

# Completed acquisition by HFD Ltd of Garrod Bros (London) Ltd's business of distribution of floorcovering materials

## Decision on relevant merger situation and substantial lessening of competition

**ME/50717**

The CMA's decision on reference under section 22(1) of the Enterprise Act 2002 given on 28 March 2019. Full text of the decision published on 09 April 2019

Please note that [X] indicates 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.

### SUMMARY

1. On 26 October 2018 HFD Ltd (**Headlam**) acquired Garrod Bros (London) Ltd's business of distribution of floorcovering materials (**Garrod Bros**) (the **Merger**). Headlam and Garrod Bros are together referred to as the **Parties**.
2. The Competition and Markets Authority (**CMA**) believes that it is or may be the case that each of Headlam and Garrod Bros is an enterprise; that these enterprises have ceased to be distinct as a result of the Merger; and that the share of supply test is met. The four-month period for a decision, as extended, has not yet expired. The CMA therefore believes that it is or may be the case that a relevant merger situation has been created.
3. The Parties are wholesalers that supply flooring products in the UK. The Parties overlap in the supply of palletised flooring products within the M25.<sup>1</sup> On the basis of limited demand-side and supply-side substitution between the wholesale supply of palletised flooring and broadloom flooring, commercial

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<sup>1</sup> See definitions of broadloom and palletised flooring and of independent retailers and contractors in paragraphs 30-50 below.

and residential customers, and the wholesale supply channels and other routes to customers, the CMA has considered the competitive effects of the Merger within the following frames of reference:

- (a) the wholesale supply of palletised flooring to contractors within the M25; and
  - (b) the wholesale supply of flooring UK to contractors.
4. The CMA found that, absent the Merger, there is a realistic prospect that Garrod Bros would have been purchased by an alternative purchaser which may be considered to be a more competitive counterfactual given Headlam's existing position within the applicable frames of reference. Consistent with its guidance and established practice, the CMA has assessed the Merger against a counterfactual in which Headlam owns Rackhams Limited (Rackhams), a transaction that is being considered in parallel by the CMA.
5. The CMA considered whether the Merger would give rise to:
- (a) Horizontal unilateral effects in the wholesale supply of palletised flooring to contractors within the M25; and
  - (b) A loss of dynamic competition in the supply of palletised flooring by hindering the entry and or expansion of a competitor that, absent the Merger, might have acquired Garrod Bros, and, by achieving a wider coverage and benefiting from economies of scale, would compete more effectively with Headlam regionally or nationally.
6. The CMA believes that the Merger does not give rise to a realistic prospect of a substantial lessening of competition (SLC) in particular because:
- (a) In the wholesale supply of palletised flooring to contractors within the M25, the CMA considers that while there is a significant degree of competitive interaction between the Parties, the overall change in market structure brought about by the Merger is limited (in particular because the increment in share of supply is small) and the merged entity will continue to be constrained by a sufficient number of credible competitors.
  - (b) In the supply of palletised flooring to contractors across the UK, the CMA considers that the available evidence does not support the position that the Garrod Bros business is a strategically significant asset within the broader supply of palletised flooring at a national or regional level, and therefore that the acquisition of Garrod Bros by Headlam does not hinder the entry and/or expansion of a competitively significant force at a national or regional level.

7. The Merger will therefore **not be referred** under section 22(1) of the Enterprise Act 2002 (the **Act**).

## **ASSESSMENT**

### **Parties**

8. Headlam is a national distributor of flooring materials to both commercial and residential customers in the UK. Headlam sells a variety of manufacturer branded and own-brand products (which are manufactured by third parties for Headlam). In terms of revenue, approximately [X] of Headlam's sales are to commercial customers while [X] are to retail customers. The turnover of Headlam in the financial year ending 31 December 2018 was approximately £604 million in the UK.
9. Garrod Bros is a distributor of flooring materials, predominantly non-carpeting products, in the South East of England and in London. The turnover of Garrod Bros in the financial year to 28 February 2018 was approximately £[X] million in the UK.

### **Transaction**

10. Headlam acquired Garrod Bros (London) Ltd's business of distribution of floorcovering materials on 26 October 2018.
11. Internal documents from Headlam state that the rationale for the transaction was to:
  - (a) [X];
  - (b) [X];
  - (c) [X]; and
  - (d) [X].
12. The Parties submitted that Garrod Bros' [X]

## Procedure

13. The CMA's mergers intelligence function identified this transaction as warranting an investigation.<sup>2</sup>
14. The Merger was considered at a Case Review Meeting.<sup>3</sup>

## Jurisdiction

15. Each of Headlam and Garrod Bros is an enterprise. As a result of the Merger, these enterprises have ceased to be distinct.
16. The share of supply test under section 23(2)(b) of the Act is met because the Parties' combined share of supply of palletised goods to contractors in North London is higher than 25% (by value, 2017, with an increment of more than 5%).
17. The Merger completed on 26 October 2018 and the CMA was first informed about it on 30 October 2018. The four month deadline for a decision under section 24 of the Act is 21 April 2019, following an extension under section 25(2) of the Act.
18. The CMA therefore believes that it is or may be the case that a relevant merger situation has been created.
19. The initial period for consideration of the Merger under section 34ZA(3) of the Act started on 11 February 2019 and the statutory 40 working day deadline for a decision is therefore 5 April 2019.

## Counterfactual

20. The CMA assesses a merger's impact relative to the situation that would prevail absent the merger (ie the counterfactual). For completed mergers the CMA generally adopts the pre-merger conditions of competition as the counterfactual against which to assess the impact of the merger. However, the CMA may also assess a completed merger against an alternative counterfactual where, based on the evidence available to it, it believes that, in the absence of the merger, the prospect of these conditions continuing is not

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<sup>2</sup> See [Mergers: Guidance on the CMA's jurisdiction and procedure](#) (CMA2), January 2014, paragraphs 6.9-6.19 and 6.59-60.

<sup>3</sup> See [Mergers: Guidance on the CMA's jurisdiction and procedure](#) (CMA2), January 2014, from paragraph 7.34.

realistic, or there is a realistic prospect of a counterfactual that is more competitive than these conditions.<sup>4</sup>

21. Headlam submitted that the owners of Garrod Bros had intended to exit the business, and that if Headlam had not purchased the business, it would likely have continued under different ownership. The CMA therefore considered whether there is a realistic prospect that there would have been an alternative owner of Garrod Bros, absent the Merger, and whether this would have been more competitive than the pre-merger conditions of competition.
22. The CMA considered that the available evidence, including evidence relating to recent market developments and submissions from a number of third parties, indicated that Garrod Bros would have been purchased by an alternative purchaser absent the Merger. The CMA found that certain players active at a national or regional level would have been plausible alternative purchasers for the Garrod Bros business. The CMA considers that this would have been more competitive than the prevailing conditions of competition because it could have enabled the purchaser to compete more effectively (including against Headlam) at the national or regional level (for the reasons explained further in paragraphs 88 to 112 below).
23. The CMA has, however, not been required to conclude on whether a more competitive counterfactual is realistic because, for the reasons explained below, the Merger does not give rise to competition concerns on any plausible basis (including if a more competitive counterfactual were to be adopted).
24. In reviewing mergers at phase 1, the CMA may be required to consider a merger at a time when there is the prospect of another merger in the same market (a parallel transaction). The CMA is likely to consider whether the statutory test for reference would be met whether or not the parallel transaction proceeds (unless the parallel transaction can clearly be ruled out as too speculative).
25. Headlam acquired Rackhams on 28 September 2018. This transaction and the Merger are not conditional on each other. Headlam's acquisition of Rackhams has been completed and the CMA has cleared Headlam's acquisition of this business. The CMA has therefore assessed the Merger against a counterfactual in which Headlam owns Rackhams.

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<sup>4</sup> [Merger Assessment Guidelines](#) (OFT1254/CC2), September 2010, from paragraph 4.3.5. The [Merger Assessment Guidelines](#) have been adopted by the CMA (see [Mergers: Guidance on the CMA's jurisdiction and procedure](#) (CMA2), January 2014, Annex D).

## Background

26. The flooring market in the UK involves a significant number of companies operating at different levels of the supply chain. Flooring enters the market through both UK-based manufacturers and importers who supply distributors. In some circumstances manufacturers supply contractors, retailers and end users directly.
27. Distributors, such as Headlam, distribute manufacturers' products and own-brand products to contractors and retailers. Typically, contractors operate in the commercial flooring market, supplying commercial customers (such as building companies, property developers and public authorities) while multi-site retailers and independent retailers supply and fit domestic flooring.

## Frame of reference

28. Market definition provides a framework for assessing the competitive effects of a merger and involves an element of judgement. The boundaries of the market do not determine the outcome of the analysis of the competitive effects of the merger, as it is recognised that there can be constraints on merging parties from outside the relevant market, segmentation within the relevant market, or other ways in which some constraints are more important than others. The CMA will take these factors into account in its competitive assessment.<sup>5</sup>
29. The Parties overlap in the supply of flooring in the UK.

## Product scope

30. The Parties overlap in the supply of palletised flooring to independent contractors.<sup>6</sup>

### *The Parties' submissions*

31. Headlam submitted that the appropriate frame of reference for the assessment of the Merger should be the overall supply of flooring in the UK, including not only the wholesale supply of flooring, but also the other routes to end customers (see paragraph 28 above).
32. In particular, Headlam submitted that the supply of flooring should not be segmented by distribution type, because the distribution route which Headlam

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<sup>5</sup> [Merger Assessment Guidelines](#), paragraph 5.2.2.

<sup>6</sup> Garrod Bros does not make material sales to retailers.

offers represents only one of the routes to market. Headlam stated its offer to its customers is constrained by other distribution routes to customers, including:

- (a) Direct sales by floorcoverings manufacturers to retailers who compete with its retailer customers;
  - (b) Manufacturers supplying direct to Headlam's core (independent) retail and contractor customer base;
  - (c) Larger contractor groups who source direct from manufacturers (at least for Headlam's contractor customers); and
  - (d) Online sale of flooring (which Headlam submits are increasing).
33. For the reasons explained below, however, the evidence that the CMA has received indicates that it is appropriate to distinguish between: (i) the supply of flooring based on the format in which the products are distributed (ie broadloom and palletised products), (ii) the type of customer (eg independent flooring retailers, contractors and multi-site retailers), and (iii) the supply of flooring by distributors as distinct from other routes to customers.

#### *Broadloom versus palletised flooring*

34. From a demand-side perspective, customers will substitute between flooring products to the extent that they consider them alternatives. Although some flooring products may be alternatives to each other (for example, a consumer may consider switching between laminate and wood flooring), many flooring products have very distinct purposes. For example, underlay and adhesives which are used to lay flooring cannot be substituted for top surface products such as carpet. Even between different top surface flooring products such as carpet and ceramic tiles, customers may have strong preferences for specific product types for particular purposes. For example, tiles or other types of hard flooring are more appropriate for kitchens, as they are easier to clean.
35. While there is very limited demand-side substitution between the different types flooring, the CMA has assessed whether flooring can be aggregated on the basis of supply side considerations.
36. Flooring wholesalers typically stock several types of flooring. The CMA found that flooring can be aggregated from a supply-side perspective into two main categories:
- (a) Broadloom flooring, which is distributed in rolls, such as carpets and vinyl; and

(b) Palletised flooring, which is distributed in pallets, and which includes all other flooring products, including laminates, wood, ceramics and accessories.

37. Several third parties explained that broadloom flooring and palletised flooring use different storage systems, and require different warehousing. The CMA has found that several key suppliers of palletised flooring do not make significant sales of broadloom flooring (for example, the Brookvale Group's London depots); vice versa, several suppliers are much more focused on supplying palletised flooring than broadloom flooring, and have a more limited range of palletised flooring as a result. Accordingly, the CMA has found that the conditions of competition in palletised and broadloom flooring are different.
38. The CMA has therefore found that it is appropriate to distinguish between the wholesale supply of broadloom flooring and the wholesale supply of palletised flooring.

*Independent flooring retailers, contractors and multi-site retailers*

39. Headlam's management divides its business into two types, and a Headlam internal document states that 'the market is segmented between the residential and commercial sectors'. The 'residential' sector involves the wholesale supply to retailers for sale to end consumers, while the 'commercial' sector involves wholesale supply to contractors fitting out new housing developments and offices, for example.
40. From a demand-side perspective, retailers and contractors typically purchase different products. In particular, retailers purchase broadloom products, while contractors rarely do; similarly, contractors have demands for safety matting, carpet tiles and other products which are rarely sold to retailers.
41. The available evidence also indicated that the scope for supply-side substitution by distributors between supplying retailers and contractors is likely to be limited. Many suppliers of commercial flooring make some palletised sales to retailers. However, distributors that supply both broadloom and palletised flooring to independent retailers tend to make very few sales to contractors (if any at all).
42. Accordingly, for the reasons set out above, the CMA considers that it is appropriate to distinguish between the wholesale supply of flooring to contractors, and the wholesale supply of flooring to other types of customers.



### *Distributors versus other routes to market*

43. Evidence submitted by third parties indicates that, at least for independent retailers and contractors, supply by manufacturers is not a close alternative to the supply by a flooring distributor.
44. In particular, when presented with a multiple-choice question which asked customers what they would do if their current distributor of flooring were to raise its prices by 5%, the majority of customers (contractors) that responded to the CMA's questionnaire did not indicate that they would 'buy from manufacturers'. While some customers noted the possibility of purchasing from manufacturers. Three customers said that if possible they would buy from manufacturers, others noted the longer delivery times (which are typically between 3-7 days), or the lack of accessories offered by manufacturers.
45. Some third parties also suggested that manufacturers are wary of harming their relationship with distributors when approached by customers (with one customer submitting that it was, as a result, effectively 'impossible' to buy directly from some manufacturers).
46. The CMA also notes that some customers may have certain requirements (such as for next day delivery) that are not met by manufacturers without a distribution network. The AMA Research's 2018 Floorcoverings Report notes that for small commercial projects, direct supply is not a major distribution route, "with smaller operators relying on local and regional distributors/wholesalers".
47. Therefore, the CMA has distinguished between the supply of flooring by manufacturers and distributors and, as the Parties only overlap in the distribution of flooring, assessed the effect of the Merger at distribution level.
48. To the extent that manufacturers have distribution network, and offer a comprehensive range of brands, this has been taken into account within the CMA's competitive assessment.
49. To the extent that manufacturers supply multi-site retailers, and these multi-site retailers compete with the Parties' customers (ie contractors), this limits the ability of the Parties to worsen their terms to their customers. Therefore, the CMA has considered supply from manufacturers and multi-site retailers as an out-of-market constraint, to the extent relevant, within its competitive assessment.

### *Conclusion on product scope*

50. For the reasons set out above, the CMA has considered the impact of the Merger in relation to the wholesale supply of palletised flooring to contractors.<sup>7</sup>

### **Geographic scope**

51. Based on customer postcodes for Garrod Bros' sales in November 2018, Garrod Bros makes 80% of its delivered sales within [redacted] miles of its depot.
52. The CMA understands that Garrod Bros primarily serves customers within the M25, as reflected by these sales figures.
53. The short delivery distance may be reflected by the fact that Garrod Bros has a relatively small fleet of three delivery vehicles. Alternatively, this may be explained by the fact that palletised goods are heavier than broadloom products, and therefore costlier to transport, and/or by the fact that palletised goods are low margin products, relative to broadloom products, and transport costs are a relatively high proportion of their overall sales value.
54. Evidence from Headlam's internal documents also suggests that it views the M25 as a distinct geographic area. For instance: the 'prework strategy' email from Headlam's former chief of operations under the heading "M and A / Market Consolidation" lists "Commercial product distribution (within M25 and Nationally)" as relevant markets.
55. Another internal document from Headlam states the rationale for the Merger as: '[redacted]'. This suggests an even narrower frame of reference than the M25 may be applicable.
56. Given Garrod Bros' sales focus and evidence from third parties and internal documents, the CMA, at this stage, will assess the effects of the Merger in relation to the supply of palletised goods to contractors within the M25.
57. Given the national scale of Headlam and the prospect that the acquisition Garrod Bros could have formed part of the strategy to enable an alternative purchaser to compete more effectively at a national or regional level, the CMA has also assessed the effects of the Merger on the supply of palletised flooring across the UK.

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<sup>7</sup> Garrod Bros does not supply broadloom products or palletised goods to independent retailers in material quantities.

### *Conclusion on geographic scope*

58. For the reasons set out above, on a cautious basis the CMA has considered the impact of the Merger in the following geographic frames of reference:
- (a) the wholesale supply of palletised flooring to contractors within the M25 area; and
  - (b) the wholesale supply of palletised flooring to contractors in the UK.

### *Conclusion on frame of reference*

59. For the reasons set out above, the CMA has considered the impact of the Merger in the following frames of reference:
- (a) the wholesale supply of palletised flooring to contractors within the M25 area; and
  - (b) the wholesale supply of flooring to contractors in the UK.

## **Competitive assessment**

60. Horizontal unilateral effects may arise when one firm merges with a competitor that previously provided a competitive constraint, allowing the merged firm profitably to raise prices or to degrade quality on its own and without needing to coordinate with its rivals.<sup>8</sup> Horizontal unilateral effects are more likely when the merging parties are close competitors. The CMA has assessed whether it is or may be the case that the Merger has resulted, or may be expected to result, in an SLC as a result of:
- (a) Horizontal unilateral effects in the wholesale supply of palletised flooring to contractors, in the M25; and/or
  - (b) A loss of dynamic competition in the supply of palletised flooring to contractors across the UK, in particular by hindering the entry and/or expansion of a competitively significant force.

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<sup>8</sup> [Merger Assessment Guidelines](#), from paragraph 5.4.1.

***Horizontal unilateral effects in the wholesale supply of palletised flooring to contractors in the M25***

61. The concern under this theory of harm is that the removal of one party as a competitor could allow the Parties to increase prices, lower quality and/or reduce the range of their products and/or services.
62. In order to assess the likelihood of the Merger resulting in unilateral effects, the CMA has considered:
  - (a) Shares of supply within the Parties' catchment areas;
  - (b) The closeness of competition between the Parties; and
  - (c) Competitive constraints from alternative suppliers.

***Parties' submissions***

63. Headlam submitted that there are no particular features that distinguish the Parties from any other rivals and make them close competitors. The Parties stated that the vast majority of wholesale distributors in the UK offer to contractors a broad range of products, credit and next day delivery.
64. Headlam noted that the increment resulting from the transaction is moderate, even based on the shares estimated in Table 1, and that Garrod Bros' share is likely to be overstated.
65. Headlam also identified at least five active rivals in this market, including Brookvale which has a share of [40-50%] and three other competitors (STS, PFC Flooring and Carpets & Flooring) with a market share of at least 5%.
66. Headlam stated that there are other suppliers present within the M25 (and indeed located close to the Parties) who also supply palletised flooring to contractors such as Columbia Flooring and International Decorative Surfaces.

***Shares of supply***

67. Table 1 below shows the CMA's estimates of shares of each of the Parties and other wholesale suppliers of palletised flooring to contractors, in the M25, based on value of sales data provided by the Parties and the other suppliers.

**Table 1: Estimated share (by 2017 sales revenue) in the wholesale supply of palletised flooring to contractors, in the M25<sup>9</sup>**

Competitor	Shares of supply
<i>Garrod Bros</i>	[5-10]%
<i>Headlam</i>	[20-30]%
<b>Combined</b>	<b>[20-30]%</b>
Brookvale (Planners, Volante)	[40-50]%
STS	[10-20]%
PFC Flooring	[5-10]%
Carpet and Flooring	[5-10]%
Valley Wholesale	[0-5]%

**Source:** CMA's estimates based on the Parties and third parties' sales revenue estimates

68. The merged entity would be one of the three main providers of supplies of palletised flooring to contractors in London, with a combined share of [20-30]%, with the Merger resulting in an increment [5-10]%.
69. The CMA notes that Garrod Bros is a relatively small distributor and the increment in market share as a result of the Merger is very limited.

*Closeness of competition*

70. The CMA has examined the closeness of competition between the Parties and considered within the assessment:
- (a) Similarity of the Parties' service propositions;
  - (b) Geographic proximity between the Parties and their competitors;
  - (c) Third party views on closeness of competition; and
  - (d) Internal documents.

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<sup>9</sup> These market shares have been constructed from the responses of Headlam and third parties, based on the sales of depots within Garrod Bros' catchment area. Where only aggregate sales information has been provided (rather than depot-level information), sales have been divided evenly between a supplier's depots.

### *Service propositions*

71. Garrod Bros and Ashmounts (Headlam's closest depot which specialises in supplying commercial flooring) each make deliveries, operate trade counters and stock a similar range of product types. Each makes a little over half its sales to collection customers.

### *Geographic proximity*

72. Headlam is in close proximity to Garrod Bros in North London. In particular, Garrod Bros is in close proximity to Ashmounts, in Enfield.
73. The geographic proximity of the Parties is a strong indication of closeness of competition, in particular, because most of the sales of both Ashmounts and Garrod Bros are collected. Contractors who wish to compare prices between the Parties can easily do so and may be less willing to travel to collect flooring products from a more distant competitor.
74. Brookvale is the next closest competitor, with a warehouse in Islington in relatively close proximity to the Parties' depots.

### *Third party view on closeness of competition*

75. Several third parties that responded to the CMA's questionnaire identified the Parties as competitors.
76. Third party submissions also highlighted the importance of geographic proximity, and that the Parties are particularly close competitors:
- (a) one customer of Garrod Bros said that Brookvale's Planners depot would be their only alternative for local collection, post-merger;
  - (b) multiple third parties identified the Parties as close competitors;
  - (c) a customer from Garrod Bros only identified Headlam and two other competitors as alternative suppliers to Garrod Bros; and
  - (d) one third party stated that for London based distributors travel is more difficult and that distributors outside London will not distribute to central London.

### *Internal documents*

77. Some Headlam documents show a degree of competitive interaction between the Parties (such as one document provided to the CMA which showed that a customer requested quotes from Headlam, Garrod and one other competitor).

### *Competitive constraints*

78. Unilateral effects are more likely where customers have little choice of alternative supplier. The CMA considered whether there are alternative suppliers which would provide a competitive constraint on the combined entity.
79. The Parties face competition within the M25 from a number of competitors. This includes the market leader, Brookvale, as well as STS, PFC and Carpet and Flooring.
80. Therefore, the CMA considers that the Parties face significant competitive constraints from Brookvale and STS and at least three (albeit smaller) competitors.

### *Out of market constraints*

81. The Parties submitted that they also face significant competitive constraints from manufacturers, and from suppliers located outside M25.
82. The CMA notes that the Parties may be constrained by manufacturers without a developed distribution network. AMA Research's 2018 Floorcoverings Report notes that manufacturers often directly supply large commercial projects.
83. While there may be out-of-market constraints on the Parties from manufacturers and from competitors outside of the frame of reference, the CMA has not needed to conclude on the strength of these constraints, as it has found that sufficient competitive constraints will remain post-Merger from direct competitors to the Parties within the geographic market.

### *Third party views*

84. The majority of customers that responded to the CMA's questionnaires did not raise concerns around this market.

### *Conclusion on horizontal unilateral effects*

85. For the reasons set out above, the CMA believes that, while there is a significant degree of competitive interaction between the Parties, the overall change in market structure brought about by the Merger is limited (in particular because the increment in share of supply is small) and that the merged entity will continue to be constrained by a sufficient number of credible competitors. Accordingly, the CMA has found that the Merger does not give rise to a realistic prospect of an SLC as a result of horizontal unilateral effects in relation to the wholesale supply of palletised flooring to contractors in the M25.

### ***Dynamic effects in the wholesale supply of flooring in the UK***

86. The CMA has assessed whether the Merger may result in a loss of dynamic competition in the supply palletised flooring to contractors across the UK, in particular by hindering the entry and/or expansion of a competitively significant force.
87. The concern under this theory of harm is that Headlam's acquisition of Garrod Bros may block or deter the entry and or expansion of a competitor that, absent the Merger, might have acquired Garrod Bros, and, by achieving a wider coverage and benefiting from economies of scale, would compete more effectively with Headlam on a regional or national basis.
88. In assessing this theory of harm, the CMA has considered:
- (a) Evidence relating to the current conditions of competition at a national and regional level;
  - (b) Whether Garrod Bros would have been acquired by a competitor, absent the Merger; and
  - (c) Whether Garrod Bros is a strategically significant asset that could have a material impact on a supplier's ability to compete, in particular through entry or expansion, at the national or regional level.

### *Parties' submissions*

89. Headlam submitted that the Merger will not hinder the entry or expansion by other competitors looking to expand, mainly because:
- (a) Headlam does not have market power at a national level;
  - (b) There is no evidence of any exclusionary intent in any of Headlam's internal documents relating to the Merger;



- (c) There are multiple opportunities for other suppliers to expand in London, either through acquisition or organic growth;
- (d) Garrod Bros is not significant enough to form an important route to expansion on a national basis. It does not have any particular characteristics which indicate that a third party unable to acquire Rackhams and/or Garrod Bros would find it more difficult to expand in national terms; and
- (e) The fact that one of the Parties' national competitors, Likewise, has acquired a business in London since the completion of the Rackhams and Garrod Bros acquisitions shows that Headlam's acquisitions have represented no bar to a national competitor seeking to expand its presence

#### *Conditions of competition at the national or regional level*

90. The CMA first assessed whether the entry or expansion of an additional competitor at the national or regional level would be liable to lead to greater competition within that segment. In assessing competitive conditions within this segment (and, in particular, whether Headlam may face limited competition nationally or in some regions), the CMA considered three main sources of evidence:
- (a) Headlam's nationwide shares of supply, based on figures provided in the AMA Floorcoverings Report and Headlam's own estimates;
  - (b) Headlam's internal documents; and
  - (c) Third party views.

#### *Shares of supply*

91. The Parties submitted that Headlam has a [%] market share in the supply of all UK flooring, on the basis of its £400m in purchases. The CMA noted, however, that these estimated (which the CMA understands were produced for the purposes of the Merger investigation) were not consistent with evidence from Headlam's internal documents, which suggested that Headlam's market share at a national level - at [%] (rising from [%] five years ago) – was materially higher.
92. The Parties submitted that Headlam's market share in the supply of flooring to contractors in the UK is 10-20%. However, the CMA considers that this is likely to significantly underestimate Headlam's share of supply for two reasons:

- (a) They are based on manufacturers' shares of supply, or (equivalently) distributors' shares of purchases. Given Headlam's size, it is likely able to exert some buyer power, reducing its purchase prices relative to those of competitors. Indeed, its 2017 Annual Report notes that it experiences 'purchasing economies of scale'.<sup>10</sup> Its share of sales is therefore likely to be slightly higher.
- (b) Headlam's estimate includes direct supply from manufacturers. Although the CMA accepts that direct supply may be appropriate for some customers, the CMA has not included it in the relevant market, as manufacturers are unlikely to be well placed to supply contractors working on smaller projects (which Headlam is better placed to supply).

93. On this basis, the CMA considers that the shares of supply submitted by Headlam are likely to materially underestimate its position at the national level.

#### *Headlam's internal documents*

94. Headlam's internal documents, repeatedly describe its 'dominance' and 'market-leading position' (albeit without identifying any specific segments within which it considers that its position is particularly strong). For example:
- (a) *Headlam's* 2017 annual report notes its 'market-leading position, significant scale and longevity of operations', commenting that its 'nearest competitors [are] currently approximately 1/6th of [Headlam's] size in terms of revenue'.
  - (b) Headlam's 2018 interim report describes Headlam as 'Europe's largest distributor of floorcoverings'.
  - (c) An email from Headlam's internal management describes its '[redacted]
95. Together, these documents demonstrate that Headlam considers itself to be a market leader.

#### *Third party views*

96. Several third parties described Headlam as dominating the market. Competitors commented that Headlam's buying power made it difficult to compete with, except to the extent that its high margin expectations allowed them to compete on price.

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<sup>10</sup> Annex 01(c)(ii), annex to response to Section 109 received on 17 December 2018.

97. Several third parties told the CMA that Headlam had increased its prices since 2016 by setting strict guidelines for its branches, to prevent them from competing with each other, in contrast to previous practice within Headlam. As noted in paragraph 112, the evidence from third parties indicated that there are significant barriers to entry in this market.

#### *Conclusion on Headlam's market position*

98. The CMA considers that the above evidence suggests that there is a realistic prospect that Headlam faces limited competition in one or more flooring distribution markets in the UK.

#### *Whether Garrod Bros would have been acquired by a competitor, absent the Merger*

99. As explained above in the Counterfactual section (see paragraphs 20 to 25 above), the CMA considered evidence relating to recent market developments and submissions from a number of third parties. The CMA found that certain players active at a national or regional level would have been plausible alternative purchasers for the Garrod Bros business. The CMA considers that this would have been more competitive than the prevailing conditions of competition because it could have enabled the purchaser to compete more effectively (including against Headlam) at the national or regional level.

#### *Strategic significance of Garrod Bros to entry or expansion*

100. A Headlam strategy document notes that it is [REDACTED].
101. Multiple third parties told the CMA that they believed that the rationale for the acquisition of Garrod Bros was to stop a competitor from acquiring it.
102. [REDACTED]. However, the CMA considers that whether or not there was exclusionary intent is not the correct framework – the important consideration is the *effect* of the Merger.
103. The CMA currently considers that there is evidence that economies of scale are important for the competitiveness of flooring distributors in terms of (i) purchasing power, (ii) economies of density, and (iii) geographic reach.
104. Economies of scale are potentially beneficial if passed on to customers. However, if one large supplier prevents its competitors from also benefitting from scale economies through acquisitions, this could weaken competitive constraints on the large supplier.
105. In considering the impact of the Merger on a prospective purchaser's ability to compete with Headlam dynamically, the CMA has assessed the importance of

Garrod Bros for the expansion of a competitors in order to become an effective competitor regionally or at national level, given these economies of scale in the supply of flooring.

106. Headlam's internal documents repeatedly imply that it is very difficult and would take a long time for a competitor to achieve organically a distribution network similar to Headlam's current network, by virtue of its size:
- (a) Headlam's 2017 Annual Report notes that 'the Company's extensive distribution network has been established over the last 25 years through considerable financial investment and technical and operational expertise, and represents a significant barrier to entry to competitors and potential new entrants. It currently comprises over 67 million cubic feet of warehouse capacity and its value is underpinned by property, plant and equipment assets totalling £101.6 million'. Similarly, the Annual Report notes that Headlam's distribution network would take 'significant time and resources to replicate'. A statement by its Chairman repeats that there are 'significant barriers to entry created through years of investment and development of operational expertise'.
- (b) A document describing '[REDACTED]'.<sup>11</sup>
107. This is supported by evidence from Headlam's internal documents, which indicate that the main route to expansion at the level would be through acquisition. For example, a Headlam strategy document notes that it is '[REDACTED]'.<sup>11</sup>
108. The evidence on whether Garrod Bros is a strategically significant asset within the context of a national or regional expansion strategy is mixed:
- (a) While Garrod Bros itself is a well-established business in the distribution of palletised flooring to contractors, it ultimately accounts for only a small part of the local and national market. The most important factor in expansion is achieving scale and access to a relevant network. Garrod Bros' sales constitute a very small part of the UK market and, given its size and limited network, Garrod Bros' acquisition would not have a material impact on a competitor's ambitions of achieving scale.
- (b) A Headlam board paper notes that "[REDACTED]."
109. For the reasons given above, the CMA considers that there is no realistic prospect that the acquisition of Garrod Bros would be of strategic importance

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<sup>11</sup> ('Updated Strategy', November 2018).

for a competitor's ability to gain scale and compete effectively at national or regional level.

### *Conclusion on dynamic effects in the wholesale supply of flooring in the UK*

110. For the reasons set out above, the CMA believes that Headlam faces limited competition in the supply of flooring in the UK. There is a realistic prospect that Garrod Bros would have been acquired by other flooring wholesaler. While there are significant economies of scale in this market, which are important for a wholesale supplier to become an effective competitor, and there are competitors looking to expand through acquisition, the purchase of Garrod Bros would not be strategically important for this expansion. Accordingly, the CMA found that the Merger does not give rise to a realistic prospect of an SLC as a result of dynamic effects in the wholesale supply of palletised flooring to contractors in the UK.

### **Barriers to entry and expansion**

111. Entry, or expansion of existing firms, can mitigate the initial effect of a merger on competition, and in some cases may mean that there is no SLC. In assessing whether entry or expansion might prevent an SLC, the CMA considers whether such entry or expansion would be timely, likely and sufficient.<sup>12</sup>
112. The evidence from third parties does not indicate that entry or expansion will be timely, likely or sufficient to mitigate any SLC arising.
113. Evidence from Headlam's internal documents also show that there are high barriers to entry in the wholesale flooring distribution sector, as described above.
114. Therefore, the CMA believes that there could be significant barriers to entry and expansion in the wholesale supply of flooring in the UK.
115. However, the CMA has not had to conclude on barriers to entry or expansion as the Merger does not give rise to competition concerns on any basis.

### **Third party views**

116. The CMA contacted customers, manufacturers and competitors of the Parties. Some customers and competitors raised concerns regarding the Merger's

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<sup>12</sup> [Merger Assessment Guidelines](#), from paragraph 5.8.1.

impact on choice, the impact more generally on competition and that Headlam appear to be buying a lot of local companies.

117. Third party comments have been taken into account where appropriate in the competitive assessment above.

## **Decision**

118. Consequently, the CMA does not believe that it is or may be the case that the Merger has resulted, or may be expected to result, in an SLC within a market or markets in the United Kingdom.

119. The Merger will therefore **not be referred** under section 22(1) of the Act.

**Colin Raftery**  
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**Competition and Markets Authority**  
**28 March 2019**