almost one-quarter of sales of pens priced at £2.50 and above.
- (c) Finally, there is the business use market, supplied almost entirely through wholesalers. Although the largest sales by number of writing instruments are for business use, these sales are overwhelmingly of the cheaper disposables. Only about 4 per cent by value of pens priced at £2.50 and above are sold into this market.

There is little overlap in demand between these three trade channels and we have therefore considered the position in each separately.

The retail market and methods of marketing

6.23. As noted above, it is estimated that almost three-quarters by value of writing instruments with a retail price £2.50 or above (calculated at recommended retail prices including VAT) are sold through retail outlets. Almost all of these are refillables. The main outlets for refillables are department stores, estimated to account for about two-fifths of total retail sales by value, and specialized multiples like W H Smith and Menzies, accounting for about one-fifth with a slightly smaller share held by retail stationers, which include chains like Ryman but are more often small independent outlets. Other smaller outlets include pen

specialists and jewellers, a wide range of small independent retailers ranging from jewellers to confectionery, tobacco and newsagent shops (CTNs), mail order and catalogue stores; together these outlets cover the full range of pens although focused at different price levels.

6.24. While all larger retailers listed above, and pen specialists and jewellers among the smaller outlets, are supplied direct, smaller retailers and CTNs are usually supplied through wholesalers.

Marketing and promotion

6.25. For the large proportion of pens sold as gifts, the perceived image of the brand is particularly important. This is enhanced by consumer advertising, especially before Christmas. The major part of promotional expenditure, however, is directed at the retail trade, including provision of display cabinets, sales consultants and special promotions. Such promotions are particularly important at Christmas and in early autumn (the 'back-to-school' period) when a large proportion of sales take place.

Display arrangements

6.26. As noted in paragraph 6.20, department stores and multiples sell their more expensive pens under glass, ie from closed display counters or cases, staffed by assistants or consultants, and labelled prominently with the names of the brands of pen displayed in them. Some large retailers like John Lewis Partnership (John Lewis), W H Smith and Selfridges Ltd (Selfridges) design and install their own cases and display areas; some of these stores then require a contribution to the cost from the pen suppliers in return for guaranteed display space labelled with the brand name. Some retailers will accept cases which are provided by individual pen manufacturers to the latter's design. These are usually provided free of charge, as long as the cases named for the supplier are reserved for its pens (although we were told that this condition is not always strictly enforced). Other stores will arrange with one of the pen suppliers to design the whole pen-selling area and supply all the cabinets; other suppliers will then be asked to contribute, usually to the retailer, to the cost of the fitments.

6.27. We received a number of complaints from other pen suppliers about the way, it is alleged, the present arrangements already benefit Parker. Parker is often commissioned to design and supply units and other suppliers claimed that these existing arrangements have enabled it to secure more than its fair share of display space and the most favoured locations. There were also complaints that other suppliers had to pay more towards the cases than was justified by the cost to Parker. Parker claimed, however, that it only undertook such commissions at the request of the retailers, that the prices charged reflected the costs of the operation to Parker, and that the retailers and not Parker allocated the space according to the sales potential of each brand. This last point was confirmed by retailers.

Use of consultants

6.28. Pen specialists and pen counters in department stores are frequently manned by staff provided by pen suppliers, described as consultants or demonstrators. These staff are paid for by individual pen suppliers and their main duty is to promote sales of the supplier's pen. Some receive commission as part of their remuneration and some are paid only on commission; commission is only paid on sales of the suppliers' pens. Both Parker and Waterman pay consultants by salary, with some receiving a small additional commission. Consultants are subject to general staff rules laid down by the store, including dress, and are expected to sell other suppliers' pens to meet customer needs. In some stores they operate from the pen supplier's own branded cabinet or island; in others they stand behind their supplier's section of a general pen counter. Consultants sometimes wear a badge or uniform identifying the supplier but frequently wear only a store badge. Some stores do not permit suppliers' badges to be worn. John Lewis does not use consultants but relies on its own trained staff.

6.29. Pen suppliers told us that consultants were largely supplied by them in response to pressure from retailers and in order not to be at a disadvantage to competitors; Selfridges told us that it would not normally accept a new brand unless consultant support were supplied. It was put to us that Parker, with its large share of the retail market, is already able to afford consultants more easily and to deploy them more effectively than its smaller competitors.

Suppliers' discounts

6.30. Suppliers' discounts to retailers are substantial. One major firm's discounts, which we believe to be representative, calculated on recommended retail price exclusive of VAT range from about one-third for smaller retailers to almost 60 per cent for large retailers. In addition, retailers which meet agreed stocking and sales targets can often secure several percentage points more in overriding discounts, usually paid retrospectively. We were told by several suppliers that the level of discounts has been rising in recent years.

Pricing and promotions

6.31. Apart from catalogue and discount houses, most retailers observe recommended retail prices. Promotions are the most usual way of introducing effective price reductions, usually at Christmas or in the 'back-to-school' period, often involving the purchase of a matched set at a substantial reduction on the prices of the individual instruments or offers of a free instrument, for example a free ball pen with a fountain pen.

The business gifts market

6.32. The business gifts market includes purchases by businesses for both incentive and promotional purposes. In selling into this market pen suppliers are in competition not only with one another but with a wide range of alternative gifts. The larger part of the market consists of business gifts offered as staff incentives, personal gifts or mementoes. In this field more expensive pens are in competition with a wide range of items, from holidays and travel vouchers to desk sets, leather goods, wines or crystal, and account for only a small part of sales. The promotional part of the business gifts market is also substantial; it was recently estimated at almost £300 million by Mintel, of which £75 million was accounted for by writing instruments. Pens sold into this sector are mainly lower-priced items which can be overprinted for promotional purposes and are in competition with such alternatives as diaries, key rings or pocket calculators. Most of these promotional pens are disposables. The refillables sold into this market, however, account for almost one-quarter of sales of refillable instruments with a retail price of £2.50 or more. The Parker Vector roller ball has proved particularly attractive for overprinting and Parker has the largest share by far of sales of refillables in the £2.50 to £10 range into the business gifts market, with an estimated four-fifths of total pen sales into this segment of the market.

6.33. Brand perceptions are important in this market, particularly at the upper end, but prices, and the ability to fit the buyer's budget, are more significant determinants of choice than in the retail sector. Many of these business gift sales are handled through gift house wholesalers but more than half of purchases are made directly from the suppliers. Parker has been particularly active and successful in developing direct sales and these now account for over two-thirds of its sales into the business gifts market.

The business use market

6.34. In the business use market (ie purchases by businesses for their own use) the demand is mainly for cheap disposables and competition on price is strong. Sales to this market of pens with retail prices at £2.50 or above are estimated to account for only 4 per cent of sales of refillables. Most sales are made through wholesalers, which expressed little concern about the effects of the merger in this market. Only a small percentage of Parker's sales are into this market.

Entry and prospects of entry

6.35. As noted in paragraph 6.13, the manufacturing and assembly processes are comparatively straightforward and the technology is established. Production can be started on a small scale and pens are shipped to the UK from all over the world.

6.36. Most of the better-known brands in the UK market in refillable pens are long-established; Parker, Waterman, Cross and Sheaffer all date back to the turn of the century or earlier. There are, however, a large number of other brands, many of them well-established in other national markets, particularly elsewhere in Europe, which have a share of the UK market. Montblanc's sales of pens priced at over £50 has increased substantially over the last few years, as a result of what has been described by the industry as an outstanding marketing campaign; it now appears to be the largest supplier of pens selling for more than £100.

6.37. A number of other suppliers (for example Rotring, with a background in technical instruments, and Lamy) have secured sales in the retail under-glass sector, for instruments with distinctive designs. Tombow has also found a niche for pens of a highly distinctive shape. In the £10 to £50 price range Elysée has established a firm presence in the retail market since 1983 with little advertising support. Diplomat and L'Plume are more recent entrants which have established them-selves in the last two years. L'Plume, with pens in the £8 to £40 range, originally imported from the Far East, is now being increasingly manufactured in the UK. All these entrants produce pens that compete with the established ranges.

6.38. Some multiples supply own-brand pens. These are usually lower-priced and in blister packs, but we noted that own-brand pens have been introduced in the medium-price segment by W H Smith and sold under glass. These have been making steady progress and now, as shown in Table 3.6, W H Smith's own-brand sales, ranging from the Student pen at £1.95 to the top-priced Messenger model at almost £50, are exceeded only by those of the major brands. In the £2.50 to £10 segment they appear to be the third largest supplier.

6.39. New entrants and incumbents have both taken market share at the medium and upper ends of the retail market, not all from Parker. Parker, however, remains a strong force in the market as a whole, and particularly in the £2.50 to £10 price range. In this price range Waterman is weak and Paper Mate has been declining. The estimates provided to us suggest that Parker holds almost three-quarters of this price segment of the refillables market. This share reflects shares of about two-thirds of retail sales and four-fifths of business gift sales in this price segment of the refillables market. We looked closely therefore at opportunities for entry and increased market share for incumbents in this price segment and the effects of the merger on the position.

6.40. Suppliers and retailers both suggested to us that in order to become established in this lower-priced segment of refillables, particularly in retail sales, a brand reputation in the higher-priced segments was needed, and that it was very difficult to trade up into the refillable market from cheaper disposables. We have observed that both Pentel and Pilot, which are well-established in disposables, have some refillable instruments on sale in this price sector; both told us that with Parker's existing position in the segment substantial promotional expenditure would be needed for a company to establish itself in this part of the market. We have, however, been told of some 30 suppliers, in addition to Parker, Paper Mate and Waterman. Some of these, like Sheaffer, Pelikan, Osmiroid and Platignum, have been in this sector for a considerable time. Others are well-established in the disposables sector, like Pentel and Pilot. We have also noted W H Smith's success with own-brand refillables, and were told of plans by Zebra UK Ltd, a subsidiary of a large Japanese supplier of the full range of disposables and refillables which already markets disposables in the UK, to extend further up the price scale into refillables.

The effects of the merger

6.41. Against this background, although we considered the writing instruments market as a whole, we have focused on the effects of the merger on the refillable market in which Parker operates, and within this have considered the effect of the merger on the market channels we have discussed above. The proposed

merger would bring together three well-known brands in the UK market: Parker, Waterman and Paper Mate. The market research estimates provided by Parker for the year to mid-1991, which we regard as sufficient to provide a broad picture of market shares, suggest that Parker was then the largest supplier of refillable pens to the UK market, with over half of sales of refillables, and particularly well-represented in the lower-priced segment of that market.

6.42. Waterman is a long-established and substantial French-based supplier of quality pens, with an estimated 5 per cent of the refillables market, although weak in the lower-priced segment. Paper Mate is a US-based firm, now concentrating mainly on disposable pens but still with a small share which was estimated at about 2 per cent of the UK market for lower-priced refillables. The proposed merger would thus add only a small amount to Parker's existing market share, but together the three brands would cover all sectors of the disposable and refillable markets and Gillette would gain in particular Parker's share of the £2.50 to £10 price segment.

6.43. Opposition to the proposed merger came mainly from competing suppliers and some retailers. Most pen suppliers which gave us views expressed concern that a merged company would have a dominant position in the UK market for quality pens and would be able to exploit various marketing practices to secure display space and sales at the expense of competitors. We noted in particular the concerns expressed about a combined company's ability to use its marketing strength with retailers to secure favourable display space, provide consultants and target promotions to weaken competitors. It was suggested that this would lead to reduced choice and possibly some increase in prices. It was also argued that Gillette would also be able to influence purchasing by retailers by the use of aggregated discounts or other inducements. Some retailers were worried, on the other hand, that the possession of three brands spanning the entire range would enable Gillette to exert pressure, even on larger retailers. Some feared that Gillette, by targeting particular product areas and by rationalizing overlaps, would affect choice. Additionally, W H Smith was concerned about possible pressure on its own and other retailers' own brands if the merged company were to instigate price reductions through other outlets to squeeze these own brands out of the market, again reducing choice. Some, but not all, wholesalers and mail order companies were concerned about a reduction of competition, particularly in the lower-priced segments. Business gift houses which gave evidence were not concerned about the effects of the proposed merger.

6.44. Gillette told us that, although there would be some rationalization of marketing and administration, they proposed to keep and promote the three brands separately. In line with its world-wide strategy it was already taking steps to concentrate Paper Mate sales on cheaper high-volume disposable pens, with a few refillable products costing no more than £10, and this process would continue. Waterman had only a small share of under-£10 sales and Gillette's aim was to continue to promote it as an up-market brand, where Waterman and Parker would continue to compete and provide distinct offerings.

6.45. Gillette argued that the merger would have no adverse effects since there were numbers of overseas manufacturers able to supply competitive writing instruments. The merged company, with three separate brands, would have no material increase in the market power currently enjoyed by Parker since the strength of buyers-wholesalers, business gift purchasers, and above all retailers-would prevent any attempts by the merged enterprise to exploit its position; indeed retailers and wholesalers might well take steps after the proposed merger to source elsewhere in order to reduce dependence on the merged group. Parker commented that the merger would make little difference to the competitive situation; current ease of entry to the UK market would not be affected. It also pointed to the power of retailers, and the introduction of own-brands, by, for example, W H Smith.

Market shares of the merged group

6.46. We considered these various concerns in the light of the likely market position once the three brands were in common ownership. The market research estimates provided by Parker in Table 3.5 indicate that in the year to mid-1991 Parker was already the major supplier of refillables, with over half of the estimated total refillables market by value; Waterman sales would have added about five percentage points and Paper Mate a further two points to this share. It is notable that on these estimates Parker's share was highest in the lowest-priced segment of refillables, where it held almost three-quarters of sales by value, and tapered away to 25 per cent in the £100-plus segment. Conversely, Waterman was poorly represented in the lower segments, with most of its sales in the over-£50 price ranges. Paper Mate sold

entirely in the lower-priced bands. On these estimates the proposed merger, taking the two firms together, would appear to add some seven percentage points to Parker's share overall, with a much smaller increase in the lowest price band where Parker was strongest. Waterman's contribution to the increase in market share would be more important in the higher bands and Paper Mate's in the lower. The estimates main suppliers gave us of their sales for the slightly later period of calendar or financial year 1991 are set out in Table 3.6. These suggest rather lower sales by Parker but somewhat higher sales by Paper Mate. We have no reason, however, to doubt the broad picture the market research estimates suggest of the Gillette market position after the proposed merger.

6.47. We looked first at the £10-and-over price segment, primarily the retail under-glass sector, where the main effect of the merger is to bring together two important brands, Parker and Waterman, which on Parker's estimates currently hold 39 and 11 per cent respectively of this sector as a whole, and together therefore would account for about half of sales into this sector. Secondly we considered the lower-priced (£2.50 to £10) segment where the merger would bring together two significant brands, Parker and Paper Mate, and would add about 4 per cent to Parker's estimated 74 per cent share. As noted in paragraph 6.39, Parker's estimated 74 per cent share of this total price segment in 1991 broke down by trade channel to give them four-fifths of this price segment of the business gifts market, and two-thirds of this segment of the retail market. In our examination we have distinguished between the effects of Parker's existing position in the market and the effects of the proposed merger.

The retail under-glass sector

Display arrangements

6.48. It was put to us by some suppliers that Gillette would be able to demand more and better display space because of its increased market share and because of its ability to design and install display fitments. However, those larger multiple retailers and department stores from which we received evidence made clear that they allocated space on the basis of the perceived strength of the brands and estimated sales prospects. Gillette told us that it intends to maintain the two separate Parker and Waterman brands and we would not expect significant changes in display space to result from the merger. Parker is already involved in the design and installation of display units to a larger extent than other suppliers; Gillette does very little and has not found it a rewarding venture. Even where a pen supplier designs the fitments the retailer has the last word on space allocation and it did not appear that Parker overall had more space in units it designed than was warranted by its sales volume. We noted that other brands had good display space and that important department stores such as Selfridges, John Lewis and House of Fraser designed and installed their own units. We did not think that the merger would materially worsen the present position.

Use of consultants

6.49. The provision of consultants to department stores and pen specialists accounts for a significant part of major pen suppliers' promotional expenditure, particularly in the pre-Christmas season. It was argued that after the proposed merger other suppliers would be unable to match Gillette's expenditure and that Gillette would be able to deploy its consultants more effectively and benefit from their ability to offer two brands, Parker and Waterman. Gillette accepted that it would gain some benefit from being able to deploy more effectively the Parker and Gillette expenditure on consultants. It said, however, that this was not an area in which Gillette participated from choice and it would not be reasonable to require it to withdraw consultants if others remained free to use them. We consider that the merger would give the merged company an opportunity to deploy expenditure on consultants more effectively and, by giving the consultants the opportunity to offer another brand if the first fails to find favour, would at least increase the prospects of a sale of one of Gillette's brands, particularly in those stores where the consultants are not identified as representing the supplier.

Discounts to retailers

6.50. It was also argued that the merged company would be able to use discounts aggressively, in particular by aggregating sales of its brands for the retrospective and overriding discounts already offered by Parker to selected retailers. While this would be a possibility it would require Gillette to spend more overall. Parker is already paying the discounts it considers necessary to secure its present sales; these are already high and appear to have been increasing. If additional discounts were offered, based on all sales, Gillette would in effect be paying extra on Parker's business to support the smaller brands. It would appear to be neither cost-effective nor in Gillette's commercial interest. It does not seem to us that the merger would give Gillette any substantial extra power in this area.

Market shares and entry

6.51. Although well-established pen brands such as Cross, Sheaffer, Parker and Waterman have held substantial shares of the under-glass sector for some years, market shares in this sector are not static. Waterman itself after years of disappointing performance appears to have been increasing its share. Montblanc has over a few years become the most important supplier of higher-priced pens. Brands like Elysée, Rotring, Tombow, Diplomat, Lamy and L'Plume have all established a visible presence in a few years as have W H Smith's own-brand pens. These are mostly produced by companies with a substantial presence in their home markets and well-placed to take advantage of any opportunities offered by the merger. There are few advantages of scale, and production or assembly can be successfully undertaken on a relatively small scale. Entry can be modest and the major department stores and multiple retailers are willing to give well-designed new brands an opportunity if marketing support is provided. We believe that if Gillette were to try to use the merger to raise prices there are sufficient actual and potential suppliers offering competitive products to enable retailers to resist the pressure.

The retail self-service sector

6.52. We have looked closely at the £2.50 to £10 segment of the market, estimated to account for about £43 million of the total refillables market of £110 million, given that this is already the area where Parker's market share is highest. In this price segment over half Parker's sales are into the business gifts market but it is also estimated to hold about two-thirds of the estimated retail sales of £18.5 million in this price range (see Table 3.7). Retail sales in this price band are predominantly self-service, with the product usually in blister packs. Parker is very much the established brand name in this area of the market. Waterman is poorly represented here and Gillette proposes to concentrate on its up-market ranges. Paper Mate is the second largest supplier but small by comparison with Parker. It has been reducing its range and its sales have fallen over the last ten years. Gillette told us that it has taken a decision to concentrate Paper Mate world-wide on the cheaper bulk disposable end of the market for the brand. Over the last few years it has withdrawn a number of its higher-priced brands and plans to withdraw all its items priced over £10 during the next two years. In the circumstances of this market we do not expect the merger and the possession of the three brands to give a merged group any greater strength in this sector than the three brands currently enjoy.

6.53. It was put to us that entry was difficult in the self-service sector; suppliers which were well-established in the higher-priced segments would be afraid to damage their image by moving down into the lower price ranges, while for suppliers of cheaper disposables to establish a reputation in the refillables market would require time and money. We accept that these factors may have contributed to Parker's present position. However, Parker's share of the total £2.50 to £10 price segment has grown rapidly-more than doubled since 1982 from 30 to nearly 70 per cent according to its market research estimates. This has coincided with a decline in the share of brands like Paper Mate and Sheaffer, which may reflect strategic decisions by those companies as much as Parker's competitive strength.

6.54. We have noted in paragraph 6.40 the large number of brands already available in this sector of the market-we have identified over 30, some from companies well-known in disposables, others from companies established in the under-glass sector. There are other European firms, well-established in their home markets, and substantial Japanese suppliers known mainly at the moment in this market for cheaper disposable pens, which may be prepared to supply the refillable market in the UK. A number of other

brands have established shares in the lower end of the under-glass sector and are well-placed to expand into the self-service sector. This is also the price band where own-brand products are well-established and are likely to be most acceptable. We have seen no evidence that Parker has exploited its position in the lower-priced end of the retail market and indeed some evidence that it was recently unable to hold an attempted price increase on its Jotter pen.

6.55. We consider that if Gillette were to attempt to exploit Parker's position in this sector retailers and wholesalers would resist and rapidly take steps to encourage the entry of competitors. Gillette would be constrained not only by retailer power but also by the strength of own-label brands in this price segment, by the presence of existing suppliers in the sector and the prospect of new entry and by the alternatives posed by a wide range of increasingly effective disposables.

Retailer power

6.56. Although some large retailers expressed concern about the proposed merger we are struck generally by the strength of retailer power in both the under-glass and self-service sectors. We were told that the general level of discounts had increased by several points over recent years. Retailers may also secure retrospective and overriding discounts. Department stores and multiples are able to secure substantial support for consultants, display space and promotions of immediate benefit to them even though suppliers, we were told, might prefer to spend a greater part of their marketing budgets on advertising to strengthen their brand image. In spite of the concerns expressed we do not see the retailers' present position being significantly affected by the merger.

6.57. At the lower-priced end of the market many suppliers, including Parker and Gillette, drew attention to the power of multiple retailers. We noted that W H Smith, the largest retailer of writing instruments in the UK, regarded the present balance of power between itself and suppliers as reasonable. It has established its own-label brands and gradually moved them into the higher-priced segments. We have no doubt that the multiple retailers would respond by developing other sources of supply, were there any attempt by Gillette to exploit its position by demanding extra display space or a greater share of orders, or by offering less attractive terms.

6.58. Smaller retailers are already likely to devote much of their space to Parker. For those which deal direct the proposed merger might encourage them to stock Waterman and Paper Mate products for the convenience of dealing with a single supplier. This would be unlikely to continue, however, if the merged group's prices moved out of line. Most smaller retailers deal through wholesalers and can order from a range of products. We noted that the major groups of wholesalers supplying smaller retailers did not think the merger would adversely affect them and consider that if put under pressure they would readily find alternative supplies.

6.59. Similarly we believe that Parker's power is limited in other parts of the retail trade by the countervailing power of large customers. For example, we were told by Parker that one major catalogue house had in the last year cut its allocation of catalogue space for Parker products because Parker had not agreed to provide promotional support on the scale requested.

6.60. We were surprised at the apparent lack of price competition between retailers, notwithstanding the high margins available. Most retailers adopt recommended prices although there are some whose policy is to sell at a discount. Competition takes place mainly through special offers. We considered whether the merged company might be in a position to lead prices upwards with the acquiescence of retailers. However, if there were to be such an opportunity it should already exist for Parker, given its market share. We had no complaints of excessive price rises in recent years and indeed there is some evidence that Parker was unable to hold a price increase introduced on the Jotter range. We think that competition from disposables will also continue to act as a constraint in the lower price ranges.

6.61. Taking all these factors into account we do not expect the proposed merger to lead to a reduction in competition, higher prices or less choice in the retail market.

The business gifts market

6.62. Parker has been active in developing opportunities for pens in the business gifts market and now has a substantial share of sales into this market, particularly in the lower-priced ranges of refillables, where its Vector pen has proved particularly attractive as an overprinted promotional gift. The market research estimates supplied by Parker give it about four-fifths of total sales of about £22 million in this price segment. All the major pen firms supply the market, either direct or through business gift houses. While brands are important in this market, particularly with more expensive gifts, price is a significant factor in choice at all levels and is particularly important in selling the cheaper pens, overprinted for promotional purposes. The business gifts market is large and competitive. Refillable pens are in competition not only with one another but also with disposables and other types of gift. Gift agents do not appear concerned that the merger will affect price or choice. While Parker's expertise in this market may enable Waterman to improve its sales performance we do not think that choice will be reduced or that the merged company will be able to raise prices.

The business use market

6.63. In the business use market most sales are of disposable pens. Refillables play only a small part in this market with sales of refillables priced at £2.50 or more of perhaps £4.5 million in total. Paper Mate is a substantial supplier of disposables but Parker and Waterman sell little into this market; only 5 per cent of Parker's sales go into it. Sales are mainly through wholesalers, which expressed little concern about the merger. Price is the main factor in this market and competition appears to be strong. We do not think that the merger will adversely affect price or choice in this market.

Refills

6.64. All the main suppliers provide refills for their own brands of refillables. Although it is worth producing cheaper alternatives to the larger-volume branded refills, particularly those of Parker, most customers appear to prefer to buy the branded refill and most retail outlets apart from some multiples stock only these. The refills market is thus directly linked to that for refillable pens and it is unlikely that the merger will have any effect on the present limited competition in refills.

Other considerations

6.65. Gillette told us that as a result of the merger it expected to reorganize its marketing and distribution activities with the prospect of some job losses. If, however, as expected, Parker's world-wide sales growth continued, it would expect a small net gain of employment in the UK in the medium term. Gillette also saw some limited scope for sharing of technologies although it did not envisage that it would be possible to integrate production facilities between the three distinct brands. Parker currently has no significant patent protection. Pooling of research results and technical knowledge might, however, produce some advantages for both parties. We do not think that these possible consequences significantly affect our evaluation of the proposed merger as a whole.

6.66. During the inquiry we received a complaint from a wholesaler in another EC country that Parker was impeding parallel imports by preventing Parker subsidiaries from supplying buyers outside the subsidiaries' domestic markets. An export ban included in an agreement concluded between Parker and another undertaking was referred to the EC Commission which decided in 1992 that the ban was a restriction on competition within the meaning of Article 85(1) of the EEC Treaty and imposed a fine of 700,000 ECU. But a second complaint concerning obligations imposed on its own subsidiaries by Parker, to restrict themselves to their assigned distribution areas when distributing Parker products, was rejected by the EC Commission. Appeals are pending against both decisions. Following the first decision by the EC Commission, we understand that Parker introduced a wide-ranging EC competition law compliance programme. Parker also told us that all of its distributors throughout the EC, wholesalers and retailers, were free to export or import Parker products as they wished. We do not consider that the complaint made to us raises issues affecting the proposed acquisition of Parker by Gillette.

Conclusions

6.67. The proposed merger would bring together three well-known names in the UK writing instruments market: the Parker brand and Gillette's Paper Mate and Waterman brands. This market covers both disposable instruments (which are estimated to account for about half of writing instrument sales by value) and refillables. The great majority of Paper Mate's sales both by volume and value are of disposables but they also sell lower-priced refillables. Waterman and Parker produce only refillable instruments with a retail price above £2.50. We have therefore considered primarily the effects of the merger in the refillables market, while taking into account the possibility of competition between disposables and refillables in the lower price ranges.

6.68. We have borne in mind throughout the need to distinguish between the effects of Parker's present market position and the potential effects of the proposed merger. Parker is a well-established firm, with a strong brand reputation, which has made good progress over the seven years since the buy-out by the present managerial team and has built up a strong position in the refillables market, estimated at over half of total sales by value. Gillette's two brands are weak in the lower-priced refillables market where Parker is strongest.

6.69. As noted earlier, there are three main trade channels for refillable writing instruments: the retail, business gifts and the much less important business use market. We deal first with the business use and business gifts markets. As explained more fully in paragraphs 6.57 and 6.58, we do not think that the bringing together of the three brands will lead to adverse effects in these markets. Refillables play a small part in the business use market, which is dominated by sales of cheaper disposables and where price is the main factor. In the business gifts market the merger adds little to Parker's existing position and competition will continue from a wide range of pen suppliers and suppliers of other gifts. We do not think that the proposed merger would enable Gillette to raise prices or would lead to a reduction of choice in either of these markets.

6.70. As noted in paragraph 6.64, we consider that, given the strong apparent preference of users for branded refills, the market for refills must be considered as directly linked to that for pens. Again we do not think the proposed merger would have any direct effect on the limited competition that currently exists.

6.71. We have considered the effects of the proposed merger on the retail market in the light of concerns expressed by some parties and bearing in mind the fact that Parker's share of retail sales in the £2.50 to £10 range is around two-thirds. This price segment covers the greater part of sales of refillables to the self-service sector. Market shares have not remained static in the self-service sector; over the last ten years some well-known brands have lost sales in lower-priced refillables while Parker has markedly increased its share. There are already a large number of other brands on sale in this sector, some of which are recent entrants. There are also other European and overseas manufacturers and suppliers which are potentially able to enter this price segment. Some of these potential entrants are already established in disposables in the UK market and others have substantial resources and experience in the refillables range in other markets. It is possible to enter on a comparatively small scale by securing a trial with a major retailer. The presence of a wide range of well-designed and functional instruments in the under-£2.50 price range and the ability of multiple retailers to promote own-label sales will also exercise a restraining influence on any attempt to exploit market position in the lower-priced segment of refillables.

6.72. In the under-glass sector of the retail market we were struck by the number of different brands, types and styles of pen at a wide range of prices already available in the market and the choice offered to the consumer. A completely new entrant can start production on a small scale and can find retailers willing to offer space, provided the price and the direct promotional support are right. As we note in paragraphs 6.15 and 6.37, a number of brands new to the UK have established themselves in recent years and secured significant sales. Market shares of existing suppliers have also changed significantly, with some improving their position in particular segments of the market. We noted the concern of some suppliers and retailers that a merged company would have the strength to use pricing, discounts and other forms of support aggressively both in this and the self-service sector. Such action would already be open to Parker given its market position; it would be costly and, given the number of competitors and comparative ease of entry to this market, we do not think that a merged company could gain any sustainable advantage by these means.

6.73. The major retailers exercise considerable strength in this sector as witnessed by their ability to secure substantial discounts and such other types of support as assistance with consultants and display space. We consider that a merged group would gain some advantage by deploying the consultants it provides to department stores and pen specialists to sell both the Waterman and Parker brands. In the context of the present merger proposal, however, we did not think any advantage that Gillette might acquire in deploying consultants would be sufficient in itself to enable it to exploit its position in this sector, given the power of the retailers and the range of competition. We noted, however, that the possibility of consumers being influenced to favour these brands would be increased in those department stores and pen specialists where consultants were not clearly identified as representing their sponsoring suppliers. We regard this practice, which may well mislead the consumer into assuming that he or she is receiving completely unbiased advice in choosing a pen, as one which may well deserve further investigation on consumer protection grounds.

6.74. Overall we consider that, both in the under-glass and self-service sectors of the retail market, any increase in strength of the merged company would be held in check by a combination of retailer power and the existence of both actual and potential competitors.

6.75. We therefore conclude that the creation of the merger situation that we have identified may not be expected to operate against the public interest.

M S LIPWORTH (*Chairman*)

C C BAILLIEU

P K R MANN

G C S MATHER

L PRIESTLEY

S N BURBRIDGE (*Secretary*)

13 January 1993