Anticipated acquisition by Mothercare plc of Chelsea Stores Holdings Ltd

The OFT's decision on reference under section 33(1) given on 11 June 2007. Full text of decision published on 19 June 2007.

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

PARTIES

1. **Mothercare plc** (Mothercare) is a specialist retailer of products (including clothing, travel products, furniture and toys) for mothers-to-be, babies and children up to the age of eight. It operates out of 554 stores, of which 226 are located in the UK and 328 are international franchised stores.

2. **Chelsea Stores Holdings Ltd** (CSHL) is a retailer of toys and other children's products primarily for the 0-6 age range with the focus on 'learning through playing'. It has 214 stores in the UK and Ireland, and 87 international franchises, all branded as the Early Learning Centre (ELC). Its UK turnover in the year ended 5 May 2006 was £186.1 million.

TRANSACTION

3. Mothercare proposes to acquire the entire issued, and to be issued, share capital of CSHL. The parties notified the transaction, by way of a merger notice, on 30 April 2007. The statutory deadline is 13 June 2007.

JURISDICTION

4. As a result of this transaction Mothercare and CSHL will cease to be distinct. The UK turnover of CSHL exceeds £70 million, so the turnover test in section 23(1)(b) of the Enterprise Act 2002 (the Act) is satisfied. The OFT therefore believes that it is or may be the case that arrangements

are in progress or in contemplation which, if carried into effect, will result in the creation of a relevant merger situation.

FRAME OF REFERENCE

5. The parties overlap in the supply of toys.[1]

Product scope

6. The parties submitted that the relevant product frame of reference is the supply of toys by specialised toy retail outlets,[2] as defined in the European Commission's *Blokker/Toys 'R' Us* decision.[3]

7. However, in the *Argos/Littlewoods* Competition Act 1998 infringement decision,[4] the OFT noted that toys are highly differentiated products and that the relevant product market in that case was not as wide as the supply of all toys and games.[5] The supply of toys was therefore subdivided into a number of product categories: Infant and pre-school toys and games ('pre-school toys'), Boys' toys, Girls' toys, Games and puzzles, Creative toys, Construction, Plush/soft toys, Ride-ons, Electronic learning aids, and Hand-held electronic games. These categories were subsequently adopted in the OFT's *GUS/Littlewoods* merger decision.[6]

8. The majority of third parties considered that the supply of toys should be segmented, but offered variations for the segmentation. However, all stated that age and gender are factors in customers' purchasing decisions.

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[1] Toys are considered in this case to be all toys including games, puzzles, skateboards, scooters, art & craft products for children, ride-ons and hand-held electronic games. Computer games and video/console games are excluded.

[2] These are retail outlets which sell a broad assortment of toys to final consumers throughout the year. This definition includes specialised toy shops as well as shops with a specialised toy department such as department stores and household articles stores.

[3] Case IV/M.890 – Blokker/Toys 'R' Us (II) decision of 26 June 1997.

[4] OFT Competition Act 1998 decision of 21 November 2003, Agreements between Hasbro UK Ltd, Argos Ltd and Littlewoods Ltd.

[5] This approach was taken for calculating the level of penalties and was upheld by the Competition Appeal Tribunal in Argos Limited & Littlewoods Limited v Office of Fair Trading, Judgement on penalty, [2005] CAT 13, paragraph 192.

[6] The OFT's decision relating to the anticipated acquisition by GUS plc of the Index business of Littlewoods Ltd (June 2005).

9. In this case, it has not been necessary to reach a definitive conclusion on the relevant product frame of reference as it does not affect the competitive assessment in this case. However, for the sake of completeness, a cautious approach has been taken. The OFT has therefore examined the transaction on the basis of the supply of all toys and by category of toy.[7]

Geographic scope

10. The parties submitted that, based on the approach adopted in previous OFT decisions[8], the relevant geographic frame of reference for the supply of toys is the UK. The majority of third parties supported this view stating that their prices do not vary by location and they have national advertising campaigns.

11. However, some third parties stated that there is also local competition in toy retailing. Previous OFT decisions[9] involving national retail chains, including the retailing of toys, have considered both national and local perspectives. Therefore for the purposes of the analysis in this case, the OFT has followed its previous approach, and considered both a national and local geographic frame of reference.

HORIZONTAL ISSUES

National analysis

Retailing of toys

12. On a national basis, the parties have a combined share of supply of [0-10] per cent in the retail of toys and the transaction only results in a relatively small increment ([0-5] per cent). [10]

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[7] Broadly based on the categories identified in the OFT's Argos/Littlewoods decision.

[8] The parties gave the examples of the OFT's decisions relating to the proposed acquisition by Dixons Group plc of Kingfisher plc (May 1990) and the proposed acquisition by Ladbrokes Group plc of the Coral betting business (September 1998).

[9] For example, OFT's decisions relating to the completed acquisition by Eagle Retail Investments Ltd of the Early Learning Centre (May 2004); the anticipated acquisition by GUS plc of the Index business of Littlewoods Ltd (June 2005); anticipated acquisition by Mosaic Fashions hf of Rubicon Retail Ltd (September 2006 – women's fashion); anticipated acquisition by HMV Group plc of Ottakar's plc (December 2005 – books).

[10] Figures provided by the parties based on NPD data collated in June 2006.

13. Furthermore, there are a number of larger competitors present, including Argos, Woolworths and Toys 'R' Us, who will continue to act as a competitive constraint on the parties' behaviour. Given these factors, the OFT considers that the merger does not give rise to competition concerns in respect of the retailing of toys at the national level.

Retailing of toys by category

14. If the supply of toys is divided into categories, the parties' post merger shares of supply are highest in three categories of toys: ride-ons; creative toys; and pre-school toys. For the remaining product categories,[11] the parties' combined shares of supply are [0-10] per cent and, in each case, a number of significant competitors are present. The proposed transaction, therefore, is not considered to give rise to competition concerns in these remaining categories and they are not considered further.

15. For the supply of ride-ons and creative toys, the parties have a combined share of supply of [10-20] per cent (increments of [5-10] per cent and [0-5] per cent respectively). [12] However, in both these categories, there are several large competitors present which will continue to constrain the parties' behaviour post-merger. Therefore, competition concerns are not considered to arise in relation to the supply of ride-ons and creative toys.

16. With regards to the pre-school toy category, the merged entity will be the largest supplier with a [20-30] per cent share of supply (increment of [5-10] per cent).[13] In addition, competitors generally considered the merging parties to be close competitors in the retailing of toys for young (pre-school) children. One competitor raised the concern that the proposed merger has the potential to reduce consumer choice in the pre-school and educational/fun learning segments.

[11] These categories are: Boys' toys, Girls' toys, Games and puzzles, Construction, Plush/soft toys, Electronic learning aids, and Hand-held electronic games.
[12] Figures provided by the parties based on NPD data collated in June 2006.
[13] Figures provided by the parties based on NPD data collated in June 2006.

17. The parties argued that they are not close competitors as their products differ significantly. Mothercare retails a range of products for mothers-to-be, babies and children up to the age of eight (clothing and nursery equipment), with toys only accounting for [5-15] per cent of its total sales. ELC, on the other hand, is a specialist toy retailer focussing on 'learning through playing'.

18. Internal documents provided by the parties indicated that mothers with children with age ranges 0-2 and 2-4 purchased most of their toys from ELC and Argos. While Mothercare was ranked alongside Woolworths and Toys 'R' for mothers with children between the ages 0-2.

19. In addition, there are other strong competitors present in this category. Both Woolworths and Argos have shares of supply of [10-20] per cent.[14] Tesco has also been increasing its presence in toy retailing and its own-brand toy range for children up to the age of eight, with a strong focus on early learning materials.[15] It currently has a share of supply of [0-10] per cent.[16]

20. Post-merger, although the parties combined will be the largest supplier in the pre-school toy category, the parties will continue to face competition from the number of other retailers, including Woolworths, Argos Toys 'R' Us and Tesco. As a result, sufficient competitive constraints are considered to exist at the national level such that no competition concerns arise in relation to the supply of pre-school toys.

Local analysis

21. The parties carried out local analysis on all of the ELC stores.[17] Out of all the areas of overlap, there were no locations where the merger would result in a reduction in the number of retailers present to less than three. There were only five locations where the merger would reduce choice from five to four retailers and in all of these locations at least one strong competitor (either Woolworths or Argos) is present.

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[14] Figures provided by the parties based on NPD data collated in June 2006.
[15] Source: 'Non-foods in grocery multiples', Mintel Market Intelligence (25 April 2007).
[16] Figures provided by the parties based on NPD data collated in June 2006.
[17] The parties carried out a fascia test based on all of the CHSL stores using 10 minute drive time, 15 minute drive time, 3 mile and 2 mile isochrones.

22. On this basis, and taking into account the relatively low barriers to entry and expansion (discussed below) competition concerns are not considered to arise at a local level.

Barriers to entry and expansion

23. The parties submitted that barriers to entry and expansion in toy retailing are low. For example, the parties commented on the successful entry and expansion in recent years by supermarkets and internet sellers.

24. An independent market report[18] states that there are an estimated 1,200 specialist independent toy retailers in the UK, which suggests that small scale entry is possible. The report also states that the supermarkets are increasing their presence in toys and that consumer research show that Tesco and Asda are now in the top five stores used for shopping for toys.

25. Overall, new entry and expansion by existing competitors would appear to provide a credible constraint on the parties' behaviour post-merger.

THIRD PARTY VIEWS

26. The majority of third parties were not concerned by this transaction. Only one concern was raised regarding the potential reduction in consumer choice in pre-school and education/learning toys, which has been addressed above.

ASSESSMENT

27. The parties overlap in the supply of toys. Consistent with the approach taken in previous OFT decisions and views expressed by third parties, the OFT has considered the merger on the basis of the supply of all toys, by category of toy, and on a national and local basis.

28. With regards to the supply of all toys in the UK, the parties have a small share of supply of [0-10] per cent (increment [0-5] per cent). Furthermore, there are a number of larger retailers who will continue to act as a constraint on the parties' behaviour post-merger so competition concerns do not arise.

[18] Source: 'Toy retailing', Mintel Market Intelligence (October 2006).

29. If the supply of toys in the UK is subdivided into categories, the parties primarily overlap in the pre-school, ride-on and creative toy categories. However the constraint imposed by strong competitors (such as Argos and Woolworths), combined with the potential for expansion by retailers such as Tesco, are considered by the OFT to pose a sufficient competitive constraint on the parties' behaviour post-merger.

30. Similarly, at a local level, the OFT considers that the presence of a number of competitors in each of the areas where the merging parties are both present, combined with the potential for new entry and expansion by existing competitors, would appear sufficient to constrain the parties' behaviour post-merger.

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

DECISION

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