



**FOOTASYLUM** 

**JD SPORTS / FOOTASYLUM  
RESPONSE TO THE PROVISIONAL FINDINGS**

**SUBMITTED ON BEHALF OF JD SPORTS FASHION PLC  
& FOOTASYLUM LIMITED**

**9 MARCH 2020**

<b>EXECUTIVE SUMMARY</b>	<b>1</b>
I. Introduction: a dynamic competitive backdrop and pro-competitive Merger rationale	1
II. The central finding of the PFs is implausible	2
III. Conclusion: flawed in the round assessment and erroneous application of the SLC test	8
<b>CHAPTER 1 THE USE AND MISUSE OF QUANTITATIVE TOOLS TO PREDICT SLC: GUPPI, SURVEYS, MARKET SHARES</b>	<b>10</b>
I. Introduction and Summary	10
II. In giving undue and decisive SLC weight to a static GUPPI model, the PFs engage in a serious misreading of all other evidence to 'fit' SLC	12
III. Beyond the inherent unsuitability of GUPPI, there are specific problems with the CMA's survey diversion ratios: they are hypothetical, likely biased and used as a trump card on other evidence	20
IV. Proper evaluation of all the 'non-GUPPI' evidence points to no SLC	30
<b>CHAPTER 2 REPOSITIONING AND EXPANSION POINT TO NO SLC</b>	<b>31</b>
I. Introduction	31
II. Repositioning and expansion by SDI point to no SLC	32
III. Brands' DTC expansion points to no SLC	41
IV. Other market dynamics are not properly accounted for	43
<b>CHAPTER 3 THE COUNTERFACTUAL</b>	<b>46</b>
<b>CHAPTER 4 SUPPLIER CONSTRAINTS POINT TO NO SLC</b>	<b>61</b>
I. Overview	61
II. The PFs address the wrong question	61
III. The PFs apply the wrong test	61
IV. The PFs' analysis of supplier constraints is misdirected and incomplete	61
V. The PFs fail to take into account relevant evidence and misinterpret evidence	62
VI. The PFs reach the wrong conclusion	64
<b>CHAPTER 5 INTERNAL DOCUMENTS AND ECONOMETRIC EVIDENCE DO NOT SUPPORT AN SLC ON ANY IDENTIFIED PARAMETER OF COMPETITION</b>	<b>65</b>
I. Overview	65
II. The assessment of the Parties' approach to competitor monitoring is flawed	67
III. The claim in the PFs that certain documents show that monitoring was followed by competitive responses is flawed	70
IV. The PFs cite no evidence to support the proposition of significant bilateral interaction between the Parties on any identified parameter of competition	71
V. Price parameters	77
VI. Non-price parameters	80
<b>CHAPTER 6 THE CMA DOES NOT TAKE PROPER ACCOUNT OF EXPECTED EFFICIENCIES</b>	<b>84</b>

## EXECUTIVE SUMMARY

### EXECUTIVE SUMMARY

- (1) This submission sets out the response of JD Sports Fashion plc (“**JD Sports**” or “**JD**”) and Footasylum Ltd (“**Footasylum**” or “**FA**”) (together, the “**Parties**”) to the CMA’s Provisional Findings (“**PFs**”) that the acquisition of Footasylum by JD Sports (the “**Merger**”) provisionally results in an expectation of a substantial lessening of competition (“**SLC**”) in the markets for sports-inspired casual footwear and apparel in the UK, respectively, under section 35(1)(b) of the Enterprise Act (the “**Act**”) (the “**Response**”).

#### I. Introduction: a dynamic competitive backdrop and pro-competitive Merger rationale

- (2) JD Sports and Footasylum operate in a dynamic and crowded marketplace of competing retailers. In addition to intense existing competition, the markets in which the Parties operate are subject to dynamic and volatile demand, competitive disruption and the strengthening of aggregate competitive constraints in the form of supplier-enabled expansion and repositioning by, amongst others, Sports Direct International / Frasers Group (“**SDI**” or “**SDI / USC**” or “**SDI / Frasers Group**”) via its elevation strategy and Nike’s and adidas’ own direct to consumer channels (“**DTC**”).
- (3) This scale of competitor expansion and elevation (or “repositioning”) is, on those third parties’ own information, large relative to the small scale of Footasylum (which, on the CMA’s own calculations, has a small share of around, at most, 5% in footwear and apparel).
- (4) Furthermore, this share does not capture that Footasylum was, at best, [REDACTED] prior to the Merger with three profit warnings during 2018/2019. It was [REDACTED] and, as a result, not in a position to [REDACTED].
- (5) The unique degree of control and influence of the brands that supply the Parties – primarily Nike and adidas – is fundamental to a proper understanding of the constraints that discipline against a worsening of the retail offer at either Party’s fascia, pre and post-Merger. Again, the Parties and third parties, including the key brands, have submitted evidence clearly showing that the brands provide a very strong incentive on the Parties to maintain and elevate the quality of the retail offer (which makes sense given the brand’s own interest in their premium brand equity). They have both the ability and incentive to prevent any hypothetical deterioration of “price, quality, range or service” (“**PQRS**”) post-Merger via allocation of product franchises and lines (which they “turn on or off”) and volume of stock (which they can “dial up or down”), that is, calibrate what they give to retailers to achieve the outcome most consistent with their overall commercial interest (including brand perception). The strong growth in DTC – large relative to Footasylum’s sales – further enhances the brands’ ability and incentives to discipline a worsening retail offer of the Parties post-Merger.
- (6) The Merger would result in considerable consumer benefits. These include stabilising the Footasylum business and ensuring the continued employment of its staff; retaining critical supply of Nike and adidas branded products; maintaining and improving the “front-end” customer-facing aspects i.e. the differentiated “DNA” of Footasylum that drove the Merger rationale; extending to Footasylum JD Sports’ operational and digital / multichannel platform expertise; investment into Footasylum’s existing fashion brands and the development of new own-label and bedroom brands, including the ability to offer Footasylum brands in JD Sports’ international network (enabling return on investment to develop brands further within the UK); and improvements to the efficiency of Footasylum’s operations by putting to work JD Sports’ best of breed back office, technology, logistics and infrastructure platform.
- (7) These benefits to customers will be lost if the erroneous approach of the PFs were crystallised in the CMA’s final report.

## EXECUTIVE SUMMARY

### II. The central finding of the PFs is implausible

- (8) Despite the backdrop described above, the CMA concludes in the PFs that “*the merger removes a direct and significant constraint on each of the Parties, resulting in substantially less competition on price, quality, range and service (“PQRS”) and a weaker incentive to improve as much as they would otherwise*”. This conclusion applies to each of JD Sports and Footasylum, to footwear and apparel, and to online and in-store.
- (9) This finding is wrong and not borne out by the evidence provided to the CMA.
- (10) In effect, the CMA’s PFs position the supply of athleisure in the UK (or in the CMA’s terminology “sports-inspired casual footwear and apparel”), as a two-horse race between JD Sports and Footasylum (a retailer in a [X] prior to the Merger), and considers retailers such as SDI, with UK turnover almost 10 times that of Footasylum, to provide relatively limited constraint. The PFs reach the wrong outcome because of the following flaws in the CMA’s analysis (which apply to both apparel and footwear):

#### A. The CMA applies the wrong framework to consider competitive effects

- (11) A true reading of the PFs makes clear that once the CMA’s errors in relation to internal documents and entry / exit are corrected, the centrepiece of the PF’s SLC finding is based on a static model that fails to capture at all the relevant market dynamics. As the CMA’s CEO, Andrea Coscelli explained last week:

*Typically, we consider ‘static’ or recent evidence such as market shares, win/loss data and switching data as useful for many merger assessments as it is informative of competition in the near future. But in dynamic markets, this is not necessarily the case. As firms in dynamic markets are typically continuously evolving and releasing new products or services, historical or static data may not accurately reflect the changing market position.<sup>1</sup>*

- (12) In this case, Nike, adidas and many other brands are constantly releasing new products, which the Parties and their rivals constantly seek to acquire (by way of allocations) and resell (to consumers) in the most dynamic and relevant ways (increasingly online). The CMA’s PFs repeatedly recognise the market as “*dynamic*”, given rapid online growth and constantly-evolving “athleisure” fashion trends.
- (13) This context helps explain the Parties fundamental objection to the entire ‘static’ approach of the PFs. As set out in **Chapter 1** of this Response, the PFs place central reliance on a GUPPI model that is inherently static. In the words of the model’s authors it is a “*simple, initial screening device*” (Salop, Moresi), and one which focuses entirely on the demand side. The snapshot of a static GUPPI % is not capable of taking into account (a) the expansion, repositioning or entry rivals (either known, or as a credible threat); nor, in this case, two further critically-relevant factors, namely (b) Footasylum’s competitiveness in the counterfactual absent the Merger; and (c) the instrumental role of Nike, adidas and other suppliers in shaping these retail markets. In short, GUPPI does not capture pre-merger competition, including the central role of the brands in rewarding elevation (see e.g. SDI) and disciplining any degradation of PQRS. This is far from merely setting a “*minimum floor*” to PQRS (as the PFs assert with no evidence).
- (14) The approach of PFs is thus to miss a proper reflection of “how the market works”. It amounts to a GUPPI reflex of “*strong incentive to worsen PQRS*” (based in this case on “*survey says*”). This mechanical approach is at odds with real world evidence of how the Parties compete pre-Merger.
- (15) Indeed, as a dynamic prediction, the static GUPPI model inferences are already unrealistic when stress-tested against evidence of the reality of competition in this market, even for a couple of months. They are profoundly wrong given that this incentive “*to worsen*” is supposedly future-proof over a period of two

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<sup>1</sup> Speech given at *GCR Live: Telecoms, Media and Technology 2020*, 2 March 2020. Emphasis added.

## EXECUTIVE SUMMARY

years or more — as is necessarily implied by an SLC finding. This is despite the incentive “to worsen” allegedly operating in a market that started out as dynamic and intensely competitive at the beginning of the CMA’s Phase 2 inquiry, with those dynamics being fully evident in the last two months, as **Chapter 2** of this Response makes clear.

- (16) Whatever the GUPPI says, the merged entity will be spurred to improve its consumer offer not only by current dynamics but the prospect of future dynamics, which cannot be predicted precisely. The only conclusion available to the CMA on the evidence is that the relevant markets are, and will remain, highly dynamic. The CMA’s task is not to predict exactly how the market will evolve as nobody can and it misses the point: it is uncertainty which spurs retailers to keep improving their offers.
- (17) The PFs’ expectation of an SLC finding is centrally based on a static model (the GUPPI). While this approach is fundamentally problematic in and of itself for a dynamic supplier-shaped market, the Parties have serious additional concerns, beyond the core objection in principle. These relate to methods and measurement in this case, namely: (i) the use of a “now imagine” hypothetical-question survey as a critical basis for the GUPPI; and (ii) the particular unreliability of the store exit survey results, which are highly likely to be biased in favour of an SLC finding, given how the critical hypothetical question was phrased in conjunction with where and when it was asked. In addition, there can be no confidence that the GUPPI for JD Sports is above 5% (and may well be far below), which is not “high”, as the PFs allege; meanwhile, the GUPPI for Footasylum is liable to be materially overstated (and a static “Footasylum-only” worsened offer and an SLC also makes no sense in this case).

### **B. The PFs’ assessment of the current and dynamic constraints on the Parties is flawed and outdated due to errors of fact, and fails to consider relevant real-world evidence on rivals**

***First, the implausible conclusion that SDI, Foot Locker, Nike, adidas, ASOS ... Zalando are, collectively, “weak” or “limited” constraints that fail to prevent a SLC cannot be maintained***

- (18) On this critical finding, the PFs have thus far dismissed the full “Premier League” competitive opposition of all those that have since the outset (such as JD Sports), through to very recently, tried to capture a share of the growing demand for athleisure wear. This includes obvious UK and international retail heavyweights such as SDI and Foot Locker, brand-owner-and-supplier-and-retailers Nike and adidas (who favour their own DTC growth) and a jostling league table which, on an A to Z, starts with Amazon (to be ignored at a retailer’s peril, but is essentially ignored by the PFs)<sup>2</sup> and ASOS and includes Next, Office, Schuh ... Very ... through to Nike’s strategic online partner in Europe, Zalando.
- (19) All of these players, with the exception of Foot Locker in footwear, have been discounted as “weak” or “limited” constraints, or essentially disregarded entirely (such as Amazon), and the CMA claims it “cannot be sufficiently certain” that the expansion and repositioning of SDI and the brands’ DTC offerings will amount to a materially stronger competitive constraint on the Parties in the next few years.
- (20) These claims, already untenable, cannot be maintained in the light of new evidence now available to the CMA, set out in **Chapter 2** of this Response.

***Second, the CMA must now take account of critical new facts on Sports Direct [redacted] in the face of its £300m per annum elevation strategy***

- (21) The Parties have provided **new evidence** to the CMA in their response hearing of 2 March 2020 and in **Annexes 2.2.1 – 2.2.2** to this Response which incontrovertibly shows that in the last three months, SDI

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<sup>2</sup> The new material disclosed into the confidentiality ring on 6 March 2020 states at fns 262 and 519 [redacted]. However, searches on Amazon’s UK site on 8 March 2020 for “Nike trainers” and “adidas trainers” each returned over 20,000 responses.

## EXECUTIVE SUMMARY

has gained access to a wide range of “higher-tier” or “premium” sports-inspired casual products, including some of the Parties’ best-selling footwear franchises and apparel lines.

- (22) Accordingly, it follows that the CMA’s finding in paragraph 8.224 that “*While Sports Direct has had some limited improved access to higher tier products... this has almost exclusively been focussed on sports rather than sports inspired casual products*” represents an error of fact and cannot stand. The same is true for the provisional finding that the scope for the elevation strategy of SDI / USC to [REDACTED] given that “*a greater proportion of apparel sales come from a wide range of suppliers of branded products other than Nike and adidas*”. As demonstrated in this Response, SDI / USC itself has access to a wide range of branded suppliers other than Nike / adidas.
- (23) In addition, the Parties have provided ongoing factual evidence that the presence of SDI’s elevated stores are having a [REDACTED] It is notable that SDI/Frasers’ planned investment in its elevation strategy this year is equivalent to, if not greater than, Footasylum’s expected annual turnover.
- (24) Given this new evidence, the CMA must consider its own criterion for treating SDI as a key competitive constraint as met. In addition, the fact that the CMA’s conclusions about market developments in the PFs appear to be demonstrably wrong *within a matter of weeks* casts doubt on the CMA’s generally static approach to all prospective aspects of the competitive assessment. This necessarily leads to the conclusion that the PFs were wrong to claim a reliable foundation for a provisional expectation of an SLC.

### ***Third, the CMA’s findings in relation to DTC are illogical and flawed***

- (25) Material in the confidentiality ring shows that the brands project sales to [REDACTED] in the UK in the next few years. [REDACTED], the constraint posed by the aggregate DTC threat of Nike’s “*Consumer Direct Offense*”, together with comparable initiatives of adidas and other suppliers, appears to carry untenably little weight in the PFs consideration of an SLC. This is not explained and is contrary to all available industry commentary (and the brands’ own public statements as to strategic DTC ambition, direction and track record of successful growth).<sup>3</sup>
- (26) In addition to ignoring direct relevant evidence, there are four material flaws in the CMA’s assessment which are explained in detail in Annex 2.1:
- (a) First, the CMA inexplicably treats the DTC constraint as irrelevant as a constraint in-store because it is forecast to grow mostly online. This is entirely inconsistent with the PFs’ evidence-led finding that there is a single market encompassing online as a constraint on in-store channels (see paragraphs 7.47 and 7.89 of the PFs) and results in the illogicality that a constraint inside the market is attributed a weight of zero.
  - (b) Secondly, the PFs finding that “*the ratio of DTC sales to wholesale sales will not change significantly in the foreseeable future*” is inconsistent with the evidence provided by the Parties (which shows progressive disintermediation of the wholesale channel) and inconsistent with the evidence provided by the brands of recent DTC growth relative to wholesale revenues. These two facts cannot both be correct unless the inquiry is very coincidentally at a point of inflection where a ratio that has been growing stops and stays flat.
  - (c) Thirdly, the PFs fail to compare Nike’s stated UK DTC growth to Footasylum. Had this been done the CMA would have appreciated that Nike’s expected UK DTC growth will [REDACTED] times as large as

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<sup>3</sup> In addition to the previous submissions provided on this topic, the Parties note that on 18 February 2020 Nike announced the appointment of Heidi O’Neill, currently head of Nike Direct, as President of Consumer and Marketplace with effect from April 2020. As mentioned at JD Sports’ Response Hearing, Ms O’Neill played a large role in shaping the direction of Nike’s digital transformation, and her appointment aligns with the previous appointment of John Donahue, which was widely seen as an acceleration of Nike’s digital transformation given his technology background.

## EXECUTIVE SUMMARY

Footasylum's Nike sales within a year; and [X] times as large in 3 years. As a result any lost constraint from Footasylum relative to fast-evolving market dynamics is very small.

- (d) Finally, the evidence also demonstrates that the PFs reach a conclusion that will cease to be valid within two-three years. If Nike's forecasts are adopted and adidas' global DTC growth rate is applied to its UK sales, within three years Nike will be by far the largest diversion destination for JD Sports' customers, and instead of being one of the "most popular destinations for online diversion", Footasylum will be one player amongst a large range of substitutes for JD Sports.

### ***Fourth, the CMA's approach to online competitors is internally inconsistent and flawed***

- (27) The PFs define the online and in-store channels as being in the same market, yet view the competitive constraint from major competitors such as ASOS and Zalando as limited. This is at best counterintuitive and does not reflect the reality of this digitally driven market or the evidence provided by the Parties. For example, in paragraph 44, the PFs state that ASOS is "*strongly focused on female customers*". However, this is irrelevant. It is a significantly larger competitor than Footasylum in men's apparel and men's footwear. By way of example, in an online search undertaken by Footasylum on 27 February 2020, ASOS was found to offer a total of 989 men's trainers compared to Footasylum, whose offering at the time was comprised of a total of 823 men's trainers. Moreover, to the extent that the CMA considers that the competitive monitoring undertaken by the Parties in their internal documents provides a measure of closeness of competition (which the Parties do not agree with) then the CMA must give greater weight to [X] which shows that online players such as ASOS and Zalando compete closely with Footasylum and its more fashion-focused apparel offering. The PFs fail to take account of this.

### ***Fifth, the CMA must take account of the competitive constraints on the Parties in aggregate***

- (28) The CMA's approach in the PFs appears to be to isolate each competitive constraint and dismiss it individually, without considering properly the cumulative effect of these constraints (for example, finding that while Foot Locker imposes a strong constraint on the Parties, "*on its own we do not consider that it would sufficiently constrain the Parties...*"<sup>4</sup>).
- (29) This approach, which is generally wrong, is particularly egregious when competition is faced from many diverse sources, with the effect that the sum is self-evidently greater than its parts. A competitor facing a single type of "me too" set of rivals faces less competitive threat than one that has the possibility, and associated uncertainty, of being attacked from all sides.

### **C. The PFs exhibit pervasive pessimism with respect to JD Sports' largest rivals ... but flawed optimism for Footasylum's prospects absent the Merger**

- (30) Against the backdrop of the PFs' overwhelming pessimism with respect to the range of competitors faced by the Parties, the PFs are overwhelmingly optimistic that Footasylum was a serious contender as the binding constraint on JD Sports, despite being unarguably a small player in an unarguably [X] financial condition pre-Merger which, in the best-case scenario, [X]. When the pessimism and optimism are juxtaposed, they highlight an approach that is unmistakably – and improperly – skewed by the underlying current of a presumption of an SLC derived from the CMA's inferences from GUPPI, based in this case on questionable (hypothetical, biased) survey evidence.
- (31) While expanding small players can be disrupters of digital markets, including digitally-inspired retail, Footasylum was not such a player. The disruptive forces in the market emanate from elsewhere: in particular SDI and the brands' own DTC channels as described above. Footasylum considers that the facts and evidence presented to the CMA do not support the CMA's provisional finding that the most likely

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<sup>4</sup> PFs, paragraph 8.196.

## EXECUTIVE SUMMARY

counterfactual, absent the Merger, is one in which Footasylum would have continued to compete effectively. Rather, the facts and evidence show that the most likely counterfactual is one in which, on any scenario, [REDACTED].

- (32) To assist the CMA in its assessment of the counterfactual, this Response set out new evidence from [REDACTED] for a number of years prior to the Merger, which provides further evidence for concluding that absent the Merger Footasylum [REDACTED]. **Chapter 3** of this Response also demonstrates that the CMA's PFs on the counterfactual are fundamentally flawed; and that even if the PFs are correct in asserting that Footasylum would have [REDACTED], it remains the case that Footasylum would have been a [REDACTED].

### **D. The PFs apply the entirely wrong framework for analysing branded supplier constraints**

- (33) While the PFs recognise that suppliers have an important role in this market via their selective distribution networks, the CMA concludes that the restrictions and influence imposed by suppliers on downstream retailers simply establish a "floor" above which retailers are free to compete. This provisional conclusion fails to take into account relevant evidence provided by the Parties which demonstrate the granular compliance standards and protocols that are applied by suppliers, and the consequences of any failure to comply with such requirements (which apply not only to the current retail offering but also to forward-looking strategy).
- (34) However, the relevant question is not simply whether the Parties have the ability to flex their offering (notwithstanding the restrictions and influence imposed by suppliers), but whether they would have the incentive post-Merger to degrade their offer significantly and permanently, taking into account the ability and incentive of suppliers to react to any such degradation.
- (35) Indeed, in focusing on its static demand-side analysis the CMA has failed to address this essential question, namely how other market participants – including the Parties' suppliers – would respond to a hypothetical degradation of PQRS by the merged entity.<sup>5</sup> In this respect, the CMA's supposition that suppliers' incentives must be fully aligned with those of consumers to prevent an SLC is a fallacy. There is no indication in PFs that the CMA has even asked the brands this critical question. To be clear, the brands have no interest in allowing the merged business to worsen any element of its offer – they would increase their sales and profits by reallocating their products elsewhere.
- (36) By way of example, the PFs assume, without evidence in support, that suppliers will continue to favour JD Sports and Footasylum over the elevated SDI stores when allocating desirable stock, without considering how suppliers and SDI (and others) would respond to a worsening of the merged group's offer (including whether, if the merged entity worsens its PQRS, suppliers will work with existing or potential retailers, including SDI / Frasers Group, to respond).
- (37) It is illogical – having accepted that suppliers play an important role in shaping the retail market – to treat the degree of retail competition independently of supplier constraints, and to ignore the effect on retailers' incentives that results from the threat of reduced allocations and disintermediation. The failure to ask and / or investigate this critical question means that the PFs reach a conclusion that is not based on relevant considerations or supported by evidence, as set out in **Chapter 4** of this Response.

### **E. Internal documents and the CMA's econometric analysis do not support an SLC on any parameter of competition**

- (38) The PFs place great weight on the degree of "competitor monitoring" found in the Parties' documents, which the CMA considers in itself as evidence of "closeness of competition". However, on a correct

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<sup>5</sup> This need to consider responses to a lessening of competition is highlighted in the CMA's *Merger Assessment Guidelines*. OFT 1254/CC2, paragraph 5.4.11



## EXECUTIVE SUMMARY

analysis of the Parties' internal documents, there is no basis for a finding that they are closer competitors to one another than they are to the host of other competitors mentioned in those documents.

- (39) In particular, as set out in **Chapter 5** of this Response, the PFs misrepresent a number of documents cited, fail to acknowledge explanations made by the Parties in previous submissions regarding the purpose or context of particular documents, and fail to take proper account of a number of documents submitted by the Parties which have not been referenced, but which demonstrate the constraints imposed by other competitors.
- (40) In any event, simple "monitoring" does not of itself support an SLC finding without evidence that the Parties are reacting to each other when they choose to set their national PQRS variables (as opposed to competitive pressure in aggregate, other rivals or consumer expectations). To support their claim, the PFs cite just four documents (out of several thousand submitted by the Parties, of which the CMA conducted "targeted reviews" of over 2,500) as evidence of "*competitive responses*" between the Parties in relation to student discounts and pay-later schemes. A proper analysis of these documents reveals they either support the opposite conclusion, or in any event are not capable of supporting the conclusion that the CMA draws. Additional evidence provided in relation to student discounts and pay-later schemes further demonstrates a lack of bilateral competitive interaction (such as price matching or following) between the Parties on these parameters.
- (41) The econometric analysis conducted by the CMA on certain parameters also provides no support for an SLC finding, as neither the price nor refurbishment results are consistently found by the CMA itself, and moreover collapse: (i) in the case of price, if region-time fixed effects are included; and (ii) in the case of refurbishment, using more refined controls for local demand conditions and time trends.
- (42) The PFs identify a number of additional parameters in relation to which the CMA considers the Parties could worsen their offer post-Merger. However, the PFs provide no evidence at all to support the proposition that the Parties are materially influencing and / or responding to each other on these additional parameters (or on any other parameter of competition) at the national level (where the SLC is found<sup>6</sup>) such that the loss of this dynamic would likely have a material impact on any aspect of PQRS. Nor does the CMA address the question whether any degradation of non-price parameters post-Merger would be expected to be profitable (which it must be for the incentive to degrade to exist).

### F. Process and procedural failings

- (43) In the Parties' view, the errors identified above arise in large part from the failure of the CMA to engage with the Parties and their advisers during the course of its investigation. The Parties or their advisers wrote to the CMA on several occasions expressing concerns and requesting meetings to discuss a range of issues including: the scope for this process to be gamed by a complainant with a key commercial incentive to do so; the need properly to gather supplier evidence in this case, the CMA being the only one who could do so; survey design and methodology; the calculation of market shares; and the relevance, or otherwise, of a GUPPI model in this type of case.
- (44) However, the CMA has shown an apparent lack of interest in addressing the Parties' concerns or in any meaningful engagement: failing even to respond to the letters of Peter Cowgill to Kip Meek, the CMA Panel and the Case Team and declining requests for technical meetings.<sup>7</sup>
- (45) In addition, the CMA has failed to disclose sufficient gist of the case the Parties must meet (whether via the confidentiality ring or otherwise), on the following topics:

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<sup>6</sup> The PFs cite some evidence of response by way of limited local marketing activity (which represents a tiny fraction of overall advertising spend).

<sup>7</sup> Save for one short and perfunctory call on survey issues.

## EXECUTIVE SUMMARY

(a) [REDACTED]; and

(b) [REDACTED].

- (46) The CMA has also acted unreasonably in providing insufficient time to the Parties to make their case at key junctures of the Phase 2 process. In particular, the CMA refused to provide more than half a day for each Party's site visit or to visit any competitor stores during these visits. It also refused to provide the Parties with a fair opportunity to make oral representations in response to the PFs in the response hearing of 2 March 2020, despite repeated requests from the Parties in advance of and during the hearing, and despite ample time being available to accommodate both the Parties' representations and the CMA's remedies questions (with JD Sports' hearing concluding 25 minutes earlier than the CMA's intended finish time).
- (47) Whilst it is of course for the CMA to determine its own procedure, the procedure it adopts must be fair and in the present case, looked at as a whole, the conspicuous refusal to listen to what the main Parties have to say is not fair.

### III. Conclusion: flawed in the round assessment and erroneous application of the SLC test

- (48) The PFs emphasise at paragraphs 21 and paragraphs 6.16 – 6.27 the range of qualitative and quantitative evidence the CMA has reviewed and make frequent references to the CMA having assessed evidence "in the round". Despite this, it is evident that the CMA's provisional SLC conclusions are in fact based on a very limited selection of evidence. In particular, the CMA places by far the most weight on its own survey evidence and discounts, misinterprets, misrepresents or ignores a multitude of sources of relevant evidence and submissions provided by the Parties.
- (49) In particular, the CMA has failed properly to consider evidence of the constraints which will apply to the merged entity, in aggregate, and then to decide whether there is an expectation of an SLC on the balance of probabilities as required under the case law.<sup>8</sup> As the Competition Appeal Tribunal stated in its *BSkyB* judgment:

*".. in the context of an assessment as to whether there is likely to be an SLC in the future, the Commission must give full and proper consideration to the evidence which it has gathered, and apply the "probabilistic" test at the end point. In other words, it must ultimately ask itself whether it is satisfied on the balance of probabilities that there will be an SLC caused by [the relevant merger situation].. "*

- (50) In contrast, the PFs consider each competitor and each constraint in isolation (to dismiss each). It is far from clear that these are then meaningfully considered in aggregate; with the residual doubt which the CMA expresses in relation to each limb being weighed in the round at the end point, as the CAT test requires.
- (51) After a proper assessment of:
- (a) The substantial constraints presented by:
- i. Competing retailers including SDI who, as the additional new evidence provided shows, has now secured access to higher tier sports-inspired footwear and apparel, and continues to engage in the roll-out of elevated stores with demonstrable significant revenue impacts on both JD and Footasylum stores;
  - ii. Suppliers, who have the ability to divert supply post-Merger and thus shape the retail market (including via their competing, and rapidly expanding, DTC offers);

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<sup>8</sup> *BSkyB v. Competition Commission* [2005] CAT 25 at [80].

## EXECUTIVE SUMMARY

- (b) Footasylum's position in the counterfactual, including the additional new evidence provided by Footasylum's advisers; and
- (c) The Parties' internal documents, the absence of evidence to indicate that the Parties are responding to each other on price or non-price parameters of competition, as opposed to competition in aggregate, and the additional new evidence provided in relation to student discounts and pay-later schemes;

the CMA cannot reasonably reach the conclusion that "*overall, the remaining constraints post Merger will not be sufficient to prevent an SLC*".

- (52) The Parties urge the CMA to reflect this in a revised position on a provisional SLC: once the flaws in the PFs and new evidence presented in this Response are properly taken account of and addressed it is clear that there cannot credibly be a realistic prospect, let alone an expectation, of an SLC as a result of the Merger to the requisite legal standard.
- (53) The Parties' detailed submissions follow in **Chapters 1-6** of this Response. For the avoidance of doubt, with the exception of the CMA's co-ordinated effects analysis, areas of the PFs not addressed in this Response are not conceded by the Parties.

CHAPTER 1  
THE USE AND MISUSE OF QUANTITATIVE TOOLS TO PREDICT SLC:  
GUPPI, SURVEYS, MARKET SHARES

I. Introduction and Summary

(54) This Chapter may be summarised as follows:

- (a) ***An unsuitable quantitative tool should not be used at all, let alone to the exclusion of others and to colour all other evidence.*** It is important to use the right tools to assess the competitive effects of a merger, and not use (or in any event, not place decisive weight on the results from) one quantitative tool to the exclusion of others, especially if it is fundamentally ill-suited. If a tool does not describe pre-merger competition, it is very unlikely to be a good future guide to post-merger competitive effects. Moreover, even the best quantitative tools are “static”, but competitive dynamics are an essential feature of predictive merger assessments, especially in markets recognised as dynamic – so that the merger is judged not principally on the basis of “past rivalry” or a (rapidly dated) “current” snapshot but considers the responses of competitors and (in this case, crucially) suppliers, as well as consumers.
- (b) ***A static GUPPI model is unsuited to capturing how the market ‘works’ and will work in future.*** The GUPPI is a “static” and imperfect quantitative guide, and capable of flaws, as other data tools, such as market shares – and just as a case cannot be decided on market shares, it cannot be decided on a survey or a GUPPI. The fundamental limitation of GUPPI is that, while it has “*utility as a simple, initial screening device*” (in the words of GUPPI’s authors, Salop and Moresi), especially e.g. to screen at Phase 1 or rank large numbers of local markets at Phase 2, it “*cannot capture the richness of competition in real-world industries*” (Shapiro). It should not, implicitly, be treated as an (effectively irrebuttable) presumptive SLC finding by way of a “magic” high number.
- (c) ***Having wrongly been elevated to a decisive SLC predictor, the GUPPI result appears to have hijacked the analysis of all other evidence.*** The PFs can only coherently be explained as a gross misapplication of the GUPPI in markets where they do not explain pre-merger competition. The status of GUPPI appears to have morphed, regardless of the limitations outlined by its authors, and operated in the PFs to the exclusion of proper analysis of the “*richness*” of actual pre-merger competition in the “*real-world*” markets. This results in interpretations or weighting of evidence that conform to and confirm the presumptive SLC, and then reject, discount or ignore compelling contrary evidence (or interpretations). In this case, it is amply evidenced by errors of fact, errors of logic and various conclusions (at best dubious and at worst implausible) on three critical issues: (i) the dynamic strength and repositioning of various horizontal rivals as constraints (e.g. Nike, adidas, SDI, ASOS) (see Chapter 2); (ii) Footasylum’s [X] constraint as a stand-alone player in the counterfactual (see Chapter 3); and (iii) the clear ability and incentive of branded suppliers e.g. Nike / adidas to discipline a worsening of the retail offer by redirecting allocations of higher-tier products (see Chapter 4). Phase 2 cannot boil down to: “survey says SLC”, or “GUPPI says guilty” of a (strong incentive towards a) worse retail offer post-Merger.
- (d) ***Even a ‘perfect-input’ GUPPI model would fail as a ‘strong’ SLC indicator, because a static model ‘cannot capture’ critical variables in a dynamic, supplier-shaped market.*** While the method and measurement of GUPPI was flawed in this case (see below), it remains a flawed tool in principle, not least as a predictive SLC tool in this market. GUPPI says nothing about the impact on PQRS-setting incentives of: (i) competitor elevation, expansion, and entry; (ii) the role of Nike, adidas and other suppliers; and (iii) Footasylum’s [X] in the counterfactual. For example, GUPPI

## CHAPTER 1 – THE USE AND MISUSE OF QUANTITATIVE TOOLS TO PREDICT SLC

takes no account of the “important ... possibility of the reactions of other firms to the possible price changes imposed by the merged firm ... if competitors repositioned ... in order to be closer substitutes ... that could increase the diversion to rivals, reducing the [GUPPI result, and the inference of an] incentive for price increases”.<sup>9</sup> This remains the case, even assuming “perfect” GUPPI inputs that reflect (i) actual consumer behaviour; (ii) are free of bias and (iii) are as up to date as possible (i.e. are the most recent “snapshot”). So, even if the CMA could reload the GUPPI with perfect, flaw-free inputs, the static model results are still incapable of being even a “good guide” in dynamic markets, let alone a “smoking gun SLC” – not least given the evidence discussed in Chapters 2-4. These factors are particularly critical in this market where the power of the suppliers can enable more rapid repositioning (e.g. SDI) and expansion (e.g. DTC).

- (e) ***In practice, the CMA loaded its model with a hypothetical-question input, not actual customer behaviour, and this input is likely biased so as to inflate the GUPPI.*** Compounding the above, in this case the CMA derived the critical input and diversion ratios from inferences from a ‘now imagine’ question of consumers that was badly-worded. It probably biased respondents to say they would switch to stores nearby (rather than online or stores further away), which is particularly an issue in circumstances where they purchase infrequently and where other nearby stores (unlike DTC) may not stock the specific products they want to buy. The combination of (i) the inherent limitations of hypothetical-question evidence and (ii) the serious risk of bias means that the GUPPIs in this case are not capable of being relied upon to support an inference of a “strong incentive” to raise price / worsen the offer. Under no circumstances is it reasonable to allow this to colour all “conflicting” evidence that points to no SLC and use it as a “mathematical proof” or “smoking gun” for SLC. It “cannot capture the richness of competition in” this real-world industry as a predictive tool. The same applies to the inferences on “closeness of competition” derived from the survey (in which the Parties’ stores loom disproportionately large) to dismiss all other rivals as weak, limited or “less close” constraints.
- (f) ***Market shares.*** While at one extreme giving a static GUPPI decisive predictive weight for SLC purposes, at the other, the CMA simultaneously gives market shares essentially zero weight, apparently because they conflict with the survey inferences. In doing so, the CMA backtracks from Phase 1 (market shares “do not fully capture closeness”; paragraph 117) to saying “shares only give a basic indication of ... presence and do not capture the closeness of competition” at all (PFs at paragraph 8.68). (It also finds under the heading “market shares” that “the Parties are both large” (PFs at paragraph 8.67) though Footasylum’s share is, at most, 5%.) In reality, as found in parallel Phase 2 inquiries, even in “highly dynamic” markets, market share data, while imperfect because they are static, remains informative and provides “helpful context on market structure”.<sup>10</sup> It is therefore relevant context that the Merger market share increment is small (Footasylum’s 5% or less), particularly given that the CMA is advancing a national theory of harm and as this also highlights the limited expansion required to offset the loss of a small rival. In addition, the Parties’ combined shares (in the 30-35% range) are moderate for concerns to arise in such a dynamic market. The Parties submit that market shares cannot reasonably be given no weight at all, simply because they contradict inferences from the survey.

(55) These points, and others not summarised, are developed further below.

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<sup>9</sup> Russell Pittman, *Three Economist’s Tools for Antitrust Analysis*, DOJ Economic Analysis Group discussion paper, available at <https://www.justice.gov/atr/page/file/925641/download>, page 21.

<sup>10</sup> Illumina PFs, paragraph 8.269(d) and Sabre PFs, paragraph 8.87.

## CHAPTER 1 – THE USE AND MISUSE OF QUANTITATIVE TOOLS TO PREDICT SLC

### II. In giving undue and decisive SLC weight to a static GUPPI model, the PFs engage in a serious misreading of all other evidence to ‘fit’ SLC

#### A. The CMA’s ‘binary’ approach wrongly treats a static GUPPI as a powerful SLC predictor in a dynamic market while giving market shares no value at all

##### 1. Introduction

- (56) At least for dynamic markets, a trend emerging from recent CMA Phase 2 PFs is to collate and explain, in one explicit section of PFs, the weight the CMA has attached to various categories of evidence. This includes inherently “retrospective” or “static” current quantitative measures, such as market shares.
- (57) Signature examples of this include the October 2019 PFs in the *Illumina / Pacific Biosciences* merger inquiry (“**Illumina PFs**”, at paragraphs 8.268ff) and the February 2020 PFs in the ongoing *Sabre / Farelogix* inquiry (“**Sabre PFs**”, at paragraphs 11.13ff) which discusses this issue under the heading “*The weight to be placed on each piece of evidence*” (at paragraph 11.13). In contrast to the other two inquiries, while the PFs discuss categories of evidence in one place (paragraphs 6.16ff) they do not comment in that section on weight in any systematic manner.
- (58) In practice, it is clear that the CMA gives market shares no weight (see below) and the PFs give the GUPPI evidence central weight (as set out in this Chapter and see e.g. PFs paragraphs 8.147-148, 9.122-123), a double contradiction by way of a binary fallacy.
- (a) **100% decisive weight, or close to it: survey and derived GUPPI data.** First, in their approach to survey data and GUPPI outputs, the PFs ignore cautions about fundamental, decisive reliance on static measures to predict outcomes in dynamic markets.
- (b) **Zero weight, or close to it: market share data.** Second, when it comes to the traditional (and also static) measure of market shares, the PFs discard them entirely even though other inquiries find that they have value, even in markets at least as dynamic as those in question.
- (59) This presumption of an SLC based on GUPPI and surveys is deeply problematic as GUPPI is not the right tool to assess competitive effects, and the CMA’s starting position should be to seek understand pre-merger rivalry and future competitive dynamics and it should attach considerable weight to evidence on these decisive matters.

##### 2. The CMA’s position on the value of static measures in dynamic markets

- (60) The markets in the *Illumina / Pacific Biosciences* and *Sabre / Farelogix* inquiries are not retail markets, but are considered “*highly dynamic*” (*Illumina* PFs, paragraph 35(b),(d)) and “*dynamic*” (*Sabre* PFs, paragraph 11.13). In these PFs, the CMA says on multiple occasions that “[w]e recognise that the market is dynamic” (e.g. paragraphs 7.39, 8.204, 9.164) due in part to “*fast-changing nature of fashion*” (paragraph 2.3), “*shifting consumer lifestyle preferences*” (paragraph 2.4) especially for “*sports-inspired casual*” or “*athleisure*” (paragraph 2.5). On the supply side, in this respect, a “*key trend*” for the CMA is that “*online [is]... growing fast and a key driver of overall [sales] growth*” (PFs, paragraph 12(a));<sup>11</sup> another example of evidence cited by the PFs is that *JD Sports* “*was worried about the potential growing threat from Sports Direct due to its elevation strategy*” (paragraph 8.235).
- (61) It is generally agreed that where:

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<sup>11</sup> For example, in both footwear and apparel: “*ASOS is an online-only retailer that has been growing*” (paragraphs 8.87, 9.76) and “*particularly Nike and adidas but also others such as Puma and Under Armour are expanding their own retail DRC offering particular online but also through their own stores*” (paragraph 2.16; cf. also paragraphs 8.90, 9.79) such that the CMA “*consider[s] it likely that the [Nike and adidas] DTC offer will continue to grow ... predominantly online*” (paragraph 8.260, 9.185).

## CHAPTER 1 – THE USE AND MISUSE OF QUANTITATIVE TOOLS TO PREDICT SLC

*“... markets are dynamic ... [metrics of] current competitive conditions (such as market shares ...) may not offer a good guide to competition in the future” (Sabre PFs, paragraph 9.4)*

- (62) This is because such metrics are retrospective or even if current, still a static “snapshot”. As the CMA’s CEO, Andrea Coscelli explained last week:

*“Typically, we consider ‘static’ or recent evidence such as market shares, win/loss data and switching data as useful ... But in dynamic markets, this is not necessarily the case. As firms in dynamic markets are typically continuously evolving ... historical or static data may not accurately reflect the changing market position.”<sup>12</sup>*

- (63) This highlights the issues associated with the CMA’s reliance on the survey results of October 2019 and the GUPPI model since they are both prime examples of static quantitative evidence (see PFs, paragraph 8.142) and to:

*“highlight the dynamic ‘variables’ that the static GUPPI model does not capture and to explain that taking them into account should lead to a robust finding of no SLC”<sup>13</sup>.*

- (64) In *Illumina / Pacific Biosciences*, the CMA placed “limited weight” on static “quantitative” evidence such as econometric analysis and sales forecasts:

*“we place only limited weight on the quantitative evidence available, such as the econometric analysis and sales forecasts. In general, such evidence is less informative in the context of a merger in this dynamic market.” (paragraph 8.269(d))*

- (65) However, as set out above, the CMA places decisive weight in this case on GUPPI and survey inputs, even though they are static quantitative evidence in a dynamic market.

### **3. The conflict in approach to market shares between the PFs on the one hand, and Phase 1 in this case and parallel Phase 2 inquiries, on the other**

- (66) This inquiry has in common with both the *Illumina / Pacific Biosciences* and *Sabre / Farelogix* inquiries the same theory of harm: the operative SLC theory in the relevant PFs leading to a provisional SLC (and provisional prohibition) is premised on horizontal unilateral effects (cf. *Illumina* PFs, paragraph 21; *Sabre* PFs, paragraph 51 and PFs, paragraph 22) which tends to be operationalised as a focus on “*closeness of competition*” (cf. *Illumina* PFs, paragraph 7.2 and PFs, paragraph 22).

- (67) In this context, market shares by sales are of course a revenue-weighted picture of the significance of various competitors as measured by how much consumers spend with each competitor, annually, in the relevant market(s) in question. If customer switching patterns (diversion ratios) across the market were in proportion to the market shares of suppliers, then the shares can represent useful evidence of “*closeness of competition*”: the larger its market share, the closer the competitor. There can be no strong assumption that this will be the case in differentiated markets. But it does not follow that market shares are therefore worthless: most snapshot metrics are imperfect for capturing all relevant factors, and market shares are informative in conjunction with other evidence.

- (68) Of course, market share will not be indicative if a merging party is a “disrupter” or “maverick” in the market, however small its share. While the market is highly dynamic, for reasons set out in Chapter 3, Footasylum was not – and [X] – an industry disrupter absent the Merger.

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<sup>12</sup> Speech given at *GCR Live: Telecoms, Media and Technology 2020*, 2 March 2020.

<sup>13</sup> Parties’ Pre-Hearing Submission, paragraph 2.

## CHAPTER 1 – THE USE AND MISUSE OF QUANTITATIVE TOOLS TO PREDICT SLC

(69) In the CMA's Phase 1 decision in this case, the CMA's position on market shares was:

*In markets ... such as those affected by the Merger ... shares of supply may not fully capture the closeness of competition between the Parties and the extent to which other retailers pose a competitive constraint on the Parties. (Phase 1 decision, paragraph 117) and "may act as a useful starting point" (Phase 1 decision, paragraph 120).*

(70) Similarly, in the closeness of competition analysis in the *Illumina / Pacific Biosciences* inquiry, market shares were an express "exception" to the caution of having given static measures limited weight – and were "useful context".<sup>14</sup> In the *Sabre / Farelogix* inquiry with the same theory of harm of unilateral effects in a dynamic market, market shares "help to provide context" (paragraph 8.87) but were not given important weight.<sup>15</sup>

(71) The Parties' submission on market shares were fully consistent with the logic of the CMA in the *Illumina / Pacific Biosciences* and *Sabre / Farelogix* cases and the above CMA statement in Phase 1 in this case. In essence, this was that market shares are "imperfect indicators" (like other static measures) and "not decisive" but merit due consideration as they provide "useful context" on "market structure" and structural change brought about by the merger in a dynamic market.<sup>16</sup>

(72) For example, the Parties argued that they provide a sense check of: (i) the structural change in the market resulting from the Merger, and thus it is highly relevant that Footasylum is a small competitor nationally; and (ii) an initial indication of how much competition is lost (the smaller the market share increment, the less likely, all else equal, that it is irreplaceable, particularly in dynamically competitive markets).

(73) In contrast to its approach in other cases, and even its own Phase 1 decision, the CMA at Phase 2 has gone from market shares do not "fully capture closeness" to "do not capture" at all:

*"we consider that market shares only give a basic indication of ... presence and do not capture the closeness of competition between retailers in differentiated markets, such as this one." (cf. paragraphs 8.68, 8.276, 9.54 and 9.203)*

(74) In other words, while the survey scores (at or close to) 100, market shares appear to score zero as a guide to unilateral effects in a differentiated market.

(75) In light of all of the above, it is profoundly wrong of the CMA to dismiss the relevance of the market shares of Footasylum as giving only a "basic indication of [its] presence" (PFs at paragraph 9.54) in these dynamic markets, which is tantamount to disregarding market shares entirely – not limited weight, but no weight at all.

#### 4. Footasylum's low share of 5% is not 'large' and its small size does have meaning

(76) Footasylum's shares are in the lower single digit range of 5% or less, on any view: on the CMA's numbers,

<sup>14</sup> The CMA makes clear that it did not place "limited" weight on market shares because it prefaces the above quote with the caveat: "with the exception of market shares" (paragraph 8.269(d)). On market shares, the CMA says that they: ... provide useful context in showing the current structure of the market in which the Proposed Merger is taking place" (paragraph 8.269(d)).

<sup>15</sup> The CMA said: [w]e have taken historical market shares into account but give these less weight than some other evidence because we consider them to be imperfect indicators of future competitive positions, due to the dynamic factors, namely: [customers] continue to change their business models and different suppliers have varying plans and incentives to develop their offerings. (Sabre PFs, paragraph 11.16). Compare the "varying plans and incentives" of adidas, Nike and Sports Direct, for example, set out in Chapter 3.

<sup>16</sup> See Initial Submission paragraphs 285-289 and for example: "[a]s a starting point, the merger has a modest effect on retail market concentration, which remains low or at most moderate. As already emphasised, market shares are only a starting point. They say something about the plausibility of an SLC but (like GUPPI) are not determinative. However, they merit consideration in particular as they identify the structural change arising from the merger and the national scale and identity of existing competitors. Both of these are relevant to the subsequent analysis, since the smaller the change of national market structure and the more significant existing competitors, the more easily any lost constraint (even a relatively 'close' one) would be addressed, in aggregate, by the brands' influence over the retail market and/or replaced by expansion, entry or repositioning of retail rivals." Parties Pre-Hearing Submission, paragraphs 11-12.



## CHAPTER 1 – THE USE AND MISUSE OF QUANTITATIVE TOOLS TO PREDICT SLC

its share is [0-5%] in "sports-inspired" apparel (PFs at paragraph 9.53) and its share is also appropriately ranged as [0-5%] in "sports-inspired" footwear (though the PFs in this instance use a wider range).<sup>17</sup>

- (77) Strikingly, the CMA describes Footasylum under the heading of market shares as a "... *large national multi-brand retailer*" in footwear and apparel (PFs at paragraphs 8.67 and 9.53) though it finds its market shares to be 0-5% in footwear and apparel.<sup>18</sup>
- (78) A market share of at most 5% (range by the PFs as 0-5%) is not "*large*" by any rational standard, but the label does favour an SLC.
- (79) In fact, with respect to the share of 5% or less in apparel, a large chunk of Footasylum's apparel product range is actually own-label fashion which might be described as "urban" or "street" but on no reasonable industry or consumer basis qualifies as "sports-inspired": they have no sports heritage or association of any description. Despite extensive explanation, the CMA persists in treating Footasylum own-label brands such as *Glorious Gangsta* and *Kings Will Dream* as "sports-inspired" (cf. PFs at paragraphs 9.21, 9.45 and footnote 463) as if they were Nike or adidas clothing. While some brands may debatably be "sports-inspired", these are not. Their inclusion inflates Footasylum's share of sports-inspired apparel as a result.
- (80) This is relevant to the SLC finding in apparel that rivals will not replace the "sports-inspired" apparel competition that is lost by the Merger. The point is: given the more limited product overlap, the structural change is certainly less than the already small amount implied by a market share of 5% or less.
- (81) At the same time, market shares are susceptible to manipulation by competitors with respect to categorising their own revenue as between "sports", "sports-inspired fashion" (the focus of the SLC) and "fashion" (see further, Chapter 2).
- (82) Ultimately, however, even with all the muddying of the waters by a determined rival, the fact remains that on any basis, Footasylum is (i) not a disrupter and (ii) has a market share of 5% or less on any basis in (iii) a dynamic market. The facts are not consistent with the loss of competition being substantial.
- (83) Nor on the CMA's estimates does JD Sports have a share any higher than 30% in footwear (PFs at paragraph 8.67) and 20-30% in apparel (PFs at paragraph 9.53). So, in terms of the combined market shares post-Merger, this is not a case of even  $40 + 5 = 45\%$  or worse. Simply taking the midpoint of the CMA's range, the combined share is around 30% in footwear and 35% in apparel (ignoring the CMA's inflation of the Footasylum share on the issue of own-label). Again, these combined shares are not consistent with market power (to profitably worsen PQRS) post-Merger let alone presumptive of it.
- (84) Overall, these facts are strongly indicative of a relative lack of potential for competition concerns under any remotely normal standard of merger control. It is as wrong to disregard this evidence as not meaningful to the SLC assessment (as they simply "*do not capture closeness of competition*") as it would be to treat it as dispositive (automatic proof of no SLC), as is a better description to what has happened to survey results and the GUPPI.
- (85) Either way it is a binary fallacy: worth nothing, or everything, with nothing in between.

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<sup>17</sup> The PFs give a footwear market share range in the public version stretching from [0-10%] (paragraph 8.67) rather than [0-5%] as for apparel, but the actual calculated footwear shares are not higher than the calculated apparel shares, and [0-5%] is equally appropriate and indeed more so, for the sake of consistency. In other words, implying that Footasylum's footwear share is up to twice as large as its apparel share would be wrong, based on the PF's own calculations.

<sup>18</sup> See note above.

## CHAPTER 1 – THE USE AND MISUSE OF QUANTITATIVE TOOLS TO PREDICT SLC

### B. The CMA places central weight on ‘high’ GUPPIs

#### 1. The use of GUPPI by the CMA

(86) The CMA's view is that:

*“... market shares give only a basic indication of the Parties' presence and do not capture closeness of competition [whereas] other evidence is more informative on the closeness of competition, including the GUPPI which captures the significance of pricing incentives.”*  
(paragraph 8.68)

(87) The GUPPI model came into UK merger control from the United States in 2010, and came to the UK by the CMA's predecessors. It generates a percentage indicator of "upward price pressure" or GUPPI "result" as its output: e.g. GUPPI = 5%, 10%, etc.

(88) In describing GUPPI, the CMA points out that it "*has used GUPPIs in ... a number of merger inquiries*" and is a "*useful and commonly used measure*" (PFs at paragraph 35).<sup>19</sup> This makes it sound more common than it is. There are handful of CMA-era Phase 2 cases (it cites two examples<sup>20</sup>) and in any event is far from "standard practice" for the CMA to use GUPPI. The GUPPI model as such has not consistently been used even within the small set of Phase 2 merger cases in retail markets since the CMA was formed in 2014, even in parallel retail markets inquiries. For example, GUPPI was used in one but not the other two Phase 2 retail cases that spanned 2015-16, without explanation, even though GUPPI inputs were available in all 3 cases and the mode of retail analysis was similar.<sup>21</sup>

(89) The most important point, however, is the fact that the GUPPI model is a static or "snapshot picture" model of incentives that is based on "demand-side" (customer) behaviour only. Whether or not GUPPI was used, no CMA or predecessor Phase 2 retail merger case featured a more dynamic market than the markets at issue here — and in numerous cases those markets were far less dynamically "digital" or "digitally-inspired" than the athleisure fashion sector.

(90) This Chapter will explain why, even assuming "perfect" inputs to create a "perfect" GUPPI (i.e. an unimpeachable survey), a static model cannot safely be used to predict incentive and outcomes in a dynamic market: the CMA accepts that the GUPPI model is static and "demand-side" only, and cannot capture supply-side dynamics (competitor expansion, repositioning, entry; see Chapter 2), the counterfactual (Chapter 3) or the peculiar role of Nike and adidas in particular (see further, Chapter 4).

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<sup>19</sup> Paragraph 8.138.

<sup>20</sup> *Sainsbury's/Asda* (2019) and *Ladbrokes/Coral* (2016) at paragraph 8.138. The PFs also cite one pre-CMA example from 2013.

<sup>21</sup> Compare *Ladbrokes/Coral* (2016) with *Celesio/Sainsbury's pharmacies* (2016) and *Poundland/99p* (2015).

## CHAPTER 1 – THE USE AND MISUSE OF QUANTITATIVE TOOLS TO PREDICT SLC

### 2. ‘High’ and ‘low’ GUPPIs as against the 5% GUPPI threshold

(91) Even in less digitally-inspired and dynamic retail markets than this, aside from one unique case,<sup>22</sup> in terms of GUPPI thresholds, the CMA's approach to GUPPI outputs has been that a GUPPI under 5% was a "safe harbour" indicating that concerns could presumptively be ruled out.

(92) For example, in *SSE/npower* (2018) in the energy sector, the CMA said:

*"in previous cases the CMA has taken the approach that a GUPPI of less than 5% indicates that concerns can be ruled out, although occasionally a higher threshold has been used."*<sup>23</sup>

(93) In the words of one of the intellectual founders of "UPP" analysis, this logic stems from the fact that, in practice, unilateral effects-based SLC concerns:

*"... are unlikely if the [GUPPI] ... is less than 5%. The "safe harbor" [is] not .. tolerance for anti-competitive price increases. Rather, it reflects that a small amount of upward pricing pressure is unlikely, at the end of the day, to correspond to any actual post-merger price increase."*<sup>24</sup>

(94) The CMA in the *SSE/npower* case also uses the word "small" to refer to GUPPIs below 5%.<sup>25</sup>

(95) Moreover, there is no general suggestion in guidance or case practice that "breaching" 5% means that the GUPPI flips from "small" to "large" (or "low" to "high"), such that there is an automatic concern or a presumption of a likely SLC at results over 5%. It simply means that an SLC concern cannot presumptively be ruled out based on a "small" GUPPI. As the CMA has noted: *"typically, [there is a] closer examination of markets where the GUPPI was 5% or higher."*<sup>26</sup>

(96) The context for those cases cited by the CMA and (almost) all CMA cases involving GUPPI has been local retail markets analysis, where GUPPI was a ranking / sorting tool (or in two cases a "decision rule" for administrability purposes given hundreds or thousands of markets). Unlike all such cases, the CMA's assessment in this case is exclusively focused on two single national markets for footwear and apparel.

### 3. At around 5%, the GUPPI on the JD side is not ‘high’ – any more than Footasylum’s 5% share makes it a ‘large’ national retailer

(97) The overpowering effect of the survey and GUPPI results appear to have led to a situation where the PFs say that "low" is "high" and "small" is "large". On the latter, see Footasylum's 5% or less share as "large" in national market share terms (PFs at paragraphs 8.67 and 9.53) and the discussion above.

(98) In this case, the GUPPI results centred on JD Sports ranged from around 4-6% across all permutations of apparel and footwear (PFs at Tables 8.7 and 9.7, paragraphs 8.144 and 9.120).

(99) These are at or around the level at which *"in previous cases the CMA [took] the approach that ... [this] indicates that concerns can be ruled out"* (cf. *SSE/npower*, above). It follows from this "small" or "low"

<sup>22</sup> In justifying a GUPPI threshold of SLC intervention below 5% in the case of *Sainsbury's/Asda* (2019), the CMA placed weight on the fact that GUPPI was used to deal with local analysis in over a thousand local grocery and fuel markets; that the case combined the numbers 2 and 3 in the largest of all UK retail markets (worth around £190 billion) and involved the repeated e.g. weekly sale of essential i.e. non-discretionary food and non-grocery items for UK households on a weekly basis; cf. e.g. CMA, *Sainsbury's/Asda* (2019), paragraphs 8.283. This constellation of factors has not applied to retail markets in other CMA cases and does not apply in this case.

<sup>23</sup> CMA, *SSE/npower* (2018), Appendix J page 1, paragraph 4.

<sup>24</sup> Professor Carl Shapiro, *Update from the Antitrust Division*, Nov. 18, 2010, Speech at pp. 24-25, available at <https://www.justice.gov/atr/file/518246/download>

<sup>25</sup> CMA, *SSE/npower* (2018), Appendix J page 5, paragraph 18.

<sup>26</sup> The CMA said: *"[i]n the past, for some (but not all) horizontal mergers, the CMA has taken the approach that a GUPPI of less than 5% indicates that concerns could be ruled out. Typically, this has been followed by closer examination of markets where the GUPPI was 5% or higher. In other cases, the CMA has signalled that a higher threshold may be appropriate"*; CMA, *Tesco/Booker*, paragraph 9.46.

## CHAPTER 1 – THE USE AND MISUSE OF QUANTITATIVE TOOLS TO PREDICT SLC

GUPPI that this result, in and of itself, suggest that JD Sports has little incentive to raise price or worsen the retail offer post-Merger with respect to the JD Sports-branded business even before considering the dynamics among rivals or the constraint from suppliers.

- (100) That said, on the side of Footasylum, the much smaller player (5% share), the GUPPIs (based on switching to the much larger JD Sports) are considerably higher, ranging from 12-22% in footwear (Table 8.7) and 19-26% apparel (Table 9.7).
- (101) The CMA does not take account of the relatively low JD Sports GUPPI results and lumps JD and FA results together as "*the GUPPI figures are high, particularly for Footasylum but also for JD Sports*" (PFs at paragraph 9.122).
- (102) This label of 4-6% being "*high*" is inconsistent with the CMA's position set out above. On any normal meaning of the word in light of a basic understanding of CMA policy or practice, it is not high.<sup>27</sup> The PFs are therefore unreasonable in treating the JD Sports GUPPI result as "*high*".
- (103) Conversely, the Parties agree that the Footasylum GUPPIs, and only those GUPPIs, can fairly be called "*high*". At worst, this suggests an incentive to worsen the retail offer at the Footasylum-branded business post-Merger (which will be run as a separate brand), but not on the JD Sports side.
- (104) However, this inference needs stress-testing against all other evidence and cannot support a "purely-Footasylum"-based theory of a worsened Footasylum offer and a consequent one-sided SLC finding in and of itself. This supposition from theory must take into account the likelihood that such a worsening of the retail offer could be durably sustained in:
- (a) such a dynamic market, against elevation, expansion and entry by rivals (see Chapter 2);
  - (b) in the presence of suppliers who shape the retail market, [X], and who have the ability and incentive to reallocate higher-tier and indeed all their branded products (see Chapter 4);
  - (c) despite occurring with respect to Footasylum-only post-Merger sales volumes representing, at most, a 5% share that is a fraction of that of JD Sports and other large rivals (such as SDI and Foot Locker),
  - (d) in circumstances where the no-SLC finding on the JD Sports side (given the low GUPPI and all other evidence) means that those dynamic forces do constrain the JD Sports fascia post-Merger.
- (105) In short, it is artificial to assume a worsening of the Footasylum-only PQRS could be insulated in this way, despite the much larger JD Sports being constrained competitively. A Footasylum-but-not-JD Sports SLC finding is therefore a static or cautious Phase 1 laboratory result, perhaps, but no basis for an expectation of an SLC under the Act in these relevant markets.<sup>28</sup>

### 4. The CMA wrongly claims Footasylum and JD Sports both have '*high*' GUPPIs and that this is '*strong*' evidence

- (106) The PFs takes these "*high GUPPI*" inferences as "*strong*" evidence of SLC (i.e. an incentive to worsen PQRS. The PFs note that:
- (a) At store channel level: "*GUPPI figures of this magnitude show a strong incentive for the Parties to degrade or not improve their offering post-Merger ...*"; and

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<sup>27</sup> CMA, *SSE/npower* (2018), Appendix J page 5, paragraph 18.

<sup>28</sup> For more on the fact that there are no examples in UK merger control of a Phase 2 SLC finding only with respect to a posited PQRS worsening on a target with a share of 5% or less, see the Parties Pre-Hearing Submission.

## CHAPTER 1 – THE USE AND MISUSE OF QUANTITATIVE TOOLS TO PREDICT SLC

(b) At online channel and relevant market (combined channel) level: "... *although the online and combined GUPPIs are lower ... they still indicate a strong incentive to deteriorate PQRS through raising prices or worsening elements of QRS*".<sup>29</sup>

(107) A critical issue, therefore, is what weight the CMA has attached, and ought to attach, to inferences from the outputs of the GUPPI model, not least in circumstances where only the Footasylum GUPPI is "high" and the JD Sports GUPPI result is not.

### 5. Inferences from GUPPI (even when the data input is actual customer switching)

(108) The GUPPI model relied upon in the PFs came into UK merger control from the United States in 2010. However, in practice, the PFs have lost sight of the cautions of the intellectual founders of GUPPI in this case.

(109) As described by the co-authors of GUPPI, Professors Salop and Moresi, its "*utility [is] as a simple, initial screening device*" (Salop and Moresi).<sup>30</sup> As Professor Carl Shapiro, another pioneer of upward price pressure analysis, and the "co-sponsor" of the inclusion of GUPPI into the US Horizontal Merger Guidelines, put it:

*[t]he value of diverted sales [i.e. the GUPPI model] is an excellent simple measure for diagnostic or scoring unilateral price effects, but it cannot capture the full richness of competition in real-world industries.*<sup>31</sup>

Professor Shapiro's caution applies to GUPPI results even as they tend to be compiled in the United States – based on *actual* customer switching. In retail, for example, entry/exit analysis might assess the actual revenue impact of a competitor store entering a local retail market and taking away *actual* sales from an incumbent store i.e. customers "voting with their wallets" (and feet) and switching from the original store to the new competitor store.

(110) Of course, all data becomes "historical" and "stale" over time: the more dynamic the market, the shorter the shelf-life of the data. Therefore, even if the CMA were to use the most up-to-date version of "historical" data on actual customer switching to predict customer switching on a forward-looking basis (e.g. rest of 2020 through 2022), these cautions remain fully valid.

(111) In particular, even a perfectly-constructed model that generates a "high" GUPPI is not a "strong" indicator let alone presumptive SLC in any (and especially this) dynamic market. GUPPI says nothing about the impact on diversion ratios, or the GUPPI "score", or inferences on price-rise incentives of (i) competitor elevation, expansion, and entry; (ii) the role of Nike, adidas and other suppliers; and (iii) Footasylum's [X] in the counterfactual. For example, GUPPI takes no account of the "*possibility of the reactions of other firms to the possible price changes imposed by the merged firm ... if competitors repositioned ... in order to be closer substitutes to ... the merged firm, that could increase the diversion to rivals, reducing the [GUPPI result, and the inference of an] incentive for price increases*".<sup>32</sup> This remains the case, even assuming "perfect" GUPPI inputs that reflect (i) actual consumer behaviour and (ii) are free of bias and (iii) are as up to date as possible (i.e. are the most recent "snapshot") So, if the CMA reloaded the GUPPI

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<sup>29</sup> PFs paragraph 8.148.

<sup>30</sup> The paper that introduced GUPPI was: Steven C. Salop and Serge Moresi, *Updating the Merger Guidelines: Comments*, November 9, 2009, available at <https://www.crai.com/sites/default/files/publications/Salop-Moresi-Comments-to-HMG-2009.pdf>; see p. 23.

<sup>31</sup> Shapiro, *The 2010 Horizontal Merger Guidelines: From Hedgehog to Fox in Forty Years*, 77 *Antitrust Law Journal*, 701-759 (2010) at p. 729. Professor Shapiro was in charge of economics at the US Department of Justice Antitrust Division at the time these guidelines were introduced, as Deputy Assistant Attorney General for Economics.

<sup>32</sup>

## CHAPTER 1 – THE USE AND MISUSE OF QUANTITATIVE TOOLS TO PREDICT SLC

with better inputs it is still incapable of being a "smoking gun" SLC, even before considering all the dynamics it does not capture (see Chapters 2-4).

(112) However, the PFs raise a host of further issues, as they do not rely on actual customer switching.

### III. **Beyond the inherent unsuitability of GUPPI, there are specific problems with the CMA's survey diversion ratios: they are hypothetical, likely biased and used as a trump card on other evidence**

#### A. **In this case, the GUPPI relies on inherently hypothetical data inputs**

(113) There is a multiplicity of sources of evidence in this case: factual, economic analysis, and internal documentary evidence. There is also new evidence, since the PFs, and prior evidence which the PFs does not mention, and appear to have missed. This is all real-world evidence, and is addressed in turn, by key issue, in the remaining Chapters in this Response.

(114) Only one piece of evidence is unequivocally based on a hypothetical: the CMA's hypothetical-question (*what-would-you-do?*) survey of consumers. The responses to this hypothetical generate inferences as to customer switching. Of course, it cannot constitute evidence of actual customer switching.

(115) These inferences are one of two key inputs into the CMA's version of the GUPPI used in the PFs. On the weakest-link principle, the reliability of GUPPI is only as reliable as that of its weakest input. Ultimately, therefore, the GUPPI model is based on simple inferences as to customer behaviour generated by hypothetical questions. This raises issues above and beyond the inherently unsuitable nature of GUPPI as an SLC predictor in any dynamic market, let alone ones where the role of suppliers and the correct counterfactual are crucial pieces of the puzzle.

#### B. **Problematic inferences when the data input derives from 'now imagine ...'**

(116) Unlike the norm for calculating "diversion ratios" (i.e. proportions of customer switching) in the US, the incriminating SLC evidence to derive "diversion ratios" for use in the GUPPI in the PFs have at their source a hypothetical-question consumer survey.

(117) The CMA surveyed a sample of the Parties' stores (not chosen to be nationally representative) over a several-week period in October 2019 interviewed consumers (core demographic: 16-24 year olds) as they exited the relevant stores, provided they had just purchased footwear or apparel or both (PFs, paragraph 6.24). The survey company retained by the CMA then asked these consumers a series of questions, some factual, but the critical question used to generate the "customer diversion ratio" was a hypothetical:

*Now I want you to imagine that, before deciding to come here today, you knew that all [JD Sports] physical stores had closed and their website was closed down. What would you have done instead?<sup>33</sup>*

(118) This requires quite some imagining. Broadly speaking, this concern is why the CMA's counterpart agencies in the United States tend not to collect and try out this calibre of evidence in court in a merger case. One does not need to be an expert in the rules of evidence in civil cases to understand why this is. Fact witnesses (e.g. eye-witnesses) attend court to testify as to what they did, saw, or heard. If a lawyer began to ask: "*I want you to imagine ...*", counsel for the other party might object to the judge that the answer is unreliable (and therefore inadmissible) because it calls upon the witness to imagine – and thus speculate about – facts rather than testify to what facts were.

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<sup>33</sup> See CMA, 'Good Practice in the Design and Presentation of Customer Survey Evidence' <[https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment\\_data/file/708169/Survey\\_good\\_practice.pdf](https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/708169/Survey_good_practice.pdf)>

## CHAPTER 1 – THE USE AND MISUSE OF QUANTITATIVE TOOLS TO PREDICT SLC

- (119) As a result, US agencies tend not to generate hypothetical-question consumer survey evidence in merger cases, because the judge is likely to throw it out.
- (120) So while Professor Shapiro's caution was in the context of a system that focuses on evidence of actual customer switching, this caution must apply to a much greater extent, and urgently, to hypothetical switching based on consumers imagining what they would do when confronted with the question by a survey-taker, on the hoof, as they exit a store.
- (121) This is generally recognised, not least by the CMA itself. For example, the issue is an "*inherent limitation*" (see CMA, JD Sports/Go Outdoors, Annex 2, paragraph 4) and a "*weakness*" (see CMA, Poundland/99p, paragraph 4.17), such that "*greater weight should be given to ... evidence ... based on revealed preferences (actual customer behaviour) rather than stated customer preferences*" (ibid, paragraph 4.18) that is, less weight should be given to answers to hypothetical questions.
- (122) In this case, we do not ask for the CMA to throw the survey evidence out. We ask for hypothetical question evidence to be treated with extreme caution, not to use it in GUPPIs as apparently powerful if not decisive evidence, and certainly not the exclusion or degradation of much more robust, reliable and powerful evidence in this case: factual, documentary, and economic.

### C. Serious risk of restrictive bias in survey design and execution

- (123) Over and above the inherent limitations of such surveys, there are better and worse ways to design critical questions. Various technical concerns about the survey design set out in more detail in the Parties' submissions at the time.<sup>34</sup>

#### 1. Restrictive bias

- (124) For brevity, we focus in the main text on one common-sense issue here. The CMA's own best-practice guidelines<sup>35</sup> note the risk of "restrictive bias" as follows:

*Restrictive bias, where the question leads the customer to think only of certain options. For example, asking 'If you had known before you went there that this branch of X was closed for refurbishment for one year, what would you have done instead?' – without an explicit encouragement in the question wording to respondents to consider all options, such as 'Please imagine that you had known before you went there that this branch of X was closed for refurbishment for one year. Thinking of all the options open to you, what would you have done instead?' – may cause respondents to discount shopping online as an alternative source of supply* (paragraph 3.11.(b))

- (125) Single words added or subtracted in the phrasing of such a delicate question can make an important difference to diversion results, and in turn GUPPI results. The context of the store exit survey is that consumers are asked these survey questions literally as they exit the threshold of the store having made a purchase.
- (126) Turning to the CMA's critical question, it inserted the word "today":

*Now I want you to imagine that, before deciding to come here **today**, you knew that all [JD Sports] physical stores had closed and their website was closed down. What would you have done instead?*

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<sup>34</sup> See Parties' *Initial comments on CMA surveys*, 15 October 2019.

<sup>35</sup> CMA, *Good practice in the design and presentation of customer survey evidence in merger cases*, rev. May 2018, CMA78 (**best-practice guidelines**).

## CHAPTER 1 – THE USE AND MISUSE OF QUANTITATIVE TOOLS TO PREDICT SLC

- (127) The "store closure" hypothetical is supposed to be proxy for the SLC theory of harm of a prolonged degradation of store quality or other PQRS variables, to see what customers (say they would) do in response. However, the point about a prolonged worsening is the premise that some consumers notice this over time, are put off, and switch away to alternatives. For this reason, it is important that the consumer knew well before their shopping mission that the store quality had worsened (or the proxy scenario used in the survey: that the store had closed).
- (128) The Parties submitted comments to the effect that adding the word "today" in this context was:
- (a) Unnecessary (cf. the wording in the guidelines example, which does not feature "today") and
  - (b) Created the very risk of restrictive bias flagged by the CMA's best-practice guidelines.
- (129) This view was supported by Professor Patrick Sturgis, Professor of Quantitative Social Science at the London School of Economics and Political Science. The Parties suggested, among other things, removing the word "today" and asked for a short meeting at the CMA's convenience between Professor Sturgis and the CMA, which the CMA rejected. The Parties offered a conference call option instead. This was also rejected.
- (130) The common-sense intuition on risk of bias was as follows: the use of the word today creates an immediacy in time, rather than the clear steer that they had already known this well before they set out on their shopping mission from school, home or work. By adding "today, it may be that consumers processed this as:
- ... imagine that ... [just] before deciding to come [in] here today, you [learned] that ...*
- (131) There is a significant risk that, literally asked on the spot, a consumer may mentally process this question more or less as follows:
- Well, I'm here now .. so given that I am standing right here ... and this person is ... telling me to imagine I now knew that this store I have just walked out of was in fact shut, then .... I imagine I would probably ... have gone to the nearest local store instead" ..*
- (132) This may cause "restrictive bias". As Compass Lexecon noted at the time, the use of the word "today" in the diversion question was problematic since respondents may feel committed to a specific location or mode of purchase on the day of the purchase and find it difficult to fully re-evaluate their shopping trip, which may restrict the range of retailers that the customer could consider to be viable alternatives, including online options (such as nike.com, adidas.co.uk or asos.com) or stores in another shopping centre or high-street or edge of town retail area (for example, Sports Direct's classic store portfolio is large stores in retail parks (though this has now changed with store elevation: see Chapter 2).<sup>36</sup> These issues are likely to be increased as consumers purchase the products infrequently.
- (133) A very strong implication of restrictive bias emerges from the survey itself. The most easily to follow example of this relates to the highest diversion ratio result of all 28 areas – the 90% footwear customer diversion from Footasylum to JD Sports at Liverpool One. The Footasylum store is literally opposite the JD Sports store (though there are other retailer in the complex, such as (focusing on footwear) Foot Locker, Sports Direct, adidas, Vans, Office and Schuh. The locations of the Parties' stores are shown circled below:

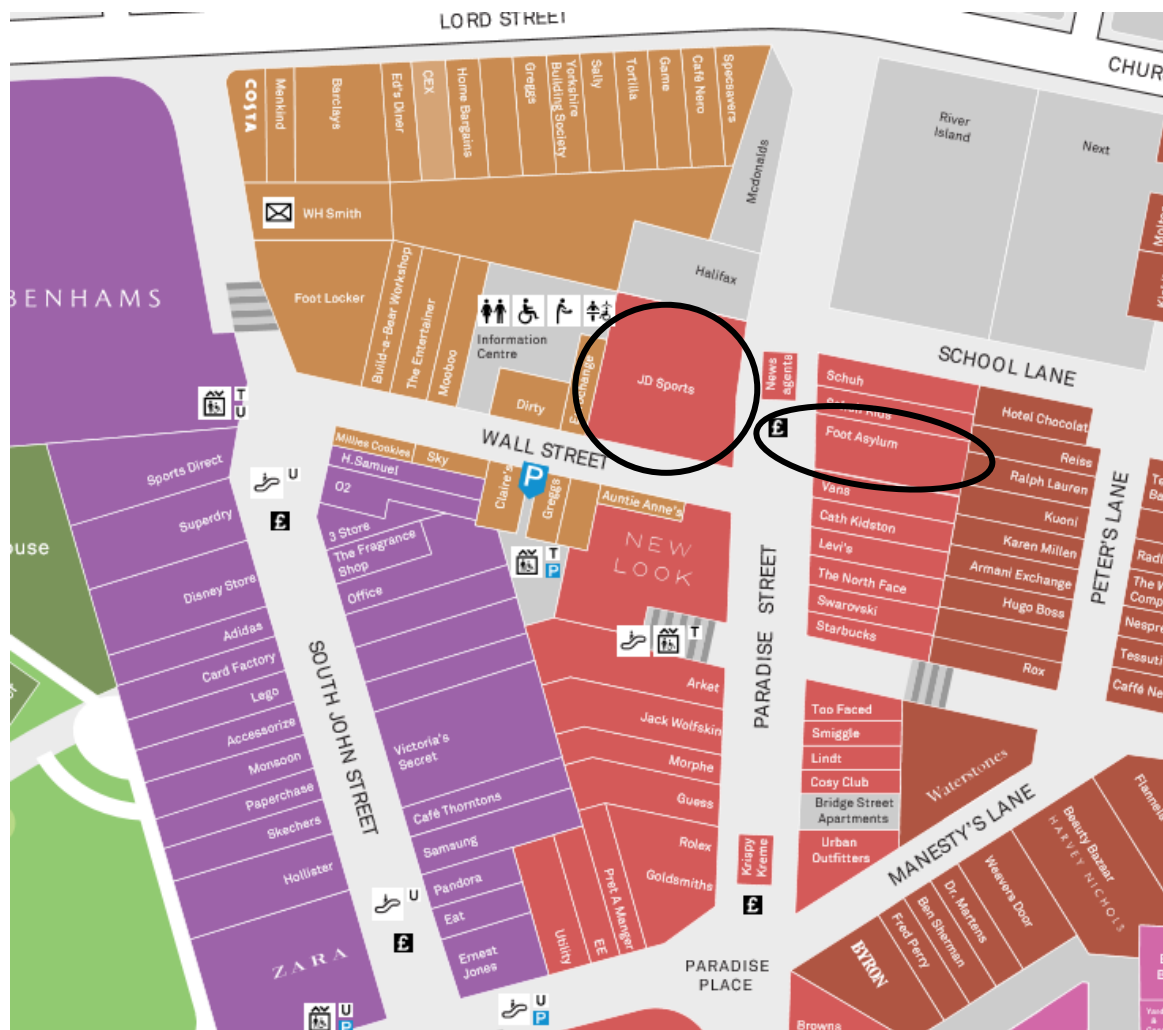
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<sup>36</sup> For example, the customer may be mentally committed or 'locked in' to making a shopping trip to that shopping centre or high street area on that day, in which case they form less viable alternatives for that customer compared to a scenario where they had known about the closure for some time in advance. See Compass Lexecon, "Comments on CMA surveys", 20 December 2019, paragraphs 4.2 to 4.7 for further details.



**CHAPTER 1 – THE USE AND MISUSE OF QUANTITATIVE TOOLS TO PREDICT SLC**

**Liverpool One Shopping Centre Site Map**



- (134) The survey yielded the entirely unsurprising result that 90 out of 100 surveyed footwear customers<sup>37</sup> exiting the Footasylum, when asked where they would have gone had that store been shut, said the store directly opposite – the JD store. This “restrictive bias” issue is also sometimes known as “framing bias” – asking people outside stores has a “framing” effect such that when asked where they would shop, it yields a bias towards answers of “other (nearby) stores”; asking consumers via an online rather than store exit survey can, conversely, created a framing bias in favour of online.
- (135) Yet taking its store survey at face value as “*robust*”, as the CMA does (Appendix E, paragraph 8) the CMA’s survey approach would conclude that the Parties’ are such close competitors (90% diversion) and all other players are so weak (10% diversion in aggregate) in footwear such that JD Sports is essentially a post-Merger monopolist in that corner of the shopping complex.
- (136) In actual fact, the framing of the survey question coupled with location and mode of survey yields a serious risk, at least, of bias such that consumers discount online (even though this accounts for 30% or more of

<sup>37</sup> For illustrative purposes this section uses 100 customers. In reality, DJS interviewed only 91 customers in total across footwear and apparel combined (DJS report, page 14), so presumably only around 35-55 customers (c. 40-60% of those 91) would have been footwear customers in the exit survey at this store.

## CHAPTER 1 – THE USE AND MISUSE OF QUANTITATIVE TOOLS TO PREDICT SLC

market-wide and the Parties' sales) and that only 10 out of 100 mentioned any of the other retailers in the complex.

- (137) But while this is a common sense concern, perhaps the most compelling "proof" that the hypothetical answers are not a good guide to actual behaviour is this: the JD Sports store at Liverpool One only stocks around 33% of the footwear products stocked by the Footasylum store opposite. This implies that, on average, only 30 of those 90 customers would find the same pair of trainers they had bought at the Footasylum store also at the JD Sports store, leaving 60 or two-thirds of the supposedly diverting 90 customers deprived of the "specific item" purpose of their visit.
- (138) This suggests as many as 60 out of 100 (if none of the "deprived" substituted to some other product) or at least 44%<sup>38</sup> of the 60 (i.e. 26 of the 90) of the supposedly diverting customers would (a) not have found what they were looking for, and (b) would appear to have been unlikely to have bought a substitute product.
- (139) Instead, they would have checked (their smartphone to shop) online or gone elsewhere – whether inside Liverpool One or another shopping area altogether, had they known well before their trip that the Footasylum Liverpool One would be shut, and their specific intended purchase be unavailable. In fact, the CMA's own product overlap analysis based on Nike and adidas sales data identifies a wide range of footwear and apparel retailers who sell the same products as the Parties, including large national chains such as Foot Locker, SDI/USC, Next, Schuh, and Office, and online pure play retailers including Zalando, ASOS, Shop Direct, End, and Pro Direct. The Parties set out more detailed comments on the product overlap results at Annex 1.1.
- (140) These inferences are simply not captured by the CMA's 90% survey diversion even if this 90% figure was not already grossly inflated given the "restriction bias" phrasing of the question and the "framing bias" location of the survey literally outside the two stores. As is evident from the above extreme example of 90%, which contributed to the overall "national" FA to JD number of 70%, these biases work in favour of higher diversion between the Parties, and higher GUPPIs, than absent any risk of bias. The CMA compounds this issue by extrapolating from the 28 surveyed stores of each party to the entirety of their respective national estates (70 FA stores and over 340 JD stores).<sup>39</sup>

### 2. The requests to mitigate bias were needlessly rejected

- (141) The CMA did not give reasons at the time for rejecting the simple request to remove the word "today". The subsequent justifications recorded in the PF Annex<sup>40</sup> are weak, do not remotely address all of the problems identified by the Parties and cannot possibly justify the "restrictive bias" risk flagged in the CMA's own guidelines that a simple one-word deletion would have addressed.
- (142) In addition, the CMA's explanation for including the word "today" in the question (i.e., to encourage respondents to think about a particular purchase) is entirely inconsistent with its decision to reject another of the Parties' suggested improvements: a request for item-specific questioning (e.g. if a consumer had

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<sup>38</sup> The DJS report shows that for Footasylum surveyed customers in footwear, 44% visited the store to buy a specific item (at Figure 7) and 44% would not buy something else if the specific item of footwear had not been available (at Figure 27).

<sup>39</sup> The Parties made it clear when commenting on the draft survey questionnaire that because the CMA has advanced a national theory of harm, the survey sample needs to be representative of (or at least allow robust extrapolation to) the national market. (JD Sports Comments on CMA surveys – 15 October 2019).

<sup>40</sup> The CMA explains that the "value add" reason for including the word today was "*to encourage respondents to think about the purchases they had made on the day of being surveyed, rather than footwear and apparel purchases generally*", and that reference to today would not have led to any "*notable bias*" because "*survey participants would have been aware that they had the option of switching online, as a question about shopping online had been asked earlier in the survey*". PFs, Appendix E, paragraph 6(c). On a cost/benefit basis, the "value add" benefit of including "today" was negligible, while the cost (risk of bias) was substantial, in line with the reflections in the CMA's best-practice guidelines.

## CHAPTER 1 – THE USE AND MISUSE OF QUANTITATIVE TOOLS TO PREDICT SLC

bought trainers and an item of apparel, for example, which would have directly focused respondents' thinking on a particular item, rather than at basket level).<sup>41</sup>

- (143) The CMA's reasons for rejecting the item-specific approach to diversion are also not credible.<sup>42</sup> There are objectively good reasons for item-specific questioning and the CMA's reasons in no way justify the failure to gather economically relevant information.
- (144) The net effect of the CMA's failure to make the necessary revisions to the survey questionnaire is that the diversion ratios and GUPPIs estimated from the survey carry a substantial risk of bias, over and above the inherent limitations of a hypothetical question survey.
- (145) This bias if present would operate to inflate diversion to stores nearby which, given the 28 survey locations used by the CMA, will likely bias upward diversion between the Parties' stores, and thus bias the GUPPI upward.

### D. The CMA interprets the survey (and derived GUPPI) with disregard for its inherently-hypothetical nature and serious risk of bias in its design

- (146) Separate from the probable bias in this case that (quite needlessly) infected the critical survey question, the CMA pays lip-service to the inherent problem of hypothetical-question evidence in the PFs, consistent with past cases:

*"We acknowledge the difficulties in wording diversion questions and that their hypothetical nature necessitates careful interpretation"* (Appendix E, paragraph 7(a)).

- (147) But in practice, the CMA discards such caution in interpretation in this case. Rather, it says:

*"We consider that the store exit survey was robustly designed and carried out. We have given it full evidential weight in our assessment"* (Appendix E, paragraph 8).

On the issue of inherent survey limitations, the main body of the PFs is confident:

*"The evidence from the store exit survey is highly informative of the constraint that the Parties place on each other ... as this is derived from views of the Parties' customers on which retailer is their next best alternative"* (PFs, paragraph 8.118).

- (148) This approach is on a critical plank of the SLC analysis, and fails to take into account two relevant considerations: (i) inherent limitations of hypothetical-question evidence and (ii) risk of bias in survey design.<sup>43</sup>
- (149) Moreover, no "careful interpretation" acknowledgement is made that here the surveyed customer is (i) often youthful (target demographic: a 16-24 year old youth, accounting for 43% of surveyed Footasylum

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<sup>41</sup> The reason for this suggestion was two-fold. First, to remove uncertainty about which items respondents' answers related and so that diversion could have been investigated by product type, brand and own label. Second, so that responses could have been reweighted according to the (known) distribution of spend on different items.

<sup>42</sup> The CMA's reasons for considering it "*reasonable for respondents to answer based on their basket in general*" are nonsensical: there is no reason why item-specific questions would have made the survey longer and more complicated (and none is given) and the fact that most consumers only buy a single item is not a reason not to ask item-specific questions. The PFs argue that item-specific questions would "*have made the surveys more complicated and longer, reducing respondents' ability to engage with it*" and that only a small proportion of respondents purchased more than one item, in either the in-store or online survey. PFs, Appendix E, paragraph 6(b). We note that when it came to the Parties' suggestion that the CMA should exclude the customers who bought both footwear and apparel from the GUPPI calculations, the CMA stated that this is not suitable due to the impact it would have on the sample size, which suggests that even in their view the proportion of respondents purchasing more than one item is not "*small*". PFs, Appendix E, paragraph 7(c).

<sup>43</sup> This reference to "customer views" is presented as authoritative, as it might be if the CMA were asking for the considered view of sophisticated corporate customers of their actual procurement preferences and first and second (next-best) alternatives in real-world practice.

## CHAPTER 1 – THE USE AND MISUSE OF QUANTITATIVE TOOLS TO PREDICT SLC

customers (while 64% were under 35)); (ii) they may lack some patience towards the end of a survey having agreed to be taken aside upon store exit by a survey-taker, and the critical question comes towards the end of the survey; and, as noted, (iii) the "next-best preference" prediction is a hypothetical response prompted by a hypothetical store closure.

- (150) Nor is it sufficient cosmetically to graft the missing words "*these have been carefully interpreted*" into paragraph 8.118 in any revised PFs or the Final Report. The hypothetical-question results, and the GUPPI inputs that depend on them for robustness and predictive value, have not been carefully interpreted and nor is there any evidence to suggest that they have. They have been treated as incriminating, unimpeachable "DNA-sample" evidence of a worsening of PQRS.

### **E. The 'now imagine'-based GUPPIs remain the central incriminating evidence of SLC**

- (151) The CMA's use of consumer survey at both Parties stores, and sometimes using them to derive GUPPIs, is not novel in UK retail merger cases. The Parties of course take no issue with the mandatory nature of this process in this case and conscientiously assisted the CMA on survey execution.
- (152) The disputed issue is one of interpretation and weight of what is a (i) notional or indicative profit incentive based on (ii) an inference from (iii) a hypothetical question.
- (153) Of course, the PFs do not say – outright – that the GUPPIs are "DNA-quality" or "smoking gun" evidence for an SLC. But this is the only coherent explanation the Parties have for the treatment of evidence and parts of the CMA provisional analysis and logic in the PFs on other issues, as set out below and in the remainder of the Response.<sup>44</sup>

### **F. The use of survey diversions as a trump card to dismiss other (more probative) evidence on closeness of competition**

#### **1. Hypothetical trumps actual: switching to SDI based on consumers' survey predictions trumps switching to SDI based on their actual behaviour (impacts)**

- (154) A prime example of this underlying presumption of SLC at work is on the critical issue of SDI elevation and whether it is (already now and likely future) a strategic threat to JD Sports in the relevant markets as both a large and "close", indeed "ever closer" competitor to JD Sports.
- (155) The chain of logic in the PFs is as follows. First, for SDI elevated stores, there is "actual diversion" customer behaviour (impacts) vs. "hypothetical diversion" (survey) behaviour.<sup>45</sup>
- (156) The CMA approaches this issue by asking itself whether the evidence disturbs the presumptive conclusion from the survey results (hypothetical diversion): it finds "*no clear difference in [survey] diversion when an elevated Sports Direct was present*" (PFs at paragraph 8.241), so the presumption of strong incentives to raise price, and therefore of SLC, are undisturbed by this evidence (i.e. it finds that the presumption is not rebutted).
- (157) For its critical overall conclusion on SDI, it says "*the evidence on [Sports Direct's] elevation strategy is mixed...*" and reaches for its prime adverse evidence relied upon for a presumptive SLC: "*... for example, findings from our store exit survey that diversion ratios [from JD stores to Sports Direct stores] are similar for elevated and non-elevated Sports Direct stores*" (PFs at paragraph 8.246) The conclusion is that "we

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<sup>44</sup> This was set out in more detail in the Prepared Remarks document presented at the Response hearing. For good measure, Company A has in this case probably done its level best to reaffirm the bias as it wishes for a forced (divestiture trustee) sale of Footasylum to it.

<sup>45</sup> The Parties presented customer switching evidence (actual diversion) based on "impact evidence" from SDI store elevation (cited at PFs paragraphs 8.240) that took away sales (customer footfall and spend) from JD Sports.

**CHAPTER 1 – THE USE AND MISUSE OF QUANTITATIVE TOOLS TO PREDICT SLC**

cannot conclude with sufficient certainty that [SDI’s] elevation strategy will significantly change the strength of the competitive constraint” [implied by the survey]” (paragraph 8.246).<sup>46</sup>

- (158) The PFs are replete with further examples of the central weight given to the store exit survey (and, to a lesser degree, the online survey which does not carry the restriction bias risk explained below which would bias findings against diversion to online-centric rivals).

**2. Survey diversion to third parties is treated as decisive and colours the CMA’s reading of other evidence as to strength of rivals**

- (159) This is also apparent from the following table. While the quotes below do not purport to capture the totality of the evidence cited by the PFs in respect of each rival, they highlight the point that the survey has coloured the appreciation of other evidence, which is either dismissed or read in a way consistent with the survey inferences. In particular, the store exit results have a crushing impact on the weight attached to pure-play online rivals (ASOS, Amazon, Zalando) and on online-centric DTC (Nike and adidas). However, because the Parties loom so large in the survey (given likely bias, discussed below), in general all third party rivals fall victim to the proposition that Footasylum primarily competes against JD Sports and other rivals are, in aggregate, relatively “loose change” as competitors.

Competitor	Adverse inference on “closeness” or “strength” of constraint
<b>Examples: pure-play online and online-skewed DTC rivals</b>	
<b>asos.com</b>	“...our store exit survey shows that ASOS is a <u>very weak</u> constraint on both [Parties]” (paragraph 9.158)
<b>amazon.co.uk</b>	“[o]ur store exit survey shows Amazon is a <u>very weak</u> constraint on the Parties.” (paragraph 9.161)
<b>zalando.co.uk</b>	“... [not] a close competitor to the Parties. This <u>lack of direct competition</u> is supported by our store exit survey, where Zalando and Amazon had levels of diversion below 2%” (paragraph 8.202)
<b>adidas.co.uk (&amp; stores)</b>	“[o]ur store exit survey shows that it exerts <u>some</u> constraint on JD Sports but <u>much less</u> so than Footasylum...” (paragraph 9.160)
<b>nike.com / gb (&amp; stores)</b>	“our store exit survey shows that while it exerts <u>some</u> constraint on JD Sports, it is a <u>weak</u> constraint on Footasylum. The online survey suggests Nike may be a closer competitor to JD Sports’ online customers than for [JD] in-store ... but a <u>weaker</u> constraint on Footasylum”. (paragraph 9.156)
<b>Examples: multi-channel rivals with (probable) skew towards store sales</b>	
<b>Sports Direct (stores &amp; .com)</b>	“although Sports Direct does impose <u>some</u> constraint, particularly for JD Sports according to our surveys, this is <u>substantially less</u> than that imposed by the Parties on each other”. (paragraph 8.201)
<b>Foot Locker (stores &amp; .com)</b>	“[o]ur store exit survey shows that it exerts only <u>some</u> constraint on JD Sports, <u>much less</u> than Footasylum; and a <u>weak</u> constraint on Footasylum (paragraph 9.157)
<b>Office (stores &amp; .com)</b>	“... [o]ur surveys found that <u>some</u> customers would divert to their stores or website but to a <u>much lesser degree</u> than to either of the Parties”. (paragraph 8.200)
<b>Schuh (stores &amp; .com)</b>	“... [o]ur surveys found that <u>some</u> customers would divert to their stores or website but to a <u>much lesser degree</u> than to either of the Parties”.

<sup>46</sup> Chapter 2 explains why the CMA’s analysis is factually wrong, and misconceived and unsustainable on this point.

### 3. Survey colours approach to internal documentary and other evidence

- (160) For example, though competitor monitoring of various third party rivals by the Parties in no way “matches” the proportions implied by the low store exit diversion ratios, the CMA reads the internal documents in a slanted way so as to dismiss the significance of various rivals monitored by one or both Parties (particularly but not only fast-fashion retailers that overlap with Footasylum’s apparel range) if they scored “low” or “non-existent” on the survey even if they feature with some significance in the internal documents.
- (161) This problem infects the analysis of internal documents evidence generally. (See further, Chapter 5) While not explicit, the Parties suggest the same has happened with the counterfactual (see Chapter 3).

#### G. The PFs also rely on a subjective competitor scoring exercise from Phase 1 which suffers from comparably severe flaws and unreliability

- (162) While it is not hypothetical in the exact manner of the consumer survey, the PFs also rely on the competitor scoring “opinion survey” exercise conducted during Phase 1 to judge “closeness of competition”.
- (163) This analysis suffers from comparably severe flaws as the CMA’s survey in that it is not based on actual customer behaviour to underpin findings of closeness. The question is prone to confuse competitors by taking “*closeness of competition*” language that for a layperson can be – and is in all probability likely to have been – interpreted simply “*what is your general industry sense of the overall similarity of product range?*” and taken the results as probative of the technical unilateral effects theory of SLC meaning of “*closeness of competition*” (a *demand-side*-only concept measured by diversion ratio / customer substitution patterns) in the technical sense used in SLC analysis.
- (164) In fact, the PFs’ recycling at Phase 2 on this subjective scoring exercise from Phase 1 is alarming and misguided. While consumer surveys are not at all uncommon, despite their limitations, there is a set way of trying to achieve the most robust version possible via. e.g. the best-practice guidelines. This “ask-around” approach on the supply-side to the question or “*closeness*” on the demand-side is novel, to the best of the Parties’ knowledge, and in any event conspicuously lacking in quality control and robustness.

#### 1. Incomplete entries highlight lack of robustness

For example, while it appears that 100% of respondents provided rankings for the Parties, around 50% of these respondents provided no additional rankings for any other retailer at all. The CMA would throw out half-completed consumer survey results but relies on half (or less)-complete competitor survey results.

- (165) This is also peculiar given respondents could have selected a rank of zero if they believed a particular retailer had little to no closeness of competition to the Parties. The PFs fail to acknowledge that the significant lack of mentions of any retailer whatsoever may likely be indicative of: (i) the framing of the survey question, which did not prompt rankings of any additional retailers; and (ii) a lack of incentive for respondents to provide further information than that required, rather than indicating a distinct ignorance to obvious market players or a belief that such players were very distant as opposed to very close competitors to the Parties. This suggests an unsystematic approach and rather simply an interpretation: *ignoring everyone else, are the Parties’ quite similar?*

## CHAPTER 1 – THE USE AND MISUSE OF QUANTITATIVE TOOLS TO PREDICT SLC

### 2. When mentioned, SDI, Nike and adidas scored as ‘closer’ to the Parties than JD Sports and Footasylum did to each other

(166) The lack of robustness and slanted drawing of conclusions by the PFs is emphasised by the fact that obvious competitors such as SDI, Nike and adidas all received overall higher scores than the Parties – i.e. an implication that they were *closer competitors to JD Sports (or Footasylum) than each Party was to each other* – a fact dismissed by the PFs – but gained relatively fewer mentions. The latter should not surprise: after all, the questionnaire came in the context of an RFI concerning the Merger of JD Sports and Footasylum – hence naturally creating a bilateral answering focus among respondents – and was not (perceived as) a systematic market-wide inquiry of competition.

### 3. The average score approach is dubious and lacks reliability

(167) Moreover, the PFs do not appropriately consider the selection bias inherent in the average "scores" attributed to other retailers and as such the weakness of such scores as evidence for the lack of closeness of competition. Given third parties were not requested (but had proactively to choose) to provide a ranking for retailers other than the Parties, it is likely that only those retailers with a particular incentive to provide additional rankings for other retailers would go through the effort of actually doing so.

(168) As such, the sample population that actually provided rankings for other retailers (around 50% the size of that for the Parties) had a bias towards including those who had a particular incentive to provide such rankings (i.e. the population would likely only include retailers with strategic incentives strong enough to elicit a response, rather than the more independent respondents). Thus, when coupled with the purely subjective nature of the "scoring" exercise, it is clear that no weight should be given to the average rankings attributed to other retailers as well as their comparisons to the average rankings attributed to the Parties.

### 4. Failure to ask respondents whether they considered themselves ‘close competitors’

(169) Additionally, even if we accept the validity or robustness of this type of question to competitors, it is unclear why respondents' views of their own "closeness of competition" to the Parties have been excluded from this exercise. Presumably, such retailers would be in the best position to opine on how closely they compete with the Parties (if they knew that meant degree of customer substitution). This omission is particularly concerning given the PFs note that certain retailers self-identified "both Parties as its closest competitors" (paragraph 8.189). As this information was considered by the CMA qualitatively, the Parties see no reason why it was omitted in the CMA's quantitative assessment.

(170) In the event such results were omitted by the CMA for fear of bias from particular third-party respondents' strategic incentives, it is clear (as noted above) that this omission would not be sufficient to eliminate the prospect of such bias in their other responses and as such all third-party responses should have been disregarded on the same grounds.

(171) Finally, it is notable that the PFs fail to consider that competitor concerns that the Merger would "strengthen JD Sports' position in the market" may relate to concerns that the Merger would make JD Sports more competitive, not less. As to JD Sports allegedly being able to squeeze Nike or adidas to reduce supply to rivals simply due to the accretion of Footasylum purchasing volumes, this is entirely fanciful on the evidence and it is difficult to see why horizontal rivals would suffer from less competition, higher prices, or other hypothetical worsening of JD Sports' or Footasylum's retail offer.

## CHAPTER 1 – THE USE AND MISUSE OF QUANTITATIVE TOOLS TO PREDICT SLC

### IV. Proper evaluation of all the 'non-GUPPI' evidence points to no SLC

- (172) The remaining Chapters in this Response discuss several critical issues and the evidence that pertains to them. These have all fallen victim to the framing question of the GUPPI model's predictions as to "*strong incentives*" to degrade PQRS post-Merger.
- (173) It is common ground between the CMA and the Parties that the GUPPI model is a static "demand-side" model, and as such does not capture "supply-side" repositioning (e.g. competitor elevation), expansion and entry: "*we agree these are not captured within the GUPPI*"; see PFs paragraph 8.146(c).
- (174) The fact that GUPPI does not capture these dynamics matters immensely to the "*strong incentive*" to raise price inference relied upon by the CMA. **Chapter 2** examines these issues both as discussed by the PFs and in the light of new evidence, with particular references to (i) SDI's elevation i.e. repositioning; (ii) the direct-to-consumer expansion of the brands, Nike and adidas; and (iii) further expansion and entry by Foot Locker and an array of other rivals.
- (175) The CMA [X] concludes that Footasylum is an "effective competitor" in the "most likely" counterfactual. This is [X] as explained in **Chapter 3**. It is also not the relevant question for interpreting the GUPPI or survey diversions, notably from JD Sports to Footasylum (where the GUPPI is already not high; for the Footasylum GUPPI as a basis for SLC, see section II.B.3 above). The issue is not the binary one of whether Footasylum is "ineffective" or "effective" but whether it would have been as "close" a competitor absent the Merger as it was imputed to be in the days of October 2019 when the survey was conducted, and when under the financial guarantee and stable ownership of JD Sports.
- (176) Last but by no means least, while the CMA does not disagree that the GUPPI does not capture the vertical role of suppliers, it argues that this does not matter in this case. **Chapter 4** explains why this premise is fundamentally wrong.
- (177) The inferences from the GUPPI are further not consistent with a careful forensic approach to the evidence from the internal documents, and the results of econometrics once corrected for errors. These issues are addressed in **Chapter 5**.



CHAPTER 2  
REPOSITIONING AND EXPANSION POINT TO NO SLC

I. Introduction

- (178) The disproportionate reliance by the CMA on its survey results and the subjective views of other retailers, combined with the flawed approach to the econometrics analysis and review of internal documents results in the CMA discounting virtually every competitor to the Parties:
- (a) For footwear, the PFs find that only Foot Locker is a close competitor to the Parties. SDI is found to provide "*some competitive constraint*" and other retailers such as ASOS, Schuh and Office also impose "*some competitive constraint*" but that this constraint is "*relatively limited*". Nike is similarly found to exert "*some constraint*" on the Parties, with adidas being "*a weaker constraint*". Other online-only retailers are not currently close competitors, according to the PFs. The PFs add that while SDI and others may become a stronger constraint over time, "*the evidence does not show with sufficient certainty that this would amount to a materially stronger constraint on the Parties in the next few years*".
  - (b) For apparel, PFs state that "*no other retailers clearly exert a strong constraint on the Parties in apparel*". Foot Locker is dismissed on the grounds of its limited apparel offering. SDI is noted to provide "*some competitive constraint*" but is also discounted given its "*different apparel offering from the Parties with currently a much greater focus on lower-priced products*". ASOS, Nike and adidas are considered to provide "*some constraint*" online, but a weak constraint in-store (which is inconsistent with the finding of a single market for both online and stores), and other high street retailers are considered to be "*relatively weak*". Again, the PFs state that while the constraint from some of these retailers "*may grow over time ... the evidence does not show with sufficient certainty that this would result in a materially strong competitive constraint on the Parties in the next few years*".
- (179) In the sections that follow, the Parties demonstrate that these findings – particularly as they relate to SDI and the brands' DTC offerings – cannot stand.
- (180) For footwear, the suggestion that SDI's access to higher tier products has "*almost exclusively been focused on sports rather than sports-inspired casual products*" is wrong. As shown below, SDI is increasingly gaining access to the same premium sports-inspired products as the Parties, including some of the Parties' best-selling footwear franchises and apparel lines.
- (181) For apparel, the suggestion that no other retailer provides a strong constraint on the Parties is simply not credible given the range of alternative retailers supplying both branded and own-brand sports-inspired apparel, and the differentiated propositions of the Parties.
- (182) In this respect, the CMA again takes an inconsistent approach to the evidence before it. On the one hand, the PFs concede that the Parties' apparel offerings have "*some similarities*", but considers this to be sufficient (given the survey evidence and the subjective "scoring" by competitors discussed in Chapter 1) to find that they exercise a strong constraint upon each other. On the other hand, the PFs find that the constraint imposed by SDI is weaker, given its offering "*is different in some respects*" to that of the Parties (another way of saying "some similarities"), notwithstanding the comparable diversions in the survey. The lack of credibility is further underlined by the fact that the Parties combined share is estimated to be less than [X] in online.

## CHAPTER 2 – REPOSITIONING AND EXPANSION POINT TO NO SLC

- (183) Again, the sections below demonstrate that the combined SDI / USC offering includes a wide range of sports-inspired and fashion-inspired premium brands, including Nike, Nicce, Lyle & Scott, Lacoste, Champion, Calvin Klein, Diesel and many others.
- (184) There are also at least four material flaws in the CMA's assessment of the brands' DTC growth which must be corrected, along with a number of omissions with respect to other retailers that must be reappraised.

### II. Repositioning and expansion by SDI point to no SLC

#### A. Overview

- (185) At paragraph 8.247 the PFs state "*on the basis of the evidence available, we cannot conclude with sufficient certainty that Frasers Group's elevation strategy will significantly change the strength of the competitive constraint on the Parties from Sports Direct*".<sup>47</sup>
- (186) In reaching this conclusion the CMA has erred in its interpretation and weighting of evidence provided by the Parties, SDI and key suppliers. Once these fundamental errors have been corrected and the new evidence submitted by the Parties has been considered, the CMA's conclusions in paragraphs 8.247 and 9.177 can no longer be maintained. SDI's ongoing elevation strategy means it must be considered a significant and growing competitive constraint on the Parties. This section makes the following points:
- (a) The PFs do not appropriately take account of SDI's continued repositioning and expansion, and its corresponding impact on the Parties.
  - (b) SDI is increasingly gaining access to the same premium sports-inspired casual products as the Parties (both apparel and footwear) and this submission presents new evidence to demonstrate this.
  - (c) There are a number of flaws in the CMA's assessment of evidence provided by the Parties regarding the success of SDI's elevation strategy.
  - (d) The PFs adopt a flawed market share methodology which significantly underestimates SDI's position in the market and bears no resemblance to the markets in which the Parties operate.
- (187) Even before examining the detail below, the Parties note that it may be inferred from its ongoing investments that SDI expects its elevation strategy to work; i.e. expects product allocations and then consumer spend to follow the large investment expenditure. The evidential burden required to supplant this revealed expectation of a market participant with a contrary expectation on the part of the CMA is high and not remotely made out.
- (188) Nor are the issues at hand ones that are resolved by looking at week-to-week impact analyses. An SLC finding should be robust and durable. If it is somehow contingent on 'today's data feed' it is neither robust nor durable, irrespective of what the precise read-out of that data is.
- (189) The remainder of this section addresses each of these points in turn.

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<sup>47</sup> See also paragraph 9.177 (sports-inspired casual apparel). The CMA states that most of its assessment of Frasers Group in paragraphs 8.212 to 8.241 also applies to apparel (paragraph 9.174). The points made in this section of the response to the PFs therefore apply equally to apparel.

**CHAPTER 2 – REPOSITIONING AND EXPANSION  
POINT TO NO SLC**

**B. Continued repositioning and expansion of SDI, and its impact on the Parties**

**1. SDI is aggressively pursuing its elevation strategy**

(190) SDI presently has 16 elevated stores (paragraph 8.217). It plans to open a further [REDACTED] in 2020 (paragraph 8.217), taking the total to [REDACTED] and plans to have [REDACTED] (paragraph 8.244). This evidence shows that: [REDACTED].<sup>48</sup> It is notable that SDI/Frasers' planned investment in its elevation strategy this year is equivalent to, if not greater than, Footasylum's expected annual turnover.

(191) The PFs note that SDI [REDACTED] and that such exogenous events may occur in the future (paragraph 8.238). It is not clear whether the numbers of stores quoted in the paragraph above are [REDACTED]. In any event, [REDACTED] Furthermore, [REDACTED] SDI's own statements to the public and investors which suggest that it intends to aggressively roll out its elevation strategy in the near future and beyond 2021.<sup>49</sup>

(192) Furthermore, the CMA's concern regarding SDI slowing its elevation strategy appears to be based on a single email (Annex 1228) supposedly suggesting that [REDACTED] The extrapolation of one-off negative events to the future prospects of SDI is clearly inconsistent with the CMA's approach to Footasylum's future prospects. It is unclear why similar weight is not given to positive prospective forecasts regarding SDI's elevation strategy in the PFs as was given to such evidence in the analysis of Footasylum's future prospects.

**2. SDI's elevated stores are having a significant negative impact on the Parties' stores**

(193) As noted in the Parties' previous submission, the opening of an elevated SDI store typically has a [REDACTED].<sup>50</sup>

**Table 1** [REDACTED][REDACTED]

[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]

[REDACTED]

(194) [REDACTED]

<sup>48</sup> Contrast paragraph 11.44, which talks about the "long timescales to establish a national in-store footprint". Whilst this paragraph is discussing entry by overseas retailers, it is evident that, when applied to SDI's elevated stores[REDACTED]  
<sup>49</sup> See for example - <https://www.sportsdirectplc.com/our-multi-channel-elevation-strategy.aspx>.  
<sup>50</sup> The CMA sets out this evidence at paragraphs 8.239 (and Figure 1) and 8.240.

**CHAPTER 2 – REPOSITIONING AND EXPANSION  
POINT TO NO SLC**

(195) Compass Lexecon has replicated JD Sports' internal impact analysis for Footasylum and also finds [REDACTED]

Table 2 [REDACTED]

[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]

[REDACTED]  
[REDACTED]

(196) The CMA responds to the evidence about the impact on JD Sports of the opening of an elevated SDI store by saying at paragraph 8.246 that the evidence is "mixed, for example findings from our store exit survey that diversion ratios are similar for elevated and non-elevated Sports Direct Stores". However, it is not credible to suggest that the evidence is only "mixed".

(197) In reaching this conclusion, the PFs note that there are non-differential survey diversion ratios between the Parties when looking at surveyed stores affected by an SDI elevation vs. surveyed stores not affected. As the survey diversion ratios are not lower for affected stores (vs. unaffected), the CMA concludes that the SDI elevation has not impacted the competitive dynamics between the Parties. As set out in detail in Annex 2.1, the PFs conclusion cannot be objectively justified:

- (a) Only four of the stores surveyed by the CMA have been affected by an SDI elevation (two from JD Sports and two from Footasylum). Due to an error in identifying one of the JD Sports stores, this is effectively only three stores.
- (b) In total, these three stores amount to the stated preferences of around 300 relevant respondents (in response to a hypothetical question), measured over the course of about three weeks in November 2019.
- (c) By comparison, the JD Sports internal impact analysis reporting [REDACTED] impacts on JD Sports stores reflects 225 weeks of data following an SDI elevation, and over [REDACTED] switching transactions (i.e. revealed preferences) from JD Sports to SDI.
- (d) Similarly, for Footasylum, the impact analysis conducted by Compass Lexecon shows [REDACTED] impacts reflecting [REDACTED] [REDACTED] following an SDI elevation, and over [REDACTED] [REDACTED].
- (e) The relative weighting applied by the CMA as between these two sources of evidence cannot be objectively justified.

(198) Furthermore, even leaving to one side this recognition that only limited weight could be attributed to the survey on this point, the survey records only stated preferences by shoppers, whereas the evidence submitted by the Parties is actual real-world behaviour of shoppers. For the reasons noted above in Chapter 1 the CMA's position is not credible. In other words, the CMA accepts that limited weight can be ascribed to evidence that it is in any event less probative than other evidence which shows clear evidence of an impact. Thus, there is evidence on both sides of the scales, but it is not accurate to describe it as "mixed": the evidence shows clearly that elevated SDI stores impose real economic hurt on the Parties.

**C. The CMA now has before it new evidence showing that elevated SDI is obtaining elevated access to 'higher-tier' sports-inspired casual products**

(199) The Provisional Findings reach the following provisional conclusion with respect to footwear, in paragraph 8.224:

**CHAPTER 2 – REPOSITIONING AND EXPANSION  
POINT TO NO SLC**

*"While Sports Direct has had some limited improved access to higher-tier products in these elevated stores, to date this has almost exclusively been focused on sports rather than sports-inspired casual products. We consider that for its elevation to materially change the competitive constraint that Sports Direct exerts on the Parties... in the foreseeable future, its elevation would need to lead to access to products similar to those stocked by the Parties in the sports-inspired casual footwear market, as well as a change in how consumers perceive the Sports Direct offer."*

- (200) Paragraph 8.224's statement that SDI has only received improved access to higher-tier "sports rather than sports-inspired casual products" does not reflect SDI's current product offering with regard to footwear. In the last three months, since the start of this Phase 2 process, SDI has gained access to a wide range of higher-tier sports-inspired casual products including some of the Parties' best-selling footwear franchises. Once this critical error of fact is corrected and is taken into account with the Parties' impacts analysis the only rational conclusion is that SDI's elevation strategy makes it a key competitive constraint on the Parties.
- (201) For apparel, the PFs take the position that SDI is a relatively weak constraint on the basis that its offering "is different in some respect" from that of the Parties (paragraph 9.155). The PFs also state at paragraph 9.176 that "[w]e consider that the scope for Frasers' Group's elevation strategy to significantly change the constraint that its Sports Direct and USC fascia exert on the Parties is more limited in apparel than in footwear. This is due to the fact that a greater proportion of apparel sales come from a wide range of suppliers of branded products other than Nike and adidas (who are generally less restrictive)".
- (202) The view expressed in the PFs with respect to apparel is also not reflective of the current competitive reality, in which the combined SDI / USC offering includes a wide range of sports-inspired and fashion-inspired premium brands, including Nike, Nicce, Lyle & Scott, Lacoste, Champion, Calvin Klein, Diesel and many others.

**1. Overview of new evidence**

(203) [redacted]<sup>51</sup>[redacted].

(204) [redacted].

**Table 3** [redacted][redacted]

[redacted]

**2. Higher-tier or 'premium' sports-inspired casual footwear**

(205) [redacted]

(a) [redacted]

(b) [redacted]

(c) [redacted]

(d) [redacted].

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<sup>51</sup> Aintree, **Camden**, Cardiff, Darlington, **Denton**, **Didcot**, **Glasgow Fort**, **Lakeside**, Leeds, **Leicester**, Meadowhall, **Merry Hill**, Middlesbrough, **Northwich**, Oxford Street, Romford, Southport, Stratford, **Watford**, **Widnes**, **Woolwich**, **Worksop**, **York** (elevated stores in bold).

**CHAPTER 2 – REPOSITIONING AND EXPANSION  
POINT TO NO SLC**

(206) [X]<sup>52</sup>[X]

(207) [X][X].

[X]

[X]

(208) [X].

(209) [X]

(210) [X].



**3. Higher-tier or 'premium' sports-inspired casual apparel**

(211) [X]

(a) [X]

<sup>52</sup> Save for Nike Cortez.

**CHAPTER 2 – REPOSITIONING AND EXPANSION  
POINT TO NO SLC**

(b) [X]

(c) [X]

(d) [X]

(212) [X][X].

[X]

[X]

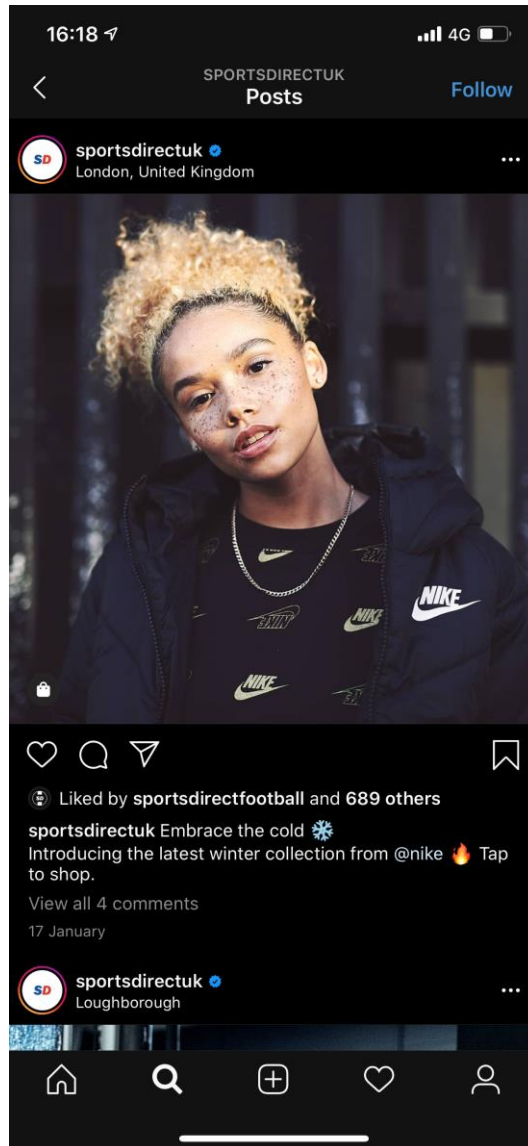
[X]

[X]

(213) This evidence undermines the PFs' conclusion in paragraph 9.176 that the "*constraint that... Sports Direct and [its] USC fascia exert on the Parties is more limited in apparel than in footwear.*" It is clear that SDI / USC's apparel offering [X] and that they offer a wider range of sports-inspired and fashion apparel due to the fact that their stores are typically larger so can stock more products and can also house two fasciae within the same building.

(214) As with footwear, [X]

**CHAPTER 2 – REPOSITIONING AND EXPANSION  
POINT TO NO SLC**



**4. Elevated store displays and website/social media**

(215) [X]:

[X]

(216) [X][X]:

[X]

[X]

(217) [X].

**5. SDI / USC's access to higher-tier sports-inspired products is already having an impact on the Parties' store sales**

(218) The PFs note that even if SDI obtains access to similar products to JD Sports, it may "take time for perceptions of Sports Direct to change" (paragraph 8.237 and see also paragraph 8.234). This is no more than speculation and ignores the many ways in which SDI's offering is closely mimicking that of JD Sports.



## CHAPTER 2 – REPOSITIONING AND EXPANSION POINT TO NO SLC

(219) In any event, it is inconsistent with the impacts data which the Parties have submitted at Section B above. New elevated SDI / USC stores are having [REDACTED] on the Parties. This impact will only increase as SDI gains access to an increasing number of higher-tier products.

### 6. The PFs do not appear to have interrogated SDI's submissions regarding product access

(220) The CMA has relied upon a number of submissions presented by SDI where there appears to be little interrogation of its completeness or accuracy. Moreover, the PFs have ignored fundamental documentary evidence from verifiable sources in favour of evidence from a key competitor. For example, while SDI's submissions emphasise the [REDACTED]<sup>53</sup>[REDACTED] the CMA has dismissed JD Sports' submissions highlighting that various [REDACTED] franchises were available on SDI's website (thus nationally).<sup>54</sup> The Parties' recent analysis above demonstrates that SDI has gained access to a wide range of sports-inspired premium products.

### 7. This new evidence demonstrates that SDI / USC's elevation strategy is supported by the brands

(221) Paragraph 2.228(a) states that "[REDACTED]

(222) This appears to be wording [REDACTED] The paragraph goes on with what cannot be further wording but is in fact the CMA's own provisional conclusion:

[REDACTED]"

Similarly, the PFs state at paragraph 8.245 "[REDACTED]."

(223) The new evidence above unequivocally demonstrates that none of the conclusions drawn by the CMA are supportable or correct. In fact, as is to be expected, it was the [REDACTED]" and not the [REDACTED]: SDI / USC's elevation strategy now has the support of the brands. SDI / USC is gaining access to a large range of sports-inspired premium casual products in significant volumes.

(224) Even if this new evidence had not been available, there is sufficient evidence within the PFs to demonstrate that [REDACTED].

(a) The PFs note [REDACTED].

(b) Additionally, [REDACTED] demonstrated in paragraph 8.226 which notes that [REDACTED]

(225) [REDACTED].

(226) In any event, the CMA is not asking the relevant question. The issue is not whether suppliers would maintain the status quo in terms of access to SKUs if the merged group continued to operate in exactly the same way as the two Parties. If that were the case, there would be no SLC. Thus, even if the CMA was not satisfied that SDI is securing allocations of premium product in the relevant markets (despite all of the evidence to the contrary), the issue that would then have required investigation and analysis is instead: how would the suppliers and SDI react if the merged group sought post-Merger to reduce its PQRS? The PFs do not consider this question, even though the Merger Assessment Guidelines make clear at paragraph 5.4.11 the importance of considering responses to any attempt by the merged group to impose a reduction in PQRS. As shown above, it is clear that key suppliers are already giving SDI / USC access to premium sports-inspired casual products and there is no evidence to suggest that this

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<sup>53</sup> PFs, paragraph 8.226(d)

<sup>54</sup> JD Sports' note on Repositioning of Sports Direct Brand and Multichannel Offer, paragraph 2.3

## CHAPTER 2 – REPOSITIONING AND EXPANSION POINT TO NO SLC

trend would not continue or accelerate if the Parties opted to deteriorate the PQRS of their stores and online offering.

### D. These new facts compound existing flaws in the PF's assessment of the Parties' evidence

- (227) The CMA looked in detail at the responses of the Parties to SDI / Frasers Group's elevation strategy (paragraphs 8.229 to 8.240).
- (a) The PFs argue that some of the more recent documents submitted by the Parties "may" be undermined or "could be influenced" by the fact that the Merger was then in contemplation. However, the CMA cites no evidence that large numbers of documents were or might have been created including false or misleading statements about the operation of the market. The reality is that the documents were created in the normal course of business and they were created after SDI began to implement its elevation strategy, because that was when the Parties started to be affected.
  - (b) At paragraph 8.233 the PFs note that [REDACTED] This is incorrect – at the time JD Sports did have [REDACTED] (as it does all of its key competitors), but the [REDACTED] was used in the email referred to by the CMA to indicate that the SDI was an elevated store.
  - (c) At paragraph 8.235, the CMA notes that an email that described an elevated store as a [REDACTED] did not [REDACTED]. However, it seems entirely sensible and unexceptionable that a company facing a [REDACTED] threat should [REDACTED] before formulating the detail of its response.
  - (d) At paragraph 8.234, the PFs cite an email which notes that SDI is [REDACTED] recent evidence which shows that SDI is rolling out its new elevated stores in prime city-centre locations which are in close proximity to the Parties' stores.
  - (e) At paragraph 8.243, the CMA relies on the fact that "JD Sports is unsure of the likely success of Frasers Group's elevation strategy". The internal documents cited in the PFs suggest that it is difficult to forecast the impact of an SDI store pre-opening (see paragraph 8.237), not that JD Sports is unsure of the success of the strategy. The impacts data presented above makes it clear that SDI is having a [REDACTED] on both Parties. In any event, as the CMA will appreciate, "[REDACTED]" (to quote Peter Cowgill, as the PFs do at paragraph 8.234). If JD Sports competes successfully, it will defeat or mitigate the effects of SDI / Frasers Group's elevation strategy. But there is no doubting that SDI believes that it is likely to succeed, given the amount of capital it is allocating, the statements quoted above in its interims of 18 December 2019 and, indeed, its quote in the PFs at paragraph 8.225(a) saying elevation "[REDACTED]".

### E. The CMA's market share methodologies are also flawed

- (228) In reaching its conclusion that SDI is a limited constraint on the Parties, the CMA places some weight on its market share analysis which states that SDI has a market share of 0-30% for sports-inspired footwear and 0-40% for sports-inspired apparel. The CMA uses two market share methodologies (which yield significantly different results) and adopts the mid-point as its estimate of each retailers' share. This approach obfuscates the fact that under 'Methodology 1', SDI is [REDACTED]
- (229) The Parties have a number of concerns regarding the robustness of these shares and believe they should not be given any weight by the CMA in its analysis. The Parties' observations are as follows:
- (a) First, neither the Parties nor the sector typically segment their products into 'sports-inspired' and 'non-sports-inspired', meaning that a level of discretion is required to determine how a product

## CHAPTER 2 – REPOSITIONING AND EXPANSION POINT TO NO SLC

should be classified<sup>55</sup> (and the CMA itself acknowledges that "[t]he distinction between sportswear and fashionwear and consumers' perceptions of them is often fluid, with sportswear also being worn as fashionwear. This, coupled with the fast-changing nature of fashion, makes it difficult to distinguish clearly between the sectors and different products within them")<sup>56</sup>.

- (b) Second, the CMA recognised this as an issue (for market share purposes), yet proceeded to ask retailers to "self-categorise their data".<sup>57</sup> This discretion can easily result in inconsistencies if a retailer is under-inclusive or over-inclusive in determining whether a product or brand is 'sports-inspired' or not. For example, JD Sports classified its sales of The North Face in the JD Sports fascia (£[redacted] million in-store) as 'sports-inspired' when it would have been equally as defensible to classify that brand as 'outdoors' or 'non-sports-inspired'. Similarly, JD Sports also classified football training apparel (£[redacted] million in-store) and running apparel and footwear as 'sports-inspired'. If JD Sports adopted a different approach it could have significantly reduced its sales and market share. As stated in Peter Cowgill's cover letter to the response to the Annotated Issues Statement: without ensuring each retailer's revenues for sports-inspired footwear and apparel are comparable and produced on a like-for-like basis, the current market shares are uninterpretable and cannot be relied upon.
- (c) Third, by allowing retailers like SDI this level of discretion, the PFs arrive at entirely meaningless market share ranges [redacted]. The fact that the CMA continues to state both figures without arriving at any conclusion on SDI's presence in the market does not address any of the concerns JD Sports expressed in its cover letter to the response to the Annotated Issues Statement.
- (d) Fourth, it is clear that the CMA has not interrogated the figures submitted by SDI to calculate the market shares. For example, there is huge variance in the share of revenues which is in the frame of reference between the Parties and SDI – the share of JD Sports' total revenues in the frame of reference is in the range [redacted]% for footwear and [redacted]% for apparel and for Footasylum it is in the range [redacted]%, while for [redacted] Market shares become uninterpretable if each retailer is able to define the market as it wishes, as has clearly been the case with the CMA's market share analysis in this case.
- (e) Fifth, retailers for which the CMA had estimated shares in Phase 1 now no longer have a separate share in the latest market shares (e.g. Clarks, Intersport and brands like New Balance, Converse, Vans, Fila, Asics, Under Armour, etc.), and it is not clear whether they have been grouped into 'other' or entirely removed from the analysis.
- (f) Last, the CMA provides no reconciliation between its market share analysis and the estimated market shares for Nike, adidas and non-Nike-adidas prepared by Compass Lexecon and submitted by the Parties to the CMA on 26 November 2019. Annex 2.3 contains an update on these "decomposed" shares, using the CMA's updated market shares from the PFs, which continue to show low increments for all market segments.

### III. Brands' DTC expansion points to no SLC

- (230) The CMA's PFs recognise the growth of DTC as an important and competitive dynamic in the market, but this ultimately does not appear to have any bearing on its view of the likelihood of an SLC.
- (231) The PFs take the position that:

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<sup>55</sup> For example, PFs acknowledge that both [redacted] do not apply this segmentation in the ordinary course.

<sup>56</sup> Provisional Findings, paragraph 2.3.

<sup>57</sup> Provisional Findings, Appendix G, paragraph 12.

## CHAPTER 2 – REPOSITIONING AND EXPANSION POINT TO NO SLC

- (a) DTC will grow in absolute terms, but predominantly online, and this will not constrain the in-store channel; and
  - (b) This DTC growth is likely to reflect "*general growth in the market*" and therefore the DTC-wholesale ratio (and competitive dynamics) will essentially remain unchanged going forward (paragraph 8.260).
- (232) There are at least four material flaws to the CMA's assessment of DTC growth, which are explained in further detail in Annex 2.1 to this response and summarised below.
- (233) First, the proposition in the PFs that DTC growth online will not constrain the Parties in-store is fundamentally inconsistent with its treatment of online as a constraint on in-store channels at the prior stages of its consideration of the relevant market. The CMA states in the PFs at paragraph 8.262:
- "... our provisional view is that over time the key suppliers' DTC offer may become more of a constraint online but not in-store. The evidence does not show with sufficient certainty that Nike's and adidas' DTC offer across either channel will become a significantly strong constraint on the Parties in the market for the retail supply of sports-inspired casual footwear in the foreseeable future."*
- (234) In adopting this approach, the CMA is acting inconsistently with its provisional findings on market definition. At paragraphs 7.62 and 7.63, the CMA found:
- "in relation to the demand-side, there is an apparent willingness of a sizeable proportion of consumers within each channel to divert to the other channel and that past spending behaviour of consumers is consistent with these switching proportions. We consider that these switching proportions are likely to be large enough to act as a constraint on the alternative channel. On the supply-side, generally retailers operate their instore and online businesses together, although we recognise some retailers are present only online."*
- On balance, our provisional view is that a sufficient proportion of consumers currently shop in both the in-store and online channels, or would be prepared to move between the two channels, in order for the two channels to be considered within the same product market. Nevertheless, we have examined any material differences between the channels in the constraints on the Parties and the strength of constraint on the Parties of retailers who operate only or primarily in each channel, in our competitive assessment (see chapter 8)."*
- (235) If (as the CMA provisionally found) a sizeable proportion of in-store customers is willing to switch to online, then the key suppliers' DTC offerings must be an important constraint on the parties' stores. The PFs' approach seems remarkable and appears to be a new form of 'zero-one' fallacy, with a constraint inside the market being attributed a weight of zero.
- (236) Second, the CMA's view that the DTC-wholesale ratio will remain constant going forward:
- (a) Is inconsistent with the evidence submitted by the Parties showing progressive disintermediation of the wholesale channel, as well as the evidence of recent growth of DTC relative to wholesale revenues quoted in PFs;
  - (b) Is simply an incorrect reading of the facts provided by the brands, which already predict their wholesale share of revenues to fall relative to total revenues going forward, and the decrease is not trivial given the evidence that DTC growth is ongoing and material; and
  - (c) Implies an implausibly large increase in the growth of wholesale revenues relative to current and historic growth.

## CHAPTER 2 – REPOSITIONING AND EXPANSION POINT TO NO SLC

- (237) In assessing the growth of DTC, it is also very important to bear firmly in mind just how large a constraint it is already. Some of the Parties' advisers now have the market shares which have been disclosed into the confidentiality ring. [REDACTED].
- (238) Third, the PFs fail to consider the relevant issue of how DTC will grow relative to Footasylum. In previous submissions, the Parties found that the growth of DTC could [REDACTED]. The conclusions hold even after updating the analysis using figures from the PFs.
- (239) Lastly, the CMA makes a number of claims regarding the diversion from JD Sports to Footasylum in the PFs. Following from statements that the brands are planning to grow DTC in the next few years, the CMA's claims regarding the diversion from JD Sports to Footasylum will cease to be valid in two-three years.
- (240) It follows that the CMA's assessment of the constraint from DTC growth going forward needs to be fundamentally reappraised.

### IV. Other market dynamics are not properly accounted for

- (241) In reaching their conclusion, the PFs do not take account of the evidence submitted by the Parties regarding Foot Locker's expansion plans or the evidence of other third-parties' expansion plans.

#### A. Foot Locker

- (242) There are a number of flaws in the PFs' assessment of the competitive constraint posed by Foot Locker:
- (a) **The CMA has not considered the Parties' submissions regarding Foot Locker:** JD Sports submitted over 133 internal documents regarding Foot Locker's expansion plans, none of which are referenced or addressed by the PFs.
  - (b) **The PFs do not take account of the fact that Foot Locker's new openings are typically large stores which stock both apparel and footwear:** Whilst the PFs acknowledge that Foot Locker has plans to open [REDACTED]. In reaching this conclusion, the CMA points to the uncertainty around whether the [REDACTED]. However, this ignores the fact that even Foot Locker's new stores are large and stock both footwear and apparel (even if those which are not power stores). For example, one of JD Sports' internal documents (Annexes 1317-1319) notes that Foot Locker's new flagship store in Manchester Arndale will be [REDACTED]". A store this size cannot only stock footwear and will stock both apparel and footwear.
  - (c) **The PFs do not appear to assess whether Foot Locker is refurbishing its stores:** The PFs make no mention of whether Foot Locker is refurbishing its stores to include both apparel and footwear.
  - (d) **The PFs do not consider Foot Locker's plans to open community stores:** JD Sports submitted internal documents that indicate that, as part of its expansion strategy, Foot Locker is intending to open stores in "lower grade locations" called "Community Stores" which it would not have historically targeted.<sup>58</sup>

#### B. ASOS

- (243) There are also a number of flaws in the PF's assessment of the competitive constraint posed by ASOS:
- (a) **The PFs erroneously conclude that ASOS is primarily focused on female customers:** The PFs state at paragraph 44 that ASOS is "strongly focused on female customers". However, this

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<sup>58</sup> See Annex 1316.

## CHAPTER 2 – REPOSITIONING AND EXPANSION POINT TO NO SLC

is not borne out by the evidence which shows that ASOS is a significantly larger competitor than Footasylum in men's apparel and men's footwear. By way of example, in an online search undertaken by Footasylum on 27 February 2020, ASOS was found to offer a total of 989 men's trainers compared to Footasylum, whose offering at the time was comprised of a total of [REDACTED] men's trainers.

- (b) **The PFs give no weight to the Parties' internal documents which monitor ASOS:** Moreover, to the extent that the CMA considers that the competitive monitoring undertaken by the Parties in their internal documents provides a measure of closeness of competition (which the Parties do not agree with) then the CMA must give greater weight to the internal documentary evidence which shows that online players such as ASOS and Zalando compete closely with Footasylum and its more fashion-focused apparel offering, The PFs fail to take account of this.

### C. Other retailers

- (244) While a number of other retailers have submitted evidence detailing their expansion plans, the CMA has failed to take the individual or aggregate impact of these growing competitive constraints into account.
- (245) For example, while [REDACTED] submitted evidence that it was planning around [REDACTED] new store openings a year in the UK, its expansion does not appear to have been given any weight in the PFs. The omission of [REDACTED] is particularly concerning given the CMA's entry-exit survey which evidences that [REDACTED] store and retailer entry has a significant negative impact on JD Sports' footwear revenues, highlighting that its stores impose a particularly strong competitive constraint. Instead, the PFs inexplicably dismiss [REDACTED] on the basis that the retailer *"only sold footwear and not apparel, and that it did not deal with Nike or adidas"* (paragraph 21 to Appendix H of the PFs). Given the CMA's market definition approaches footwear and apparel as distinct markets, it is unclear why the CMA has completely excluded a significant constraint in footwear on this basis. Further, while [REDACTED] may or may not deal with Nike or adidas directly, this is irrelevant. The retailer sells a broad array of Nike and adidas products online and throughout its store estate, posing a competitive constraint on the Parties as evidenced by the CMA's own admission that [REDACTED].
- (246) Further, the CMA briefly outlines evidence from another six unidentified competitors' store expansion plans, which project a further 18 store openings over the next two years (Footnote 126, Appendix H of the PFs). This figure is not negligible, and it is unclear why the CMA has not addressed the growing aggregate constraint of these competitors in the PFs.
- (247) Moreover, the PFs cite a number of examples of supply side response to change in demand in terms of entry into the segment, but then downplays the prospects for effective repositioning and entry / expansion in response to the Merger. For example, in paragraph 2.7 the PFs note that there are *"a number of online-only retailers... such as ASOS, Amazon, BoohooMAN and Zalando which sell sports-inspired casual products"* and that *"some of these retailers – such as ASOS – have launched their own athleisure brands."* The PFs also note that a number of fashion specialists have launched their own active wear range (including, Zara, Topshop, H&M, Gap, Primark, next, Joules and BoohooMAN).
- (248) Similarly, the PFs identify recent expansion by multi-brand retailers such as ASOS and Next into 'sports-inspired products' and then dismiss this on the basis that [REDACTED]. The CMA has not provided the Parties' advisers with full access to information relating to these expansion plans such that this evidence could be properly contextualised and the likelihood of their ongoing expansion could be appropriately substantiated. The Parties note that had the opportunity for a full and comprehensive analysis of this evidence been permitted, it would demonstrate that these retailers pose a significantly growing constraint on the Parties.

**CHAPTER 2 – REPOSITIONING AND EXPANSION  
POINT TO NO SLC**

- (249) JD Sports also submitted evidence which demonstrates that [REDACTED]
- (250) Finally, when these omissions are set against the context (acknowledged by the CMA) that Footasylum would be operating in this period with [REDACTED] (see for example paragraph 5.27 of the PFs and further detailed at Chapter 3), it is clear that such expansion from these other retailers, when appropriately taken into account, demonstrates a significantly increased competitive constraint to the Parties.

## CHAPTER 3 THE COUNTERFACTUAL

### Introduction and executive summary

- 1.1 Footasylum considers that the facts and evidence presented to the CMA do not support the CMA's Provisional Findings that the most likely counterfactual, absent the Merger, is one in which Footasylum trades in line with its FY20 budget (referred to by the CMA as the "central forecast"), overcomes any short term financial difficulties [REDACTED]
- 1.2 Rather, as set out in Footasylum's previous responses on the counterfactual<sup>59</sup>, Footasylum's view is that the facts and evidence show that the most likely counterfactual is one in which, in any scenario, Footasylum [REDACTED]<sup>60</sup>[REDACTED]
- 1.3 To assist the CMA in its assessment of the counterfactual, this paper set outs new evidence from [REDACTED] for a number of years prior to the Merger.
- 1.4 This new evidence is provided by way of a witness statement from [REDACTED]<sup>61</sup>, [REDACTED].
- 1.5 [REDACTED] In the absence of the Merger:
  - 1.5.1 an equity fundraise, suitable alternative debt-funding and a sale to private equity [REDACTED];

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59 Footasylum's Response to Question F1 of the CMA's Financial Questionnaire dated 15 October 2019; Footasylum's response to Questions F9, F10 of Section 109 Notice (Financial) dated 15 October 2019; Response to CMA Counterfactual Working Paper

60 Footasylum notes that it is not suggesting that the exiting firm scenario (or failing firm defence) applies in this case. This is explicitly acknowledged by the Provisional Findings at paragraph 5.11. Rather, Footasylum submits that in the counterfactual it would have been a materially diminished competitor. This is an approach which the CMA has recognised in other cases, most recently in its Provisional Findings relating to Bottomline's purchase of Experian Payments Gateway business where the CMA stated "the CMA has now provisionally found that the merger is not likely to raise competition concerns. This is largely because the CMA has found that EPG was no longer a strong force in the market ..."

61 Annex 3.1. Please note that Annex 3.1 contains business secrets to Footasylum and GCA Altium. This witness statement and the identity of [REDACTED] should be kept strictly confidential.



## CHAPTER 3 – COUNTERFACTUAL

- 1.5.2 [REDACTED] evidence is that “*We had also understood [REDACTED]*”<sup>62</sup>;
- 1.5.3 “*the company was [REDACTED]*”<sup>63</sup>; and
- 1.5.4 “*... it is most likely that Footasylum would have continued to [REDACTED] This would have [REDACTED]*.”<sup>64</sup>
- 1.6 Footasylum therefore submits that this new evidence provides further evidence for concluding that absent the Merger, Footasylum [REDACTED]
- 1.7 In addition to [REDACTED] new evidence, this paper also sets out the facts and evidence which show that:
- 1.7.1 the CMA’s Provisional Findings on the counterfactual are fundamentally flawed; and
- 1.7.2 even if the Provisional Findings are correct in that Footasylum would have passed its going concern test then, [REDACTED]
- 1.8 As discussed with the CMA at the Response Hearing, Footasylum considers that the outcome of the CMA’s analysis of the counterfactual is critical to the CMA’s overall assessment of the Merger. As the Provisional Findings acknowledge, “*the choice of the counterfactual could be a situation either more or less competitive than the competitive conditions prevailing at the time the merger occurred. Therefore, the selection of the appropriate counterfactual may increase or reduce the prospect of an SLC finding*”<sup>65</sup>.
- 1.9 In this case, the counterfactual is one where [REDACTED] [REDACTED] the time the Merger occurred. Consequently, the counterfactual reduces the basis for an SLC finding: [REDACTED]. The CMA must take this into account in its substantive analysis. This includes its interpretation of its survey results and GUPPI and the CMA’s entry-exit impact analysis. [REDACTED] absent the Merger, it is likely that a dynamic assessment would see a reduction in competition between the parties. This is particularly the case [REDACTED] In addition, Footasylum’s [REDACTED] the growth in rivalry from entry and expansion required to offset its loss as an independent competitor.
- 1.10 The remainder of this paper is structured as follows:
- 1.10.1 section 2 sets out the legal framework for assessing the counterfactual;
- 1.10.2 section 3 summarises the CMA’s Provisional Findings on the counterfactual;
- 1.10.3 section 4 sets out the new evidence from [REDACTED], which further substantiates Footasylum’s view that, [REDACTED];
- 1.10.4 section 5 explains why the Provisional Findings’ analysis of the counterfactual is fundamentally flawed;

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<sup>62</sup> Ibid.

<sup>63</sup> Ibid.

<sup>64</sup> Ibid.

<sup>65</sup> Paragraph 5.5 of the Provisional Findings Report dated 11 February 2020

## CHAPTER 3 – COUNTERFACTUAL

- 1.10.5 section **Error! Reference source not found.** shows that even assuming that the Provisional Findings’ assessment of the counterfactual is correct, then even in that instance Footasylum [✗];
- 1.10.6 section 7 explains why Footasylum’s performance [✗] cannot be taken as evidence to support the CMA’s provisional findings – [✗] and is not therefore relevant to an assessment of the counterfactual; and
- 1.10.7 section 8 concludes why it is Footasylum’s view that in any scenario Footasylum [✗].

### 2. Legal framework for assessing the counterfactual

- 2.1 As set out in the Provisional Findings<sup>66</sup>, in its assessment of the counterfactual, the CMA must select what it considers to be the “*most likely*” scenario “*based on the facts of the case*”. The CMA must therefore incorporate into the counterfactual only those aspects of scenarios that appear “*likely*” and foreseeable, and avoid including any “*spurious claims*”. The CMA considers that it should not be “*necessary to make finely balanced judgements about what is and what is not included in the counterfactual*”<sup>67</sup>.
- 2.2 This test requires the CMA to ensure that its findings are on the most likely counterfactual, therefore take into account of all relevant evidence and facts presented during this inquiry.

### 3. Summary of the CMA’s Provisional Findings on the counterfactual

- 3.1 Footasylum understands that the Provisional Findings consider that the most likely counterfactual is one in which Footasylum “*would have remained an effective competitor despite its financial issues*”.<sup>68</sup> This is based on the following:
  - 3.1.1 Footasylum’s [✗] were largely one-off and steps had been taken to mitigate them;
  - 3.1.2 [✗] and therefore the most likely outcome and the assumptions underpinning it are reasonable and it is largely in line with third-party analysts;
  - 3.1.3 [✗] “*very pessimistic*”<sup>69</sup> and given very little weight;
  - 3.1.4 Footasylum would have [✗];
  - 3.1.5 Footasylum would have been considered [✗];
  - 3.1.6 Footasylum would [✗];
  - 3.1.7 [✗];
  - 3.1.8 although the CMA recognises that [✗];
  - 3.1.9 [✗]; and

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<sup>66</sup> Paragraphs 5.3 to 5.5 of the Provisional Findings Report dated 11 February 2020

<sup>67</sup> Paragraph 5.4 of the Provisional Findings Report dated 11 February 2020

<sup>68</sup> Paragraph 5.49 of the Provisional Findings Report dated 11 February 2020

<sup>69</sup> Paragraph 5.44(a) of the Provisional Findings Report dated 11 February 2020

## CHAPTER 3 – COUNTERFACTUAL

3.1.10 [X].

3.2 These findings are wrong for the reasons addressed in this paper.

### 4. **New evidence from [X] further supports Footasylum’s view that the most likely counterfactual [X]**

4.1 In order to assist the CMA’s investigation, Footasylum has obtained new evidence from [X]. This is in addition to the contemporaneous evidence from GCA Altium previously provided to the CMA<sup>70</sup>. This evidence is provided by way of a witness statement from [X], which is attached at Annex 3.1.

4.2 [X]

4.3 [X] was highly familiar with the Footasylum business and the challenges it faced. [X]

4.4 [X]<sup>71</sup>

4.5 [X] is that there are a number of reasons for this. These are summarised below.

4.6 January 2019 market announcement was [X] for the company:

4.6.1 [X].

4.6.2 [X] explains that: “By November 2018, after two profit warnings within the first year of an IPO and a sharp fall in share price, [X].”<sup>72</sup>

4.6.3 [X]

4.7 [X]: The market announcements made by Footasylum reflect that it was [X].

4.8 [X]: “[X]<sup>73</sup>. This is consistent with the message the bank had given directly to the CFO of Footasylum at the time: [X]<sup>74</sup> (referred to at paragraph 5.27.1 below).

4.9 Equity fundraise, alternative debt-finance and private equity [X] By November 2018, Footasylum’s [X] [X]

4.10 [X]

4.10.1 As the CMA is aware, Footasylum approached [X]<sup>75</sup>

4.10.2 [X].<sup>76</sup>

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<sup>70</sup> See, for example, Annex 004 of our response to Question F9 of the s. 109 (financial) notice dated 15 October 2019 (004. Notes from call with Sam Fuller 9 Jan)

<sup>71</sup> Annex 3.1.

<sup>72</sup> Ibid.

<sup>73</sup> Ibid.

<sup>74</sup> Annex 388 of our response to Question 3 of the s. 109 notice dated 23 May 2019 (Notes from HSBC Meeting.docx)

<sup>75</sup> Ibid.

<sup>76</sup> Ibid.

## CHAPTER 3 – COUNTERFACTUAL

4.10.3 As a listed company with [REDACTED]<sup>77</sup>

### 4.11 Footasylum [REDACTED]:

4.11.1 By "... February 2019, the company was [REDACTED]"<sup>78</sup>

4.11.2 "Clearly given this backdrop, [REDACTED], against a volatile and generally negative wider UK retail backdrop [REDACTED]"<sup>79</sup>

4.11.3 [REDACTED] therefore believed that Footasylum [REDACTED] [REDACTED] [REDACTED]<sup>80</sup>

4.12 For these reasons [REDACTED] considers that "[i]n the period of time up until the Merger, [REDACTED]. The position it was in by January 2019 [REDACTED]"<sup>81</sup>

4.13 Footasylum considers that this witness statement from a key witness to events at the time further corroborates Footasylum's view that the facts and evidence available to the CMA (a) do not support the CMA's Provisional Findings on the counterfactual and (b) do support Footasylum's view that absent the Merger it is most likely that [REDACTED].

## 5. **An explanation of why the Provisional Findings' analysis is fundamentally flawed**

[REDACTED]

5.1 Prior to the Merger, [REDACTED].

5.2 A key part of the audit process is the "going concern test". As set out in the Provisional Findings<sup>82</sup>, this is a regulatory requirement which requires an assessment by the directors and the auditors as to whether the business will be a going concern for the foreseeable future (12 months from the date of the audit). As recognised by the Provisional Findings, as part of this process, auditors will undertake a sensitivity analysis of a company's forecast / budget based on key assumptions.

5.3 The Provisional Findings determine that "the evidence shows that under its central forecast, Footasylum [REDACTED]"<sup>83</sup>

5.4 Footasylum understands that because [REDACTED]<sup>84</sup>[REDACTED]<sup>85</sup>

5.5 [REDACTED]. [REDACTED] The Provisional Findings make clear that auditors must "... review and challenge forecasts, test, historic and forecast covenant compliance, including review of the forecast level of headroom available under these covenants and undertake sensitivity analysis on key assumptions."<sup>86</sup> [REDACTED]

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<sup>77</sup> Ibid.

<sup>78</sup> Ibid.

<sup>79</sup> Ibid.

<sup>80</sup> Ibid.

<sup>81</sup> Ibid.

<sup>82</sup> Footnote 71 of the Provisional Findings Report dated 11 February 2020

<sup>83</sup> Paragraph 5.37 of the Provisional Findings Report dated 11 February 2020

<sup>84</sup> Ibid.

<sup>85</sup> Ibid.

<sup>86</sup> Footnote 71 of the Provisional Findings Report dated 11 February 2020

## CHAPTER 3 – COUNTERFACTUAL

- 5.6 Footasylum’s internal documents from prior to the Merger show that Footasylum’s directors and management [REDACTED]
- 5.6.1 [REDACTED]<sup>87</sup> [REDACTED]
- 5.6.2 [REDACTED]<sup>88</sup> [REDACTED]
- 5.6.3 [REDACTED]<sup>89</sup> [REDACTED]The CMA quotes [REDACTED]
- 5.7 Based on the evidence referred to above, the Provisional Findings’ analysis is flawed in [REDACTED] This was a key factor in the counterfactual [REDACTED]
- [REDACTED]
- 5.8 [REDACTED] [REDACTED] regulatory responsibilities would have meant that such [REDACTED].
- 5.9 The International Standard on Auditing (UK) (ISA (UK)) published by the Financial Reporting Council deals with the auditor’s responsibilities in the audit of financial statements relating to going concern<sup>90</sup>. These guidelines apply stringent requirements on auditors:
- 5.9.1 the auditor is obliged "*[t]o conclude, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the entity’s ability to continue as a going concern*"<sup>91</sup>;
- 5.9.2 if a preliminary assessment has been performed by the company’s management "*the auditor shall discuss the assessment with management and determine whether management has identified events or conditions that, individually or collectively, may cast significant doubt on the entity’s ability to continue as a going concern and, if so, management’s plans to address them*"<sup>92</sup>;
- 5.9.3 "*the auditor shall maintain professional skepticism throughout the audit*"<sup>93</sup>;
- 5.9.4 the auditors must determine "*whether there is adequate support for the assumptions underlying the forecast*"<sup>94</sup>; and
- 5.9.5 examples of events that may cast significant doubt on an entity’s ability to continue as a going concern include: "*Inability to comply with the terms of loan agreements*"; and "*Inability to obtain financing for essential new product development or other essential investments*". The latest ISA guidelines include an additional event which is a reduction in share price<sup>95</sup>.

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<sup>87</sup> Annex 248 of our response to Question 9 of the s. 109 notice dated 2 October 2019 (248. Footasylum plc Audit Plan FY19)

<sup>88</sup> Annex 560 of our response to Question 3 of the s. 109 notice dated 23 May 2019 (Post Board Jan 18)

<sup>89</sup> Annex 003 of our response to Question 3 of the s. 109 notice dated 23 May 2019 (Board minutes 24 Jan 19 V2.docx)

<sup>90</sup> International Standard on Auditing (UK) 570 (Revised June 2016), Going Concern (ISA (UK) (June 2016): [https://www.frc.org.uk/getattachment/8eab510c-17a7-4ac5-a91a-fc590bb3d7dd/ISA-\(UK\)-570.pdf](https://www.frc.org.uk/getattachment/8eab510c-17a7-4ac5-a91a-fc590bb3d7dd/ISA-(UK)-570.pdf)

<sup>91</sup> Paragraph 9(b) ISA (UK) (June 2016)

<sup>92</sup> Paragraph 10(a) ISA (UK) (June 2016)

<sup>93</sup> Paragraph 12D(1) ISA (UK) (June 2016)

<sup>94</sup> Paragraph 16(2)(c) ISA (UK) (June 2016)

<sup>95</sup> International Standard on Auditing (UK) 570 (Revised September 2019), Going Concern (ISA (UK) (September 2019): <https://www.frc.org.uk/news/september-2019/frc-strengthens-going-concern-audit-standard>

## CHAPTER 3 – COUNTERFACTUAL

5.10 [REDACTED]

5.11 [REDACTED]<sup>96</sup>[REDACTED]

### (c) Footasylum's [REDACTED] in a number of scenarios

5.12 In its assessment, the Provisional Findings ignore evidence provided by Footasylum which shows that Footasylum's management [REDACTED]. This is relevant as it evidences [REDACTED] had already taken place and was carried out in preparation of the audit.

5.13 The evidence is set out in a [REDACTED], to which [REDACTED]<sup>97</sup>[REDACTED]

5.14 In her presentation, the CFO explained that [REDACTED]<sup>98</sup>[REDACTED]

5.15 It is important to note that this revised draft budget contained two alternative budgets. A first [REDACTED]

5.15.1 [REDACTED]<sup>99</sup>.

5.15.2 [REDACTED]<sup>100</sup>[REDACTED]

5.16 Footasylum's CFO then [REDACTED]<sup>101</sup>[REDACTED]

5.17 [REDACTED]

5.17.1 the application of the [REDACTED];

5.17.2 the [REDACTED]<sup>102</sup>;

5.17.3 [REDACTED] in this example;

5.17.4 in addition to the measures outlined at paragraph 5.16.2 additional steps would need to be considered including [REDACTED]<sup>103</sup>.

### (d) AlixPartners' paper assesses [REDACTED]

5.18 There are two separate parts to AlixPartners' analysis which are set out in their paper:

5.18.1 AlixPartners' assessment of the [REDACTED]. This is set out in section 5.2 of the AlixPartners' paper; and

5.18.2 AlixPartners' opinion that if [REDACTED]

5.19 However, the Provisional Findings do not appear to recognise these two separate analyses, but instead dismiss the AlixPartners report in its entirety on the basis that:

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<sup>96</sup> Annex 003 of our response to Question 3 of the s. 109 notice dated 23 May 2019 (Board minutes 24 Jan 19 V2.docx)

<sup>97</sup> Annex 560 of our response to Question 3 of the s. 109 notice dated 23 May 2019 (Post Board Jan 18)

<sup>98</sup> Ibid.

<sup>99</sup> Ibid.

<sup>100</sup> Ibid.

<sup>101</sup> Ibid.

<sup>102</sup> Ibid.

<sup>103</sup> Ibid.

## CHAPTER 3 – COUNTERFACTUAL

- 5.19.1 it does not consider this scenario would have been the most likely outcome<sup>104</sup>;
- 5.19.2 “the downside scenario was prepared by the Parties’ external economic advisers specifically for the purpose of this inquiry”<sup>105</sup>;
- 5.19.3 it is “very pessimistic, even for a downside scenario”<sup>106</sup>; and
- 5.19.4 so the Provisional Findings place “very limited weight”<sup>107</sup> on the AlixPartners paper.
- 5.20 Footasylum submits that the CMA’s views of AlixPartners’ paper should not colour the weight that the CMA applies to AlixPartners’ assessment of Footasylum’s downside sensitivity analysis.
- 5.21 This first part of AlixPartners’ work was not “prepared ... for the purposes of this [the CMA’s] inquiry”<sup>108</sup> nor is it “very pessimistic”<sup>109</sup>.
- 5.21.1 In fact, AlixPartners’ analysis simply assesses whether Footasylum’s [REDACTED].
- 5.21.2 The sensitivities applied by Footasylum and assessed by AlixPartners are in fact entirely reasonable. As described in paragraph 5.14 above, Footasylum’s CFO considered that the sensitivities she applied [REDACTED]<sup>110</sup> Moreover, [REDACTED] has in fact commented to Footasylum that [REDACTED].
- 5.22 AlixPartners’ assessment of Footasylum’s downside sensitivity analysis is therefore [REDACTED]. As set out in the Provisional Findings and as described in section 5.6 above, in the absence of the Merger, [REDACTED]. In addition, the HSBC facility would have been drawn to [REDACTED], [REDACTED] [REDACTED]<sup>111</sup>
- (e) [REDACTED] [REDACTED]**
- 5.23 Footasylum’s [REDACTED]<sup>112</sup>.
- 5.24 The conclusion in the Provisional Findings that [REDACTED]. This is because the Provisional Findings’ analysis is based on:
- 5.24.1 [REDACTED]; and
- 5.24.2 [REDACTED]
- 5.25 This is not the case. Footasylum is concerned that [REDACTED]

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<sup>104</sup> Paragraph 5.44 of the Provisional Findings Report dated 11 February 2020

<sup>105</sup> Paragraph 5.50(b) of the Provisional Findings Report dated 11 February 2020

<sup>106</sup> Paragraph 5.44(a) of the Provisional Findings Report dated 11 February 2020

<sup>107</sup> Paragraph 5.45 of the Provisional Findings Report dated 11 February 2020

<sup>108</sup> Paragraph 5.50(b) of the Provisional Findings Report dated 11 February 2020

<sup>109</sup> Paragraph 5.44(a) of the Provisional Findings Report dated 11 February 2020

<sup>110</sup> Annex 560 of our response to Question 3 of the s. 109 notice dated 23 May 2019 (Post Board Jan 18)

<sup>111</sup> See paragraph 5.2.19 of the AlixPartners report.

<sup>112</sup> Ibid.

## CHAPTER 3 – COUNTERFACTUAL

- 5.26 The Provisional Findings recognise that [REDACTED]<sup>113</sup> Footasylum submits that the CMA should take this statement at face value.
- 5.27 This is supported by other contemporaneous documentary evidence including the following:
- 5.27.1 Footasylum’s [REDACTED] “[REDACTED]”<sup>114</sup>;
- 5.27.2 Footasylum’s [REDACTED] highlights that the position of the bank was that [REDACTED] (which were not thought to be available)<sup>115</sup>; and
- 5.27.3 [REDACTED]<sup>116</sup>.
- 5.28 It is clear on the evidence that looking forward had there been an issue [REDACTED]. [REDACTED]
- 5.29 As regards [REDACTED]. This is because:
- 5.29.1 it is likely that this [REDACTED];
- 5.29.2 [REDACTED]; and
- 5.29.3 [REDACTED]
- 5.30 The evidence shows that [REDACTED]. To draw any other conclusion represents a failure to assess the context at the time as well as the evidence presented.
- (f) [REDACTED]**
- 5.31 In this context, [REDACTED]. The Provisional Findings do not take sufficient account of this evidence and [REDACTED].
- 5.32 The Provisional Findings do not provide an adequate explanation however of the evidential basis upon which this conclusion is based and Footasylum fails to understand how the Provisional Findings have arrived at this conclusion. This was in fact [REDACTED] at the time prior to the Merger and the magnitude of the issue should not be underestimated by the CMA in its assessment.
- 5.33 [REDACTED] for Footasylum in the year ahead:
- 5.33.1 The [REDACTED],<sup>117</sup> had identified [REDACTED] as a “[REDACTED]” for the first time in a [REDACTED]. This is important because it establishes [REDACTED] because of the general market conditions in the retail sector;
- 5.33.2 In the [REDACTED] provided that [REDACTED]<sup>118</sup>;

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<sup>113</sup> Paragraph 5.38 of the Provisional Findings Report dated 11 February 2020

<sup>114</sup> Annex 388 of our response to Question 3 of the s. 109 notice dated 23 May 2019 (Notes from HSBC Meeting.docx)

<sup>115</sup> Annex 003 of our response to Question 3 of the s. 109 notice dated 23 May 2019 (Board minutes 24 Jan 19 V2.docx)

<sup>116</sup> Annex 004 of our response to Question F9 of the s. 109 (financial) notice dated 15 October 2019 (004. Notes from call with Sam Fuller 9 Jan).

<sup>117</sup> Annex 248 of our response to Question 9 of the s. 109 notice dated 2 October 2019 (248. Footasylum plc Audit Plan FY19)

<sup>118</sup> Ibid.



## CHAPTER 3 – COUNTERFACTUAL

5.33.3 [X] considered [X] [X]. This is reflected in the [X]<sup>119</sup>[X]

5.34 [X]

5.35 In fact, [X]<sup>120</sup>.

5.36 Footasylum submits that the evidence available, and as referred to above, [X] at paragraph 5.37 of the Provisional Findings Report and [X]

5.37 An assessment of all the facts support the conclusion that, [X].

6. [X]

### (a) Third party and other evidence [X]

6.1 In the Provisional Findings, the CMA concludes that "we consider it is likely that, absent the Merger, Footasylum would have continued to trade in line with its management's central forecast [X]"<sup>121</sup>.

6.2 However, Footasylum submits that the facts and evidence show that [X]

6.3 Third party analysts report show a [X]: the Provisional Findings rely on third party analyst reports to show that Footasylum would have performed according to the central forecast. However, these analyst reports in fact forecast significantly lower levels of [X]<sup>122</sup>.

6.4 [X] [X] resulting in three separate downward guidance announcements to the market. This recent history [X] This view is supported by the evidence provided by [X]<sup>123</sup>, and is also made in the AlixPartners report.<sup>124</sup>

6.5 [X] to drive sales: The central forecast included a number of [X]. Footasylum also needed to recruit to support these plans and [X]<sup>125</sup>[X] These pillars were budgeted to deliver EBITDA of [X].

6.6 Structure of the budget [X] meant that [X] (this is illustrated by developments in FY19 where revenue increased by [X] and gross profit grew by [X] but EBTDA fell by [X]).<sup>126</sup> [X]

6.7 Exogeneous factors would have impaired Footasylum's performance: the CMA notes that any assessment of Footasylum's performance absent the Merger would need to take account of exogeneous factors such as the spread of the Covid-19 virus. This is likely to impact retailers such as Footasylum in two ways. Firstly through a decline in footfall at its stores and secondly potential supply chain issues. If, for example, a major brand has a reduction in supply available to it of key products they are likely to favour their own DTC channel ahead of retailers. A reduction in footfall and supply is foreseeable and would have

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<sup>119</sup> Annex 560 of our response to Question 3 of the s. 109 notice dated 23 May 2019 (Post Board Jan 18)

<sup>120</sup> Annex 004 of our response to Question F9 of the s. 109 (financial) notice dated 15 October 2019 (004. Notes from call with Sam Fuller 9 Jan).

<sup>121</sup> Paragraph 5.39 of the Provisional Findings Report dated 11 February 2020

<sup>122</sup> Paragraph 5.25 of the Provisional Findings Report dated 11 February 2020

<sup>123</sup> Annex 3.1.

<sup>124</sup> Paragraph 5.1.21 of the Provisional Findings Report dated 11 February 2020

<sup>125</sup> Annex 3 of our response to Question 4 of the s. 109 notice dated 23 December 2019 (FY20 budget board pack – Final.pdf)

<sup>126</sup> See Table 3 and paragraph 5.1.4 of the AlixPartners report

## CHAPTER 3 – COUNTERFACTUAL

potentially impacted Footasylum's ability to stay within its banking covenants in the counterfactual. The same is true of any [REDACTED]

6.8 These factors indicate that there is no evidential basis on which the CMA can assume that [REDACTED].

### (b) [REDACTED]

6.9 The Provisional Findings recognise that "Footasylum had [REDACTED]<sup>127</sup>[REDACTED]

6.10 The CMA also accepts in the Provisional Findings that it is "not clear how [REDACTED]"<sup>128</sup>.

6.11 Footasylum accepts that Footasylum had [REDACTED] In fact, the increased EBITDA under the central forecast was arrived at through [REDACTED] (as evidenced in the workings included in the draft budget presentation<sup>129</sup>).

6.12 Footasylum submits however that even [REDACTED]:

6.12.1 capex had [REDACTED] [REDACTED] to [REDACTED], which was [REDACTED] than in FY19 and FY18. This meant that even on the basis of [REDACTED];<sup>130</sup>

6.12.2 under the central forecast [REDACTED];<sup>131</sup>

6.12.3 the forecast planned for [REDACTED]

6.12.4 [REDACTED]

6.12.5 the ongoing [REDACTED] of [REDACTED] of [REDACTED], noting that "this could be higher"<sup>132</sup>;

6.12.6 third party analyst forecasts, on which the CMA has relied, had forecast that Footasylum's EBITDA for FY21 would only grow to £8.7 million and £9 million respectively. This would mean that although the analysts projected growth, EBITDA would continue to be well below the previous levels of EBITDA and would therefore [REDACTED];

6.12.7 to arrive at the central forecast, and EBITDA of [REDACTED], Footasylum had [REDACTED]. For example the [REDACTED] [REDACTED] had been [REDACTED] had increased due to the [REDACTED] [REDACTED] from [REDACTED] and the budget provided for [REDACTED].

6.13 The [REDACTED] under the central forecast would therefore have further [REDACTED] [REDACTED]. On the basis of the evidence collected by the CMA during its investigation, failure to respond to brand feedback would lead to [REDACTED]. Without or with [REDACTED]

6.14 Even under the central forecast, it is therefore more likely that Footasylum would have [REDACTED]

6.15 Footasylum had been advised that it was highly unlikely to [REDACTED] had advised that:

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<sup>127</sup> Paragraph 5.18 of the Provisional Findings Report dated 11 February 2020

<sup>128</sup> Paragraph 5.27 of the Provisional Findings Report dated 11 February 2020

<sup>129</sup> Annex 560 of our response to Question 3 of the s. 109 notice dated 23 May 2019 (Post Board Jan 18)

<sup>130</sup> See Table 3 and paragraph 5.2.4 of the AlixPartners report

<sup>131</sup> See Table 3 and paragraph 5.2.3 of the AlixPartners report

<sup>132</sup> Ibid.

## CHAPTER 3 – COUNTERFACTUAL

6.15.1 [REDACTED]

6.15.2 [REDACTED]

6.15.3 [REDACTED]

- [REDACTED]
- [REDACTED]
- [REDACTED]
- [REDACTED]
- [REDACTED]

6.15.4 [REDACTED]

6.15.5 [REDACTED]

6.15.6 [REDACTED]<sup>133</sup>.

6.16 [REDACTED]

6.16.1 [REDACTED]

6.16.2 [REDACTED]

6.16.3 "[REDACTED]<sup>134</sup>".

6.17 [REDACTED]

[REDACTED]

6.18 The Provisional Findings conclude that had trading conditions been less favourable than forecast, "[REDACTED]"<sup>135</sup>.

6.19 As described above, in order to arrive at the central budget, Footasylum had [REDACTED] as far as it could. This included [REDACTED] [REDACTED].

6.20 Had Footasylum needed to [REDACTED]:

6.20.1 a further reduction in [REDACTED]

6.20.2 [REDACTED]

6.20.3 [REDACTED]

6.20.4 [REDACTED]

6.20.5 [REDACTED]

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<sup>133</sup> Annex 004 of our response to Question F9 of the s. 109 (financial) notice dated 15 October 2019 (004. Notes from call with Sam Fuller 9 Jan).

<sup>134</sup> Annex 3.1

<sup>135</sup> Paragraph 5.37 of the Provisional Findings Report dated 11 February 2020

## CHAPTER 3 – COUNTERFACTUAL

- 6.20.6 Footasylum had [REDACTED];
- 6.20.7 the only possible measure Footasylum would have been able to take to would have been [REDACTED].
- 6.21 According to the AlixPartners Report [REDACTED]. On the basis of Footasylum’s own figures, AlixPartners assessed that Footasylum could have [REDACTED]<sup>136</sup>[REDACTED]<sup>137</sup>[REDACTED]<sup>138</sup>[REDACTED]
- 6.22 [REDACTED]<sup>139</sup>[REDACTED]
- 6.23 The evidence therefore [REDACTED].
- [REDACTED]
- 6.24 The CMA also “recognise that had Footasylum continued to have sustained financial problems, this may have reduced its investment in its store portfolio. Any such reduction could have negatively impacted its relationship with its suppliers and potentially led to a decrease in product access and/or volume allocations”<sup>140</sup>
- 6.25 The Provisional Findings, however, conclude that “absent the Merger, Footasylum would have been likely to have continued to take steps to improve and stabilise its business performance, [REDACTED], without materially affecting its competitive position”<sup>141</sup>.
- 6.26 This does [REDACTED]:
- 6.26.1 As described in paragraph 6.3.5 above, Footasylum needed to invest in its store portfolio [REDACTED]. And in any event third party analysts (which the Provisional Findings rely upon) predicted that Footasylum [REDACTED].
- 6.26.2 If, as set out in paragraphs 6.3 above, Footasylum had [REDACTED] and above those already required by the FY20 budget there was [REDACTED] and anything Footasylum would have done [REDACTED]
- 6.27 In these circumstances, it is clear that the Provisional Findings’ conclusion that rephrasing of expenditure and similar actions would have enabled Footasylum to “[REDACTED] without materially affecting its competitive position”<sup>142</sup> is [REDACTED] Footasylum is firmly of the view that the evidence provided to the CMA shows that [REDACTED]<sup>143</sup>[REDACTED] as the Provisional Findings recognise.
- 6.28 In any event, it is not clear, due to the redactions in certain parts of the Provisional Findings, exactly what evidence was sought from / provided by suppliers (in particular Nike and adidas) with respect to the counterfactual. Paragraph 5.32 of the Provisional Findings suggest that certain suppliers had not changed their supply and payment terms, certain suppliers were not “at that stage” concerned about Footasylum’s [REDACTED], and that

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<sup>136</sup> So as to increase its EBITDA by £1.6 million

<sup>137</sup> So as to increase its EBITDA by £2.6 million

<sup>138</sup> These figures are taken from Table 5 of the AlixPartners report, which reports Footasylum’s own calculations

<sup>139</sup> Annex 388 of our response to Question 3 of the s. 109 notice dated 23 May 2019 (Notes from HSBC Meeting.docx)

<sup>140</sup> Paragraph 5.33 of the Provisional Findings Report dated 11 February 2020

<sup>141</sup> Paragraph 5.40 of the Provisional Findings Report dated 11 February 2020

<sup>142</sup> Paragraph 5.40 of the Provisional Findings Report dated 11 February 2020

<sup>143</sup> Paragraph 5.33 of the Provisional Findings Report dated 11 February 2020

## CHAPTER 3 – COUNTERFACTUAL

one supplier had offered some kind of support to Footasylum to improve its sales. It is not clear which suppliers gave evidence in this respect.

- 6.29 Nor is it clear whether the CMA asked suppliers what they would have done if Footasylum's [X]. The Provisional Findings recognise that a reduction in investment "could have negatively impacted [Footasylum's] relationship with its suppliers and potentially led to a decrease in product access and/or volume allocations" (noting the example provided of [X]), but the Provisional Findings do not present any evidence that this possibility was properly investigated with suppliers, as it should have been. Indeed, the CMA's Suppliers working paper [X]

### 7. Footasylum's performance since the Merger cannot be taken as evidence to support the CMA's provisional findings

- 7.1 Footasylum's performance since the Merger is not relevant to the CMA's assessment of the counterfactual. The counterfactual is specifically to determine the most likely outcome in the absence of the Merger. Any improvement in performance since the Merger is not relevant for these purposes.

- 7.2 In particular:

7.2.1 [X] As explained in this paper, absent the Merger, [X] around [X] absent the Merger, this could have [X]

7.2.2 The Merger removed the need for Footasylum [X] [X]. For reasons explained in this paper, absent the Merger, it is likely that [X] would have been required by the bank who are likely to have wanted [X]

7.2.3 [X]

7.2.4 The acquisition by JD Sports returned confidence to Footasylum's [X] and Footasylum's relationship with its [X] [X]. [X] faced by Footasylum prior to the Merger, and which, absent the Merger [X]

- 7.3 Footasylum's improvement in performance since the Merger should not therefore be relied on as evidence in the CMA's assessment of the most likely counterfactual in any way.

### 8. On any scenario Footasylum would have [X]

- 8.1 As set out in section 2 of this paper, the CMA must base its assessment of the most likely counterfactual on the facts of the case and ignore any spurious claims.

- 8.2 Based on the new evidence provided by [X] and the full body of evidence already presented to the CMA, and an explanation of the flaws in the CMA's assessment, Footasylum submits that the most likely outcome in any scenario is one in which Footasylum [X] The evidence to support this finding is overwhelming and therefore does not require the CMA "to make finely balanced judgements about what is and what is not included in the counterfactual"<sup>144</sup>.

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<sup>144</sup> Paragraph 5.4 of the Provisional Findings Report dated 11 February 2020

**CHAPTER 3 – COUNTERFACTUAL**

**CHAPTER 4  
SUPPLIER CONSTRAINTS POINT TO NO SLC**

**I. Overview**

- (251) The PFs' assessment of the implications of supply-side responses for the SLC question reflects a complete failure to engage with the relevant question and evidence on this issue and must be reconsidered.
- (252) For the reasons briefly explained below and set out in more detail in the Compass Lexecon submission of 6 March 2020 (Annex 4.1), the PFs' framework for addressing supplier constraints is wrong in terms of its approach, test, assessment and conclusion.
- (253) In any case, on a correct approach, even taking the evidence in the PFs on its own terms, there is no credible basis for an SLC finding in relation to any parameter of competition, as discussed in detail in Chapter 5 of this Response.

**II. The PFs address the wrong question**

- (254) The PFs state that the CMA's assessment of supplier constraints is concerned with "*the Parties' ability to flex their offering*".
- (255) However, the relevant question is not whether the Parties have the ability to degrade PQRS post-Merger (it is common ground that they have that ability), but whether they would have the incentive post-Merger to significantly and permanently degrade their offer, taking account of the ability and incentive for suppliers to react to any such degradation.
- (256) The consequence of the PFs adopting the wrong starting point is that the CMA's analysis of supplier constraints is confused and misdirected, and essential evidential points are unaddressed.

**III. The PFs apply the wrong test**

- (257) In assessing the role of suppliers, the PFs apply a two-stage test. The first limb of this test assesses whether, taking into account the restrictions and influence imposed by suppliers, "*any remaining retail competitive interaction is largely immaterial*".
- (258) This approach by the CMA repeats the mistake of focusing on retailers' ability to change PQRS. However, the presence of retail competition in no way contradicts the relevance of supplier constraints. It is therefore illogical – having accepted that suppliers play an important role in shaping the retail market – to treat the degree of retail competition independently of supplier constraints and to ignore the effect on retailers' incentives that results from the threat of reduced allocations and disintermediation.
- (259) The second limb of the CMA's test is concerned with whether "*suppliers' incentives are fully aligned with those of consumers*".
- (260) However, the requirement for supplier and consumer interests to be aligned is a fallacy. As long as suppliers, acting in their own interests, would prevent a deterioration in competition post-Merger, that is sufficient for consumers to be no worse off from the Merger.

**IV. The PFs' analysis of supplier constraints is misdirected and incomplete**

- (261) The PFs' analysis of supplier constraints is also problematic for a number of reasons.
- (262) First, the assessment of supplier restrictions (paragraphs 8.26-8.34) is incorrectly concerned with the notion of a 'floor', above which retailers are free to set their offer. However, that approach:

## CHAPTER 4 – SUPPLIER CONSTRAINTS POINT TO NO SLC

- (a) ignores the Parties' evidence that they are not constrained to any explicit minimum standard (described further below) and that the threat of reduced allocations entails substantial influence for suppliers across all aspects of their PQRS-setting; and
  - (b) fails to include any meaningful analysis or evidence establishing that retailers are above the notional floor.
- (263) Second, the assessment of supplier influence (paragraphs 8.35-8.37) similarly includes no consideration of the impact on retailer incentives that would be expected to result from the threat of reduced allocations, despite evidence that suppliers [REDACTED].
- (264) Third, the assessment of supplier incentives (paragraphs 8.38-8.43) is based on the flawed logic described above that suppliers' and consumers' interests need to be aligned.
- (265) Fourth, there is no evidence that the CMA has asked key suppliers, or received sufficient responses to, the critical question of how they would react post-Merger to a deterioration in the parties' PQRS, despite the obvious importance of that information and the relative ease of gathering it (compared to survey evidence on demand-side constraints).

### V. The PFs fail to take into account relevant evidence and misinterpret evidence

- (266) As noted above, the PFs have failed to take proper account of evidence submitted by the Parties which demonstrates the degree of constraint imposed by suppliers. This is the case for both Parties, as follows.

#### A. JD Sports

- (267) The PFs make no reference to the 58 internal documents that JD Sports submitted evidencing the degree to which the brands dictate and enforce standards regarding their retail offering both in-store and online. These documents evidence the following conclusions.

##### 1. [REDACTED]

- (268) The PFs make no mention of the [REDACTED]<sup>145</sup> For example, the Parties submitted a [REDACTED]
- (269) The level of [REDACTED] in these documents undermines the CMA's assertions that suppliers' standards constitute a floor above which retailers are free to determine how they compete or – in this instance – lay out their stores.
- (270) Similarly, the PFs do not mention the documents submitted to the CMA which show [REDACTED].<sup>146</sup>
- (271) These documents, which are not mentioned in the PFs, show that the brands: (i) [REDACTED]; and (ii) [REDACTED].

##### 2. [REDACTED]

- (272) The PFs give no weight to the documents submitted to the CMA which demonstrate that if [REDACTED]
- (273) The Parties also submitted documents to the CMA which demonstrate that the [REDACTED] extend to JD Sports' online offering. In one example, [REDACTED]
- (274) Similarly, [REDACTED] [REDACTED].<sup>147</sup>

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<sup>145</sup>[REDACTED]

<sup>146</sup>[REDACTED]

<sup>147</sup>[REDACTED]



## CHAPTER 4 – SUPPLIER CONSTRAINTS POINT TO NO SLC

- (275) The only time these documents are referenced is in footnote 222, where the CMA erroneously concludes that JD Sports has the ability to push back on suppliers' demands, citing one of JD Sports' documents in support of that conclusion.<sup>148</sup> This is an incorrect characterisation of that conversation and there is [REDACTED]:
- (a) The supplier terms [REDACTED] contain granular requirements regarding the content on JD Sports' website (in particular, JD Sports' homepage) and social media channels.
  - (b) Occasionally, JD Sports recommends alternative approaches [REDACTED] to ensure that their proposals are as successful as possible. [REDACTED]
  - (c) [REDACTED]
  - (d) Rather than evidencing JD Sports pushing back [REDACTED], Annex 1280 shows JD Sports commenting on [REDACTED] under its supplier agreement [REDACTED] to ensure that the proposal is as effective as possible for both parties. It does not show JD Sports pushing back on the concept of supplier control.

### 3. The brands' control over JD Sports is not only limited to their retail store offering, but also extends to their forward-looking strategy

- (276) The CMA also makes no reference to the board documents submitted by JD Sports which demonstrate [REDACTED] For example, in one set of board minutes, JD Sports notes that [REDACTED].<sup>149</sup> Similarly, JD Sports also submitted documents that show [REDACTED].<sup>150</sup>

#### B. Footasylum

- (277) The PFs fundamentally mischaracterise the nature of Footasylum's relationship with its key suppliers Nike and adidas. By way of example, in paragraph 8.36 of the PFs, the CMA states that retailers may "*typically negotiate individual discounts from suppliers' wholesale price, which are often subject to the retailer meeting certain conditions or KPIs*". Footasylum submits that the CMA has incorrectly characterised this process as a "[REDACTED]
- (278) Footasylum notes that the PFs largely ignore the large body of evidence that Footasylum submitted showing [REDACTED]. By way of example:

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<sup>148</sup> [REDACTED]

<sup>149</sup> [REDACTED]

<sup>150</sup> [REDACTED]

## CHAPTER 4 – SUPPLIER CONSTRAINTS POINT TO NO SLC

- (a) [REDACTED], this is simply to support the CMA's argument that suppliers' incentives are not always aligned with those of consumers, which as outlined in paragraphs (259) and (260) above, is the incorrect test to apply. [REDACTED].
- (b) [REDACTED] which the CMA fails to acknowledge in its PFs.
- (c) [REDACTED].<sup>151</sup> There is no reference to these submissions in the PFs in relation to footwear (see paragraphs 8.15-8.17) and only vague reference to them in relation to apparel (see paragraphs 9.15-9.16).<sup>152</sup>

### VI. The PFs reach the wrong conclusion

- (279) As a consequence of the above errors and omissions, the PFs reach the fundamentally mistaken conclusion (see paragraph 8.146(b)) that it is not necessary to consider supplier responses in the interpretation of GUPPIs. The PFs accept that suppliers shape the retail market and that suppliers have a range of levers available to them to constrain retailer PQRS, including through allocations and whether to supply at all. Despite this, and Compass Lexecon's submissions at an early stage of the Phase 2 investigation that the interpretation of GUPPIs must be fundamentally modified when a supplier constraint is present, the PFs go on to interpret the GUPPIs as if that evidence did not exist and thus reach the wrong conclusion.

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<sup>151</sup> Footasylum party hearing transcript, pages 20-21: [REDACTED]

<sup>152</sup> Footasylum main party hearing transcript, pages 33-34: [REDACTED]

CHAPTER 5  
INTERNAL DOCUMENTS AND ECONOMETRIC EVIDENCE DO NOT SUPPORT  
AN SLC ON ANY IDENTIFIED PARAMETER OF COMPETITION

I. Overview

A. Assessment of the evidence on the Parties' competitor monitoring is flawed

- (280) The PFs place great weight on the degree of “competitor monitoring” found in the Parties' internal documents, which it considers in itself as evidence of “closeness of competition” between them.<sup>153</sup>
- (281) However, on a correct analysis of the Parties' internal documents, there is no basis for a finding that they are closer competitors to one another than they are to the host of other competitors mentioned in those documents.
- (282) This is because, as set out in the further analysis summarised below in sections II.A (JD Sports) and II.B (Footasylum) and set out in detail in Annexes 5.1 and 5.2, the PFs misrepresent a number of the documents cited, fail to acknowledge explanations made by the Parties in previous submissions with respect to particular documents and fail to take proper account of a number of documents submitted by the Parties which have not been referenced in the PFs.
- (283) In any event, simple “monitoring” does not of itself support an SLC finding without evidence that the Parties are reacting to each other when they choose to set their national PQRS variables (as opposed to competitive pressure in aggregate, other rivals or consumer expectations).

B. Neither the internal documents cited by the CMA nor its econometric analysis of competition between the Parties provide evidence of competitive interaction on the identified parameters

- (284) The PFs claim that:

*“[A number of] documents [set out in para 8.106] show that, in some instances, the Parties' monitoring of each other and of other retailers is likely to have influenced their strategic decisions and was sometimes followed by competitive responses to each other (for example around student discounts and pay later offers).”*

- (285) Even without an analysis of the documents underlying this conclusion (just four documents out of a population of over 8,000<sup>154</sup>, of which the CMA states it conducted targeted reviews of over 2,500), it is notable that the CMA in this respect refers to “other retailers” (not just the Parties). In addition, the use of the phrases “in some instances” and “sometimes” indicates that any evidence of competitive responses between the Parties is neither material nor widespread.
- (286) In any event, a proper analysis of the four documents relied upon by the CMA reveals that they either support the opposite conclusion, or in any event are not capable of supporting the conclusion that the CMA draws. This is further supported by additional evidence in relation to the two parameters of competition cited by the CMA in this respect, namely

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<sup>153</sup> PFs, paragraph 8.108.

<sup>154</sup> 1,485 JD Sports internal documents and 6,696 Footasylum internal documents. The Footasylum figure includes duplicates.

## CHAPTER 5 – INTERNAL DOCUMENTS AND PARAMETERS OF COMPETITION

student discounts and pay-later schemes, showing a lack of bilateral competitive interaction (such as price matching or following) between the Parties on these parameters.

- (287) The CMA's econometric analysis also contains serious flaws and the results should be given no weight at all in the competitive assessment of rivalry between the Parties:
- (a) **Sales impact model** – The CMA concludes that ““*Only for Footasylum does both store entry and retailer entry result in a statistically significant and negative fall in the local JD Sports store's footwear revenue*”<sup>155</sup> (emphasis added). However, the CMA admits that its estimates are “*likely*” to be biased, and that its models may fail to find statistically significant impacts for rivals that do in fact affect JD Sports' sales. The CMA's econometric models also find that there is a large number of rivals whose entry has a negative effect on JD Sports' sales (albeit not systematically statistically significant). Notwithstanding these findings, the CMA dismisses all other rivals, individually and collectively, on the basis that the results are not statistically significant. This is not a robust conclusion.
  - (b) **Impact of retailer entry on JD Sports' discounting** – the CMA finds that retailer entry by Footasylum has a statistically significant impact on the percentage of goods JD Sports sold at full price, but not as regards store entry. However, there are no significant effects of retailer entry when using specifications with region-time fixed effects, with such region-time effects being statistically significant. The CMA thus states that these results are given “*limited weight*”, but puzzlingly still relies on them. These results should be given no weight at all. In short, variations in sales mix should not be conflated with local discounting, particularly as the CMA finds that local price flexing is limited and that local competition is not a material factor in driving the variation.
  - (c) **Impact of retailer entry on JD Sports' store refurbishment** – The CMA concludes that Footasylum store entry has a statistically significant and negative impact on the time since the local JD Sports store was last refurbished<sup>156</sup>. However, the Parties' economic advisors find no significant effect when using controls for local demand conditions and time trends. In addition, it does not measure the time between refurbishment (which would be more logical) and it plainly ignores when the entry occurs, which in many instances is after refurbishment and in many cases the refurbishment is *many years after entry* (and the CMA demonstrates no causal link). Furthermore, the CMA's own analysis of internal documents also acknowledges “*where local store refurbishment has occurred, local competitive conditions were not a material factor in these decisions*”<sup>157</sup>.
- (288) Therefore, the econometric analysis cannot be relied upon to conclude whether JD Sports has refurbished stores more frequently in response to competition from Footasylum. Further detail on the Parties' economic advisor's views on the CMA's entry-exit econometric analysis is attached at Annex 5.3.
- (289) The PFs also identify a number of additional competitive parameters in relation to which the CMA considers the Parties could worsen their consumer offer post-Merger.

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<sup>155</sup> PFs, paragraph 8.168.

<sup>156</sup> PFs, paragraph 8.171(a).

<sup>157</sup> PFs, paragraph 7.118.

## CHAPTER 5 – INTERNAL DOCUMENTS AND PARAMETERS OF COMPETITION

- (290) However, the PFs provide no evidence at all to support the proposition that the Parties are materially influencing and / or responding to each other on these additional parameters (or indeed any other parameter) at the national level (where the SLC is found)<sup>158</sup> such that the loss of this dynamic would likely have a material impact on any aspect of PQRS. Nor does the CMA address the question of whether any degradation of non-price parameters post-Merger would be expected to be profitable (which it must be for the incentive to degrade to exist).
- (291) The merged entity will continue to be constrained on all price and non-price parameters, both by its suppliers and by other retailers. It is therefore clear that the CMA's analysis does not support an SLC finding.

### II. The assessment of the Parties' approach to competitor monitoring is flawed

- (292) The CMA places great weight on the degree of "competitor monitoring" found in the Parties' internal documents as evidence of closeness of competition between them. The PFs state:

*"The Parties submitted that references to each other in internal documents were merely part of general market monitoring and, as such, this was not an indicator of closeness of competition. We disagree with the Parties as we consider that such detailed monitoring is in itself evidence of closeness of competition. We do not consider it would be commercially rational to engage in detailed monitoring of retailers which the Parties did not consider to be competitors".<sup>159</sup>*

- (293) It is not the Parties' position that they do "*not consider [each other] to be competitors*", as suggested above. Rather, the Parties remain of the strong view that the simple fact and degree of competitor monitoring of each other as reflected in the internal documents cited in the PFs does not sustain a finding of "closeness" of competition between them and is in any event clearly insufficient to support an SLC finding without evidence that the Parties are reacting to each other when they choose to set their national PQRS variables (as opposed to competitive pressure in aggregate, or other rivals).
- (294) In any event, as seen in the further analysis summarised below and set out in detail in Annexes 5.1 and 5.2, the PFs misrepresent a number of documents, fail to acknowledge explanations provided by the Parties in previous submissions with respect to particular documents, and fail to take proper account of additional evidence submitted by the Parties.

#### A. JD Sports

- (295) Paragraph 8.104 of the PFs states that Footasylum is "*prominent*" in the monitoring that JD Sports conducts alongside other retailers. However, it is clear from the population of documents available to the CMA that by the same token a number of competitors are "prominent" in the monitoring that JD Sports conducts, including SDI, ASOS, Foot Locker, Nike and adidas among others.
- (296) The individual documents / categories of documents cited by the CMA are addressed in detail in Annex 5.1 to this Response. In summary, a proper analysis of these documents indicates that:
- (a) Many of the documents – e.g. JD Sports' [X] and [X] – do not give greater prominence to Footasylum than to other competitors, and the PFs do not give

<sup>158</sup> The PFs cite some evidence of response by way of limited local marketing activity (which represents a tiny fraction of overall advertising spend).

<sup>159</sup> PFs, paragraph 8.108.

## CHAPTER 5 – INTERNAL DOCUMENTS AND PARAMETERS OF COMPETITION

sufficient weight to the fact that a wide competitor set is mentioned in these documents.

- (b) Many of the documents were created over two years ago – i.e. prior to Footasylum’s financial difficulties, SDI’s elevation strategy and recent online growth benefitting DTC and online pureplayers – and thus do not reflect the current competitive dynamics of the market.
  - (c) Many of the documents cited are factual in nature with little or no strategic commentary (for example documents recording competitors’ Black Friday offers), but this fact has not been acknowledged in the PFs.
  - (d) Certain documents have been taken out of context. For example, the PFs rely on a [REDACTED] presentation describing Footasylum’s advertising activity, but make no mention of JD Sports’ explanation that [REDACTED] provides a regular report on competitor advertising activity, with the content varying depending on which competitors are actively advertising at any given time.
  - (e) Two documents cited by the CMA (at footnote 341) [REDACTED] contain no information at all about Footasylum, but contain information for a range of other competitors (which is not acknowledged).
  - (f) The CMA has not acknowledged the Parties’ submissions (at paragraph 35 of the Parties’ Response to the CMA’s Internal Documents Working Paper) with respect to JD Sports’ Property Board Minutes, in which references to SDI account for [REDACTED] of competitor mentions, relative to [REDACTED] for Footasylum.
  - (g) The CMA has also not acknowledged or addressed JD Sports’ submissions (at paragraphs 43 to 49 of the Parties’ Response to the CMA’s Internal Documents Working Paper) with regard to the [REDACTED] documents referenced in the PFs (in particular, the fact that the documents referred to are part of a wider set of analysis performed by [REDACTED]).
- (297) JD Sports also notes that footnote 330 in the PFs states that the CMA has given less weight to some of JD Sports’ [REDACTED] on the basis that they were prepared for the purpose of the Merger. Whilst the document itself was produced as part of the CMA process, the underlying database of competitor activity from which the information was drawn is part of JD Sports’ ordinary course of business competitor monitoring and was in place before the Merger. It is also apparent from the data that JD Sports has been monitoring competitor activity (for competitors other than Footasylum, Foot Locker and SDI) since 2016. There is therefore no reason to disregard this evidence. As noted in Chapter 2, it is clear from the JD Sports’ impact data that SDI has a [REDACTED] impact on JD Sports’ stores.
- (298) There are a number of key internal documents provided by JD Sports which have not been considered or given any weight by the CMA. For example, even though it was annexed to a letter from JD Sports’ CEO to the CMA dated 7 January 2020, the PFs give no weight to an email from Peter Cowgill to JD Sports’ senior management asking them to prepare competitor analysis for [REDACTED].<sup>160</sup> This internal document constitutes important evidence for two reasons: first, it is a discussion between JD Sports’ most senior employees (the PFs state

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<sup>160</sup> Annex 1324 and an attachment to the letter from Peter Cowgill to Kip Meek, the CMA Panel and the Case Team dated 7 January 2020.

## CHAPTER 5 – INTERNAL DOCUMENTS AND PARAMETERS OF COMPETITION

that the CMA has placed more weight on documents prepared by or for more senior levels of decision making within the Parties<sup>161</sup>); and second, it demonstrates that JD Sports' CEO was concerned to monitor a wide competitor set (with the email making no reference to Footasylum).

- (299) Similarly, the PFs make no mention of JD Sports' "[REDACTED]" internal document, other than through an incorrect quotation in paragraph 8.106.<sup>162</sup> This document is also important evidence as it is one of the few instances where JD Sports takes strategic decisions as a result of competitor monitoring, and shows that those decisions were influenced by [REDACTED], rather than Footasylum. Within this document JD Sports comments that [REDACTED]". This conclusion is furthered by the [REDACTED] document referenced during the JD Sports' Remedies Hearing (submitted to the CMA on 2 March 2020), which states that [REDACTED]. Finally, the "[REDACTED]" document sets out a list of 18 action items under the heading "*clear set of actions underway to mitigate growing threat*" for how JD Sports can respond to the [REDACTED].

### B. Footasylum

- (300) Paragraph 8.102 of the PFs states that JD Sports is "*highly prominent*" in the monitoring that Footasylum conducts, however, [REDACTED]. For example, in [REDACTED] which the CMA refers to in footnote 311 of the PFs, a total of [REDACTED] competitors are referred to, and in the majority of these documents between [REDACTED] competitors are referenced on average. By way of example, in [REDACTED].
- (301) In any event, as a smaller player in the market, it is inevitable that Footasylum will observe [REDACTED]. As the CMA rightly recognises, it is important to consider the context in which competitors are mentioned in internal documents. The context here is purely Footasylum observing broader actions in the market, and references to JD Sports are not indicative of any particular competitive closeness between the Parties.
- (302) In addition, the PFs focus on Footasylum "monitoring" the conduct of JD Sports, but monitoring in and of itself does not evidence closeness of competition. [REDACTED].
- (303) Further, Footasylum is surprised that the main section in the PFs considering Footasylum's internal documents (i.e. paragraph 8.102) fails to refer to any documents which were submitted by Footasylum during the course of the CMA's Phase 2 investigation. This is particularly the case given that Footasylum submitted a much larger volume of internal documents at Phase 2 than it did at Phase 1 ([REDACTED] documents were submitted by Footasylum at Phase 2 compared to [REDACTED] documents at Phase 1).
- (304) The individual documents / categories of documents cited by the CMA are addressed in detail in Annex 5.2 to this response. In summary, a proper analysis of these documents indicates that:
- (a) Many of the documents (e.g. [REDACTED]) do not give greater prominence to JD Sports than to other competitors, and the PFs do not give sufficient weight to the fact that a wide competitor set is mentioned in many documents;
  - (b) The PFs often draw conclusions about an entire category of documents from an analysis of a small proportion of those documents (e.g., [REDACTED]) and in some cases

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<sup>161</sup> PFs, paragraph 8.99.

<sup>162</sup> Annex 157 or 1341.

## CHAPTER 5 – INTERNAL DOCUMENTS AND PARAMETERS OF COMPETITION

from a single document within that category (e.g. [REDACTED]). Observations made by the CMA in relation to such small proportions of a category of documents are unlikely to be representative, and as such, provide limited support to the overall conclusion;

- (c) The PFs rely on documents created by independent third parties (e.g. analyst reports created by Peel Hunt) which cannot support a conclusion about the monitoring which Footasylum itself undertakes;
- (d) The PFs make sweeping statements about JD Sports being featured in “all” documents within a given category when this is patently not the case (e.g. in relation to [REDACTED], the PFs state that JD Sports is “*consistently monitored across all of these documents*” (emphasis added), but [REDACTED] documents cited by the CMA do not include any reference to JD Sports whatsoever);
- (e) The PFs refer to a number of documents in which references to JD Sports and other competitors are purely observational, and do not provide evidence of Footasylum taking any action in response to these observations (e.g. [REDACTED]). As such, these documents do not provide evidence of any particular competitive closeness between the Parties; and
- (f) Many of the documents cited in the PFs were created over two years ago and may therefore no longer reflect the current competitive dynamics in the market.

### III. The claim in the PFs that certain documents show that monitoring was followed by competitive responses is flawed

(305) The PFs further claim that:

*“[A number of] documents [set out in para 8.106] show that, in some instances, the Parties’ monitoring of each other and of other retailers is likely to have influenced their strategic decisions and was sometimes followed by competitive responses to each other (for example around student discounts and pay later offers).”*

(306) As noted above, even without an analysis of the documents underlying this conclusion it is notable that the CMA in this respect refers to “other retailers” (not just the Parties). In addition, the use of the phrases “in some instances” and “sometimes” indicates that any evidence of competitive responses as between the Parties is neither material nor widespread.

(307) In any event, a proper analysis of the four documents relied upon by the CMA in making this statement (noting that the CMA carried out a “*detailed in-depth review of over 2,500 internal documents from the Parties*”<sup>163</sup>) reveals they either support the opposite conclusion, or in any event are not capable of supporting the conclusion that the CMA draws, as set out below.

(308) Paragraph 8.106(a) references “*a series of internal documents*” regarding student discounts, but only two are cited. Neither provides evidence that JD Sports was responding to Footasylum in the implementation of its student scheme, and both make reference to a range of other retailers ([REDACTED]), with a particular emphasis on the [REDACTED] in this regard. Indeed, the opening line of the first document (which pre-dated the introduction of a student discount in the JD Sports fascia) refers to an “*increasingly competitive environment*”. There is no evidence that specific monitoring of Footasylum (distinct from the other competitors

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<sup>163</sup> PFs, paragraph 6.19.



## CHAPTER 5 – INTERNAL DOCUMENTS AND PARAMETERS OF COMPETITION

referenced) influenced JD Sports' strategic decisions in this respect. While the document does make reference to Footasylum, and sets out some hypothetical scenarios which consider [REDACTED] (ASOS having no store network of its own), none of these scenarios were implemented. The second document (which post-dates the introduction of the discount in the JD Sports fascia) notes that [REDACTED]. Further evidence with respect to student discounts is set out at section V.C below.

- (309) The document referenced in paragraph 8.106(b) is in fact one of the documents already discussed in sub-paragraph (a), and the CMA itself notes the references in this document to the discounts offered by a number of other retailers. However, the further comment in this sub-paragraph (b) that "*The end of the document sets out 18 actions under the heading 'Clear set of actions underway to mitigate growing threat'*" is simply incorrect. Neither of the student discount documents referenced in paragraphs 8.106(a) or 8.106(b) contain any such heading or list of actions. Rather, this content features in another document [REDACTED] which contains no references to Footasylum but discusses the threat from [REDACTED].
- (310) Paragraph 8.106(c) discusses a Footasylum document. It is notable that the quote referred to in paragraph 8.106(c) makes no reference to JD Sports, but instead refers to Footasylum's strategic goals of [REDACTED]. The underlying document also makes reference to [REDACTED]. This document therefore provides no evidence of a specific competitive response by Footasylum to JD Sports.
- (311) Paragraph 8.106(d) references a JD Sports document which "*considers which other retailers signed up to pay-later providers*". Again, this document does not support the conclusion in paragraph 8.107 that the Parties monitor one another and directly respond with competitive actions. Rather, the document describes the different schemes available as well as the schemes used by other retailers. As the PFs mention, the document notes that Footasylum has launched the Laybuy scheme, and also notes that [REDACTED] use Klarna. However, the document does not contain any suggestion of Footasylum influencing JD Sports' decisions in this respect, or of JD Sports responding to Footasylum in some way. Further evidence with respect to pay-later schemes is set out at section V.D below.
- (312) In summary, therefore, none of the four documents cited, out of a significant population of documents, in fact show evidence of strategic influence or response.

### **IV. The PFs cite no evidence to support the proposition of significant bilateral interaction between the Parties on any identified parameter of competition**

- (313) The PFs identify a range of parameters of competition in relation to which the CMA considers the Parties compete.
- (314) However, a consideration of the evidence presented in relation to each parameter, including the econometric analysis carried out with respect to two parameters (discounts and refurbishments), does not support this finding. In fact the PFs provide no evidence at all to support the proposition that the Parties are materially influencing and / or responding to each other on these additional parameters (or indeed on any other parameter of competition) at the national level (where the SLC is found<sup>164</sup>) such that the loss of this dynamic is significant, unlikely to be replaced by the aggregate dynamic of all other competing rivals, and would thus likely have a durable, material impact on any aspect of PQRS.

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<sup>164</sup> The PFs cite some evidence of response by way of limited local marketing activity (which represents a tiny fraction of overall advertising spend).

## CHAPTER 5 – INTERNAL DOCUMENTS AND PARAMETERS OF COMPETITION

- (315) In this respect, the Parties repeat the observation that, for several of the parameters identified, the CMA itself has acknowledged that pre-Merger outcomes in relation to these parameters are often due to factors other than competition between the Parties (e.g. clearance discounts). Furthermore, as noted previously, JD Sports sets many of its QRS parameters at a group level (including its UK and international businesses). Therefore, an analysis of incentive which is rooted in a single fascia (or two fasciae) in the UK does not correctly capture the investment decisions that the JD Sports group makes, for example in respect of technological improvements.
- (316) The PFs also fail to consider whether the extent of costs saved from a worsening of non-price parameters would be sufficiently profitable to justify an SLC finding (which it must be for the incentive to degrade to exist), taking into account the likelihood of adverse responses by the branded suppliers to a deterioration of the retail offer which can be expected to be a strong disciplining factor on all aspects of the Parties' quality and service offering (as discussed further in Annex 4.1).
- (317) Further points in relation to each of the parameters of competition identified by the CMA are summarised in the table below, followed by more detailed discussion in the sections that follow.

## CHAPTER 5 – INTERNAL DOCUMENTS AND PARAMETERS OF COMPETITION

### Overview of competitive parameters

PFs ref	Parameter	Evidence of monitoring / response / other cited in PFs	Parties' observations
8.55	Clearance discounts	Econometric analysis of percentage of JD Sports' sales at full price (Annex 5.3).	This analysis is simply not robust. See further at Annex 5.3. The CMA admits that the results should be given " <i>limited weight</i> ", but it puzzlingly still relies on them. They should instead be given no weight since the results are not statistically significant once region-time fixed effects are allowed for and such effects are statistically significant. Variations in sales mix should not be conflated with local discounting, particularly as the CMA finds that local price flexing is limited and that local competition is not a material factor in driving the variation.
8.104(d); 8.102(l)	Promotional discounts	JD Sports: 3 Black Friday monitoring documents cited as evidence of monitoring.  Footasylum: post mortem documents cited as evidence of monitoring.	Documents cited relate to a period characterised by intense competition across a broad competitor set, contain retrospective intelligence gathering for a range of retailers and provide no evidence of competitive response.  Parties will continue to face competition on this parameter from a range of competitors.
8.55; 8.106(a); 8.106(b); 8.102(i); 8.102(n)	Student discounts	JD Sports: 2 documents incorrectly cited as evidence of competitive response. Other documents cited as evidence of monitoring.  Footasylum: documents cited as evidence of monitoring.	Documents cited provide no evidence of competitive response and also monitor other retailers' discounts.  Additional evidence provided on introduction and variation of discounts indicates no competitive interaction between the Parties.  Parties will continue to face competition on this parameter from a range of competitors.
8.55; 8.106(d); 8.102(k)	Pay-later	JD Sports: 1 document incorrectly cited as evidence of competitive response.  Footasylum: 1 document cited as evidence of monitoring.	Document cited provides no evidence of competitive response (see above).  Additional evidence provided below on introduction of pay-later schemes indicates no competitive interaction between the Parties. Parties will continue to face competition on this parameter from a range of competitors.

**CHAPTER 5 – INTERNAL DOCUMENTS AND PARAMETERS OF COMPETITION**

PFs ref	Parameter	Evidence of monitoring / response / other cited in PFs	Parties' observations
8.57; 8.104(a)	Online delivery	JD Sports: competitor monitoring documents cited. Footasylum: No evidence cited.	JD Sports marketplace reviews provide no evidence of competitive response. Parties will continue to face competition on this parameter from a range of competitors.
8.55; 8.104(a)	Cashback	JD Sports: competitor monitoring documents cited. Footasylum: competitor monitoring documents cited.	JD Sports marketplace reviews do not assess Footasylum's cashback policy. Footasylum documents mention JD's cashback policy alongside 5 other competitors. No evidence of competitive response. Parties will continue to face competition on this parameter from a range of competitors.
8.56	Refurbishments	Econometric analysis on the recency of refurbishments (Annex 5.3).	The Parties' economic advisors find no significant effect when using controls for local demand conditions and time trends. In addition, it does not measure the time between refurbishment (which would be more logical) and it plainly ignores when the entry occurs, which in many instances is <u>after</u> refurbishment and in many cases the refurbishment is <u>many years after entry</u> (and the CMA demonstrates no causal link). Furthermore, the CMA's own analysis of internal documents also acknowledges " <i>where local store refurbishment has occurred, local competitive conditions were not a material factor in these decisions</i> " <sup>165</sup> .
8.56; 8.102(l)	Marketing	JD Sports: Various documents cited as evidence of competitor monitoring. Limited instances identified of local marketing initiatives in response to Footasylum.	JD Sports national marketing documents cover other competitors and a number are misrepresented. Local marketing spend accounts for a very small proportion of overall marketing spend, and local marketing initiatives are employed in a range of scenarios (including in relation to other competitor openings, JD Sports store openings / anniversaries, seasonal events etc.).

<sup>165</sup> PFs, paragraph 7.118.

**CHAPTER 5 – INTERNAL DOCUMENTS AND PARAMETERS OF COMPETITION**

PFs ref	Parameter	Evidence of monitoring / response / other cited in PFs	Parties' observations
		Footasylum: 1 incorrectly referenced document cited as evidence of competitor monitoring	
8.56	Store opening times	JD Sports: No evidence cited. Footasylum: No evidence cited.	No evidence cited by the CMA in relation to competition between the Parties on this parameter. Parties will continue to face competition on this parameter from a range of competitors (noting also that online competitors are “always open”).
8.56	Store fittings	JD Sports: No evidence cited. Footasylum: No evidence cited.	No evidence cited by the CMA in relation to competition between the Parties on this parameter. Parties will continue to face competition on this parameter from a range of competitors.
8.56	Loyalty programmes	JD Sports: No evidence cited. Footasylum: No evidence cited.	No evidence cited by the CMA in relation to competition between the Parties on this parameter. Parties offer differentiated loyalty programmes and do not have regard to each other in setting the terms of these schemes.  Parties will continue to face competition on this parameter from a range of competitors.
8.56	Range of brands	JD Sports: competitor monitoring documents cited. Footasylum: No evidence cited.	JD Sports marketplace reviews provide no evidence of competitive response. For Nike and adidas – post-Merger the Parties will continue to make procurement decisions within the segments within which they sit.  For own brands / bedroom brands – the Parties are not close competitors (JD Sports' sales of such brands are very limited) and the rationale for the Merger is to develop these brands for the benefit of both JD Sports' and Footasylum's customers. The Parties will continue to face competitive pressure from a wide range of players in relation to both footwear and apparel.
8.56	Staff levels / staff quality /	JD Sports: No evidence cited. Footasylum: No evidence cited.	No evidence cited by the CMA in relation to competition between the Parties on this parameter. Parties will continue to face competition on this parameter from a range of competitors.

**CHAPTER 5 – INTERNAL DOCUMENTS AND PARAMETERS OF COMPETITION**

PFs ref	Parameter	Evidence of monitoring / response / other cited in PFs	Parties' observations
	staff training / queuing times		
8.56	Website functionality	JD Sports: No evidence cited. Footasylum: No evidence cited.	No evidence cited by the CMA in relation to competition between the Parties on this parameter. Parties will continue to face competition on this parameter from a range of competitors, in particular online-only players.  E.g. JD Sports' " <i>multi-channel threats</i> " document is focused on [redacted], and the Footasylum document cited in the PFs notes the goal of providing the Footasylum website with [redacted]
8.58	Technology improvements	JD Sports: No evidence cited. Footasylum: No evidence cited.	No evidence cited by the CMA in relation to competition between the Parties on this parameter. JD Sports' investment in innovation and technology is shared across the wider JD Sports group in the UK and internationally. Its activities in this respect are not influenced by Footasylum, which is severely capital constrained and currently unable to make material investments in technology or other innovations.

## CHAPTER 5 – INTERNAL DOCUMENTS AND PARAMETERS OF COMPETITION

### V. Price parameters

#### A. Clearance discounts

- (318) The PFs accept that retailers generally price in line with the RRP provided by suppliers, but note that “*however they also undertake discounting*”, including both clearance discounts and non-clearance discounts. However, the PFs fail to cite any robust evidence that the Parties are responding to each other when setting clearance discounts.
- (319) The CMA’s entry-exit analysis finds that retailer entry by Footasylum has a statistically significant impact on the percentage of goods JD Sports sold at full price, but not as regards store entry.<sup>166</sup> Moreover, small variations in sales mix should not be conflated with local discounting, particularly as the CMA finds that local price flexing is limited and that local competition is not a material factor in driving the variation.
- (320) In addition, even as regards the retailer entry model, there are no significant effects in the model when using specifications with region-time fixed effects. The CMA thus states that these results are given “*limited weight*”, but puzzlingly it still relies on them. However, these results should be given no weight at all because:
- (a) Entry by some retailers is associated with a statistically significant increase in the proportion of goods sold by JD Sports at full prices, which is entirely unexplained. In the PFs, the CMA states that this model suffers from upward bias (which is not a valid explanation for econometric reasons), and that it may be hard to find statistically significant effects (which fails to explain to why variables have the wrong signs). The CMA also ignores its sensible statement in the Working Paper that the direction of the bias in the discounting and refurbishment models could be upwards or downwards.
  - (b) The sensitivity of the results suggests that the observed variation in the proportion of sales at full prices is attributable to regional variations in demand, which is why the results collapse if region-time fixed effects are included.
  - (c) These region-time fixed effects are also statistically significant, and thus omitting these effects may cause omitted variable bias.
- (321) Further discussion of this analysis is set out in Annex 5.3.

#### B. Promotional discounts

- (322) The PFs note that Footasylum features prominently in three JD Sports internal documents which compare different retailers’ Black Friday offerings. However, the CMA presents no evidence that the Parties are strategically influencing or responding to each other when setting promotional discounts.
- (323) The CMA’s assessment also mischaracterises JD Sports’ internal documents. The fact that, in a single document which simply reports the Black Friday offers of competitors (without additional commentary), more slides are devoted to describing Footasylum’s Black Friday offering than those of other competitors is not evidence that the Parties compete particularly closely on promotional discounts, but simply reflects the fact that Footasylum offered a wider and more complex range of discounts than other competitors over the period in question.
- (324) Furthermore, as explained in its submissions and at its hearing on 16 December 2019, while JD Sports monitors the Black Friday discounting activities of competitors, its own promotional decisions (which are determined well in advance of the Black Friday period) are not influenced by the discounting decisions of

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<sup>166</sup> PFs, Appendix C, paragraph 61.

**CHAPTER 5 – INTERNAL DOCUMENTS AND PARAMETERS OF COMPETITION**

competitors. In addition, JD Sports notes that the documents referenced by the CMA are factual only and do not contain any strategic commentary or suggest any competitive response.

- (325) The PFs cite Footasylum’s [REDACTED], noting that in certain documents, only JD Sports or JD Sports and Footlocker are referred to in terms of competitors. The CMA fails to note that Footasylum monitors a wide range of competitors and their activities around key trading periods, and that in [REDACTED] cited in footnote 311 of the PFs, a total of [REDACTED] competitors are referred to. In the majority of these documents, Footasylum refers to between [REDACTED] competitors on average. In addition, Footasylum notes that the documents referred to by the CMA do not evidence Footasylum [REDACTED], and as such, the documents are not indicative of any particular competitive closeness.
- (326) The CMA presents no other evidence to support the proposition that the Merger could be expected to result in adverse effects with respect to this parameter. The “key sale periods” referenced by the CMA are characterised by intense competition on promotional activity across a broad competitor set, and post-Merger the merged entity will continue to be constrained by a large number of competitors. Therefore, there is no basis to assume (and no evidence presented in the PFs to suggest) that the Merger will result in a deterioration of this parameter.

**C. Student discounts**

- (327) As set out above, the two student discount documents cited by the PFs as showing “competitive response” as between the Parties do not provide any such evidence.
- (328) By way of further evidence, JD Sports has prepared two chronologies which show: (i) the date at which different retailers started to offer student discounts via the UniDAYS scheme; and (ii) the size of the student discount offered by UK retailers from 1 January 2018 to 26 March 2019 (just after the Footasylum acquisition).
- (329) The first chronology shows that JD Sports did not respond to Footasylum when it launched its student discount in 2012. Indeed, JD Sports waited a further six years to launch its own policy and this was after a number of other retailers started to offer a student discount (notably [REDACTED]).

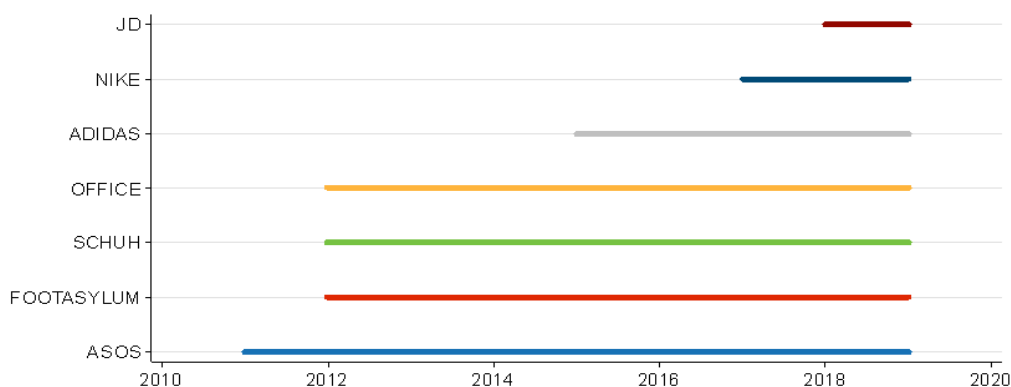
The following table depicts JD and its competitors' year of entry on the UniDAYS platform.

Table 2: JD and competitors' entry on Unidays

Entry year	2011	2012	2013	2014	2015	2016	2017	2018
Store (s)	Asos	Footasylum Schuh Office			Adidas		Nike	JD

Source: Email chain, [EXTERNAL] FW: Insight - JD - Urgent

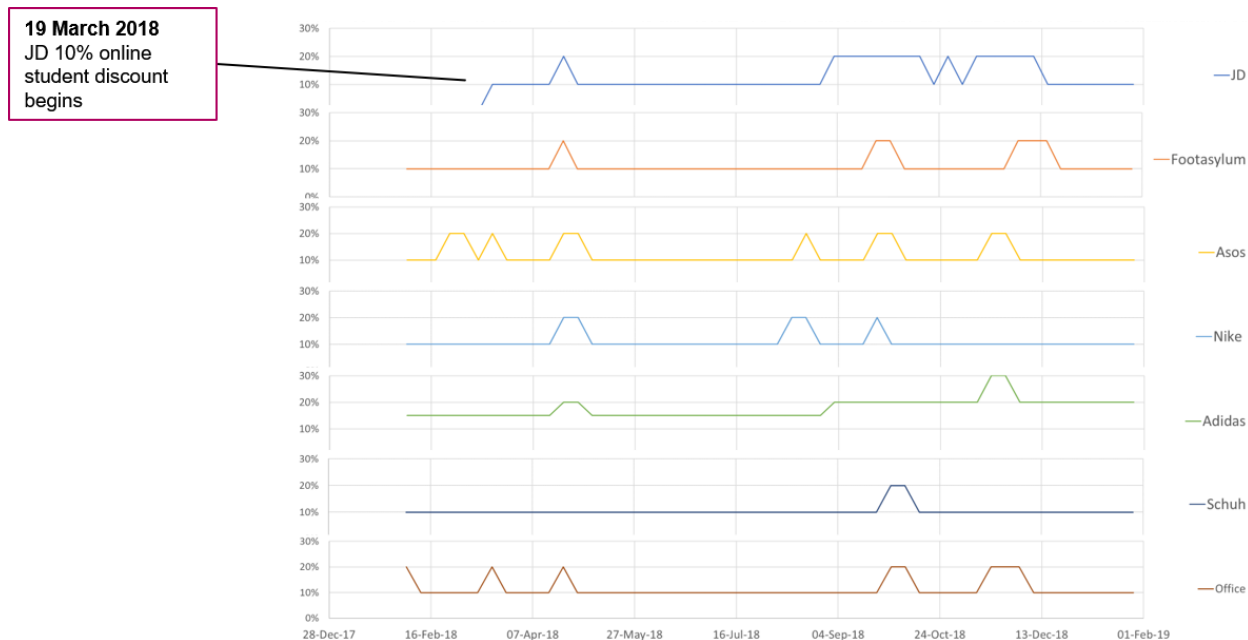
Chart 2: JD and competitors' entry on UniDAYS





## CHAPTER 5 – INTERNAL DOCUMENTS AND PARAMETERS OF COMPETITION

- (330) The second chronology<sup>167</sup> shows no evidence that JD Sports follows Footasylum when setting its student discount. For example, the chronology shows that Footasylum regularly increases its student discount to 20% and there is no response from JD Sports to match it. Similarly, the chronology shows that Footasylum does not follow JD Sports when setting its student discount.



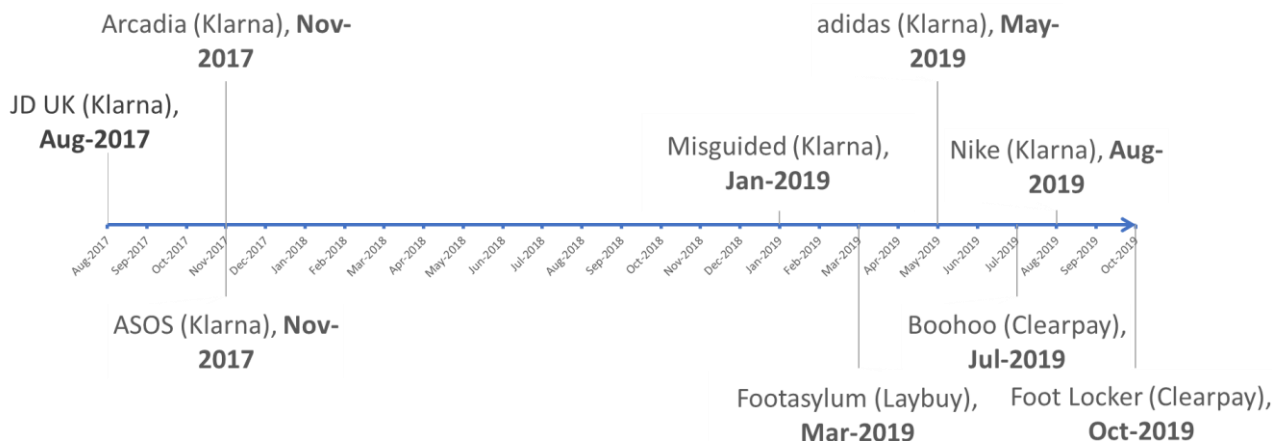
- (331) Together, both chronologies demonstrate that student discounts are not a parameter of competition in relation to which the Parties compete to any material extent. Neither Party's actions appear to be influenced by the other Party and there is no obvious ongoing matching between the Parties regarding the level of student discount offered. Significant competition would remain post-Merger, undermining any hypothesis that the Merger would result in an SLC in this respect.

### D. Pay-Later

- (332) As noted in paragraph (311) above, the single document discussing pay-later schemes that is cited in paragraph 8.106 of the PFs does not provide any evidence of strategic influence or competitive response between the Parties: the document simply references the schemes used by other retailers, and sets out a range of other factors under consideration by JD Sports as it assesses the possible expansion of its pay-later schemes (which it typically implements globally – noting that [REDACTED]).
- (333) The PFs cite one document ([REDACTED]) in which Footasylum notes that [REDACTED]. Footasylum notes that in this document it simply made the observation that [REDACTED], and it did not [REDACTED]. Indeed, Footasylum did not introduce a pay-later scheme until March 2019 ([REDACTED]), and this was not in response to JD Sports or any other competitor.
- (334) By way of further evidence, JD Sports has prepared a chronology which plots the introduction of pay-later solutions by different retailers. As can be seen, JD Sports implemented its pay-later solution two years prior to Footasylum, and in the intervening period a number of other retailers also adopted pay-later solutions. It is clear from this chart that there is no particular bilateral interaction between the Parties with respect to the implementation of pay-later solutions which are a wider industry trend.

<sup>167</sup> Source: Internal JD Sports data based on market observations collected weekly by the JD Sports trading team.

## CHAPTER 5 – INTERNAL DOCUMENTS AND PARAMETERS OF COMPETITION



### E. Online delivery prices

- (335) The PFs cite no evidence to support the proposition that the Parties are strategically influencing or responding to each other when determining their delivery prices.

### F. Cashback

- (336) The PFs cite no evidence to support the proposition that the Parties are strategically influencing or responding to each other in relation to their participation in cashback schemes. Indeed, this suggestion is contradictory to the Parties' internal documents. JD Sports' marketplace reviews do not mention Footasylum's cashback policy, but do assess seven other competitors ([redacted]). Similarly, Footasylum's documents on the same topic assess a wide competitor set including [redacted].
- (337) Furthermore, the Parties note that their respective decisions to take part in cashback websites were not taken in response to the other Party and were instead a proactive decision in response to a general shift across online retail more generally to offer this type of benefit.

## VI. Non-price parameters

- (338) As set out in Compass Lexecon's submission attached at Annex 4.1 to this response, the evidence shows that a material quality or service degradation by the merging Parties post-Merger would be met by adverse responses from the brands. This is a strong disciplining factor on all aspects of the merging Parties' quality and service offering. The PFs also reach a finding on supplier constraints on quality and service, describing both direct restrictions imposed by suppliers on retailers' quality and service and evidence of suppliers monitoring retailers' performance on other quality and service metrics.
- (339) As described in Chapter 4, there is also further evidence consistent with this proposition that has been provided to the CMA but which is not reflected in PFs.

### A. Refurbishments

- (340) The CMA's entry-exit model finds that "store entry by Footasylum is found to have a statistically significant and negative... impact on the time since the local JD Sports store was last refurbished"<sup>168</sup> (emphasis added). However, disregarding for the moment the flaws in the CMA's modelling (addressed below), the results are clearly not robust:
- (a) The CMA does not consider the fact that the very same omitted factors driving the "upward bias" in the specifications focusing on the revenue will likely lead to a "downward bias" whether the

<sup>168</sup> PFs, paragraph 8.171(a).

## CHAPTER 5 – INTERNAL DOCUMENTS AND PARAMETERS OF COMPETITION

refurbishment time is considered, i.e. leading to a possible overstatement of the impact of entry.<sup>169</sup> Indeed, AlixPartners show empirically that, within the CMA econometric framework, using more refined controls for local demand conditions and time trends to better account for the potential omitted variable problem leads to there being no statistically significant effect.

- (b) The CMA does not address why in relation to the “retailer entry” specifications Footasylum’s entry does not have a statistically significant effect.
- (c) Furthermore, the CMA’s own analysis of internal documents also acknowledges “*where local store refurbishment has occurred, local competitive conditions were not a material factor in these decisions*”<sup>170</sup>.

(341) There is also an array of flaws in the CMA’s modelling:

- (a) It ignores whether a refurbishment decision occurs before entry. Absent any evidence brought by the CMA that JD Sports was able to anticipate entry decisions six months or more prior to observing entry, it is hard to claim that the entry variable used in the model is capturing a causal relationship between the two events.
- (b) It ignores that, regardless of entry, the probability of refurbishment increases over time as leases come up for renewal or adjacent properties become available. This may lead to an overstatement of the impact of entry for stores normally associated with longer refurbishment cycles.
- (c) It does not measure at all the time between refurbishments and entry. The CMA’s econometric model only considers time since refurbishment, not whether entry speeds up refurbishment cycles. Indeed, excluding refurbishments made six months or more before Footasylum’s entry, 82% of the remainder occur more than four years after Footasylum’s entry.
- (d) The model does not measure differences in how recently stores are refurbished in the way envisaged by the CMA. This is because small differences in the timing of refurbishment across stores will make a large difference in comparisons of when a store was last refurbished.

(342) Therefore, as discussed in further detail in Annex 5.3, the econometric analysis cannot be relied upon to conclude whether JD Sports has refurbished stores more frequently in response to competition from Footasylum.

### B. Marketing

(343) The PFs cite very little evidence to support the proposition that the Parties are strategically influencing and responding to each other in relation to marketing activities.

(344) Paragraph 8.104 of the PFs notes a very small number of instances in which JD Sports has engaged in local marketing initiatives (such as an in-store DJ) in response to a new Footasylum store opening. However, such activities are also used in a range of other circumstances, for example JD Sports store openings / anniversary events, to promote JD Sports stores in the event of roadworks or local factors that may be impacting the store, as well as other competitor activities.

(345) As set out in JD Sports’ response to question 25 of the s.109 dated 15 October 2019, JD Sports’ [REDACTED]. The PFs cite no evidence to support the proposition that the Parties are strategically influencing or responding to each other in relation to national marketing activities (where the SLC is found). As discussed above, the [REDACTED] document cited at paragraph 8.104 is a single example of a regular report that covers a range of retailers (depending on the marketing activity in a given week), and the OOH reports

<sup>169</sup> The extent and direction of the bias may vary across competitors for the same reason as why this is the case as regards the impact of entry on JD Sports’ sales.

<sup>170</sup> PFs, paragraph 7.118.

## **CHAPTER 5 – INTERNAL DOCUMENTS AND PARAMETERS OF COMPETITION**

cited in the PFs cover a range of retailers (and in some cases do not contain any data for Footasylum), without additional strategic commentary.

### **C. Store fittings**

- (346) The PFs cite no evidence to support the proposition that the Parties are strategically influencing or responding to each other in relation to store fittings, distinct from other competitors (including SDI with its ongoing focus on its elevation strategy and Foot Locker's renewed expansion through a number of new stores).
- (347) As discussed in Chapter 4 above, the PFs clearly acknowledge that suppliers have an incentive to maintain retail competition for quality of stores, and suppliers already ensure that retailers achieve and maintain high levels of store quality via a range of mechanisms including their allocation strategies, the provision of free or subsidised fixtures and fittings, wholesale incentives and store audits. The Merger will not change this.

### **D. Loyalty programme**

- (348) The PFs cite no evidence to support the proposition that the Parties are strategically influencing or responding to each other in relation to their loyalty programmes.
- (349) As described previously, JD Sports' decisions with respect to its loyalty programme are not influenced by Footasylum. The Parties' loyalty schemes are different in nature, with Footasylum offering a points-based scheme, whereas JD Sports' JDX scheme is positioned as a "value add" scheme that is more focused on providing its customers with "money can't buy" experiences.
- (350) A number of other retailers operate loyalty schemes, including Foot Locker's "FLX" scheme which has similar characteristics to that of JD Sports. A number of retailers also offer free delivery loyalty schemes including ASOS and Next. The strength of competition on this parameter will not be impacted by the Merger.

### **E. Range of brands**

- (351) The PFs cite no evidence to support the proposition that the Parties are strategically influencing or responding to each other in relation to the range of brands offered.
- (352) As set out in detail in the Parties' previous submissions, the Parties are both dependent on the supply of products from Nike and adidas, and their stock and ranging decisions are driven by the allocations made available to them by the brands, not by each other. Post-Merger, the merged entity will continue to make procurement decisions within the segments within which JD Sports and Footasylum sit (which will remain at the discretion of the branded suppliers) to best serve JD Sports' and Footasylum's customers.
- (353) With respect to own brands and smaller "bedroom brands" it is clear that the Parties are not close competitors, and a key part of the rationale for the Merger (as described in detail in earlier submissions) is the continued development of these brands for the benefit of both Footasylum's and JD Sports' customers. Post-Merger the Parties will continue to face competitive pressure from a wide range of other players in relation to both footwear and apparel.

### **F. Service levels in store (opening hours / staff levels / quality / training / queuing times)**

- (354) The PFs cite no evidence to support the proposition that the Parties are strategically influencing or responding to each other with respect to service levels in-store.
- (355) As noted above, there are several mechanisms through which suppliers ensure that retailers achieve and maintain high levels of store quality and service, which will not be impacted by the Merger.

## CHAPTER 5 – INTERNAL DOCUMENTS AND PARAMETERS OF COMPETITION

### G. Website functionality

- (356) The PFs cite no evidence to support the proposition that the Parties are strategically influencing or responding to each other in relation to website functionality.
- (357) As noted above, the Footasylum document referenced in paragraph 8.106(c) referred to Footasylum's strategy of [REDACTED] but made no reference to JD Sports in this respect. Similarly, JD Sports' "[REDACTED]" is focused on [REDACTED] (and does not reference Footasylum).

### H. Technological improvements

- (358) The PFs cite no evidence to support the proposition that the Parties are strategically influencing or responding to each other in relation to technological improvements.
- (359) JD Sports' investment in innovation and technology is shared across the various JD Sports group fasciae in the UK and internationally. It is therefore not meaningful to assess incentives to innovate for the JD Sports fascia in the UK on an isolated basis.
- (360) In any event, it is clear that Nike, adidas and others such as Amazon, Zalando and Apple are leaders in this space, with significant budgets to invest in innovation. JD Sports' activities in this respect are not influenced by Footasylum, which is [REDACTED] [REDACTED]. A clear benefit arising from the Merger will be the opportunity for JD Sports to extend its technology and innovations to Footasylum.

CHAPTER 6

THE CMA DOES NOT TAKE PROPER ACCOUNT OF EXPECTED EFFICIENCIES

- (361) Both JD Sports and Footasylum submitted that there were a number of efficiencies arising from the Merger. However, the CMA has concluded that several of the efficiencies, despite being timely and likely to occur, are not Merger-specific or rivalry-enhancing. The Parties disagree.
- (362) First, the CMA suggests that “we consider it likely that Footasylum would have stabilised its financial position absent the Merger”<sup>171</sup>. For the reasons set out at section 6 of Chapter 3, [REDACTED] Further, the Merger resulted in the return of [REDACTED], which, prior to the Merger, [REDACTED]. JD Sports was therefore integral to the [REDACTED] of Footasylum’s financial position and therefore JD Sports’ support to Footasylum is a direct rivalry-enhancing outcome of the Merger.
- (363) Secondly, the CMA considers that “the proposed efficiencies to improve the Parties’ consumer offering and brand portfolio could be achieved through other means such as outsourcing or employing specialists and trading with Footasylum’s wholesale channel”. However, this ignores Footasylum’s financial position (as noted above), which would have [REDACTED] in any event, and, as set out in JD Sports’ response to the CMA’s Efficiencies Working Paper, digital experience is not something that can just be purchased. As noted previously, JD Sports has spent more than a decade building this facet of the business, which has been a large contributor to JD Sports’ growth and success in the market.
- (364) Thirdly, JD Sports has also highlighted the desire to invest in Footasylum’s own-brands (including ‘Kings Will Dream’) and its own-brand and wholesale channels.<sup>172</sup> However, the CMA dismisses this as not Merger-specific or rivalry-enhancing on the basis that Footasylum will continue to push its own-brands to make it distinctive in the marketplace, and will likely receive investment to continue expanding the wholesale channel<sup>173</sup>, and that “the merged entity’s ability to successfully develop own-brands would be no better than Footasylum would have on its own”.<sup>174</sup> However, this is not supported by the facts. As noted in Chapter 3 above, Footasylum was in [REDACTED] in its own-brand and wholesale channels to the extent it did (and will continue to do so) without JD Sports’ intervention (see section 6 of Chapter 3). JD Sports’ plan has always been to invest in Footasylum, which it will be able to do if the Initial Enforcement Order is lifted.
- (365) Fourthly, the CMA dismisses JD Sports’ desire to diversify its own-brand offering by bringing Footasylum’s brands in-house and leveraging the unique knowledge and expertise Footasylum has acquired to grow its brands. The CMA concludes that “JD Sports could achieve the same efficiency to acquire these products absent the Merger through trade with Footasylum’s wholesale channel”<sup>175</sup>. However, the CMA continues to ignore the fact that Footasylum’s wholesale sales are [REDACTED] proportion ([REDACTED]%) of its total sales<sup>176</sup> and that any small increase in wholesale sales would not replicate the proposed plans to diversify JD Sports’ brand portfolio and therefore enhance JD Sports’ product offering. The CMA also dismisses Footasylum’s ‘unique’ knowledge, suggesting that “successfully building own brands is not a skill that is unique to Footasylum”<sup>177</sup>. However, again JD Sports disagrees as it has spent many years unsuccessfully trying to grow its own-brand proposition. Footasylum has created an attractive own-brand offering, which

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<sup>171</sup> PFs, paragraph 11.73.

<sup>172</sup> PFs, Appendix I, paragraph 41.

<sup>173</sup> PFs, Appendix I, paragraph 41.

<sup>174</sup> PFs, Appendix I, paragraph 51.

<sup>175</sup> PFs, Appendix I, paragraph 42.

<sup>176</sup> 12 months to 30 September 2019.

<sup>177</sup> PFs, Appendix I, paragraph 43.

## CHAPTER 6 – EFFICIENCIES

has not been replicated by any competitor in the sports-inspired casual footwear or apparel markets. This will be of great value to JD Sports and, in turn, its customers through a rivalry-enhancing offering.

- (366) The CMA ignores several of the non-price synergies identified by the Parties, concluding “[t]he other synergies are limited in their improvement to consumers and would not contribute to an overall increase in rivalry in the market”<sup>178</sup>. These include operational efficiencies such as improving Footasylum’s in-store and online functionality (e.g. collection points, customer service, stock management, and payment possibilities). However, the CMA dismisses this as not rivalry-enhancing, but rather bringing the Footasylum part of the Merged Entity up to the JD Sports standard, rather than an overall improvement in the Merged Entity’s offer.<sup>179</sup> This is illogical. Since the CMA has determined that Footasylum’s lost competitive pressure in the market can support an SLC, then, equally, an improvement in Footasylum’s offering as part of the merged entity should help to offset that same SLC.
- (367) In the PFs, the CMA does not address the improved customer choice which would result from the wider distribution of Footasylum’s unique bedroom and incubator brands via JD Sports’ larger in-store and online offer.

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<sup>178</sup> PFs, paragraph 11.74.

<sup>179</sup> PFs, Appendix I, paragraph 53.