

VTECH/LEAPFROG MERGER INQUIRY

Summary of hearing with Shop Direct on 28 September 2016

Product Choice

1. Shop Direct told us that the way products were grouped on their website was based on their internal classification of products and took into account how their competitors classified products, with the overall aim of making it easy for customers to find the products they were looking for.
2. Shop Direct told us customers that came to the Shop Direct website might be searching for latest offers, individual items, requests for specific toys by a child, etc, and could shop by age, brand, categories, etc. A number of customers searched by licence and other customers searched by brand. The website could also recommend different products for the child if the age of the child was provided.
3. Shop Direct told us that they had a wish list of 'must have' products across all their categories and these products were marketed by them in a certain way. These 'must have' products were specific to Shop Direct and influenced by the marketing plans behind these products and whether Shop Direct had a strategic plan with the brand (linked to how big the licence and support was). The products with the biggest TV advertising support and content (ie branding from movies, content and viral trends) tended to be 'must have' products. There were also annual best sellers which Shop Direct would always include on any list of 'must have' products. The 'must have' from LeapFrog for this season is the LeapStart range launched in July 2016 and VTech had a number of products including the Toot-Toot range, the baby walker and DigiGo.

Contract/supply agreement negotiation

4. Shop Direct told us that VTech and LeapFrog negotiated in a similar manner. Negotiations for terms (eg rebates, funding, etc) for products to be sold in the autumn/winter season were started in November and finalised by February. Negotiation on prices for ranges took place twice a year.
5. Shop Direct said that the Parties would bring a price list of all products and negotiations occurred on individual products. The aim for Shop Direct was to ensure that the overall range delivers the margins they want. In addition to

price negotiations, negotiations were undertaken in relation to packaging, returns, launch dates, intake plans marketing support, rebates, funding for promotions, etc.

6. Shop Direct did not threaten to de-list products during negotiations as VTech and LeapFrog were unique and VTech had a huge range of toys whereas other manufacturers did not have a lot of the products which VTech and LeapFrog offer in their range.
7. Shop Direct told us that they agreed season estimates for product sales with the supplier and then they started to call up the stock as sales progressed.
8. Shop Direct worked with selected brands and built online events such that selected brands got a prominent space on their website.

Current and potential suppliers

9. [✂].
10. Shop Direct said that the market for child tablets had declined and was not as popular as it was two to three years ago. The general tablet market had reduced and people were more willing to hand down tablets to children and this had contributed to a decline in the demand for child tablets.

Entry and expansion by toy manufacturers

11. Shop Direct told us that they would not be averse to opening a new account for a new supplier who came in with a new toy. However, such a company would have to have a certain turnover, a range of products and could deliver sales.
12. Shop Direct said that they were not aware of any potential entrants in relation to child electronic reading systems. They were aware of Learning Resources who provide a basic version of a reading system (as compared to the LeapFrog reading system which comes with accessories).

Innovation

13. Shop Direct told us that both VTech and LeapFrog supply products which show incremental innovation (ie that improve on existing products), as well as products that were breakthrough innovations (ie that create new products). They noted that VTech was very strong in innovation of toddler electronic learning toys.