

Anticipated acquisition by Co-operative Group Limited of David Sands Limited

ME/5317/12

The OFT's decision on reference under section 33(1) given on 16 April 2012. Full text of decision published 2 May 2012.

Please note that the square brackets indicate figures or text which have been deleted or replaced in ranges at the request of the parties or third parties for reasons of commercial confidentiality.

PARTIES

1. **Co-operative Group Limited (CGL)** is the United Kingdom's (UK) largest co-operative society with a diverse range of activities that include banking, insurance, travel, funeral services, farming and food retail. CGL has approximately 2,900 food retail stores across the UK. CGL generated a turnover in the UK of £13.7 billion in 2010 of which £8.2 billion was related to its food retail business.
2. **David Sands Limited (DSL)** is a family-owned business that operates 28 food retail stores (26 convenience stores and two mid-sized stores) in Scotland. DSL is supplied by Nisa, an independent retail consortium. DSL generated a turnover in the UK of £41.1 million in 2010.

TRANSACTION

3. On 18 November 2011, CGL entered into a sale and purchase agreement with DSL to acquire the entire share capital of DSL. As part of the proposed transaction, CGL will acquire the 28 food retail stores currently operated by DSL. Also, CGL will acquire the head office and warehouse of

DSL located in Kinross, two sites currently being developed as retail stores by DSL in Glenrothes and Kirkcaldy, and certain other properties.¹

4. The parties notified the proposed transaction on 2 February 2012 and the OFT's administrative deadline is 16 April 2012.

JURISDICTION

5. As a result of the proposed transaction, CGL and DSL will cease to be distinct. As the UK turnover of DSL for the last financial year was below the financial threshold of £70 million, the turnover test contained in section 23(1)(b) of the Enterprise Act (the **Act**) is not met.

Share of supply test

6. The OFT will have regard to any reasonable description of a set of goods or services when determining whether the share of supply test as set out in section 23 of the Act is met.²
7. The parties stated that the net sales area of convenience and mid-sized stores that excludes one-stop stores is not an appropriate frame of reference for the purposes of the share of supply test.³ However, in this instance, in light of the nature of the parties' activities, the OFT considers that the supply of groceries through convenience and mid-sized stores, based on the combined net sales area, is a reasonable description of the supply of goods.⁴
8. Section 23(4) of the Act specifies that the share of supply test is measured on the basis of supply in the UK or a substantial part of the UK. A

¹ These include a public house at Argyll Road, Perth, two upper floor flats in Perth and a small retail unit in Kinglassie.

² The OFT's Jurisdictional and Procedural Guidance, OFT527, June 2009, at paragraph 3.55.

³ Please see the Frame of Reference section for a description of mid-sized and convenience stores.

⁴ Sections 23(6)-(8) of the Act provide the OFT with some discretion in terms of how the share of supply is determined.

substantial part of the UK has been found⁵ to refer to an area of such size, character and importance as to make it worth consideration. The parties' activities overlap in the retail supply of groceries through convenience and mid-sized stores in the local authority area of Perth and Kinross, and the area of Fife in Scotland. The OFT, therefore, had to consider whether these areas constitute a substantial part of the UK for the purposes of the share of supply test.

9. The parties stated that it was unclear whether the areas where the parties' activities overlap form a substantial part of the UK.ⁱ
10. The OFT notes that the population size for the administrative area of Perth and Kinross is approximately 148,000⁶ with the city of Perth being the administrative centre for the Perth and Kinross Council. In previous decisions, the Competition Commission (the **CC**), in considering whether a particular area constituted a substantial part of the UK, has considered such factors as population size, demographics, the presence of a higher education establishment, and whether the area represents an administrative centre. In particular, the local nature of the markets in which parties operate has also been considered a relevant economic factor.⁷
11. The OFT considers that there are a number of relevant factors that should be taken into account in this case, namely: the population size, the fact that Perth and Kinross is representative of an administrative area, and in particular, the local nature of the supply of groceries.⁸ In light of these factors, the OFT considers that the area of Perth and Kinross is a substantial part of the UK.

⁵ R. v MMC Ex p. South Yorkshire Transport Limited [1993] 1 W.L.R. 23 at pp.32. Although this case refers to the provisions of the Fair Trading Act 1973, the OFT considers that the same principles apply.

⁶ As noted by Perth and Kinross Council for the year 2010 based on mid-year estimates by the General Register Office of Scotland.

⁷ A report on the acquisition of the Co-operative Group (CWS) Limited's store at Uxbridge Road, Slough, by Tesco plc dated 28 November 2007; a report on the completed acquisition by Stagecoach Group plc of Preston Bus Limited dated 11 November 2009; and, a report on the completed acquisition by Stagecoach Group plc of Eastbourne Buses Limited and Cavendish Motor Services Limited dated 22 October 2009.

⁸ The local dimension to the supply of groceries has been found by the OFT and the CC in previous grocery related cases. See Frame of Reference section for further information.

12. The parties estimate that their combined share of supply of groceries, based on the combined net sales area of all convenience and mid-sized stores in Perth and Kinross, would be approximately [25-30] per cent, with an increment of approximately [five-10] per cent.
13. In light of the above, the OFT considers that the share of supply test as per section 23(3) of the Act is met, and that arrangements are in progress or contemplation which, if carried into effect, will result in the creation of a relevant merger situation.

RATIONALE

14. CGL stated that the proposed transaction is pursuant to one of its strategic aims to grow its business through a programme of targeted acquisitions and new store developments. CGL stated that DSL was identified as a key strategic target due to its store locations in a number of key target towns in Scotland.

BACKGROUND

15. The OFT and the CC have previously examined the market for the retail supply of groceries,⁹ with the CC publishing its 'Groceries Report' in 2008.¹⁰ Furthermore, the OFT and the CC jointly published a guidance document in relation to retail mergers in April 2011.¹¹

⁹ For example, Case ME/3777/08, Anticipated acquisition by Co-Operative Group Limited of Somerfield Limited, OFT decision dated 20 October 2008 (*CGL/Somerfield*), Case ME/4551/10, Anticipated acquisition by Asda Stores Limited of Netto Foodstores Limited, OFT decision dated 23 September 2010 (*Asda/Netto*), and Case ME/4810/10, Anticipated acquisition by One Stop Stores Limited of 76 stores of the Mills Group of companies, OFT decision dated 14 March 2011 (*Tesco/Mills*).

¹⁰ CC Report, 'The supply of groceries in the UK' dated 30 April 2008.

¹¹ OFT/CC Commentary on retail mergers dated March 2011, OFT1305.

FRAME OF REFERENCE

Product scope

16. The parties referred to previous decisions of the OFT and the CC in relation to the relevant product scope. In particular, the parties highlighted the approach adopted by the OFT in *Tesco/Mills*, a case that primarily concerned convenience stores.
17. The approach adopted by the OFT in *Tesco/Mills*, which followed the CC's Groceries Report and the OFT's previous decisional practice, classified grocery stores according to their size:
 - one-stop stores: those with a net sales area of 1,400 square metres (sqm) or more. Stores in this category compete with other stores of the same size and constrain stores of a smaller size
 - mid-sized stores: those with a net sales area of between 280 sqm and 1,400 sqm. Stores in this category compete with other stores of the same size, are constrained by one-stop stores but do not in turn constrain them, and
 - convenience stores: those with a net sales area of less than 280 sqm. Stores in this category compete with all other stores of the same size, and are constrained by mid-sized and one-stop stores. Convenience stores do not constrain mid-sized or one-stop stores.
18. The parties stated that the OFT should adopt the previous approach of the OFT and the CC and consider all stores under 280 sqm as a single convenience category. According to the parties, this reflects the fact that a fairly narrow range of products (newspapers, tobacco and 'top-up' items such as bread and milk) typically drives purchases in these stores.
19. A number of third parties responding to the OFT's request for information indicated that smaller convenience stores may not pose a competitive constraint on all convenience stores.
20. The OFT considers that smaller convenience stores, that is, those that sell only a small range of products and which may more appropriately be

classified as CTNs (Confectionery, Tobacconist and Newsagents) may comprise a separate product market. However, as there are no competition concerns arising from the proposed transaction, the OFT did not consider it necessary to reach a conclusion on this matter. For the purposes of this assessment, the OFT has considered all convenience stores within the same product scope.

Conclusion on product scope

21. In line with previous decisions, the OFT considers that the relevant product market is comprised of three categories of stores, segmented by store size, namely: one-stop stores, mid-sized stores and convenience stores. The OFT considers that there may be further segmentation of convenience stores according to product offering (resulting in a segmentation by CTN) but as stated above, the OFT does not need to reach a definite conclusion on this.
22. Therefore, the OFT considers that there is no evidence in this case to deviate from the classification of stores according to the size of their net sales area, as adopted in its previous decisions.

Geographic scope

23. Previous OFT decisions and the CC's Groceries Report have concluded that the relevant geographic market is essentially local, but that national dimensions of competition exist.¹² More specifically, in relation to the three product markets identified above, the geographic scope has been defined as follows:
 - one-stop stores – 10-minute drive-time in urban areas and 15 minutes in rural areas
 - mid-sized stores – five-minute drive-time in urban areas and 10 minutes in rural areas, and
 - convenience stores – five-minute drive-time in all areas.

¹² *Supra*, *Tesco/Mills* paragraph 13 and the CC's Groceries Report paragraphs 4.134.

24. The CC's Groceries Report concluded that the precise delineation of the geographic scope will vary across local markets according to local topographic and other conditions.¹³ As the parties are primarily active in the areas of Perth and Kinross, and Fife in Scotland, the OFT has considered whether there are any local characteristics pertinent to the DSL stores in these areas which would lead the OFT to move away from the geographic scope used in previous cases.
25. The parties provided information in the form of Convenience Tracking Program (CTP) survey data conducted by him!, a retail consultancy firm based in the UK. The CTP data is comprised of responses from about 25,000 convenience store customers and is conducted on an annual basis.
26. From an analysis of the CTP data provided to the OFT, and information provided by the parties, the following points are noted:
- the average catchment area (that is, the area from which 80 per cent of its members come from)¹⁴ for CGL convenience stores is [0-five] kilometres (approximately [0-five] miles)
 - the average catchment area (based on 76 per cent of customers) for all DSL stores is less than half a mile, and
 - the average distance travelled to a DSL stores is 0.83 miles and over 50 per cent of DSL customers walk to a store.
27. In light of the above information, the OFT has investigated further whether it is appropriate to use a five-minute drive-time geographic scope for the assessment of the acquisition of the convenience stores in this case.¹⁵

Five-minute drive-time

28. The majority of third parties that responded to the OFT's questionnaire stated that the five-minute drive-time isochrone¹⁶ for convenience stores

¹³ *Supra*, paragraph 4.146.

¹⁴ CGL provided this information on the basis of its members' purchases. It should be noted that not all customers are members which may distort the results.

¹⁵ The parties only overlap at a local level with regard to convenience stores.

was appropriate. However, in addition to highlighting that not all convenience stores are comparable (see discussion above in paragraphs 19-20 in relation to CTNs), third party information indicated that local characteristics should be assessed when concluding on the relevant geographic scope. In particular, third party information indicated that certain areas affected by the proposed transaction relate to villages in rural areas, and whilst the nearest town or village may come within a five-minute drive-time, a competitor within this area would not necessarily pose a sufficient competitive constraint in the local area concerned.

29. The parties stated that, although prior to the Groceries Report a one-mile radius was often used as an appropriate catchment area for convenience stores,¹⁷ this was replaced by a five-minute drive-time isochrone in *CGL/Somerfield* and subsequent cases on the basis that it was broadly equivalent in terms of catchment size and was consistent with the catchments determined for larger stores. The parties provided catchment area maps that showed that for some areas the five-minute drive-time catchment isochrone extended beyond a one-mile radius.
30. The parties also stated that given the wealth of evidence used to inform the CC's Groceries Report, the OFT should not depart from the 'standard' approach as it remains the most appropriate, authoritative and reliable analytical framework for mergers in food retail sector.
31. The OFT is mindful in this case of the evidence in relation to the specific catchment area for DSL stores (see paragraph 26 above). It also notes the caution in the CC's Groceries Report that the relevant geographic scope of a particular local market will depend on topographic and other conditions. As such, the OFT has taken a cautious approach and assessed the proposed transaction on the basis of both a five-minute drive-time isochrone and a one-mile radius.

¹⁶ An isochrone is a line joining points of equal travel time (usually drive-time) from a given point.

¹⁷ Although not referred to by the parties, the OFT notes that its previous decisions involving the supply of groceries that pre-date the CC's Groceries Report considered areas of one-mile radius and less for mid-sized and convenience stores. See, Case ME/1582/04, Anticipated acquisition by Tesco plc of 45 outlets from Adminstore Limited, OFT decision dated 5 March 2004, and Case ME/1581/02, Proposed acquisition by Tesco plc of T&S Stores plc, OFT decision dated 9 December 2002.

Asymmetric constraint from one-stop and mid-sized stores

32. The CTP data indicates that [95-100] per cent of DSL's customers use a DSL store on the basis of its convenient location. The OFT further notes that [65-70] per cent of DSL customers go to a DSL store at least every other day (with [35-40] per cent going every day), and [40-45] per cent of customers stated that their reason for visiting the DSL store was that they did not have to travel to a supermarket. This data, particularly when combined with the catchment area data discussed above, casts significant doubt on whether it is appropriate to regard mid-sized and one-stop stores outside the convenience store catchment area (whether a five-minute drive-time isochrone or one-mile radius) as constraining convenience stores within this catchment area.
33. The parties stated that the asymmetric nature of the groceries sector was confirmed by the CC in its Groceries Report and that there is no reason to believe that Perth and Kinross, and Fife differ from the rest of UK on this point. Indeed, the parties pointed to CTP data that shows that DSL customers stated they would continue to shop at the one-stop stores Tesco ([0-10] per cent), Asda ([0-10] per cent) and Morrisons ([0-10] per cent). The parties also stated that these results were higher than the CTP average and CGL's score of [0-10] per cent. The parties stated that this indicates that the DSL convenience stores are constrained by mid-sized and one-stop stores and not by CGL.
34. Furthermore, the parties stated that the incidence of car ownership in the local areas under consideration is higher than the national average and that there is nothing to suggest that Perth and Kinross, and Fife should be treated differently from any other areas.
35. The parties also submitted evidence on the opening of four competitor stores near to DSL stores from 2008 to 2010. This evidence indicates that the DSL stores in closest proximity to the new competitor store experienced a decrease in average revenue following the opening of the competitor's store.
36. However, the OFT notes that for those DSL stores with the largest decrease in revenues, the new competitor store was located less than one

mile away, and for the one new competitor store which was further than three miles away (a new Asda one-stop shop), the revenue decrease experienced by the closest DSL store was less than [0-10] per cent.¹⁸

37. On the basis of the above evidence, the OFT considers it questionable whether mid-sized and one-stop stores outside of the five-minute drive-time isochrone or one-mile radius are a strong constraint on DSL stores within those areas.

Conclusion on geographic scope

38. On the basis of the evidence gathered, the OFT considers that a cautious approach is warranted in this case. Consequently, at the local level, the OFT considers it appropriate to examine this case on the basis of a both five-minute drive-time isochrone and a one-mile radius. The OFT also considers the case on a national level.
39. Furthermore, the OFT considers that the asymmetric constraint from one-stop and mid-sized stores should be limited, at least for the purposes of any preliminary filtering exercise, to those stores within the five-minute drive-time isochrone and one-mile radius. Therefore, one-stop and mid-sized stores outside of the five-minute drive-time isochrone and one-mile radius are not considered when identifying the possible areas where competition concerns may arise post-transaction (although such stores may be considered in a more detailed review of a particular area).

HORIZONTAL ISSUES

40. The OFT has assessed the proposed transaction on both a national and local level. At the local level, the OFT has considered the level of competition that will remain post-transaction within a five-minute drive-time isochrone and a one-mile radius, taking account of mid-sized and one-stop stores within these geographic areas but excluding those outside of them.

¹⁸ The evidence submitted did not estimate this to be statistically significant.

National analysis

41. Data compiled by Kantar Worldpanel (formerly TNS) estimates that total consumer spend on groceries in the 52 weeks to the week ending 25 December 2011 was approximately £104 billion on a UK-wide basis with approximately £10 billion for Scotland.¹⁹ This gives CGL a UK-wide share of sales of approximately [0-10] per cent and approximately [0-10] per cent in Scotland. The increment to these shares of supply as a result of the proposed transaction will be less than one per cent.
42. The OFT therefore considers that the merger does not give rise to a realistic prospect of a substantial lessening of competition on a national basis in the retail supply of groceries.

Local area analysis

43. For the purposes of assessing the local effects of the proposed transaction, the OFT employs a filtering methodology (essentially a fascia counting exercise) whereby areas raising prima facie competition concerns are identified. Where the merger would lead to a reduction in competing fascia of three or less, and consequently raise prima facie competition concerns,²⁰ a more detailed assessment is carried out on an area by area basis.
44. In its previous decisions,²¹ the OFT has concluded that the effective competitor set of grocery retailers consists of large national grocery retailers and regional grocers, and symbol groups. Specialist retailers (for example, bakers or butchers),²² Limited Assortment Discounters (LADs) and frozen food specialists have previously been excluded from this set.²³ The OFT considers that the effective competitor set previously adopted by the

¹⁹ Information provided by the parties.

²⁰ *Merger Assessment Guidelines*, joint publication of the OFT and the CC dated September 2010, paragraph 5.3.5.

²¹ *Supra*, *Tesco/Mills* and *CGL/Somerfield*.

²² Specialist stores will typically offer a limited range of products and operate during restricted hours.

²³ *Supra*, *CGL/Somerfield*, paragraph 18.

OFT, and set out in Annex 1, is the appropriate frame of reference for the purposes of the filtering methodology in this case.

45. The parties conducted a filtering assessment based on fascia counting for each local area where the parties' stores overlap within a five-minute drive-time isochrone and a one-mile radius. This filtering assessment was conducted by centring on both the DSL and CGL stores, using only the fascia in the effective competitor set (see Annex 1).
46. On a five-minute drive-time isochrone there are four overlap areas in which there will be a reduction in fascia from four to three or less post-transaction, namely: Crossford, Motion Street, Lochgelly, Main Street, Thornton and Burntisland. Based on a one-mile radius, two additional overlap areas are identified with a reduction in fascia from four to three or less: North Street, Lochgelly and Oakbank Road, Perth.
47. The OFT assessed each of the six local areas identified in terms of the local characteristics of the area (for example, whether the local area is a rural village or on the edge of a large town), whether there are competing stores (one-stop stores, mid-sized stores or convenience stores) just outside of the relevant geographic scope, the presence of additional competitors within the geographic scope but outside of the effective competitor set that may impose a competitive constraint (see paragraph 49 below), and the closeness of competition in terms of proximity of the DSL store to the nearest CGL store and the relative proximities of competing fascia.
48. The OFT considers, in line with the CC's findings in its Groceries Report,²⁴ that it is appropriate to take into account the nature of the retail offer by the different stores in each local market – including those outside the effective competitor set – when assessing the stores that should be regarded as imposing a competitive constraint in a specific local area. Therefore, for the purposes of examining the competitive effects of the proposed transaction in the six areas identified as raising prima facie competition concerns based on a fascia counting filter, the OFT has considered additional stores outside of the effective competitor set where it has sufficient information to do so.

²⁴ CC Grocery Report, paragraph 4.136.

49. The OFT has assessed the additional competitors on the following characteristics: geographical proximity to the parties' stores, product offering, store size (net sales area), opening hours, parking availability and association with a multi-store operator (such as a regional chain of stores). The parties provided a range of documentary evidence to inform the OFT's assessment of competing fascia in these six local areas based on the above criteria.
50. Following its analysis of each of the six local areas, the OFT considers that there is no realistic prospect of a substantial lessening of competition in each area. A summary of the OFT's local analyses is set out below.
- In the village of Crossford there is no overlap within the one-mile radius as there is only one store, a DSL store, present. Within the five-minute drive-time isochrone, incorporating the area outside of the village, CGL has one store.²⁵ This CGL store is located on the edge of the five-minute drive-time isochrone, and just within the area of Dunfermline where there is a one-stop store less than two miles from Crossford.
 - In three local areas (Motion Street, Lochgelly, Main Street, Thornton and Burntisland) the OFT considers that the merged firm will face competition from the presence of one or more additional competitors outside of the effective competitor set. These additional competitors have been assessed on the basis of the characteristics set out in paragraph 49 above. In particular, the OFT notes that the additional competitors are closer competitors in terms of proximity to the DSL stores in these areas than the parties' stores are to each other.
 - In the remaining two local areas (North Street, Lochgelly and Oakbank Road, Perth) prima facie competition concerns arise within a one-mile radius only. In North Street, Lochgelly, the OFT considers that the merged entity will continue to face competition from an additional competitor that is both larger than the DSL store and in very close proximity to it. Furthermore, flexing just outside the one-mile radius,

²⁵ It should be noted that the OFT considers ScotMid co-operative stores to belong to the same fascia as CGL stores. ScotMid is a regional co-operative which is separately owned and managed, however it has a common brand and forms part of the same buying group as CGL. This treatment of a regional co-operative under the same fascia as CGL is consistent with the analysis in the *CGL/Somerfield* case.

there is an effective competitor at approximately 1.13 miles from the DSL store. In Oakbank Road, Perth, there is a one-stop store (Tesco) just over one mile from the DSL store and less than one mile from the CGL store. In light of the above, the OFT considers that the merged firm will face a competitive constraint post-transaction such that there is no realistic prospect of a substantial lessening of competition in these areas.

51. The OFT considers that a more detailed examination of competitive conditions in the six local areas identified indicates that the merged entity will face a sufficient constraint in each local area post-transaction such as to prevent competition concerns from arising.

Conclusion on unilateral effects

52. In light of the evidence gathered during the course of its market investigation, the OFT considers that there is no realistic prospect of a substantial lessening of competition in the retail supply of groceries at the national or local level.

Barriers to entry and expansion

53. As the merger does not raise a realistic prospect of a substantial lessening of competition at the national or local level, the OFT has not needed to consider the barriers to entry or expansion in relation to the retail supply of groceries.

THIRD PARTY VIEWS

54. Third party views have been incorporated above where appropriate. Further to this no third party raised competition concerns about the merger at either the national or local level.

ASSESSMENT

55. In accordance with previous decisions of the OFT, the relevant product market is considered to comprise retail grocery stores categorised by size into one-stop, mid-sized and convenience stores.

56. The OFT considers that it is appropriate to examine the merger, in terms of geographic scope, on the basis of a five-minute drive-time isochrone and, on a cautious basis, a one-mile radius. The OFT has included the asymmetric constraint on convenience stores from one-stop and mid-sized stores within these geographic areas, but has not, for the purposes of its preliminary filtering assessment, included one-stop and mid-sized stores outside these areas.
57. At the national level the merging parties will have a combined share of supply in the retail supply of groceries of less than 10 per cent with a minimal increment.
58. At the local level, and based on a five-minute drive-time isochrone, four local overlap areas will see a reduction in fascia from four to three or less post-transaction, with an additional two areas of similar fascia reduction based on a one-mile radius.
59. The parties provided the OFT with information on these six local areas, including information pertaining to competing fascia in the areas that were not included in the effective competitor set. Following an analysis of a number of factors in each of these local areas that includes the particular geographic characteristics of the areas and the presence of additional competitors outside of the effective competitor set, the OFT considers that there is no realistic prospect of a substantial lessening of competition at the local level.

DECISION

60. This merger will therefore **not be referred** to the Competition Commission under section 33(1) of the Act.

Annex 1: Effective Competitor Set

1. The OFT has adopted this effective competitor set in its decisions in *Tesco/Mills* and *CGL/Somerfield*. This set includes stores operated by the large grocery retailers (Asda, CGL, M&S, Morrisons, Sainsbury's, Somerfield, Tesco and Waitrose), regional grocery retailers (for example, Booths and regional Co-ops) and symbol groups (for example, Budgens and Spar). Figure A1 below shows the full list of effective competitors.

Figure A1: List of effective competitor set

Asda	Nisa-Todays
Booths	P&H Retail
Budgens	Select & Save
CK Supermarkets	Centra
Co-operative group	Best-One
Dunnes	Spar
Harry Tuffins	VG/Vivo
Longs	Premier (Booker)
Marks & Spencer	Londis
Morrison	Costcutter
Proudfoot	Key Store/Key Shop
Roys	
Sainsbury's	
Tesco	
Waitrose	
Whole Foods	

ⁱ The parties clarified that they did not dispute the fact that a local authority area such as Perth and Kinross might constitute a substantial part of the UK, but said it was unclear whether a smaller area may be considered 'substantial'.