
Anticipated acquisition by Honeywell International Inc of Gardiner Groupe Europe SAS

The OFT's Decision on reference under section 33 given on 24 April 2006. Full text published 12 May 2006.

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

PARTIES

1. Honeywell International Inc. (Honeywell) is a US company active in the manufacture of various technologies used in the aviation and automotive industries, as well as products for the home. Honeywell's products are diverse and include aircraft engines, avionics, alarm systems, heating and ventilation controls, sensors and electronics used in cars, turbochargers, speciality chemicals and gas detectors. Its worldwide turnover was US\$25.6 billion (around £14 billion) in 2004.
2. Honeywell is active in the manufacture of security systems and fire alarm systems and its subsidiary company, ADI International (ADI), distributes security systems in the UK and other European countries.
3. Gardiner Groupe Europe SAS (Gardiner) is a French distributor of security and fire alarm systems in the UK and other European countries. It does not manufacture the products but rather sources them from a wide range of suppliers. Gardiner is owned by Electra Partners Europe, an equity fund. In 2005 Gardiner's UK turnover was [over £70] million.

TRANSACTION

4. Honeywell proposes to acquire all of Gardiner's issued shares for approximately €[] million (around £[] million). Gardiner will then become a wholly owned subsidiary of Honeywell.

5. The merger was notified to the Office of Fair Trading (OFT) by informal submission on 15 March and the OFT has set itself an administrative deadline of 15 May by which to announce a decision. The transaction has been notified to competition authorities in France, Germany, Ireland and Norway.

JURISDICTION

6. As a result of this transaction the enterprises, Honeywell and Gardiner, will cease to be distinct. The turnover test in section 23(1) of the Enterprise Act 2002 (the Act) is met.
7. 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.

RELEVANT MARKET

8. The parties overlap in the distribution in the UK of security systems. Further, Honeywell manufactures both security systems and fire alarm systems and, in addition to security systems, Gardiner distributes fire alarm systems.

Product scope

Manufacture of security systems

9. All security systems guard against unwanted intrusion on to a property but different security systems have different specific functions in meeting this end (and therefore, on the demand side, may not be substitutes for each other). Honeywell submitted to the OFT that the appropriate product scope for security systems could be segmented into intrusion alarm systems, access control systems and CCTV systems. These three segments are discussed briefly below.
10. Intrusion alarm systems alert someone (e.g. a security company or the police) of intrusion on to a property. There are different methods for detecting intrusion representing different degrees of security. The two main methods are through a break in an electric circuit around a door or window which triggers an alarm, and through motion sensors which trigger an alarm when motion is sensed in the area.
11. Access control systems electronically control entry into a building or an area by using keypads with an entry code or magnetic swipe cards.

12. Closed circuit television (CCTV) systems enable someone in a remote location to observe what is happening at a separate location.
13. In 2005 the European Commission (EC) examined a merger between Honeywell and Novar plc.¹ In that case the EC left open the product market definition for security systems although it did distinguish security systems from fire alarm systems. In an earlier case the EC also considered fire alarm systems were separate from security systems.²
14. In the current case it is not necessary to conclude on the product market as the competition assessment set out below would not be affected irrespective of the conclusion in this regard. However, the OFT has taken a cautious approach and examined the merger in terms of the three product segments mentioned above, as well as in aggregate.

Manufacture of fire alarm systems

15. All commercial fire alarm systems essentially operate on one of two bases. Either they detect smoke or heat and trigger an alarm (which may notify the local fire brigade) or they have a call point from which someone on location triggers an alarm (by operating a 'break glass unit').
16. Honeywell does not believe that segmenting fire alarm systems by components and integrated packages affects the competition assessment and therefore submitted to the OFT that this question be left open.
17. In Honeywell / Novar, the EC considered that four relevant product markets could be identified:
 - the supply of components for fire alarm systems;
 - the supply of packaged fire alarm systems to installers;
 - the installation of fire alarm systems (including the design of the system for the end user); and
 - the servicing and maintenance of fire alarm systems.
18. However, the EC did leave open the questions as to whether components formed one market or should be segmented further, whether installation and servicing should be considered as one market, and whether servicing of fire alarm systems should be considered to be in the same product market as servicing of security systems. In Siemens / Elektrowatt the EC did not decide whether the servicing of

¹ Case No. COMP/M.3686 Honeywell / Novar, decision of 30 March 2005.

² Case No. IV/M.913 Siemens AG / Elektrowatt AG, decision of 18 November 1997.

security or fire alarm systems constituted a separate product market from the systems market.

19. In the current case it is not necessary to conclude on the product market as the outcome of the competition assessment set out below would not be affected irrespective of the conclusion in this regard. The OFT has examined the merger on the basis of total fire alarm equipment and components.

Distribution of security and fire alarm systems

20. The OFT has been told by the parties as well as by third party distributors that it is common for distributors to distribute, install and service both security systems and fire alarm systems.
21. However, the supply of security and fire alarm systems via distributors is not the only way in which the products are supplied to installers or end users. Manufacturers also supply both installers and end users directly. The parties estimated that the supply of security systems was worth approximately £1.5 billion in the UK in 2005. However, around £[] million of that ([40-45] per cent) was accounted for by sales through distributors.³ The extent to which manufacturers do this differs between segments of security systems. For intrusion alarm systems, [55-60] per cent were supplied via distributors, for access control systems only [20-25] per cent were and for CCTVs the figure was around [40-45] per cent.
22. It may be the case that the supply of the products to installers and end users forms one market irrespective of whether they are supplied by manufacturers or distributors. Alternatively, it may be the case that supply by manufacturers and supply by distributors form separate markets. Finally, it is possible that the distribution of the products could be separated between the supply to installers and the supply to end users. The OFT has taken a cautious approach in this case and analysed the merger in terms of the distribution of security and fire alarm systems from wholesale distributors only. In the current case it is not necessary to conclude on the product markets as the outcome of the competition assessment set out below would not be affected irrespective of the conclusion in this regard. The remainder of this decision paper focuses on the wholesale distribution route of supplying installers and end users.

³ The parties based their estimates on the i&i Limited-Proplan report 'Security Systems: the European market 2001-2006' May 2002. Data in this report are actual figures for 2001 and forecasted figures for 2002–2006.

Geographic scope

Manufacture of security systems

23. Honeywell has submitted that the manufacture and supply of security systems may well be wider than the UK but does not consider it important that the OFT decides on this as it does not, in Honeywell's opinion, affect the competition analysis.
24. In Honeywell / Novar the EC did not find it necessary to define the geographic market for security system products.
25. Third parties distributors told the OFT that they sourced their security products from a large number of suppliers from different countries.
26. The OFT has examined the merger on both a UK and EU/EEA basis. Given the outcome of the competition assessment set out below, the OFT has not found it necessary to reach a conclusion on the geographic assessment.

Manufacture of fire alarm systems

27. Like security systems, Honeywell has submitted that it believes the market for fire alarm systems may well be wider than the UK but does not consider that the competition assessment is affected by the geographical definition.
28. The EC found in Honeywell / Novar that the relevant market for the supply of fire alarm systems was national because standards and product approval differed between countries.
29. The OFT has examined the merger on both a UK and EU/EEA basis. Given the outcome of the competition assessment set out below, the OFT has not found it necessary to reach a conclusion on the geographic assessment.

Distribution of security and fire alarm systems

30. Customers of Gardiner have told the OFT that they only source their products from within the UK as there is no reason to go further. This suggests that the geographic scope for distribution might be national.
31. In Siemens / Elektrowatt, the EC considered that the markets for security installations and the servicing of those installations were national, in part because a local presence was important for these activities. In both the Honeywell / Novar

and Siemens / Elektrowatt cases the EC considered that the markets for the installation and servicing of fire alarm systems must be considered as national.

32. In the current case it is not necessary to conclude on the geographic market as the outcome of the competition assessment set out below would not be affected irrespective of the conclusion in this regard. The OFT has taken a cautious approach and analysed the merger on both a UK and EU/EEA basis.

HORIZONTAL ISSUES

Shares of supply

33. The only horizontal overlaps that the transaction presents are on the distribution of security systems.
34. The parties' estimated shares of supply together with some of their competitors' estimates of their own share of supply are set out below (table 1 for the UK and table 2 for the EU/EEA).⁴

Table 1: Distribution of security systems in the UK, 2005 (per cent)

	<i>Intrusion alarms</i>	<i>Access control</i>	<i>CCTV</i>	<i>Total security</i>
Honeywell	[0-5]	[0-5]	[5-10]	[0-5]
Gardiner	[5-10]	[10-15]	[5-10]	[10-15]
Combined	[5-10]	[10-15]	[15-20]	[10-15]
Norbain	[]	[]	[]	[]
Rokonet	[]	[]	[]	[]
Videcon	[]	[]	[]	[]

Source: The parties and third parties.

Table 2: Distribution of security systems in the EU/EEA, 2005 (per cent)⁵

	<i>Intrusion alarms</i>	<i>Access control</i>	<i>CCTV</i>	<i>Total security</i>
Honeywell	[0-5]	[0-5]	[0-5]	[0-5]
Gardiner	[0-5]	[0-5]	[0-5]	[0-5]
Combined	[0-5]	[0-5]	[5-10]	[5-10]
Norbain	[]	[]	[]	[]
Videcon	[]	[]	[]	[]

Source: The parties and third parties.

⁴ These shares are estimated shares of distributors only. Therefore, they do not include supply by manufacturers direct to installers or end users.

35. The parties' combined shares of supply are low in all of the segments (at both a UK and EU/EEA level) and the increments are small. The distribution of security systems is extremely fragmented. The parties did not estimate shares of supply of their competitors as they judged that they did not have adequate information. However, they told the OFT that they faced strong competition from Aritech and AlarmCom in Europe and Norbain, Enterprise Security Distribution, City Electrical Factors and Rokonet in the UK.
36. Customers listed their main suppliers (in addition to Gardiner) to the OFT; a list which included (among others) Norbain, Guardall, Verex, Cooper Security, Bosch Security Systems, PAC International and Vicon. Competitors told the OFT that their main competitors (in addition to Honeywell and Gardiner) included (among others) Rokonet, Enterprise Security, Richardson Electronics, Dynamic CCTV, Alarm Supplies, Elvey Security Technology and GSL.

VERTICAL ISSUES

37. When examining vertical issues the OFT considers both the ability and the incentive of the merging parties to exclude competitors from the market place (or raise their costs), or to significantly increase the potential for coordinated behaviour between those firms in the market(s).
38. Exclusion in a vertical context could take two forms: (i) Gardiner excluding suppliers other than Honeywell from its product range; and (ii) Honeywell refusing to supply distributors other than Gardiner.
39. Tables 3 and 4 show the Honeywell's estimated industry structures for the manufacture and supply of security system products in the UK and the EEA.

⁵ The parties have provided data on an EEA wide basis while third parties provided data on an EU basis. The parties consider that this discrepancy makes little if any difference to shares of supply figures.

Table 3: Manufacture and supply of security systems in the UK, 2005 (per cent)

	<i>Intrusion alarms</i>	<i>Access control</i>	<i>CCTV</i>	<i>Total security</i>
Honeywell	15-20	5-10	5-10	15-20
Cooper	5-10			
GE	5-10	5-10	< 5	5-10
Guardall	5-10			
Siemens	5			5
Tyco	5	5-10	5-10	10
PAC		10		
Paxton		5-10		
Bewator		5-10		
Vista			5-10	
Dedicated Micros			5-10	
Pelco			5-10	

Source: The parties.

Table 4: Manufacture and supply of security systems in the EEA, 2005 (per cent)

	<i>Intrusion alarms</i>	<i>Access control</i>	<i>CCTV</i>	<i>Total security</i>
Honeywell	10-15	5	5	5-10
Cooper	5			
GE	< 15	5	5	< 15
Guardall	5			
Siemens	< 15	< 5		< 15
Tyco		5	5	< 15
Bewator		5		
Dedicated Micros			5	
Pelco			5-10	
Bosch	10		5-10	< 15
HID		5-10		
Panasonic				< 15

Source: The parties.

40. The tables show that Honeywell's share of supply is low in all of the security systems segments. Further, in all of the segments there are several suppliers with shares of around the same size as Honeywell and numerous other suppliers, indicating the fragmented nature of the industry. What is more, Honeywell is strongest in the manufacture and supply of intrusion alarm systems (in both the UK and EU/EEA) but post-merger, the parties will not have a large share of supply for the distribution of these products in either the UK or EU/EEA.
41. One third party distributor told the OFT that Honeywell's products are not 'must stock' products, further suggesting that customers have a choice between Honeywell's products and competing products.

42. It should also be borne in mind that more than half of the security systems sold in the UK do not come via a distributor (such as Gardiner).
43. Therefore, for security systems, the merged entity would not have the ability to foreclose competing manufacturers or distributors by either refusing to distribute other manufacturers' products, or by refusing to supply other distributors.
44. Further, Honeywell has not embarked on either of these foreclosure strategies since acquiring ADI. ADI distributes products from around 175 suppliers. Internal documents supplied by Honeywell show that that the company intends to continue distributing rival manufacturers' products through Gardiner.
45. Given the OFT considers that the merged entity will not have the ability to foreclose rivals, there is no need to consider its incentives to do so.
46. For fire alarm systems, Honeywell estimated its share of manufacture and supply in the UK is low ([10-15] per cent). It also estimated its main competitors had approximate UK shares of 20 per cent (Tyco), 10 per cent (Siemens and Apollo) and 5 per cent (Advanced Electronics and Protect). On an EEA basis, Honeywell estimated its share to be [15-20] per cent with its competitors accounting for [15-20] per cent (Siemens), [5-10] per cent (Bosch), [0-5] per cent (Tyco) and [0-5] per cent (UTC and GE).
47. For the distribution of fire alarms, Gardiner accounted for around [15-20] per cent in the UK and <5 per cent in the EEA.
48. Therefore, neither Honeywell's share of manufacture and supply, nor Gardiner's share of distribution of fire alarm systems make foreclosure strategies feasible.
49. In terms of increasing the possibility of coordinated behaviour, the structure of the distribution of both security systems and fire alarm systems is highly fragmented. The products and services offered by these distributors are not homogenous. Therefore, coordinating behaviour and monitoring any deviations from such behaviour would appear to be difficult.

THIRD PARTY VIEWS

50. Seven customers commented to the OFT about the proposed merger and none had concerns. One customer told the OFT that even if Honeywell did substitute some of its competitors' products in Gardiner's range for some of its own

products there are enough competing distributors to switch to if customers wanted.

51. Three competitors responded to the OFT's queries about the proposed merger. Two did not have any concerns but one had serious concerns. The concerned distribution competitor estimated that Gardiner distributes around 35 per cent of intrusion alarm systems in the UK and that Honeywell manufactures around 25 per cent of such systems for distribution in the UK.⁶ The competitor thought that the vertical integration between the parties would allow a greater scope and incentive for Honeywell to refuse to supply other distributors. The vertical aspect to the proposed merger has been discussed above.

ASSESSMENT

Horizontal issues

52. The proposed merger does not present any horizontal concerns. The parties' combined shares of supply are small in all segments and the increments are very low. Further, all customers who contacted the OFT were unconcerned about the merger because of the choice available to them.

Vertical issues

53. The OFT is generally concerned about vertical mergers when rivals lack a reasonable alternative to the vertically integrated firm. In this case, security and fire alarm system manufacturers will continue to have the choice of many distributors for the distribution of their products in the UK. Likewise, rival distributors will have access to many other manufacturers' products other than Honeywell's. Consequently, the merger does not present any vertical concerns.

DECISION

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

⁶ By using an independent market research report (i&i Limited-Proplan) and turnover figures from the parties, the OFT is satisfied that Gardiner's share of supply of intrusion alarm systems in the UK is much lower than 35 per cent (probably around 10 per cent).