

**COMPETITION TRIBUNAL
REPUBLIC OF SOUTH AFRICA**

Case No: 56/LM/Oct01

In the large merger between:

Bidvest Group Limited

And

Paragon Business Communications Limited

Reasons for the Competition Tribunal's Decision

1. Introduction

1. This transaction will result in the merger of Paragon Business Communications Ltd ("Paragon") and Lithotech Limited ("Lithotec"), a subsidiary of Bidvest.
2. The Competition Commission recommended that the proposed merger between the above-mentioned parties be prohibited. It avers that the parties are leaders in most of the product markets that it has identified. The Commission holds that the merger will eliminate Lithotech's only significant competitor and create an environment in which the merged entity can behave to an appreciable extent independently of its remaining competitors.

Proceeding

3. At a pre-hearing conference held on 14 November 2001 it was decided that the Tribunal panel would, before the hearing was to start on 5 December, hold an inspection *in loco* at Lithotec's factory in Johannesburg in order to familiarize itself with the different products involved in this merger. The Tribunal also requested additional information from the parties and the Competition Commission on, *inter alia*, the different product markets, the parties' competitors and the joint venture.

4. At the hearing the parties called two expert witnesses, Mr Michiel Bester of Econometrix (Pty) Ltd, who provided a broad economic perspective of the printing market, and Mr Nick Rockey of Trialogue (Pty) Ltd, who provided a product market analysis. Mr Neil Birch, the group Managing Director of Lithotec and Mr David Kidd, the CEO of Paragon provided testimony on the businesses of the parties to the merger.
5. The Competition Commission called Mr Victor Gordon of Readers Digest, one of Paragon's customers, and Ms Anet Jansen, the Deputy Chief Procurement Officer of the South African Revenue Services (SARS). SARS has, on different occasions, awarded tenders to both Paragon and Lithotec to print tax forms.

2. The decision

6. For reasons set out below we have decided to approve the merger unconditionally.

3. The transaction

7. Bidvest wishes to acquire all of the shares of Paragon. The transaction will be effected either directly or indirectly through Lithotech, one of Bidvest's subsidiaries. Bidvest has concluded agreements with certain shareholders of Paragon, who collectively hold 50.2% of the total number of Paragon shares in issue, as well as with Paragon. In terms of the agreements, Bidvest or Lithotech will extend an offer to the shareholders of Paragon to purchase all of their Paragon shares or propose a scheme of arrangement between Paragon and its shareholders. Pursuant to either arrangement, Paragon will become a wholly owned subsidiary of Bidvest.
8. The parties believe that the merger would result in significant efficiency gains through cost savings thus extending the life of mature products. This would also allow the merged entity to extend its operations into the more profitable and innovative areas of their business.

4. The parties to the merger

9. Bidvest is listed on the JSE in the Industrial-Service Sector. It is the holding company of a diverse group of companies whose activities span catering supplies, food and allied products, financial and related services, freight forwarding, clearing, packaging, stationery, linen rental, laundry, cleaning services and office furniture supplies and related products. Bidvest's shareholding is widely dispersed amongst institutional investors on the JSE, the largest individual shareholder being the Public Investment Commissioner with 10.4% of the issued capital and some 48.4% of its issued capital being spread among 15 institutional

shareholders holding in excess of 1% of the issued capital. Bidvest conducts its office supplies business primarily through Lithotech, its wholly owned subsidiary.

10. Paragon is listed on the JSE in the Industrial-Packaging and Printing Sector and provides a broad spectrum of business communications solutions including business forms, customer communications and fulfillment services. Paragon's shareholding is widely dispersed amongst institutional investors on the JSE. The largest individual shareholder is Lungisa Investment Holdings (Pty) Ltd with 23.56% of the issued shares capital. Lungisa is an empowerment shareholder. Including Lungisa, five shareholders hold approximately 50.2% of the issued share capital.
11. In 1998 Lithotech and Paragon entered into an arrangement in terms of which they established a joint venture company called Listings Direct (Pty) Ltd.

5. The printing industry

12. The printing industry can be divided into four specialized areas, each fulfilling a specific printing activity which does not compete with the other, namely 1) the printing of magazines and books on commercial web presses, 2) the printing of business forms, that is, the printing of stationery for businesses such as invoices, statements and self-adhesive labels, 3) the newspaper industry, which uses a cold-set web press to print, and 4) general commercial printers, which print all types of brochures, letterheads, business cards, pamphlets and catalogues on sheet-fed printers.
13. Lithotech and Paragon are both involved in the printing of business forms.

6. The merger analysis

The Joint Venture

14. In 1998 Paragon and Lithotech merged their separate 'business forms listing' operations into a joint venture, Listings Direct, owned 67% by Lithotech and 33% by Paragon¹. Listings Direct was formed to manufacture listing paper, which can be defined as blank or single ruled continuous paper with sprocket holes on the edges for use in computer printers for printing output for presentation or storage/archive. There was, at the time of the formation of the joint venture, substantial excess capacity in the manufacture of listings paper because of the decline in demand for the product. Through the merger the parties combined their separate dedicated facilities for the production of listing paper.

¹ The Competition Board approved the transaction in 1998.

15. Lithotech and Paragon are the only customers of Listings Direct. They each, in turn, distribute the product directly to the end-user or to sub-distributors of the product. This product is purchased by end-users who range from an individual using a small desk-top printer through to a variety of businesses ranging from very small to very large businesses that have large data centers and that print on large printers or large laser printers.
16. While frequently produced on large purpose-built presses, listing paper can also be produced on most business forms presses.
17. The current transaction does not change the competitive situation in this segment of the business forms market and it will not be discussed further.

The relevant product market

18. The Competition Commission adopted a two- pronged approach in defining the relevant product market.
19. Firstly, drawing on the product list identified by the parties in their initial filings, the Commission treated each product identified by the parties as constituting a distinct product market, effectively holding that the various products are not substitutable for each other by virtue of their different characteristics, prices and intended uses. The Commission avers that the parties are by far the largest players in most of these markets and are the only players positioned in *all* of these markets.
20. The parties do not agree with the Commission's analysis of the separate product markets. While acknowledging that the Commission has constructed its relevant markets on the basis of the product listings provided by the parties in their initial submissions to the Commission, they aver that, in the course of the investigation, they pointed out to the Commission that, in their view, the relevant markets were significantly wider than that suggested by the product list. However the Commission chose not to investigate the possibility of product substitutability and assumed that the products as described by the parties in their documents constituted separate markets.
21. In response the Commission points out that correspondence received from competitors tended to confirm the product listing used by the parties in their initial submissions and which formed the basis of the Commission's identification of the relevant product markets². The Commission also points out that none of the respondents to their questionnaire had queried any product markets identified by the Commission.

² The parties had provided a non-exhaustive list of competitors in each product category in their CC4(2) documents.

22. Secondly, the Commission has identified a ‘bundled product’. No other provider of the products or services in question provides the variety of business forms products or services that the parties do. This ‘bundled product’ constitutes, in the Commission’s view, a separate relevant market in which the parties to this transaction are the only players. The Commission averred that large corporate clients as well as the public sector not only require their providers of business forms to provide the full gamut of the products and services that they require - a ‘one-stop shop’ - but these large customers also require their providers to provide volumes beyond the reach of small players. For these reasons the parties are in a league of their own and the merger would, therefore, eliminate the competition that currently exists between the only firms capable of providing a ‘one-stop shop’ facility and the only firms able to provide the volume required by larger customers.

23. We will now assess the Commission’s two approaches in greater detail.

1. The separate product markets

24. The Competition Commission defines the relevant product markets as:

- 1) **Business forms - listing**, which, as already noted, is produced by the joint venture, Listings Direct. According to the Commission the merger will not substantially affect this product market. As already noted, we accept this view and this product will not be discussed further.
- 2) **Business forms – continuous** which involves the manufacturing of various types of business forms on a continuous print basis such as invoices and statements and which has the clients’ details printed on the form. This is the major market in which both Lithotech and Paragon are active. This product line represents the largest part of the parties’ income prior to the merger.
- 3) **Business forms – snap sets** which is a multi-ply form, continuous or sheeted, where two or more sheets are joined by glue along one or more edges. The multi-ply forms utilize “self carbonating” paper or they are interleaved with carbon paper. When in sheet form, many sets may be bound into books or pads. Examples of this product are bank deposit and withdrawal slips.
- 4) **Business forms – to sheet**, which is a business form that is delivered in loose sheets. The sheets are either the result of printing a roll which is then converted to separate sheets before delivery or paper purchased in sheets and merely printed. The loose sheets can be bound into books. This product line is not one of the core product lines in which the parties are active.

- 5) **Direct mail printing**, involves printing for direct mail companies. Clients such as insurance companies have their documents printed, personalized and posted to policyholders by one company.
- 6) **Laser printing** involves high quality printing using large laser printing machines. Personalized direct mail printing and bank statements are printed in this way. It involves three processes namely printing, personalization and mailing which cannot be split. A computer image is transferred to the paper at high speeds. Large laser printers can take various types of paper:
 - Plain paper sheets from the paper mills
 - Pre-printed sheets from a printer
 - Pre-printed packs of continuous paper
 - Pre-printed rolls of paper from a printer
 - Plain paper rolls from the paper mills
- 7) **Mailing** i.e. where items are inserted into an envelope, manually or mechanically. The items to be mailed are delivered to the local postal depot in bulk, facilitating discounts for the client. Items can be inserted by machine if standard. Hand insertion is effective for small runs and novel items. Items may be personalized or standard such as magazines.
- 8) **Self Adhesive Labels** is a process similar to forms printing except the substrate is a label paper and the most common print technology is flexography.
- 9) **Book Binding**, where in business forms terms, books are created by binding sheeted forms with various cover options. This is not one of the core activities of the parties.
- 10) **Equipment Sales** involves the sales of machines such as those that fold letters into envelopes, ready for posting. These machines are generally referred to as form handling equipment. This is not one of the core activities of the parties.
- 11) **Logistics and Fulfillment** relates to the outsourcing of the customer's non-core activities such as storage and distribution of printed and other consumable items on the customer's behalf. It involves a group of activities such as warehousing, picking and packaging, distribution and procurement services. According to the parties this is a growing area of business. This is a new service that the parties are entering, largely inspired by the growing desire on the part of their clients to focus on their core business activities and outsource the ancillary activities related to their business.

- 12) **Web Finishing** involves further processing of printed sheets of paper by, for example, adding pressure glue to the edges of the letter in order to make it a self-sealing envelope, or by adding stamps to letters that can be removed in order to reveal PIN codes. The most common products manufactured under this heading are salary advices and water and electricity accounts. The process is done on specialized equipment called a Hunckler machine³.
- 13) **Paper Rolls and Carbon** involves the purchasing, manufacturing and selling of till rolls, ATM rolls, fax rolls, thermo paper rolls and carbon paper.
- 14) **Sale of Paper and Envelopes**, a procurement function provided by the parties to major corporate customers to source their paper and envelopes requirements. This is not a core product of the parties and the parties generally only service major corporate customers.
25. We will focus our analysis on Business Forms – Continuous (no.2), Business Forms – Snap Sets (no.3), Business Forms – To Sheet (no.4), Direct Mail printing (no.5), Laser Printing (no. 6) Mailing (no.7) and Web Finishing (no12).⁴
26. The parties do not accept the Commission’s market definition. They essentially argue that “business forms-continuous” (no.2), “business forms-snap sets” (no.3) and “business forms-to sheet” (no.4) comprise, for the purpose of defining the relevant market, a single product and should form part of a wider market defined as “business forms”. They point out that both ‘business forms-to sheet’ and ‘business forms-snap sets’ are close derivatives of ‘business forms-continuous’ – in the former the continuous web of paper is cut into individual sheets prior to delivery to the customer while in ‘business form – snap sets’ the output of ‘business forms-continuous’ is simply bound into a pad or small booklet.
27. The same approach, they claim, should be followed with regard to direct mail printing, web finishing and laser printing, which could all be regarded as derivatives of a particular type of business forms – essentially and advertising brochure - and should not be defined by the actual processes involved.
28. The parties aver that web finishing is a secondary process because it combines more than one traditional product into a single product by adding an adhesive patch or a self-adhesive label to it, depending on the customer’s needs. Laser printing could also be regarded as a secondary process in cases where certain

³ The parties said that there were currently 5 Hunckler machines in the country all of which will be in the hands of the merged entity. Lithotech indicated that they were prepared to sell 2 machines, if they could find buyers.

⁴ We will not further consider Business Forms Listing, (no.1), because it is not affected by the merger. Furthermore, competition is not substantially affected in the market for Self Adhesive Labels, (no.8), Book Binding (no.9), Equipment Sales (no.10), Logistic and Fulfillment (no.11), Paper Rolls and Carbon (no.13) and Sale of Paper and Envelopes (no.14) and we will, therefore, not include them in our analysis.

personalized customer data is printed on a paper, which may or may not contain some other ink and image from a previous process. There are two types of laser printers, one being continuous feed and the other sheet fed.⁵

29. In defining direct mail printing the Commission followed a narrow approach as opposed to the wider approach contended for by the parties. According to Mr Birch, the MD of Lithotec, direct mailing is an advertising type message, which could either be linked to a billing message or not, and which is sent directly to an individual. These forms are produced on a machine with the capability of running a number of colours, usually more than four colours. Apart from the newsprint industry, this is the biggest print sector and it could include for example a leaflet advertising a special offer, which is not personalized but which is mailed with a personalized item. Many direct mail items are merely inserted into envelopes along with a letter. Production of Direct Mail by the forms industry is a relatively new initiative. This has traditionally been the domain of the commercial printers and web offset printers.
30. The Commission, on the other hand, regarded this as a product consisting of printing, personalization and mailing. They argue that it could not be regarded as direct mailing if one company does printing and another does personalization and mailing.
31. The evidence presented by both the Commission and the parties was inconclusive. Clearly, the mere fact that discrete elements of a product *may* be produced through distinctive processes and by separate firms does not, of necessity, place them in distinct product markets for the purpose of identifying the relevant market. Conversely, there may be – and frequently are – several distinct product markets that come in to play in the production of a single product even if all are produced by a single vertically integrated firm. Whether the distinct stages of production constitute distinct relevant markets has to be decided on the specific facts of the case in question and the Commission errs in insisting that merely because the parties have identified a number of separate products that they have, in so doing, identified discrete relevant product markets. In this case, our examination of the facts supports the parties' version – 'business form - to sheet' and business forms – snap sheet' represent minor accretions to the value of the basic product which is 'business forms continuous'. It is therefore 'business forms – continuous,' defined to include 'business forms - to sheet' and 'business forms – snap sheet', that constitutes one of the relevant product markets.

⁵ Laser printing is a secondary process where personalized information, usually customer determined data, is printed on paper that may or may not already contain some ink from a previous printing process. Usually small businesses that require less volume than a medium to large company would print their own business forms on their desk laser printers. However, they are not in the same category as medium to large companies that require more colour and detail in their print as well as higher volumes in less time. These companies would normally make use of professional laser printers or would have their own large in-house printing facilities such as Woolworths.

32. Identical conclusions follow with regard to direct mail printing, web finishing and laser printing. In our view the relevant market is 'direct mail printing', defined to include web finishing and laser printing. Again, each of these processes may be undertaken by one integrated firm or they may be undertaken in separate firms. But they are part of the direct mail printing market. This is the second relevant product market.

2. The "bundled" product market

33. What of the Commission's contention that there is a market for a bundled product - a market in which all or a great many of the services and products referred to above are provided - that is distinct from the separate product markets in which the discrete services and products are supplied?⁶ In summary the Commission holds that the unique ability of the parties to provide a broad spectrum of products and/or services place them in a distinct league of their own within the industry. The parties, in contrast with their competitors, are active in all the product lines referred to above.

34. The evidence of Mr. Victor Gordon of Readers Digest, a witness called by the Commission, tended to support this argument. Readers Digest is effectively a mail order publisher and is a large customer of Paragon. Mr. Gordon is the procurement officer, responsible for procuring the services of providers like Paragon. He suggested that there was a convenience factor attached to a bundled product and that he would not willingly sub-divide a large contract between different competitors. However on cross-examination he agreed that his contract could be divided into different sub-processes, which could be undertaken by different companies. He nevertheless expressed a clear preference for the 'one-stop shop' facility offered, uniquely, by the parties.

35. Lithotec pointed out that customers such as Readers Digest (and this, by its own admission, includes Readers Digest itself) continually sample the market with a view to comparing the cost of the various components of a bundled contract. The parties aver that margins on, for example, laser printing and mailing, are very tight. The parties also argued that the participation of printing brokers and other agents, notably advertising agencies, facilitated the ability of customers to contract out the component pieces of a job that involved a number of technically distinct processes. They provided limited concrete evidence in support of their argument. They further held, and again supported this with limited evidence, that this had enabled relatively small firms to win large contracts, key components of which were contracted out to providers of one or other of the various services comprising the total job. The parties claimed that they themselves frequently contracted to perform particular components of a larger job.

⁶ Courts have recognized that a "cluster" of distinct products or services may be combined into a single relevant market, based principally on a consumer preference for a "one-stop-shop". See Therman Industries Incorporated v Pa'n Pak Stores Incorporated, 709 F.Supp 985, 1987-1 Trade Cases page 67,591 and United States v Philadelphia National Bank, 374 U.S. 321, 356.

36. Although the evidence presented in support of these arguments was sparse, it was not effectively countered by the Commission. The fact that the parties are able to provide a 'one-stop shop' service may, in particular instances, give them a competitive advantage. It is, however, by no means clear that this immunizes them from competition from participants who are only able to provide a single component of the larger 'bundle' of services or products required by the customer. Or, expressed conversely, it does not allow the parties to behave independently of the competitive response of those who provide a less comprehensive service than that provided by the parties to this transaction. The evidence of the representative of Readers Digest clearly establishes that it is *convenient* for a large customer whose business forms product incorporates a number of discrete printing and mailing products to utilize the services of a single company. However, should the price of the 'bundled' product increase significantly, there are few barriers to seeking out less costly providers of the various discrete products and services.
37. The representative of SARS, Ms Jansen, indicated that the parties' ability to produce high volume products was another factor that put the merging parties in a league of their own.⁷ Due to the confidentiality aspects of tax information, it was imperative that one single supplier be used. In response the parties argued that tax forms do not fit into any of the normal product categories and should be distinguished from other business forms. Moreover, tax forms are a dynamic product whose specifications change from tender to tender, which are produced once per annum and which increasingly involve complex IT infrastructure thus raising the prospect of software firms competing for tax form contracts. In any event, in their view there is, in the parties' view, no reason why a broker could not, through sub-contracts that may include relatively small firms, construct a joint venture or consortium in order to tender for these large contracts. This is exactly what Lithotech, Paragon and Universal did a few years ago when a very large quantity of the IRP5 booklet was required by SARS.
38. Once again while the quantity and quality of evidence presented by the Commission and the parties was less than satisfactory, on balance we believe that it casts significant doubt on the Commission's contentions in regard to both the bundled product and the importance of volume.
39. In summary then we conclude that the relevant product markets are 'business forms – continuous' which incorporate 'business forms – to sheet' and 'business forms – snap sheet' and 'direct mailing' which includes 'laser printing' and 'web finishing'. The 'bundled product' does not, in our view, constitute a separate relevant market.

⁷ Ms. Jansen's view is lent weight by the fact that there were only three candidates in the last major SARS tender, these being Lithotec, Paragon and Merpak. The latter was eliminated because it was unable to meet all of the tender requirements, in particular, it was unable to put up the R1 million required. The contract was won by Paragon, it was previously held by Lithotec.

The relevant geographic market

40. Both the Commission and the parties contend that the geographic market is national.
41. Evidence supplied by the witness from Readers Digest seemed to suggest that the market was not national but rather local because he preferred to use only printers in the Cape Town area. He argued that the logistics of managing a complex printing job incorporating several discrete processes favoured using service providers proximate to the client. Again while we accept that *convenience* favours a narrow geographical market, there appear, in the event of a price increase, to be no significant barriers to utilizing providers elsewhere in the country – indeed, on cross-examination this was effectively admitted by the witness. The parties also re-emphasized the actual and potential role of printing brokers in coordinating the logistics of a complex process.
42. We conclude then that the geographic market is national.

7. Impact on competition

43. We are now required to consider whether the merger will substantially prevent or lessen competition in the relevant markets. In undertaking this assessment we will take account of the non-exhaustive list of criteria provided for in section 12A(2) of the Act.
44. It is common cause that the merger will result in the elimination of a significant competitor. Indeed both Lithotec and Paragon explicitly acknowledged that each consider the other to be their most significant competitor. However, while this is naturally significant, it is not dispositive of the question of market power. We must consider the share of the relevant market that the merged entity will possess as well as a number of other significant factors including barriers to entry and the dynamic characteristics of the market.

Market share

45. While market shares are by no means dispositive of the question of market power, it is widely accepted that they provide, at the very least, a sound first approximation of its extent. However, market share evidence is as reliable as the underlying definition of the relevant markets used in calculating shares. As already indicated we do not believe that either the Commission or the parties have provided us with a clear view of the relevant market.
46. We were supplied with two different sets of market shares:

- 1) The Competition Commission based its calculation of the market shares on turnover figures as supplied by the parties in their merger notification and as supplied by the market participants⁸. This method is also called a “bottom-up” approach⁹; and
- 2) The expert witness from Trialogue, Mr. Rockey, who used a ““top down”¹⁰ methodology to quantify the market. In using the “top down” approach Mr. Rocky calculated the market share for business forms by taking into account paper inputs to the business forms industry, which comprised uncoated reels and carbonless papers. Carbonless paper, in his opinion, presented the most reliable indicator of market shares in the business form market as, according to his evidence, it is used solely for the production of business forms. He also used a different method to calculate the market share for laser printing, based on the number of machines in use and the number of ‘clicks’¹¹ recorded.

Their respective conclusions predictably diverge significantly. These are summarized in the table below:

| MAIN PRODUCTS | COMPETITION COMMISSION % | EXPERT WITNESS % |
|--|-------------------------------------|-----------------------------|
| Business Form snap sets | 52.9 | - |
| Business forms continuous | 64.7 | - |
| All carbonless forms¹² | - | 36 |
| Direct mail printing | 50.7 | Small |
| Laser printing | 35 | 10 |
| Mailing | 33.1 | 20 |
| Web finishing | 87 | - |

⁸ The market information supplied by other market participants is claimed confidential information and will not be supplied in this report.

⁹ “bottom-up” is where the size of an industry is determined by assessing the size of all participants competing in a certain industry sector.

¹⁰ “top-down” refers to analysis of market share through evaluation of global inputs and outputs of an industry sector.

¹¹ A “click” represents one image placed on the paper. Xerox and Océ dominate the supply of laser printers and part of the supplier agreement is a service contract, where users pay suppliers of printers a fee ‘per click’.

¹² This is also defined by the parties as Business forms and includes Business form continuous, Business form snap sets and Business form sheet.

47. On the basis of their market share figures the Commission then calculated HHI¹³ figures to determine concentration in the each relevant product market. It identified four markets where the post-merger HHI exceeded 1800 and changed by more than 100 points in consequence of the merger. These are business forms-listing, business forms-continuous, business forms-snap sets and web finished products. In the business forms-continuous the post merger HHI would be in excess of 4000 points and the change would be 1628, which is presumptive of considerable market power.
48. However, the methodologies and empirical bases utilized by both the parties and the Commission are open to question. While the ‘bottom-up’ approach is the more conventional method utilized in calculating market shares, the parties are correct to point out that it is more reliable in markets with a limited number of participants. We should add, however, that we could find no basis to the parties’ claim that the Commission had omitted several important competitors in calculating market shares. On the contrary, the Commission has diligently tracked down participants in the industry, in the process, identifying competitors not listed in the parties’ initial submission. However, a significant ‘residual’ category remains in the Commission’s market share calculations and this may account for some of the discrepancy in the respective market share calculations. As for the ‘top-down’ approach employed by the parties, we have simply not been provided with sufficient evidence to arrive at a confident assessment of this methodology or its empirical basis.
49. The difference between the estimates provided for the direct mail market is particularly striking. This appears to be attributable to the different approaches followed in defining the market. For reasons that are not immediately apparent, the Commission appears to hold that a direct mailing service can only be provided as part of a bundled product that includes printing, web finishing, laser printing and mailing – given then that the parties are uniquely capable of providing a bundled product, their share of this market is, per definition, considerable.¹⁴ The parties, on the other hand, hold that discrete parts of the direct mailing service can be and are provided by a large number of participants.
50. The market share, and hence the HHI, calculations do not, in this instance, provide a reliable indication of market power, although even on the lower estimates of the parties, the post-merger market share in the ‘business forms – continuous’ market is, on the face of it, cause for concern.

¹³ The HHI is the Hirschman-Herfindahl Index, which measures concentration in a market. The 1992 U.S. Horizontal Merger Guidelines states that: “Where post merger HHI exceeds 1800, it would be presumed that mergers producing an increase in the HHI of more than 100 points are likely to create or enhance market power or facilitate its exercise.”

¹⁴ See the Commission’s recommendation on page 21 of the confidential version under “Direct Mail Printing”, where they say that when printing, personalization and mailing are split between different companies then it is not classified as direct printing anymore.

Level and trends of concentration

51. There is a recent history of acquisitions in this industry. Lithotec and Paragon have both participated actively in the acquisition of new businesses. On the face of it this does suggest a trend of increasing concentration. However, on closer examination it appears that both have purchased businesses in one or other niche market, generally niches in which the acquiring parties have not been active players.¹⁵
52. The parties claim that the level and trend of concentration is not accurately revealed, by simply examining the identity of those who win significant contracts in the business forms market. This would, for example, not reflect the great many occasions on which the 'main contractor' acts as a coordinator of the activities of a number of firms, including small firms. Hence it is common for a distributor company (the firm Forms Independent was specifically mentioned) to put its name to a contract and then outsource or sub-contract certain parts of the contract. Lithotech itself has performed this co-ordinating function on numerous occasions.
53. The parties made reference to relatively large players such as Universal Business Forms, Lexlines, Gillmitch and Burlington Data Print but also insisted that many smaller players such as Ren-form, Focus Forms, Manny McCann, Dusi Business Forms, Rapid Run, CNH Printers and Western Computer Forms actively participated in large contracts that were frequently, although incorrectly, identified with the 'main contractor'. According to the parties large customers were generally content to split large printing jobs between smaller players. Standard Bank exemplified a large customer well known for splitting high volume jobs between several players.
54. Sub-contracting not only enabled small companies to participate as sub-contractors in contracts won by the large players. It also enabled small players to win large contracts and then to sub-contract components of the contract to other players. Examples were provided of smaller players winning very significant contracts - hence Ren-form succeeded in winning the contract for post box renewal forms, previously a Lithotec contract. Focus Forms, another small player, had won a major tender from the Johannesburg Metro, previously a client of Lithotec.
55. We are persuaded by this evidence, which was not challenged by the Commission. Moreover it appears to be corroborated by the existence of many small firms of long-standing in this industry. Evidence presented suggests that relatively small firms have survived for extraordinarily long periods in this industry. On the face of it this seems to indicate that conditions in this industry – these may be demand conditions or technological conditions or its continuing

¹⁵ The parties have provided us with a list of acquisitions that they have made during recent years. From this it seems that both Litotech and Paragon have acquired businesses in laser printing, mailing and fulfillment.

craft characteristics – conduce to small firms establishing a product niche and a reliable customer base that enables them to remain competitive despite the relatively small scale of their operations.

The dynamic characteristics of the market

56. The parties made much of the ‘maturity’ of this market. This is presented as the key dynamic feature of this market. The traditional business form was presented as a product in terminal decline, particularly vulnerable to the advances in electronic technology. Mr. Birch claims that the industry has seen a general decline in the demand for business forms over the last 10 years - more specifically, the demand for business forms-continuous is declining by 8% per annum. New technology and product innovation, such as SAP and Adobe Acrobat¹⁶ is reducing the usage of paper in the office – the phenomenon referred to as the ‘paperless office’. Customer demand is also moving away from the traditional printing products such as ‘business forms-continuous’ towards ‘business form - to sheet’. The parties do not have a significant position in the latter market segment. The movement towards sheet is facilitated by the shift to shorter runs and quicker delivery and response in the market. In order to counter this decline the parties have started to shift their focus to novel add-on features such as web finishing and to products that are not normally regarded as business forms such as ballot forms and lottery tickets.
57. It is not immediately apparent why the competition authorities should adopt a more permissive approach to mergers in ‘mature’ product markets. Certainly business forms and direct mailing remain significant markets and there is no suggestion of a serious profit squeeze in these markets, although evidence of capacity underutilization is obviously indicative of the pressure experienced by firms in this industry. In any event, in an effectively functioning market product cycle maturity would reflect itself in lower prices and profitability. The most vulnerable firms would exit the industry and the more entrepreneurial would, as appears to be the case with respect to the parties to this transaction, seek out new products and new market niches. A competition authority dedicated to ensuring the integrity of market processes would have no call to arrest this process by approving anti-competitive mergers any more than it would have reason for turning a blind eye to collusion or other anti-competitive practices perpetrated in ‘mature’ markets. There is persuasive evidence of new technologies contributing to declines in the traditional business forms market – for example, electronic data storage and communication technologies reduce the requirement for multiple copies.

¹⁶ SAP is an accounting and materials management package used in large corporations and has the ability to present data in electronic format, which is accessible to users who are on that system. Adobe Acrobat converts existing forms to digital form, to which the user can add information and print on demand, which saves printing costs.

58. A consideration of technological development is called for when there is evidence that suggests that new alternative products constrain the ability of those in the traditional market to raise prices. Evidence in support of this contention is, at best, anecdotal. Moreover, the Commission points out that converting businesses from the use of traditional business forms to electronic data storage and communication requires costly initial investment in hardware and software and a commitment to employing high level manpower capable of operating and maintaining new technologies.
59. We are also persuaded by the Commission's contention that the 'maturity' of the product is likely to discourage new entry and may on balance militate *against* approving the merger.
60. In summary, although there is some evidence of 'maturity' or decline in certain important niches of this industry, we are not of the view that the 'maturity' of the product or the 'dynamic characteristics' of the market in question constitute grounds for approval of the merger.

Barriers to entry

61. The parties insist that the barriers to new entry are particularly low. They reason that the global decline in the output of business forms has resulted in the availability of used machinery at unusually low prices. They also argue that new entrants utilizing advanced electronic technologies are increasingly capable of entering the business forms market. The evidence presented in support of these contentions was sketchy at best. In any event we are persuaded by the Commission's argument that the maturity of the product will act as a powerful disincentive to would-be new entrants.
62. However, we are persuaded that the existence of installed excess capacity will enable a rapid supply response from existing competitors should the merged entity conduct itself in an anti-competitive manner. This is a powerful argument in favour of approving the transaction.

Countervailing power

63. The parties aver that their large customers are extremely aggressive evidenced by their willingness to split tenders and to conclude individual contracts with multiple suppliers. For example Standard Bank specifically reserves the right to show a supplier's pricing structure to a previously disadvantaged supplier in order to enable the latter to meet the quote of its competitors. Certain bidding processes have also been brought onto the internet. Shell, for example, places its tender documents on the internet and allows a period of open bidding in which the competing parties have access to the bid prices of their competitors and are able to enter new bids in an attempt to secure the company's business. The countervailing power of these large customers is exacerbated by their ability, in

the event of monopolistic conduct by their service provider, to handle their printing requirement in-house.

8. Public Interest

64. No significant public interest arguments were presented in respect of this transaction.

9. Conclusion and order

65. We have already noted that the identification of the relevant market has proved unusually complex in this case. While the evidence does not support the Commission's contention that the market for the 'bundled' product constitutes the relevant market, nor are we satisfied that the relevant markets are defined by a narrow identification of what appear to be discrete steps in the production of a final product be it a business form – with or without the addition of distinguishing 'bells and whistles' – or a directly mailed form. We have rather sought to identify the 'basic' business form or the 'basic' mailed product and to incorporate into those definition the incremental features that generally form part of those basic products without losing sight of the fact that these features may, and frequently are, added by separate, stand-alone firms.

66. On our tentative market definition market shares appear to remain reasonably high. - in 'business forms – continuous' this is so even on the parties lower estimate. However, there is evidence that small firms are able to thrive in this market and provide significant competition to the larger players, of significant installed excess capacity that will enable a rapid supply response in the face of anti-competitive conduct, and of considerable countervailing power. While we are skeptical of the imminence of the vaunted 'paperless office' clearly new technology is changing the face of this industry and will constrain the ability of the merged entity to raise price.

67. We have accordingly decided to approve the transaction unconditionally.

D. Lewis

16 January 2002

Date

Concurring: N. Manoim and M. Holden