

Completed acquisition by Electruepart Limited of Espares Limited

ME/5129/11

The OFT's decision on reference under section 22(1) given on 22 November 2011. Full text of decision published 14 December 2011.

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

PARTIES

1. **Electruepart Limited** (Electruepart) is the parent company of Connect Distribution Services Limited (Connect), which is active in the distribution of spare parts, accessories and consumables for domestic electrical goods (DEGs) to trade customers, as well as to end consumers. Connect also provides DEGs repair services and outsourced warehouse and distribution services to Original Equipment Manufacturers (OEMs). It operates its retail business through a number of online platforms, namely: (i) its own full-line websites, notably, www.buyspares.co.uk and www.4ourhouse.co.uk; (ii) via www.partmaster.co.uk, a website operated by Connect on behalf of DSG Group (Curry's, Dixons and PCWorld); (iii) numerous single line websites offering a more focused range of products on a single brand, such as www.4hotpoint.co.uk or www.4indesit.co.uk, but which are independent of the manufacturer; and (iv) 54 white labelled official manufacturer sites operated on behalf of original equipment manufacturers (OEMs), for example www.4whirlpool.co.uk. Its turnover was approximately £72 million for the financial year ended 31 October 2010, of which around £[] million was generated from sales to end-consumers.
2. **ESpares Limited** (ESpares) is an online retailer specialising in the sale of spare parts, accessories and consumables for DEGs to end-consumers, operating via www.espares.co.uk. It also operates www.hooverspares.com on behalf of Hoover. ESpares offers around

700,000 spare parts, accessories and consumables for more than 500 different brands and appliances. Its turnover for the year ended 31 December 2010 was approximately £[] million, of which £[] million was generated from sales to UK consumers.

TRANSACTION

3. Electruepart acquired the entire issued share capital of ESpares on 29 July 2011 for the consideration of £[] million.
4. Following completion of the transaction, ESpares became a wholly-owned subsidiary of Electruepart and is maintained as a separate trading entity subject to the derogations to the Initial Undertakings signed by Electruepart and accepted by the OFT.
5. The administrative deadline for a decision in this case was 11 November and the statutory deadline is 3 January 2012.

JURISDICTION

6. The OFT believes that the transaction has resulted in two or more enterprises ceasing to be distinct under section 23(1) of the Enterprise Act 2002 (the Act).
7. The parties are both active in the retail supply of spare parts for white goods by specialist online retailers in the UK and estimated that they have a combined share of supply of such goods of approximately [30-40] per cent. The OFT considers this is a reasonable description of goods for the purposes of section 23(3) of the Act.
8. The OFT therefore considers that it is or may be the case that a relevant merger situation has been created.

MARKET DEFINITION

Background

9. Spare parts form part of an aftermarket since they are 'distress' purchases, bought by end-consumers when a primary appliance becomes faulty. Once end-consumers decide to fix the appliance themselves (rather

than call out a repairman or replace the appliance), they may search for the replacement part on the internet by using specific search terms (for example, by reference to brand, appliance or model number) on search engines such as Google or Bing.

10. Results of searches in this regard will normally identify a number of potential suppliers for the consumer, namely: (i) the relevant OEM, who typically have their own online shop where customers may purchase spare parts directly; (ii) full-line, specialist independent retailers, such as the parties; (iii) single line suppliers selling particular products by product line or manufacturer, such as Dyson Doctor; and/or (iv) marketplaces such as eBay or Amazon, where, in particular, smaller retailers who do not want to incur the overhead costs associated with a full-line online shop may choose to display and sell their products.
11. Spare parts are manufactured by OEMs who sell such parts to wholesalers, retailers and/or direct to end-consumers. Some OEMs do not supply online retailers directly, but require them to buy through wholesalers. Where wholesalers and retailers are able to buy from OEMs, they are typically able to negotiate a discount. Some wholesalers commission 'pattern' or non-branded spares where there are no intellectual property restrictions which prevent this, which offer a cheaper alternative for end-consumers. In the past decade, there has been an increasing trend to sell spare parts to end-consumers online.

Product market

12. The parties overlap in the online retail¹ supply of spare parts, accessories and consumables for DEGs to end-consumers. Although the competitive landscape is likely to differ when looking on an individual basis at spare parts, accessories or consumables for DEGs, the OFT notes there is some degree of overlap between such products, for example, what may be deemed a spare part may reasonably be deemed an accessory or

¹ The parties informed the OFT that although ESpare is not able to differentiate between customers buying spare parts from its website that are trade customers and those that are end-consumers, ESpare targets non-specialist end-consumers who purchase spare parts with a view to fixing faulty DEGs themselves. ESpare assists in this process by providing videos on YouTube to show customers how to fix the product. In this regard, the parties stated that information about the purchasing patterns of ESpare customers indicated that the majority of them would be end-consumers rather than specialist tradesmen. Connect, on the other hand, has a separate wholesale business, Connect Distribution, which supplies spare parts to trade. Users of Buyspare or its other websites would therefore be likely to be end-consumers.

consumable in addition. The OFT understands that the majority of the parties' products comprise spare parts, but for the purpose of its analysis and for the reason outlined above, the OFT assesses the competitive effects of the merger with respect to spare parts, accessories and consumables.²

13. The parties' products include genuine OEM-branded items as well as pattern spares, accessories and consumables which are sold on their respective websites. DEGs comprise white goods (that is, products such as refrigerators and washing machines) and brown goods (that is, products such as televisions, music systems, personal computers and printers). ESpares is active only to a limited extent in the supply of brown goods spares, generating approximately £[] sales only in respect of sales of items for brown goods in its previous financial year. For the purposes of market definition, the OFT therefore considers that it may be appropriate to focus its analysis on the supply of spares, accessories and consumables for white goods DEGs.
14. Connect additionally has a wholesale business which sources genuine and pattern spare parts for supply to other wholesalers, online retailers and bricks and mortar retailers. ESpares has no such wholesale business. The OFT considers vertical effects created by the merger in this regard in paragraphs 58 to 64 below.
15. Connect stated that the narrowest description of supply in which the parties overlap is the online retail supply of spare parts, consumables and accessories by specialist online retailers. However, Connect argued that independent, full-line online suppliers face a strong and immediate constraint from two additional sources of supply, namely, from bricks and mortar suppliers and OEMs.
16. Third parties generally agreed with the parties that OEMs form part of the online retail market for DEGs spare parts since they typically have their

² Further, it could be argued that separate markets exist on the basis of brand, or even for each individual spare part, accessory or consumable since such products are not substitutable on the demand-side. However, the OFT considers that, on the basis of supply-side aspects, it would be possible to aggregate several narrow markets into a broader one given that: (1) suppliers have the ability and incentive to shift capacity between products depending on demand; and (2) the same suppliers compete to supply these different products, with conditions of competition between suppliers being the same for each product (Merger Assessment Guidelines, paragraph 5.2.17).

own online shop for end-consumers to buy spares direct (or at least an online website with reference to a call centre number where customers can order spare parts over the telephone). However, the majority of third parties were not of the view that bricks and mortar suppliers compete with online retailers since they would not be able to stock the same range or quantity of products as online retailers, and could not serve a broad geographic area of customers. In particular, responses from bricks and mortar retailers themselves indicated that they tended to cater to the needs of local tradesmen rather than end-consumers.

17. In assessing demand-side aspects, the OFT considers it likely that relatively few end-consumers, in response to a small but significant non-transitory increase in price (SSNIP) of a particular spare part sold online, would be likely to switch away from online suppliers to a local bricks and mortar shop in the hope that it would sell the exact specified spare part required, particularly for more specialist products.³ The OFT therefore does not consider that the competitive constraint from bricks and mortar suppliers should be considered sufficiently strong such as to be included in the relevant market.
18. On the supply-side, the OFT notes that OEMs only supply their own branded products for purchase. The OFT was not made aware, during the course of its market investigation, of any OEM that currently sells competing brands, or non-branded parts. Although the OFT notes that an OEM's products will therefore not be as wide-ranging as an independent online retailer of DEGs spares that sells a large variety of differing branded products (as well as pattern products to fit the same branded appliances), the OFT considers that, collectively, OEMs afford a similar degree of constraint in the online retail supply of DEGs spares. This is due to the way in which customers search on the internet, typically by reference to a single brand name of the faulty DEG they wish to fix. Where end-consumers have searched for a brand-specific spare part, the parties' analysis of click share evidence suggests that OEMs' sites often feature in natural search results. The OFT therefore considers that online retail sales

³ The OFT was informed that it was common practice for bricks and mortar retailers to keep limited products in stock, so that less common parts would be ordered from a wholesaler such as Connect, requiring the customer to return to the store for the part (although some retailers said they would send out parts by post in some cases).

by the OEM made direct to the end-consumer should be included in the relevant product market.⁴

19. On balance, and on the basis of demand- and supply-side aspects, the OFT has regard to the online retail supply of spare parts, consumables and accessories for white goods DEGs for the purpose of its competitive assessment.

Geographic market

20. Connect submitted that the relevant geographic market is national for the following reasons:

- i) customers can access any online retailer's website from home
- ii) spare parts tend to be stored in one location from which all orders are dispatched, regardless of location of the customer
- iii) prices are determined centrally and do not differ according to customer location
- iv) delivery charges are standardised and are usually determined by the value of the order, and
- v) orders are despatched by Royal Mail or courier so delivery times are uniform.

21. Third parties agreed with Connect's views that DEGs spares are typically despatched nationally, and sometimes even internationally, and that the nature of the online market necessarily enables customers located in any geographic location in the UK to purchase such items.

⁴ The OFT notes that market definition is a useful tool, but not an end in itself, and the boundaries of the market do not determine the outcome of the OFT's analysis of the competitive effects of the merger in a mechanistic way (Merger Assessment Guidelines, paragraph 5.2.2). The OFT considers it most informative to include OEMs in the relevant product market and to assess the competitive constraints exerted by OEMs in the market in its competitive assessment (see paragraphs 46 to 49 below). It would not be expected to make a difference were the OFT to consider a market for the online supply of DEGs spare parts, accessories and consumables by independent full-line retailers, and to take account of the constraint exerted on such suppliers by OEMs from outside that market.

22. For the reasons identified above, the OFT considers it appropriate to adopt a national geographic market in this case.

COMPETITIVE ASSESSMENT – HORIZONTAL UNILATERAL EFFECTS

Market shares

23. There is no external data available which estimate the size of the online retail market for white good DEGs spares, consumables and accessories. A recent report prepared by in relation to the potential acquisition of ESspares (the Roundstone Report⁵) estimates the value of the online retail market for white goods DEGs spares in the UK to be £53 million. On this basis, the parties would have a combined share of supply of approximately [30-40] per cent (increment of [10-20] per cent) by value (which includes the parties' revenues for accessories and consumables).
24. Connect argued, however, that this estimate of the size of the market is significantly underestimated since it excludes direct sales by OEMs to end-consumers (estimated by Connect to be £45 million) and sales of accessories and consumables for white goods (estimated by Connect to be £100 million).
25. The OFT notes the highly fragmented nature of the online retail market for white goods spares, accessories and consumables and the inherent difficulty in aggregating sales for individual products and suppliers. With respect to the supply of accessories and consumables for white goods, the OFT notes from the Roundstone Report that the estimated value of online sales for vacuum bags is £80 million alone, which may support a conservative estimate of consumables and accessories of £100m by Connect.⁶
26. With respect to online sales by OEMs to consumers for spare parts, the OFT contacted a number of OEMs for white goods including Indesit

⁵ A market report dated March 2011 which the OFT understands was commissioned by private equity investors to undergo due diligence into the ESspares business for the purpose of assisting ESspares management in a buyout which provides an overview of the competitive landscape specifically for the sale of online spares for white goods by specialist online retailers in the UK.

⁶ That said, the OFT notes that there may be good arguments on both demand- and supply- side considerations to support the view that the online retail supply of vacuum bags forms a distinct market.

(Hotpoint), Dyson, Electrolux, and Glen Dimplex Home Appliances (GDHA) to obtain an estimate of their annual online retail sales to end-consumers for DEGs spares, accessories and consumables. Together they only accounted for approximately £4 million sales annually.⁷ Although there are numerous other OEMs for white goods beyond those contacted by the OFT and listed above, the OFT considers that Connect's estimate of £45 million for direct OEM sales to end-consumers is likely to overstate the relative strength of OEMs, particularly given that the OEMs listed above are four of the largest white goods manufacturers in the UK (see further paragraphs 46 to 49 below).

27. To test the £53 million market value figure provided by the Roundstone Report, the OFT contacted the parties' main competitors, a number of whom provided their annual sales figures. Whereas the parties' combined sales for brown and white goods spares, accessories and consumables amounted to £[] million between July 2010 and June 2011, the combined sales of the major specialist full-line online retailers for DEGs spares for the previous financial year amounted to approximately £[] million.⁸ For the remainder of the more minor competitors, the OFT was told that each of these online retailers would collectively have far less than £1 million annual sales. Conservatively, the OFT estimates that the total sales by specialist online retailers would be in the region of £[] million, with the parties accounting for in excess of [75-85] per cent of such sales.
28. Connect noted that the main bulk of competition in the market comes from marketplace suppliers selling on the likes of eBay and Amazon. To support this, they provided Terapeak data based on ESspares' top 10 highest selling products. The combined estimated annual turnover for ESspares and Connect (through its various websites) for these top 10 products amounted to £[] million. However, Terapeak data showed that the top 10 most frequently appearing resellers for these products sold on eBay collectively have an estimated annual turnover (across all products

⁷ The OFT notes that for certain OEMs, this may exclude telesales which may have originated from online searches by end-consumers, such that the total revenue figure is likely to underestimated online OEM sales to consumers.

⁸ Competitors comprise Ransomspares, UK Whitegoods, Margin services/Spares 2 You, Ezeefix Exserve/Easy Spares, and Yoursparers.

they sell) of £7 million combined.⁹ The OFT notes that the data only cover 10 of the parties' products where ESspares offers [around 700,000] stock keeping units (SKUs) and Connect, through its various websites, offers [around 1,500,000] SKUs, and where they overlap in approximately [250,000-350,000] SKUs. It is therefore likely that eBay resellers would account for revenues far in excess of £7 million were it possible to review Terapeak data across all the parties' products. The OFT also notes that Terapeak data do not capture sales generated by Amazon resellers, which would also be likely to account for significant revenues. The OFT therefore considers that the £53 million market value estimated by the Roundstone report is, if anything, an underestimate of the total size of the market since marketplace suppliers are likely to account for a large share of the market, potentially significantly exceeding the parties' combined revenues.

29. The OFT has not been able in the course of its investigation to establish precise shares of supply in relation to the online retail market for white good DEGs spares, consumables and accessories. However, based on the information available to it, the OFT does not consider the parties' likely combined shares of supply raise prima facie concerns given that, using the Roundstone Report's £53 million market size which excludes OEM sales to end-consumers, the parties account for approximately [30-40] per cent of the market, and their actual share is likely to be significantly lower than this. Notwithstanding the likely low level of the combined shares, but in any event having regard to the difficulty of obtaining precise data in this respect, the OFT goes on to assess closeness of competition since it considers it to be a better proxy for analysing the competitive effects of the merger.

Closeness of competition

30. Connect argued that the parties are not close competitors. It relied on an analysis of Hitwise data which it argued shows that Buyspares and ESspares do not receive a large share of spares-related web traffic, rather that OEMs collectively receive a larger share of clicks than either of the parties. Further, Connect argued that when looking at the results for key

⁹ Whilst the OFT notes that this figure is likely to overstate significantly revenues generated by these resellers since their revenues include sales outside white good DEGs spares, consumables and accessories, the OFT is also aware that the data account for only 10 resellers, such that there are likely to be many more suppliers not captured.

individual search terms, ESpare is rarely Buyspare's main competitor. Connect also provided data on the basis of pay per click (PPC) spend by both ESpare and Buyspare to argue that there is no correlation between ESpare's revenues and Buyspare's revenues at the point at which Buyspare enhanced its competitive offering in relation to increased PPC spend in 2010.

31. The OFT has regard to the parties' internal documents and notes that ESpare seemed to monitor Buyspare's prices. For example, there are a number of references in ESpare's management minutes comparing Buyspare's pricing and marketing strategies with its own. With respect to Buyspare, the OFT notes that the Roundstone Report includes a few quotes from a former member of Buyspare's D2C e-marketing team who regarded ESpare as being 'number 1' in the market, with Buyspare as 'number 2', noting that whilst both had strong websites, Buyspare sought to [].
32. Third parties who responded to the OFT's market investigation were of the view that ESpare and Connect are each other's closest competitor and that the merger combines the number one and two online retailers of DEGs spare parts, consumables and accessories in the UK. The majority of third parties viewed ESpare as the number one independent online retailer of spares in terms of website traffic, as a result of significant website investment and marketing. On the other hand, they noted that Connect features strongly in the online retail market due to the large number of white label sites it operates, as well as the prominence of Buyspare and Partmaster in paid results.
33. The OFT reviewed the Hitwise data provided by Connect but does not consider it to be probative evidence to support Connect's view that the parties cannot be said to be close competitors. In this regard, the OFT notes that the OEM sites in Connect's analysis include the OEM's main website for finished goods, whereas numerous OEMs have separate sites for spare parts sales only. The OFT therefore believes the strength of OEMs is significantly overstated by the data. This is supported fairly consistently by the Hitwise data when looking at OEM-specified searches. For example, using the search term 'Belling cooker spares', showed that Buyspare and ESpare had the largest average click-through rate, followed by the next largest competitor, 4Belling, in fact one of Connect's white label sites rather than the OEM's site.

34. That said, the OFT notes that, in contrast to ESpare, the prevalence of Buyspare on search results comes from paid search rather than natural search. Hitwise data from Connect shows that OEMs, eBay, Amazon and even Ransomspar enjoy a greater share of total clicks from natural search than Buyspare. This would tend to suggest to the OFT that Buyspare's brand is less strong than ESpare's (although see paragraphs 42 and 54 below). This is reflected in the breakdown of Connect's 2011 revenues which shows that Buyspare only accounts for a little over [] of total turnover achieved by Connect, and is less than [] of ESpare's annual revenues. However, the OFT notes that Connect's position is bolstered by the fact that it operates 54 different websites and that it features several times amongst the top hits for natural search as well as paid search.
35. On balance, the OFT considers that, as the leading specialist full-line online retailers of DEG spare parts, consumables and accessories, the parties are likely to be each other's closest competitors, although it notes that Buyspare's and ESpare's business strategies are somewhat differentiated. The OFT goes on to assess the strength of the remaining post-merger constraints in the market.

Post-merger constraints

Remaining specialist online retailers

36. Connect argued that the parties will continue to be constrained by the remaining online specialist retailers who offer a similar range of SKUs on their respective websites. It stated that all such suppliers of DEGs spares present a credible and significant constraint on the parties since end-consumers who purchase DEGs spares tend not to be loyal to a particular supplier.
37. Competing online retailers did not consider that they were able to compete effectively with the merged firm given the prevalence of ESpare and Connect in paid search and natural search results.
38. The OFT notes the limited sales achieved by the parties' competitors to date (see paragraph 27 above). However, it is aware that such sales by specialist online retailers are increasing over time. In particular, the OFT notes that Ransomspar typically features high up on paid search and

natural search. This is also reflected in the Roundstone Report which indicates that Ransomsparcs is the next strongest competitor to ESpares and Buysparcs and is acknowledged by end-consumers to have good website functionality. In addition, the OFT understands that Yoursparcs and Ezee-fix are relatively new entrants to the UK market, and within a short period of time, Yoursparcs has achieved fairly significant sales.

39. On balance, the OFT considers that the remaining specialist online retailers are likely to continue to offer a degree of constraint on Connect post-merger. The OFT is aware that the merger may in fact increase competition, at least for paid search, given that Buysparcs and ESpares may not compete so aggressively for paid search under mutual control of Connect. This may have the effect of reducing the cost of PPC for new or existing competitors.

Marketplace suppliers

40. Connect argued that sales by eBay and Amazon traders are very significant, highlighting the fragmented nature of the market such that there are a large number of alternative suppliers that an end-consumer can choose from when purchasing a required product. It was of the view that there are currently over 100 different firms supplying spare parts to consumers directly over the internet alone in the UK.
41. Third parties generally considered that marketplace suppliers offer a more limited degree of constraint on the parties. They considered that for fast-line products such as vacuum cleaner bags, suppliers on eBay and Amazon would compete with independent online retailers. However, for the more specialist products, notably for those which require technical assistance to fit the part (for example, through the use of ESpares' YouTube videos), such suppliers were unlikely to offer the same products for purchase.
42. The OFT notes from the results of a consumer survey set out in the Roundstone Report that the key factors affecting the consumer's choice when searching for a spare part are price, availability and delivery speed. Far less important are the quality of website, brand, consumer reviews or instructional videos, features of which the likes of ESpares' and Buysparcs' sites are strong. For the more price-sensitive customers, the Roundstone Report makes clear that eBay and Amazon suppliers are likely

to appeal more than specialist online retailers since products are generally cheaper through these avenues.

43. The OFT also notes from Hitwise data provided by Connect that eBay and Amazon enjoy significant brand strength in comparison to each of ESpare or Buyspare. Whilst brand may not be important to a consumer once the desired spare part is identified, the OFT is aware that brand strength affects the ranking of eBay and Amazon on natural search when specific search terms are keyed in, and that end-consumers' may also choose to go direct to Amazon and/or eBay websites without first searching for the product via Google.
44. As noted in paragraph 28 above, the OFT considers that marketplace suppliers are likely to account for a large proportion of the market, albeit that it is very difficult to determine to what extent such suppliers are able to supply all the products the parties (or other specialist online retailers) are able to sell. The Roundstone Report notes that it was not always possible to find all of ESpare's products on eBay and Amazon. That said, the OFT notes from ESpare's 2011 Marketing Plan that ESpare's top 5,000 selling items account for [] per cent of its revenue. The OFT therefore considers that marketplace suppliers are able to exert a significant degree of constraint on Connect without necessarily needing to offer the same range of products as the parties.
45. Overall, the OFT considers that marketplace suppliers are likely to offer collectively a strong degree of constraint on Connect post-merger and that this is likely to increase over time, particularly given that end-consumers are increasingly choosing to shop online such that the product offerings on the likes of eBay and Amazon are expanding rapidly.

OEMs and single-line suppliers

46. As discussed above, Connect considered that OEMs exert a strong degree of constraint on the parties through their direct sales to end-consumers. Connect also noted that single-line suppliers, whilst not offering a broad range of products and/or brands, nonetheless exert an additional constraint in the market.
47. Third parties considered that OEMs compete with online retailers for white goods spares, although to differing degrees. Certain OEMs considered

their spare parts business to be subsidiary to their finished goods business such that they invest less into maintaining a good website for end-consumers to purchase such products direct. In this regard, the OFT notes that whereas, for example, Dyson is a major supplier direct to end consumers through its website, other OEMs such as Indesit or GDHA have far more limited direct sales, their websites are less user-friendly, and they rely primarily on end-consumers finding their sites for spare parts through natural search rather than paid search results. That said, the OFT notes from the Roundstone Report that a number of OEMs have expressed an intent to expand their retail operations and gain ownership of the consumer relationship¹⁰ (see the discussion of **Barriers to entry and expansion**, below).

48. With respect to single-line providers, the OFT notes that, for certain products, such suppliers are likely to constrain the merged firm, although it is not clear to what these suppliers exist across a wide range of the parties' products. For example, it is clear that Dyson Doctor is a strong competitor for Dyson spare parts, the OFT is not aware of single line providers across the range of brands.
49. On balance, the OFT considers that OEMs currently exert some degree of constraint in the market, although the constraint will vary significantly depending on the OEM in question.

Barriers to entry and expansion

50. Connect argued that barriers to entry into online retail supply are low since entry is quick, cheap and easy, and that consequently, many competitors have entered the market in recent years. It stated that entry requires: (i) a supply agreement with an OEM; (ii) a transactional website that meets the security standards required to process debit and credit cards; (iii) a method of attracting customers to the website; and (iv) the ability to deliver promptly any spare parts bought through the website to customers.
51. Third parties did not agree with the parties' assertions. The majority noted, in particular, that the biggest difficulty faced by new entrants would be to gain traction in search results. Given that to rank highly on natural search takes time in building up reputation, third parties stated

¹⁰ Roundstone Report, slide 46.

that the only option for a new entrant to compete would be to invest in paid search, the cost of which would be significant to compete with the likes of ESpare and Connect in being ranked among the top listings for search results and having to bid for thousands of search term combinations on Google. Other barriers to entry included the cost of setting up a user-friendly website and associated back office, the cost of advertising to compensate for lower rankings on search engines, and the difficulty in building up reputations with OEMs for direct supplies such that a new entrant would be forced to source its supplies from a wholesaler such as Connect.

52. For more small-scale entry or expansion, the OFT considers that eBay and Amazon are easy and effective avenues for suppliers to sell their products where they can benefit from search rankings from the marketplace without having to pay for paid search.
53. With respect to entry or expansion for retailers' own websites, the OFT is aware that to replicate ESpare's success on natural search is likely to be more difficult, primarily due to the inherent difficulty in attracting customers to such websites. However, these barriers do not appear to the OFT to be insurmountable, particularly due to the fast-growing nature of the market, which is expected to grow at least in the medium-term.¹¹ In this regard, the OFT notes the recent entry of specialist online retailers, Yourspare and Ezee-fix, each of which are currently active in competing with the parties. The OFT is also aware that new entrants are likely to be able to invest in paid search to increase profile on search engines. In this regard, the OFT observes that Buyspare's reputation is predominantly built through PPC which could be replicated by new or existing competitors. As noted in paragraph 39 above, the OFT considers that PPC costs may reduce as a result of ESpare and Buyspare competing less aggressively for paid search ranking post-merger. With respect to expansion by existing independent online retailers, the OFT notes that there is nothing, in principle, to prevent competitor suppliers from expanding their range of

¹¹ In this regard, the OFT notes that the parties' revenues and that of their competitors are increasing annually. Similarly, the Roundstone Report notes that the market for white goods spares is a 'growing market driven by customer propensity to purchase online and repair appliances by fixing themselves'.

products given that it is not necessary for such suppliers to stock products in a warehouse.¹²

54. The OFT also considers that end-consumers are unlikely to place a strong degree weight on brand reputation in the online retail market for DEGs spares given that products are homogenous and end-customers tend to be price-sensitive. In this respect, the Roundstone Report shows that a very large proportion of people shop around before purchase, with the majority of spare parts being purchased via search engines, comparison sites or aggregators.
55. The OFT notes that expansion by OEMs is expected. Whilst OEMs tend not to focus on online sales of spare parts direct to consumers, a number of OEMs have stated that they intend to expand their operations and 'own the consumer relationship'. Given that branded spare parts originate from OEMs and that most OEMs have designated websites for spare parts, the OFT considers that they would have the ability in terms of brand strength and financial resource to invest more heavily in online sales to consumers in response to any increase in price created by the merger.
56. In any event, given the OFT's overall finding in this case, the OFT does not consider it necessary to conclude on barriers to entry and expansion.

Conclusion on horizontal unilateral effects

57. Overall, the OFT considers that whilst ESpares and Buyspares are likely to be each other's closest competitors, there is a significant degree of remaining competition in the market which is sufficient to countervail the lost competition caused by the merger. The OFT notes that the market is highly fragmented and that there are likely to be several alternative supply options for end-consumers who search for white goods spares, accessories and consumables online. The OFT is aware that the online retail market is a dynamic and rapidly growing market which provides increasing opportunities for expansion from existing suppliers as well as encouraging small-scale new entry. The OFT therefore does not believe that the merger gives rise to a realistic prospect of a substantial lessening of competition in this case.

¹² The OFT is aware that ESpares did not previously have a warehouse since it sourced its products from OEMs and wholesalers at the point in which end-consumers placed their orders.

COMPETITIVE ASSESSMENT - VERTICAL UNILATERAL EFFECTS

58. The transaction gives rise to a vertical relationship in that Connect supplies spare parts, accessories and consumables at the wholesale level to online retailers. ESpares is not active at the wholesale level but purchases spare parts from OEMs, generic parts manufacturers and wholesalers.
59. In line with the framework set out in the Merger Assessment Guidelines, an assessment of vertical effects analyses the combined firm's ability to harm rivals, its incentive to do so, and whether the effect of its actions would substantially lessen competition in the affected market.¹³ The OFT will only identify vertical concerns where all three limbs are satisfied.¹⁴
60. Connect argued it would have no ability to engage in input foreclosure since: (i) access to Connect's wholesale operations is not necessary to compete effectively within the retail market due to the wide range of supply options available to competing online retailers (such as purchasing suppliers from alternative wholesalers or direct from the OEM); (ii) a significant proportion of Connect's downstream competitors are vertically integrated as they either have wholesale operations or are the retail arm of an OEM; and (iii) switching costs to a different wholesaler are not large.
61. Connect estimated that it has approximately [10-20] per cent of the wholesale market, generating £[] million 'B2B' sales for its previous financial year. Other wholesalers who responded to the OFT's market investigation considered that Connect is the largest wholesaler of spare parts for DEGs in the UK. However, major alternative wholesale suppliers are Qualtex, Homespares and Masterpart who, the OFT understands, collectively have less than Connect's annual wholesale revenue. However, the OFT was made aware from numerous third parties that Qualtex is a strong competitor in the wholesale market and supplies to the majority of major online retailers.
62. A number of online retailers stated that it is often difficult to obtain supplies without going through Connect since certain OEMs choose not to supply direct to retail and/or have actual or perceived exclusive

¹³ Merger Assessment Guidelines, paragraph 5.6.6.

¹⁴ Merger Assessment Guidelines, paragraph 5.6.7.

distribution agreements with Connect. Similarly, some wholesalers expressed concerns that sourcing directly from OEMs is not always possible, with one wholesaler commenting that it has been difficult for it to forge its own relationships with certain OEMs or to source products, either in the UK or Europe due to their long-established relationships with Connect.

63. The OFT notes that, prior to the merger, ESpare sourced all of its supplies outside of Connect. The OFT considers this to be strong evidence that Connect would be unlikely to have the ability to foreclose downstream rivals by raising price or refusing to supply since customers would be able to continue competing effectively by sourcing from another wholesaler or by establishing further relationships with OEMs. In this regard, the OFT understands from third parties that it is commonplace for online retailers to multisource from a variety of wholesalers and OEMs, both in the UK and wider. Although the OFT was made aware of the difficulties in obtaining supplies at the wholesale and retail levels directly from certain OEMs, the OFT notes that OEMs control the supply relationship and therefore have the ability to divert sales to Connect's competitors should Connect raise price to downstream rivals. Indeed one OEM told the OFT that the power to supply products rests with the OEMs and that all they would have to do to diminish Connect's strong wholesale position would be to support another wholesaler with supplies (whether or not on an exclusive basis), or increase supplies to retail. The OFT also understands from Connect that the sole exclusivity arrangements it has with OEMs are with [].
64. For these reasons, the OFT does not consider that Connect would have the ability to foreclose downstream rivals. Since the first limb of the vertical effects analysis is not satisfied, the OFT does not consider it necessary to go on to consider in detail the incentive and effect of any potential vertical foreclosure strategy by Connect. However, the OFT notes from its analysis above that the highly fragmented nature of the retail market is such that Connect would be unlikely to have the incentive to foreclose downstream rivals to increase its market share at the retail level. Nor does the OFT believe that the effect of any such action would be likely to be sufficient to reduce competition to any significant degree.

THIRD PARTY VIEWS

65. Third party views have been set out above where relevant.
66. The majority of competing online retailers of spare parts raised concerns with the transaction, noting Connect's strong position as a wholesaler and that the merger would combine the largest online retailers of DEGs spares in the market.
67. A number of third parties expressed concern that, as with Connect's pre-merger position through its various websites, end-consumers would be unable to tell on the face of it, when comparing websites for the most competitive price, that ESpares and Connect are under common ownership.
68. Some OEMs and bricks and mortar retailers did not raise any concern with respect to the transaction.

ASSESSMENT

69. The parties' only material area of overlap is the online retail supply of white goods spares, accessories and consumables in the UK. Connect is also active in the wholesale supply of DEGs spares.
70. The OFT considers that the online retail market is highly fragmented with OEMs, specialist online retailers, single-line suppliers and marketplace suppliers all offering products to end-consumers to varying degrees.
71. The OFT considers that the merger combines the two largest specialist online retailers in the market and that the parties are each other's closest competitor in terms of having similar ranges and service in terms of website design. There is also some evidence that the parties monitor each other in terms of pricing and marketing. That said, the OFT believes that significant competition on the merged firm comes from suppliers on eBay and Amazon and single-line suppliers given that end-consumers rank price, product availability and delivery speed as the most significant factors in purchasing items. The OFT also notes that OEMs and other specialist online retailers provide additional competition in the market which will continue to exist post-merger. In any event, the OFT considers that the online retail market for white goods spares is rapidly growing, which may

be expected to attract further entry and expansion by competitors. The OFT therefore does not consider that the merger gives rise to a realistic prospect of unilateral horizontal effects arising in this case.

72. With respect to vertical effects, the OFT considers that Connect is unlikely to have the ability to foreclose downstream rivals by withholding supply or raising price given the various alternative supply options available for online retailers.

DECISION

73. The proposed transaction will **not** be referred to the Competition Commission pursuant to section 22(1) of the Act.

ENDNOTES

74. With respect to paragraph 1, Connect clarified that 16 of Connect's 54 white-labelled sites are operated on behalf of OEMs, the remainder of which are operated by Connect but are unofficial sites.
75. With respect to paragraph 33, Connect stated that, in compiling Hitwise data, it sought to ensure that its analysis was not skewed towards OEMs by removing brand name-only search terms.