COMPETITION COMMISSION

INQUIRY INTO THE ACQUISITION BY SPORTS DIRECT INTERNATIONAL PLC OF 31 STORES FROM JJB SPORTS PLC

Provisional findings report

Published: 11 February 2010

The Competition Commission has excluded from this published version of the provisional findings report information which the inquiry group considers should be excluded having regard to the three considerations set out in section 244 of the Enterprise Act 2002 (specified information: considerations relevant to disclosure). The omissions are indicated by [✂]. Some numbers have been replaced by a range. These are shown in square brackets.

Summary

1. On 7 August 2009, the Office of Fair Trading (OFT) referred the completed acquisition of 31 JJB Sports plc (JJB) stores by Sports Direct International plc (Sports Direct) to the Competition Commission (CC) for investigation and report. The reference was made under section 22(1) of the Enterprise Act 2002 (the Act) and requires us to determine whether a relevant merger situation has been created; and, if so, whether the creation of that situation has resulted in or may be expected to result in a substantial lessening of competition (SLC) within any market or markets in the UK for goods or services.

2. Following an extension of the original 24-week inquiry period under section 39(4) of the Act, we were required to publish our final report by 24 February 2010. Following a further extension under section 39(3) of the Act, we are now required to publish our final report by 21 April 2010.

3. Sports Direct was founded in 1982 by Mike Ashley and, as of August 2009, operated 363 stores in the UK. JJB was founded in 1971 by David Whelan and, as of July 2009, operated 251 stores in the UK. Both JJB and Sports Direct are active in the retail supply of sporting and leisure clothing, equipment and footwear. In addition to its retail activities, Sports Direct owns a number of brands under which it licenses and sells products. In 2008, the retailing of sports clothing and footwear in the UK was worth an estimated £4.5 billion.

4. The transaction comprised the completed transfer of 31 stores from JJB to Sports Direct over a period between November 2007 and December 2008. Following the transfer, both JJB and Sports Direct continued to operate.

5. We considered what was likely to have happened in the absence of the store transfers (ie the ‘counterfactual’), which provided a benchmark against which we assessed the effects of the transaction. We found that JJB would probably have closed ten of the 31 stores in any event, but the remainder would have remained in JJB’s portfolio. We judged that Sports Direct would probably have sought to acquire new stores in all of the locations where it in fact acquired JJB stores, if sites had become available, but we could not predict if it would have been successful or state with confidence where any such new stores would have been located. We also judged that, of the ten Sports Direct stores which were located near to acquired JJB stores and which Sports Direct closed during the period of the store transfers, five would have closed in any event.

6. We considered the definition of the relevant markets. We found that customers considered JJB and Sports Direct to be each other’s closest competitors and that diversion ratios from Sports Direct to JJB were far higher than to other retailers. We found evidence that the entry of a new JJB store had a strong effect on a Sports Direct store, even where other retailers were already present, while entry by other retailers had only a weak effect. We found evidence that the effect of entry by JJB was consistent across the products offered by both retailers, which suggested that the product market was wider than individual products. Further, few of the respondents in our customer survey named specialist retailers as an alternative to Sports Direct, which might be expected if customers were generally shopping for specific products. Therefore, we concluded provisionally that the product market included only Sports Direct and JJB. Nevertheless, we recognized that several retailers outside this market were likely to provide some competitive constraint on the parties, albeit weaker than the parties imposed on each other.

7. We found that the geographic market was local. We found that Internet sales did not constitute a significant proportion of sports goods sales and our survey indicated that customer substitution between Sports Direct, JJB and online retailers was relatively limited. We concluded provisionally that the market was no wider than a 2- to 5-mile radius around any given store, and did not include the Internet.

8. We considered whether a new entrant could replace any competition lost by the transfer of 31 JJB stores to Sports Direct. To provide a competitive constraint, a new entrant must be able to provide similar products at similar prices to Sports Direct and JJB. Sports Direct and JJB offer low prices due to the discounts they obtain from their suppliers (in particular Nike and Adidas), which are linked to sales volumes. These volumes are such that entry would need to be on a large scale and at significant cost. We did not identify any large retailers which had the intention of entering on such a scale and we judged that smaller retailers and direct retailers (eg Internet retailers) were unlikely to increase significantly the extent of their constraint on the parties. We recognized that JJB could open new stores in areas where it was not currently competing with Sports Direct, but we judged that significant store expansion by JJB was unlikely to occur in the near term.

9. We analysed the effects of the store transfers on competition. We noted that JJB remained a strong national competitive force and continued as a competitive constraint. We considered whether the store transfers had caused or were likely to cause any worsening in price, quality, range or service (PQRS) at the local or national levels, or whether it had caused or was likely to lead to store closures (possibly harming consumers through increased travel times).

10. We found that Sports Direct varied several non-price factors (QRS) at a local level, even between similar stores. However, we found no differences caused by the

strength of local competition. Similarly, while we found some evidence of a rise in average prices after the store transfers, it was unclear that this rise was associated with the store transfers. We conducted an analysis of profit margins at a local level, but we were unable to identify any variation linked to the strength of local competition.

11. We considered whether the store transfers changed the incentives for Sports Direct to adjust its local PQRS offering. Given the substantial number of areas where Sports Direct faced no local competition from JJB before the store transfers (24 per cent of Sports Direct's stores) and the relatively small change in this number as a result of the store transfers (an increase to 33 per cent at most), we did not consider it likely that Sports Direct's incentives had changed significantly.

12. We conducted a critical loss analysis, which indicated that the store transfers had created an incentive for Sports Direct to increase its national prices by a very small amount (less than one per cent). However, there was some uncertainty surrounding our estimates. We also noted that JJB remained in the market and, over the longer term, was likely to be able to expand into areas where it was not currently competing with Sports Direct (see paragraph 8). For all these reasons, we concluded that it was unlikely that, as a result of the store transfers, Sports Direct would increase its prices significantly.

13. Following the store transfers, Sports Direct closed ten of its stores within a 5-mile radius of an acquired JJB store. We judged that five of these stores would not have closed absent the store transfers (see paragraph 5). However, we found that these five closures had resulted in little effect on consumers given the proximity of remaining stores to the stores which had been closed.

14. We found no compelling evidence that the store transfers would increase the likelihood of tacit coordination. Due to historic reasons, Sports Direct and JJB are disproportionately prevalent in different parts of the UK. We found some evidence that the store transfers changed the number of areas of relative strength, particularly in Greater London. However, we found that JJB's 2008 store closure programme and the sale of some of its stores to DW Sports Fitness were more significant in increasing any observed geographic segmentation than the transfer of the 31 stores to Sports Direct. Even in London, Sports Direct would have had twice as many stores as JJB without the store transfers. Furthermore, recent store openings by Sports Direct and JJB did not indicate any coordination. Therefore, we found that the store transfers were unlikely to lead to any coordinated effects.

15. We concluded provisionally that the acquisition of 31 stores by Sports Direct from JJB has not resulted, and may not be expected to result, in an SLC in any market in the UK.