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COMPETITION TRIBUNAL OF SOUTH AFRICA

Case No: 100/LM/Nov11

[013672]

In the matter between:

Steinhoff International Holdings Ltd	Acquiring Firm
And	
JD Group Ltd	Target Firm

Panel	:	Yasmin Carrim (Presiding Member) Medi Mokuena (Tribunal Member) Takalani Madima (Tribunal Member)
Heard on	:	30 March 2012
Order issued on	:	30 March 2012
Reasons issued on	:	15 August 2012

Reasons for Decision

APPROVAL

[1] On 30 March 2012 the Competition Tribunal ("Tribunal") unconditionally approved the acquisition by Steinhoff Holdings Ltd of the JD Group Ltd. The reasons for the approval follow below.

PARTIES TO THE TRANSACTION

[2] The primary acquiring firm is Steinhoff International Holdings Ltd ("SIH"), a public company listed on the Johannesburg Securities Exchange Ltd ("JSE"). The following shareholders held more than a 5% interest in SIH for the year ending 30 June 2011:

• Investec Asset Management	18.86%
• Public Investment Corporation	13.28%
• BS Beteiligungs und Verwaltungs GmbH	11.18%
• Eurotin SA	7.96%.

[3] SIH control various firms[1] and has a 32.4% shareholding in the target firm.

[4] The primary target firm is the JD Group Ltd ("JD Group"), a public company listed on the JSE. The following shareholders held more than a 5% interest in the JD Group for the year ending 30 June 2011:

• SIH	31.8%
• Investec Asset Management (Pty) Ltd	10.6%
• Public Investment Corporation	8.3%
• Government Employee Pension Fund	12.1%

ACTIVITIES OF THE PARTIES

SIH Group

[5] SIH is a multi-national integrated lifestyle supplier serving markets in Southern Africa, Europe and Australia. In South Africa, SIH conducts its operations through its wholly owned subsidiary Steinhoff Africa Holdings (Pty) Ltd ("SAH"). For

[1] For a complete list of firms controlled by SIH see annexure A to form CC4(2) filed by the merging parties. The merging parties also submitted to the Commission that SIH had a controlling interest in Loungefoam (Pty) Ltd ("Loungefoam") but that this company ceased to trade on 01 July 2009 and sold its remaining assets to Vitafoam.

purposes of this transaction, the business operations of SAH that are relevant are PG Bison and SHF and Toolplast.

[6] PG Bison has subsidiaries or divisions which are involved in forestry, sawmilling and pole production. It also produces processed timber products like particle board and medium density fibre board ("MDF") using, inter alia, the bison board, formica, Melawood, Supa Wood, Surinno Solid Surfacing, Woodline, Thesen and Moja brands. PG Bison has manufacturing plants in Piet Retief and Ugie where it produces raw and upgraded particle board and another manufacturing plant in Boksburg where it produces MDF.

[7] SHF and Toolplast has the following business divisions or subsidiaries: BCM Holdings ("BCM"), Vitafoam and DesleeMattex. BCM is involved in the manufacture and distribution of inner mattress springs. Vitafoam is involved in the production of flexible polyurethane foam at its plants in South Africa and Namibia. Vitafoam also manufactures economy mattresses and premium foam-based beds under the *Genessi and Suite Nite* brand. According to the merging parties the economy mattresses are supplied to national retail chains such as the Lewis Group, Ellerines Holdings and the JD Group. The Commission found that sales of the mattresses by Vitafoam to the JD Group are too insignificant to warrant any competition concerns.

[8] In relation to the foam base beds the merging parties indicated that SAH does not supply the JD Group with these bed ranges due to the restraint of trade agreement between SAH and the Bravo Group (Pty) Ltd ("Bravo") pursuant to the disposal of the furniture manufacturing business by SAH to Bravo in 2007.[2]

[9] DesleeMattex is a Cape Town-based jacquard-weaving company which manufacturers fabrics for the bedding industry (mattress ticking and circular knitted mattress fabric) in South Africa.

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[2] The parties submitted that this disposal was facilitated by forming a company by the name of Bravo Group Manco (Pty) Ltd ("Manco"). The parties further indicated that SAH acquired a redeemable participating par value preference share in this transaction. The Commission has subsequently been informed that SAH has sold its preference shareholding in Manco to Investec Bank during June 2011.

The JD Group

[10] The JD Group is a diversified mass consumer financier and a furniture, appliance, electronic goods, home entertainment and office automation retailer. The JD Group operates in Southern Africa through the following business divisions: (i) traditional retail which comprises 949 retail stores as eight different retail chains in South Africa, namely Barnetts, Bradlows, Electric Express, Joshua Doore, Morkels, Price 'n Pride and Russels and (ii) the cash retail division which operates stores such as Hi-Fi Corporation and Incredible Connections, financial services division and insurance division.

[11] The merging parties also indicated that the JD Group recently acquired Steinhoff Doors and Building Materials ("SDBM") from SIH. SDBM holds interests in the following building supply stores: Pennypinchers, Timbercity, Tilehouse, Sand and Stone, Unitraco and Truss Plant.

DESCRIPTION OF THE TRANSACTION

[12] In this proposed transaction, which is related to the SIH/KAP International Holdings transaction ("KAP" transaction), SIH has been granted certain call options to acquire further JD Group shares in exchange for shares in KAP.[3] SIH will, through the exercise of the call option, acquire a number of shares which will result in it increasing its shareholding in JD Group from 32.4% to over 50%. This exercise of the call options by SIH will result in SIH's shareholding in KAP reducing from 88% to approximately 65%. The net effect of these transactions is that SIH will have a majority shareholding in KAP and the JD Group, and be in control thereof.

[13] The structure of the proposed transaction as well as the KAP transaction is illustrated by the following organograms.

[3] The KAP transaction involves the acquisition by SIH of an additional 50% of the shares in KAP, which would increase SIH's shareholding in KAP from 34% to 88%. In exchange, KAP will acquire SIH's Industrial Assets in South Africa.

Figure 1: SIH Group structure prior to KAP and the JD transaction:

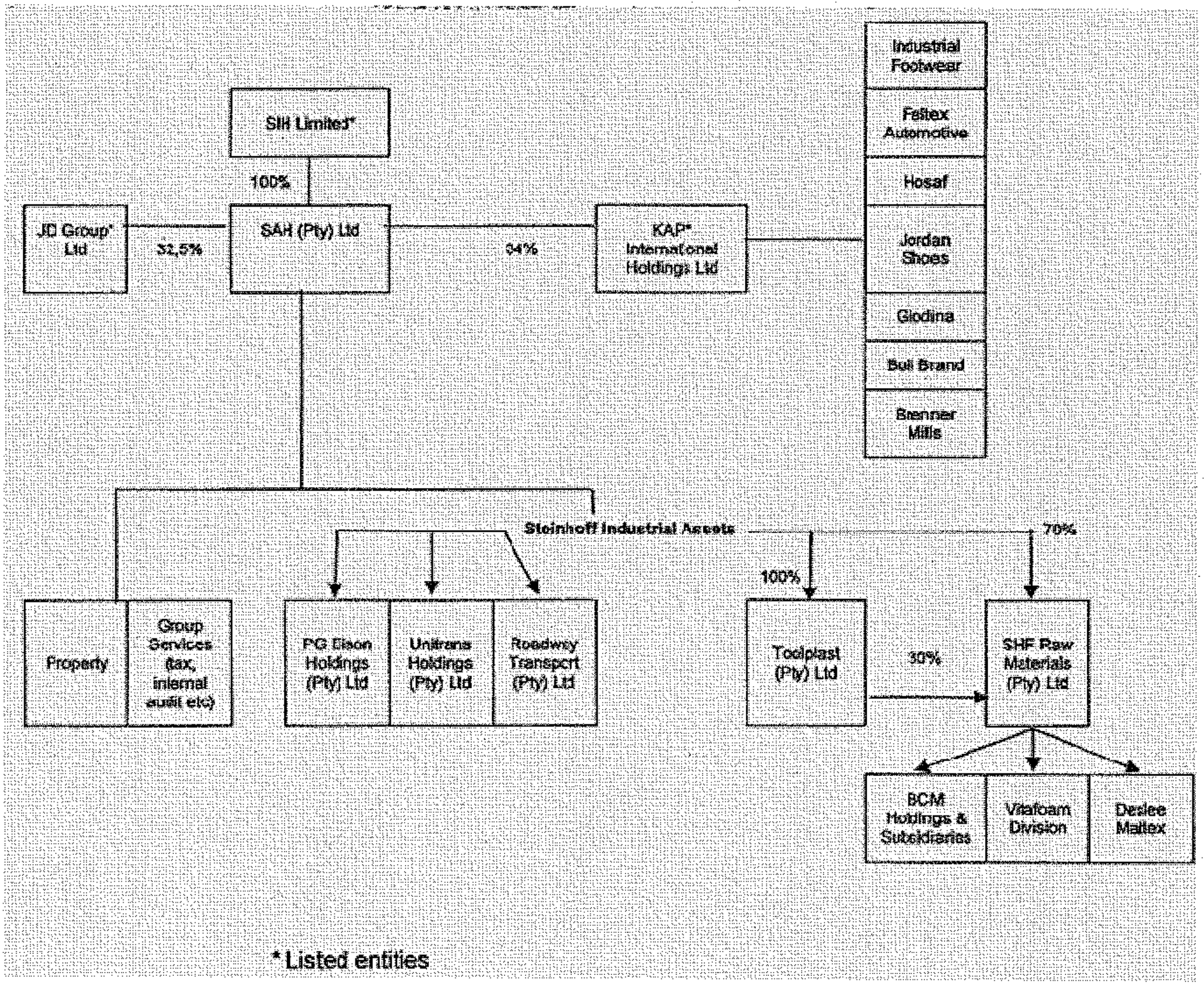
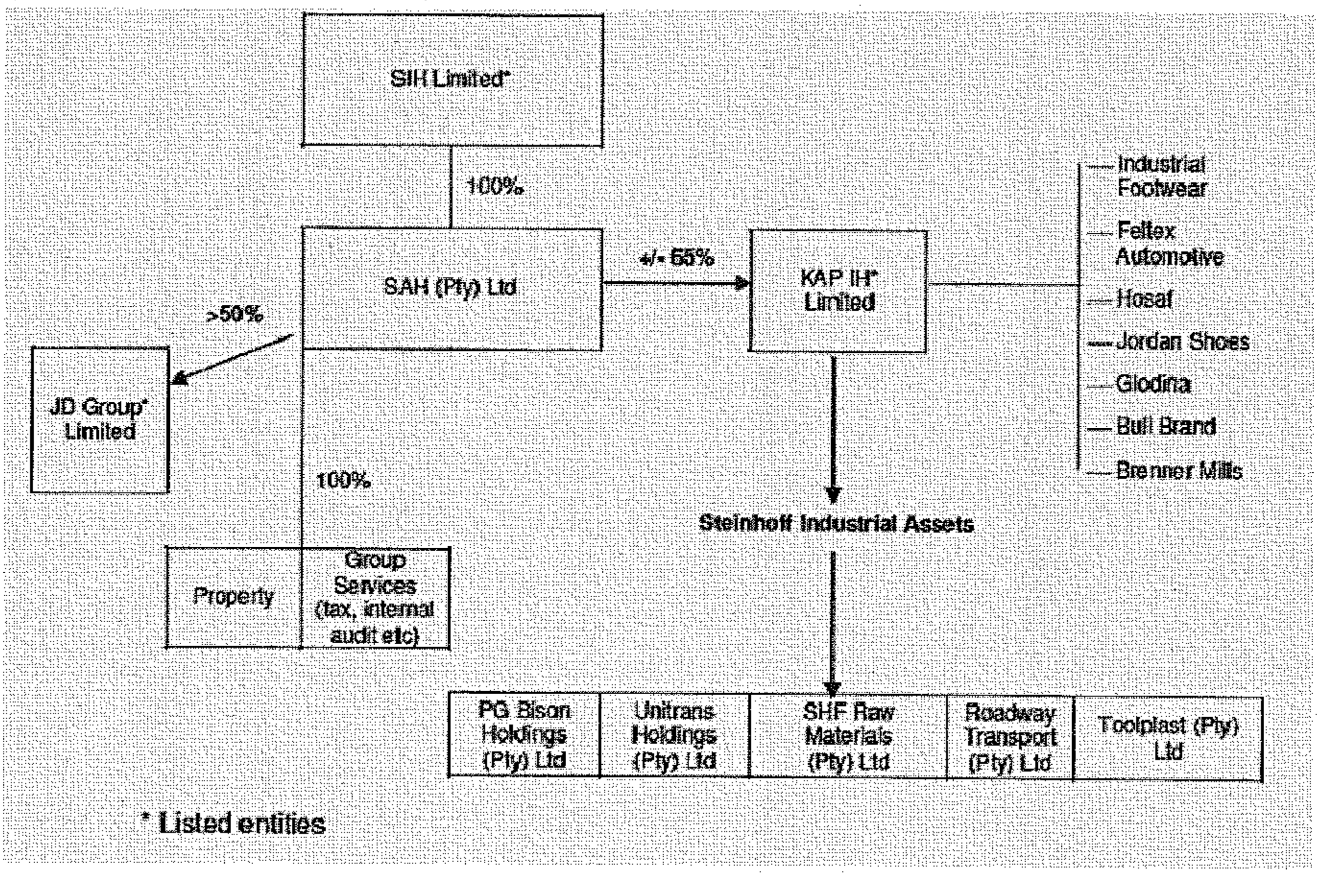


Figure 2: SIH Group structure after implementation of KAP and the JD transaction:



RATIONALE FOR THE TRANSACTION

[14] SIH submitted that this acquisition gives effect to its strategy of being an investment holding company which holds majority shareholdings in listed entities which have industrial and retail assets, but which are subject to third party inputs and controls, and are subject to extensive regulation. The merging parties further submit that SIH's strategy is to be a majority shareholder in these listed entities with a long term commitment and focus.

[15] The JD Group submitted that this transaction will enhance its position as a diversified retail and consumer services provider of scale in South Africa.

THE RELEVANT MARKETS AND IMPACT ON COMPETITION

[16] The Commission identified two broad categories of vertical relationships between SIH and the JD Group, namely, the building materials relationship and the wood to furniture relationship. The building materials relationship refers to the activities of the JD Group relating to distribution and retailing of board products, building materials, timber materials, ancillary hardware and retail goods, formica, solid surfacing, wood and wood-products through Pennypinchers and Timbercity and other subsidiaries. The wood-to-furniture relationship relates to the supply of raw input materials by SIH that are used in furniture and bedding manufacturing and which are then retailed by the JD group through its various brands. These inputs include foam, board products, springs, and mattress ticking.

(i) Building Materials Market

[17] In this market the Commission identified two separate upstream markets, namely, the market for the production and supply of raw and upgraded particle board and the market for the production and supply of raw and upgraded MDF. The Commission also identified one downstream market, namely, the market for the supply of building supplies, hardware and related products. In relation to the market shares, SIH and the JD Groups 's shares are estimated to be as follows:

- production and supply of raw and upgraded particle board – 49.3%;
- production and supply of raw and upgraded MDF – 34.6%; and
- supply of building supplies, hardware and related products – 2.5%.

(ii) Wood to Furniture Market

[18] Within this broad market the Commission identified six upstream markets as well one downstream market.

[19] The six upstream markets are defined as follows: (1) production and supply of raw and upgraded particle board, (2) production and supply of raw and upgraded MDF, (3) production and supply of polyurethane foam for the furniture and bedding market (general foam), (4) production and supply of inner mattress

springs, (5) production and supply of Z-springs and (6) production and supply of mattress ticking.

[20] The downstream market is defined as the market for the retailing of bedding and furniture products by the JD Group through its various brands such as Barnetts, Bradlows, Joshua Doore, Morkels, Price 'Pride, and Russels.

[21] In relation to market shares, the table below shows SIH group's market shares for each of the raw input materials it supplies.

Raw Input	Estimated Market Share
Particle board	49.3%
MDF	34.6%
Polyurethane foam	56%
Inner mattress springs	52.3%
Z-springs	10%
Mattress ticking	35% - 40%

[22] The merging parties compete with a number of firms for the supply of these inputs including Leggett & Platt, Kieral Springs, Quality Springs, Strandfoam, Foaming concepts, Sonae, William Tell as well as imports.

[23] In respect of the downstream market for the retailing of bedding and furniture products the JD Group has an estimated market share of 15% across all Living Standards Measure (LSM) categories (including independent furniture retailers and approximately 29% (when independent furniture manufacturers are excluded). In this market the JD Group compete with competitors such as Ellerines Holdings, Lewis and Shoprite Group.

(iii) Theories of Harm

[24] The Commission also assessed possible anti-competitive affects that may arise from the proposed transaction. In the building materials market the Commission found that any foreclosure attempt by the merged entity is likely to result in their customers switching to competitors. The Commission further found that competitors of the merging parties have access capacity and would therefore be

able to expand should the merger entity decide to engage in a foreclosure strategy.

[25] In the wood to furniture market the Commission assessed whether the merged entity would be able to engage in a tying or bundling strategy where they could tie or bundle the purchases of furniture by the JD Group from furniture manufacturers to the purchase of inputs from SIH by furniture manufacturers. The result of such a strategy would be the foreclosure of firms that compete with SIH for input supply, since absent this strategy, customers would have purchased raw input material from alternative sources. Another potential strategy assessed by the Commission would be for the merged entity to engage in a margin squeeze in which furniture and bedding manufacturers face higher prices from SIH and lower prices for sales to the JD Group.

[26] The Commission submits that the majority of the interviewed furniture and bedding manufacturers indicated that the merged entity would find it very difficult to identify is own raw material products and therefore would not be able to monitor purchases. Moreover, it appears that SIH and JD Group have not approached furniture manufacturers in the past in order to determine who their raw material suppliers are. The Commission further submits that the incentive to engage in a tying/bundling or margin squeeze strategy is put at risk by the ability of customers to punish the merged entity by switching[4] significant purchases of several inputs to alternative suppliers and not just purchases of the input in which there was a price increase. In addition, there are viable alternative retailers to which furniture manufacturers can distribute their products. These furniture retailers include national retailers such as Ellerines, Shoprite (House & Home and OK Furniture) and the Lewis Group.

[27] With regard to coordinated effects the Commission submits that this transaction is unlikely to create or strengthen coordinated effects in the upstream market for the manufacture and supply of raw input material or in the downstream market for the retail of furniture and bedding products. This view of the Commission is based

[4] For example customers such as Bravo, Restonic, Maserow and Lylax indicated that there are various alternative suppliers of raw materials that they can turn to.

on the fact the merged entity is not active at the level of furniture manufacturing.[5] In addition the Commission found that the retail market for furniture and bedding is highly fragmented, retailers offer weekly discounts and that this is also likely to undermine an attempt by retailers to coordinate their behaviour. In relation to barriers to entry the Commission established that out of all the affected markets only two markets have high entry barriers and these are the market for the manufacture and supply of particle board and MDF.

[28] Based on the above, the Commission concluded that the proposed transaction is unlikely to lead to a substantial prevention or lessening of competition in the market for the building materials or in the wood to furniture market.

THIRD PARTY VIEWS

[29] The Commission interviewed various market participants in order to obtain their views regarding the proposed transaction. Some of those interviewed include raw materials competitors (e.g. Sonae, William Tell, Leggett & Platt, Interwil, and Kieral Springs), furniture manufacturers (e.g. Bravo, Maserow, Calgan Lounge, Don-Elly, Presidential Furniture, Lylax, and Style Collections) and retail competitors (e.g.Ellerines Holdings, Shoprite Group). Certain concerns were raised by some of the interviewed market participants. The concerns raised are in relation to the ability of the merged entity to engage in strategies such as foreclosure, tying and bundling and margin squeeze. However, as indicated above, the Commission assessed these concerns and found that the proposed transaction is unlikely to create a market structure that could lead to the merged entity engaging in these strategies.

[30] A further concern raised by market participants is in relation to the relationship between SIH, the JD Group and Bravo (SIH's main customer and a major supplier of bedding and furniture to the JD Group). The concern about this relationship appears to be that post-merger the vertical links between the three firms could have a negative impact on competition and affect product choice and pricing. The Commission investigated this concern and found that the relationship

[5] According to the Commission the supply of foam beds and economy mattresses also does not facilitate coordination as SIH does not source any inputs from upstream competitors in the manufacturing of these products.

between SHI, the JD Group and Bravo is a normal business/commercial relationship wherein Bravo sources raw input materials from SIH manufactures bedding and furniture and then supply to the JD Group.

[31] Further, Bravo indicated to the Commission that it does not source all its raw input material from SIH but sources from other suppliers as well. In addition, the JD Group is not the only retailer of bedding and furniture as there are other retailers such as Ellerines and Shoprite Group.

PUBLIC INTEREST

[32] The merging parties submitted to the Commission that the proposed transaction will not have any significant effect on employment.

CONCLUSION

[33] In light of the above, we agree with the Commission that the vertical relationships between the activities of the merging parties is unlikely to give rise to any foreclosure concerns or lead the merged entity to engage in tying and bundling or a margin squeeze strategy. Furthermore, the proposed transaction raises no public interest concerns. Accordingly we approve the transaction unconditionally.

YCarrim

Yasmin Carrim 15 August 2012
Date

Medi Mokuena and Takalani Madima concurring.

Tribunal researcher: Ipeleng Selaledi

For the merging parties: Heather Irvine of Norton Rose Inc.

For the Commission: Werner Rysbergen