
Proposed acquisition by Staples Inc of Globus Office World Plc

The OFT's decision on reference under section 33 given on 21 July 2004

Affected Market: Office products

PARTIES

Staples Inc (Staples) is an international retailer of office products through a number of retail outlets, 'distant' (catalogue and internet) and contract sales operations in North America and certain parts of Europe. In the UK, Staples supplies office products through 94 stores in England and Wales and, to a limited extent, by order through the mail and internet.

Globus Office World plc (Office World) is a retailer of office products in the UK. It operates 59 outlets in England and Scotland, and supplies a limited amount of office products through the internet. Office World's UK turnover for the year ending 31 December 2003 was £114 million.

TRANSACTION

Staples proposes to acquire the entire issued share capital of Office World for £32.5 million. The transaction was notified on 5 May 2004 and the 40 day administrative deadline expires on 21 July 2004.

JURISDICTION

As a result of this transaction Staples and Office World will cease to be distinct. The UK turnover of Office World exceeds £70 million, so the turnover test in section 23(1)(b) of the Enterprise Act 2002 (the Act) is satisfied. A relevant merger situation will be created if the arrangements are carried into effect.

RELEVANT MARKET

The parties overlap in the supply of stationery and related office products, including PCs, office furniture and computer consumables (e.g. ink cartridges for printers) through office superstores, and to a lesser extent, via the internet.

Product market

Stationery products can be supplied to customers via a number of channels:

- *Office Superstores* – these are generally larger stores (averaging 10-12,000 sq.ft) located on the edge of towns and cities. The parties represent the two office superstore chains active in the UK.
- *High street stationers* – smaller stores located within shopping centres and on high streets. They include large chains of specialist stationers (e.g. Rymans), but also smaller independent stores and non-specialist stationery retailers (e.g. WH Smiths).
- *Mail order suppliers* – supply stationery and other office products via catalogue and delivery service.
- *Internet retailers* – are similar to mail order suppliers in that they operate on a next-day delivery basis, though ordering and payment are carried out on-line rather than by fax or telephone.
- *Traditional stationery dealers* – have customers on account and operate a delivery service in their local area.
- *Contract suppliers* – tend to be large companies (e.g. Banner), who supply large organizations with the totality of their office supply needs.

Demand side substitutes

The actual stationery and office products sold by the wide range of alternative supply channels identified above are effectively the same or substitutable for those sold by the parties' superstores. For certain products, such as office furniture or PCs and consumables, many additional (non-stationery supplier) outlets exist, e.g., John Lewis and IKEA for office furniture and PC retailers for computers and consumables.

The issue in this case is therefore is whether the office superstore supply channel in the UK constitutes a distinct product market from other channels. Competition authorities from other jurisdictions have considered this issue in cases involving Staples.

- In 1997, the U.S. Federal Trade Commission (FTC) was successful in seeking a court injunction preventing the acquisition by Staples of the only other U.S. office superstore operator, Office Depot¹. The court accepted the FTC's argument that, in the US, office superstores constituted a separate product market, based in part on evidence that in areas where there were two or more competing superstore fascias, prices were significantly lower than in areas where there was only one superstore fascia.
- In a 2002 case, *Staples/Guilbert*,² the European Commission considered an overlap between the parties in distance selling (i.e. internet and mail order) of office products in the UK, but did not deem it necessary to conclude on product market definition since no competition concerns arose.

The OFT's investigation into demand-side substitutability between distribution channels in the UK revealed the following.

- *Pricing across different channels.* Pricing information for a number of key products across retailers in different supply channels was supplied by the

¹ *FTC v. Staples, Inc. and Office Depot, Inc.* Case No.: 1:97CV00701

² COMP M.2965 – *Staples/Guilbert*;

parties. This information indicated that there was no significant correlation between the prices offered by Staples and Office World for most products; rather, greater correlation was observed between Staples and other channels such as high street retailers and the grocery multiples.

- *Price differences where the parties encounter one another.* Prices from a sample of 10 different products, chosen at random by the OFT, were examined across each of the parties' stores. For each product, prices were found to be identical across each of the Office World or Staples superstore chains, irrespective of whether another superstore was located nearby. Consequently, there was no evidence that the parties pricing behaviour was significantly influenced by the presence of competition from another superstore, unlike the findings in the U.S. litigation.
- *Product range.* UK stationery superstores carry a medium-size range of office products (between [] (see note 1) stock keeping units³ (SKUs)) compared to other competitors. For example, high street retailers stock a relatively small range of products ([] SKUs (see note 1)), whilst mail order, contract or internet suppliers stock a much larger range ([] SKUs (see note 1)).
- *Customer profiles.* The parties' customer base focuses on individual consumers and small and medium sized enterprises (SME's) often referred to as Small office Home office (SoHo) customers. For this reason, the closest competitors for superstores are unlikely to be contract suppliers since these firms tend to supply large volumes to large companies. Research conducted by the parties suggests that for individuals, high street retailers are a major constraint, whilst for SME's, mail order and internet supply are close competitors.
- *Views of market participants.* Third party comments indicate that customers can and do switch between supply channels relatively freely and there are no costs incurred as a result. Many customers in fact source from multiple channels. No third party thought it realistic that superstores would be able to maintain a 5 per cent increase in all prices without a significant number of customers switching to alternative sources of supply. Furthermore, one third party response indicated that when a superstore opens in a particular town, local independent dealers tend to see an immediate and significant drop in sales. This suggests that superstores constrain other channels and is at least indicative that the reverse may also be true.

Supply side substitutes

There appears to be little supply side substitutability between superstores and other stationery supply segments. No third party considered it likely that firms would enter the superstore segment in the event of a significant and sustained non-transitory increase in prices (SSNIP test) of 5-10 per cent.

³ Stock keeping unit (SKU) is an identification, usually alphanumeric, of a particular product that allows it to be tracked for inventory purposes. Typically, an SKU is associated with any purchasable item in a store or catalogue. It should be noted that different SKUs may represent the same product (e.g. paper) in different package sizes (e.g. number of sheets).

Conclusion

Based on the information provided, the appropriate product frame of reference is considered to be wider than the superstore segment. Pricing across channels and the parties pricing behaviour in the presence of each other does not support the assertion that superstores operate in a distinct and separate segment of the office products sector in the UK. This view is upheld by third party comments which indicate that customers are both price sensitive and face little or no difficulties switching to other office product channels. Furthermore, there is evidence to show that the parties compete directly with high street retailers, for individuals, and internet and mail order suppliers, for SME's.

The EC has in the past concluded that the distribution of office supplies by nation-wide contract suppliers to large customers constitute a separate market.⁴ In this case, neither of the parties are active in the contract supply channel and given no competition concerns arise whether or not contract stationers are included in the product frame it is not necessary to conclude on whether contract supply should be excluded from the product frame. Consequently, the relevant product frame of reference for assessing this merger is considered to be the supply of office products.

Geographic market

Competition appears to occur at both a national and local level. The parties set prices on a national basis and larger mail order, internet and contract suppliers provide a national delivery service, usually on a next day basis. However, information supplied by the parties indicates that the majority of customers will travel for a maximum drive time of 15 minutes to reach a superstore. Similarly, high street stationery retailers and smaller independent dealers are also likely to have a local competitive scope. It is therefore appropriate to consider the proposed transaction from both a national and local perspective.

HORIZONTAL ISSUES

While the transaction combines the two operators of UK superstores, the weight of evidence (discussed above) suggests that a 'monopolist' operator of superstores could not profitably increase prices because customers would switch to competing sales channels. The superstores supply channel is relatively small in the overall office supply sector. Sales of office supplies through superstores account for roughly [less than 10] per cent (see note 2) of all office supplies sold in the UK. In respect of the overlap in the 'distant' channel (i.e. internet and mail order), the parties' estimated combined share of supply would be approximately [10-15] per cent (increment [less than 10] per cent (see note 2)). The parties would also face strong competition from Viking Direct (controlled by Office Depot), the leading competitor within the distant segment.

Overall, the parties' combined share of supply for the supply of office products in the UK would be approximately [less than 10] per cent (see note 2). If sales from contract stationery providers are excluded, the parties' estimated share of supply would be expected to increase slightly, but remain below [5-10] per cent (see note 2).

⁴ COMP M.2286 – *Buhrmann/Samas Office Supplies*

At a local level, the OFT considered whether in any of the geographic areas in which the parties overlap, there was the prospect of a lessening of competition. The parties submitted evidence on local catchments areas for their overlap stores which showed that for all of these stores there were at least 4 competing fascias within a 5 minute drive time. Of those fascias, there were at least 2 that were specialists in office supplies as opposed to general retail outlets. Furthermore, for all of these areas, mail order and internet supplies were available.

One competitor raised the concern that the EU market would follow the pattern of the USA in which it was alleged that superstores were engaged in geographic market sharing, suggested by the fact that Staples and Office Depot⁵ do not have superstores in the same states within the EU. However, Office Depot is active in the UK through its subsidiary Viking Direct and, as discussed above, the superstore channel faces competition from a number of different channels in the office products sector. (see note 3)

Barriers to entry and expansion

The main barriers to entry in superstore retailing are the availability of suitable premises or land on which to build and the capital cost of building (or leasing) and stocking suitable premises. Third party estimates of the cost of setting up a superstore ranged from £100,000 to £10 million and it was considered that new entry in the superstore segment was unlikely in the foreseeable future. However, the parties have themselves opened 10 new superstores in the UK over the last 12 months, which would suggest that such barriers are not insurmountable.

Evidence from third parties suggests that entry into the internet sector is very easy on a smaller scale: it is relatively inexpensive to set up a web based ordering system for existing customers. However, in order to increase internet sales and build an effective internet business, significant investment must be made in advertising, sales and support. However these barriers are not considered to be any higher than for a similar mail order company and in general entry into Internet retailing was considered easier than entry to superstores retailing.

Barriers to expansion for superstores, high street and other locally based suppliers may exist with respect to the need for firms to expand their geographic scope. No such barriers to expansion exist however for mail order, contract supply and internet suppliers since these firms offer a national delivery service.

It is therefore considered that barriers to entry in general office supplies are relatively low, although they may be slightly higher in the superstores segment due to constraints on the availability of suitable premises.

Buyer power

Office superstore customers are in general individuals or small businesses and so there is little prospect of their exercising any countervailing buyer power.

⁵ Office Depot has superstores in France and Spain but not the UK.

VERTICAL ISSUES

No significant vertical concerns are raised as a consequence of this acquisition.

THIRD PARTY VIEWS

A number of third parties were contacted during the investigation. Of those who responded, most were unconcerned by the transaction. Customers took the view that there were a number of alternative suppliers from which to choose and indicated they would switch in the event of a price increase. One competitor was concerned that superstores would dominate the other channels and push out independent suppliers. Two other competitors expressed concerns that the merger would result in a reduction in competition in the superstore segment.

ASSESSMENT

The appropriate frame of reference in this case is considered to be the supply of office supplies to retail and business customers in the United Kingdom. Various evidence, including pricing data and third party comments suggested that other distribution channels are substitutes for – and effective competitors of – superstores, in particular high street retailers, internet and mail order suppliers. Unlike previous findings in other jurisdictions, the evidence did not therefore support the proposition that superstores in the UK are a distinct market within the office products sector.

Competition between office product suppliers occurs on both a national and local level. At the national level, the parties combined share of supply was approximately [less than 10] per cent (see note 2). Where the parties overlapped at a local level, a minimum of 4 competing fascias, at least 2 of which were specialist office product retailers, were identified within a 5 minute drive time. In addition, for all of these areas, mail order and internet supplies were available. Barriers to entry are considered to be relatively low and customers are able to freely switch between suppliers at little or no cost.

Consequently, the OFT does not believe that it is or may be the case that the merger may be expected to result in a substantial lessening of competition within a market or markets in the United Kingdom.

DECISION

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

NOTES

- 1 Actual figures deleted for reasons of copyright or commercial confidentiality.
- 2 Actual figures replaced by a range at the request of the parties for reasons of commercial confidentiality.
- 3 Given the conclusions reached by the Office with respect to the allegation of market sharing, it was not considered necessary for the parties to provide a response to these allegations. However, the parties have requested that it be made clear that these third party allegations are unproven and are categorically denied by both parties.