COMPETITION TRIBUNAL OF SOUTH AFRICA

Case No: LM226Nov17

In the matter between

LEWIS STORES (PTY) LTD Acquiring Firm

And

UNITED OFFICE FURNITURE OUTLETS (PTY) LTD Target Firm

Panel	: Mr N Manoim (Presiding Member)
	: Mrs M Mokuena (Tribunal Member)
	: Mr AW Wessels (Tribunal Member)
Heard on	: 10 January 2018
Last submissions received	: 11 January 2018
Order Issued on	: 16 January 2018
Reasons Issued on	: 13 February 2018

REASONS FOR DECISION

Approval

[1] On 16 January 2018, the Competition Tribunal approved the large merger between Lewis Stores (Pty) Ltd ("Lewis") and United Furniture Outlets (Pty) Ltd ("UFO") subject to conditions placing a moratorium on merger specific job retrenchments for a period of two years from the implementation date of the transaction.

[2] The reasons for the conditional approval follow.

Parties to the transaction and their activities

Primary Acquiring Firm

[3] The primary acquiring firm is Lewis, a wholly owned entity of Lewis Group Limited ("Lewis Group"), a public company listed on the Johannesburg Securities Exchange.

[4] Lewis Group is a furniture, appliance and electronics retailer focused on the lower-middle income markets in rural areas across South Africa. It conducts its business through three trading brands, namely Lewis, Best Home and Electric, and Beares. Sales at stores in the Lewis Group are predominantly facilitated by in-house credit facilities, with further support provided by the Lewis Group's financial services arm.

Primary Target Firm

[5] UFO is furniture store with a retail footprint of 30 stores in primarily urban areas.[1] UFO sells a variety of luxury brand furniture with a value offering to the upper consumer spectrum. Unlike stores in the Lewis Group its sales are cash based.

Proposed transaction and rationale

[6] Lewis will acquire the entire shareholding in UFO, with UFO becoming a wholly owned and controlled entity of Lewis post-transaction.

[7] The merging parties submitted that post-transaction, Lewis intends to operate UFO as a separate business under UFO's current business model.

[8] In terms of rationale, Lewis submits that the proposed transaction will enable it to achieve improved economies of scale and provide a platform to penetrate

[1] UFO is presently controlled by the Martini Enterprise Group Ltd. It does not control any other store.

new market sectors through a wider, more exclusive product range. In addition, Lewis stores is of the view that the proposed transaction will diversify its offering by increasing its cash-to-credit sale ratio.

[9] The Commission reviewed Lewis' presented rationale. It found that approximately 60% of Lewis' sales are credit sales whilst 100% of UFO's sales are cash based, further that approximately 60% of Lewis' stores are situated in rural areas or towns whilst UFO is based in primarily urban, affluent areas.

[10] Noting the growing regulatory requirements on credit sales and a slow-down in sales volumes presented by Lewis, the Commission concluded that the merger is most likely driven by a desire of Lewis to diversify its offering and increase its cash-to-credit sales ratio.

[11] UFO submits that its shareholders have exceeded their investment maturity and wish to divest their shares.

Relevant market and impact on competition

[12] The Commission indicates in its report that the proposed transaction raises a horizontal overlap between the activities of the merging parties in respect of the retail of household furniture. The Commission assessed the merger by analysing the national market for the retail of furniture across all LSM brackets.

[13] The Commission indicated that the post-merger entity would command approximately 15% of the national market for the retail of furniture, with an accretion of no more than 2%. It concluded that given the presence of a number of strong competitors in the market, the merger would be unlikely to result in a substantial lessening or prevention of competition in the national market. Although the Commission noted that the two firms targeted different LSM brackets it did not find this necessary to analyse the merger.

[14] The Commission also analysed the narrower regional markets, finding that even on this basis the merger would not result in if the a substantial prevention

or lessening of competition in any relevant market as sufficient competitors remained to constrain the merged firm..

[15] We find no reason to differ from the Commission's findings.

Public interest

Historic retrenchments in Lewis

[16] In submissions to the Commission, the merging parties indicated that the proposed transaction would not have any adverse effects on employment, as no retrenchments are envisioned as a result of the proposed transaction.

[17] During its assessment of the transaction, the Commission received a notice of intention to participate from the South African Commercial Catering and Allied Workers Union ("SACCAWU"). SACCAWU raised a concern that Lewis had undertaken various retrenchments in the year prior to the merger in preparation for the proposed merger.[2] Its theory was that the retrenchments formed part of a concerted effort to save costs in order to facilitate the purchase of UFO. SACCAWU raised a further concern that the retrenched employees were those in categories who would not find employment in UFO's company structure post-transaction.[3]

[18] The Commission engaged with the merging parties on SACCAWU's concerns and in response the merging parties submitted that the retrenchment processes were embarked upon due to unfavourable trading conditions in the market which informed a restructuring its business.

[19] On the merging parties' submissions, the retrenchments took place in four tranches, beginning in December 2016 and continuing up until the October 2017.

[2] These concerns were raised in correspondence with the Commission dated 22 and 29 November 2017 found at pages 721-726 of the merger record.
[3] Letter from SACCAWU to the Commission dates 29 November 2017, para 6. Merger record page 725.

[20] The merging parties submitted that the first tranche of retrenchments affected drivers and porters and was motivated by the overlap in functions of the two categories.

[21] February 2017 saw the initiation of the second tranche of retrenchments which affected a number of general positions but were as the result of store closures in areas hard hit by the slowing economic climate and protracted drought.

[22] The third tranche of retrenchments in May 2017 up until September 2017 were comprised of debtor follow up clerks and collectors and was motivated by reduced credit approvals owing to stricter credit regulations.

[23] The fourth tranche of retrenchments in October 2017, affected number of general positions and were as a result of a number of factors which meant that Lewis' staffing model was no longer sustainable.

[24] The Commission assessed the merging parties' submissions. It held that the rationale provided for each tranche of retrenchments aligned with Lewis' slowed performance and it was thus unlikely that the retrenchments were related to the merger and more likely that they were related to the unsustainability of Lewis' employment model as submitted.[4]

[25] SACCAWU however persisted with its theory at the merging hearing. Mr Ngoato of SACCAWU submitted:

> *...Lewis did not just wake up and say tomorrow we want to buy or acquire UFO. It is a plan, and part of that plan for a period of two years employees were retrenched, which, we submit, that it was a cost saving, a plan, an exercise to ensure that they acquired UFO*[5]

[26] Addressing Mr Ngoato's submissions required an assessment of the timeline along which the merger was contemplated against the timeline along which the retrenchments took place.

[4] Competition Commission Recommendations, page 30, para 68.
[5] Transcript of Proceedings before the Competition Tribunal 10 January 2018Transcript, page 14, line 204.

[27] The merging parties were unable to, at the merger hearing, provide a detailed timeline as to when the merger was considered. What was apparent however were that sale negotiations were initiated by UFO.[6] This factor on its own is sufficient to address SACCAWU's theory, in that the acquiring firm could not have been held to be shedding jobs in preparation for a merging it did not seek to initiate.

[28] However, to address the issue of timelines more fully, the Tribunal stood the matter down to allow the filing of an affidavit deposed to by the CEO of Lewis, Mr Johan Enslin ("Enslin").

[29] Enslin submitted that he was approached by Mr Wayne Brett of UFO on or about 3 May 2017 to discuss the potential acquisition of UFO by Lewis Stores and that the discussion comprised a high level, in principle, explanatory discussion.

[30] On this timeline, it becomes apparent that the first and second tranches of retrenchments were initiated prior to the consideration of the merger and could not be considered merger specific.

[31] With regard to the third tranche of retrenchments, Enslin indicates in his affidavit that whilst the retrenchments began in May, such were initially contemplated in April 2017 when Lewis assessed its shrinking debtor book post the 2017 financial year. This then addresses the third tranche of retrenchments in the same manner as the first and second.

[32] This leaves only the fourth tranche of retrenchments. Enslin indicates in his affidavit that the retrenchments initiated in October 2017 were first contemplated in June 2017. An affidavit deposed by Rinus Oliphant, the operations director of Lewis charged with the retrenchment processes confirms this fact. In terms of the timeline, it is thus conceivable that upon ordering the fourth tranche of retrenchments, the Lewis corporate structure was aware of the potential merger with UFO. Does this however mean that such retrenchments were merger specific? We say not.

[6] Tribunal Transcript, page 19, line 285.

[33] An Excel document submitted with Oliphant's affidavit, when read with Oliphant's account points to a process whereby potential retrenchments were guided by the profitability of certain stores.[7]

[34] It thus seems that on a balance of probabilities the retrenchment process was carefully considered in relation to a set of criteria divorced from the potential merger proceedings contemplated at the time. We are thus satisfied that the retrenchments were not merger related.

Employment condition

[35] In assessing the future impact of the merger on employment, the Commission was concerned with the possible integration of the business models of the merging parties.

[36] The merging parties indicated that although the final decision on the matter had not yet been made, Lewis intends to operate UFO as a separate business under UFO's current business model and it seeks to retain the use of UFO's head office, warehouses and entire staff compliment. In addition, Lewis intends to continue honouring any outsourcing contracts entered into pre-merger by UFO without any change.

[37] The Commission noted that in spite of the submissions made by the merging parties, there was a possibility that an integration of the two firms would take place, resulting in the loss of at least 15 jobs. The merging parties, tendered to escalate their undertaking given in their merger filing to a condition placing a moratorium on merger specific job losses for a period of two years post the transaction.[8] The Commission accepted.

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[7] Excel Spreadsheet submitted by the merging parties on 11 January 2018 titled "Total Group New Complement & Reductions - July 2017".

[8] Letter from the Merging parties to the Commission 20 November 2017, merger record page 670, para 16.

[38] We find no reasons to dispute the imposition of the condition tendered by the merging parties and accepted by the Commission in the circumstance in which it is not certain whether the parties would integrate business post-merger.

Conclusion

[39] In light of the above, we conclude that the proposed transaction is unlikely to substantially prevent or lessen competition in any relevant market.

[40] Although the acquiring firm undertook a series of retrenchments prior to the transaction taking place, on a balance of probabilities we do not consider such to be merger specific.

[41] The Commission expressed a concern relating to the impact of the merger should the merging parties wish to integrate the businesses. To allay this concern, the merging parties tendered an employment condition which the Commission has accepted. We thus conclude that the potential public interest effects arising from this matter are addressed by the conditions imposed.

[42] We thus approve the merger subject to the conditions attached to our order.

Mr Norman Manoim — **13 February 2018**, **Date**

Mrs Medi Mokuena and Mr AW Wessels concurring

Tribunal Researcher:	Alistair Dey-van Heerden
For the merging parties:	Lizél Blignaut of ENSAfrica
For the Commission:	Mogau Aphane
For SACCAWU:	Piet Ngoatao, Khulekani Ngubane (Union officials) and Henry Thabethe (Shop steward)