ISBN No 978-1-869456-00-9

Statement of Preliminary Issues

Essilor International and Luxottica Group

2 August 2017

Introduction

1. On 10 July 2017, the Commerce Commission registered an application seeking clearance for the global merger of Essilor International (Compagnie Generale d'Optique) S.A. (Essilor) and Luxottica Group S.p.A (Luxottica) (the proposed merger).

2. The Commission will give clearance if it is satisfied that the proposed merger will not have, or is not likely to have, the effect of substantially lessening competition in a market in New Zealand.

3. This statement of preliminary issues outlines the competition issues we currently consider to be important in deciding whether or not to grant clearance.[1]

4. We invite interested parties to provide comments on the likely competitive effects of the proposed merger. We request that parties who wish to make a submission do so by **16 August 2017**.

The parties

5. Essilor is a global manufacturer and wholesale supplier of ophthalmic lenses used by consumers to correct visual impairments. In New Zealand, Essilor is principally active in the wholesale supply of finished prescription lenses to optical retailers, although Essilor is also active in the retail market to via its online store, clearly.co.nz.

6. Luxottica is a global manufacturer and wholesale supplier of prescription frames and sunglasses. In New Zealand, Luxottica's activities are limited to the wholesale supply of prescription frames and sunglasses, and the retail of optical products and services (via its OPSM, Sunglass Hut and Oakley stores).

7. Essilor and Luxottica already have a commercial relationship. Essilor supplies finished prescription lenses to Luxottica, which Luxottica then on-supplies to consumers as complete prescription glasses. Luxottica exclusively sources its lenses from Essilor pursuant to joint venture and supply agreement between the parties. Essilor supplies lenses to Luxottica and other optical retailers.

8. Essilor and Luxottica propose to merge their businesses globally.[2] The proposed merger brings together a supplier of prescription lenses (Essilor) with a supplier of prescription frames and sunglasses (Luxottica).

---

1 The issues set out in this statement are based on the information available at the time of publication. They are not binding on us, and may change as our investigation progresses.

Our framework

9. Our approach to analysing the competition effects of the proposed merger is based on the principles set out in our Mergers and Acquisitions Guidelines.[3] As required by the Commerce Act 1986, we assess mergers using the substantial lessening of competition test.

10. We determine whether a merger is likely to substantially lessen competition in a market by comparing the likely state of competition if the merger proceeds (the scenario with the merger, often referred to as the factual), with the likely state of competition if the merger does not proceed (the scenario without the merger, often referred to as the counterfactual).[4]

11. We define markets in the way that we consider best isolates the key competition issues that arise from the merger. In many cases this may not require us to precisely define the boundaries of a market. A relevant market is ultimately determined, in the words of the Commerce Act, as a matter of fact and commercial common sense.[5]

12. We compare the extent of competition in each relevant market both with and without the merger. This allows us to assess the degree by which the proposed merger might lessen competition. If the lessening is likely to be substantial, we will not give clearance to the proposed merger. When making that assessment, we consider, among other matters:

    12.1 constraint from existing competitors – the degree to which existing competitors currently compete and the extent to which they would expand their sales if prices were increased;

    12.2 constraint from potential new entry – the extent to which new competitors would enter the market and compete effectively if prices were increased; and

    12.3 the countervailing market power of buyers – the potential for a business to be sufficiently constrained by a buyer's ability to exert substantial influence on negotiations.[6]

Market definition

13. In their application, Essilor and Luxottica submitted that the relevant markets for assessing the proposed merger are national markets for:[7]

---

2 The proposed merger was announced publically on 16 January 2017. Implementation of the proposed merger is subject to regulatory approval in a number of jurisdictions.

3 Commerce Commission, *Mergers and Acquisitions Guidelines*, July 2013. Available on our website at www.comcom.govt.nz

4 *Commerce Commission v Woolworths Limited* (2008) 12 TCLR 194 (CA) at [63].

5 Section 3(1A). See also *Brambles v Commerce Commission* (2003) 10 TCLR 868 at [81].

6 Countervailing power is more than a customer's ability to switch from buying products from the merged entity to buying products from a competitor. Similarly, a customer's size and commercial importance is not sufficient in itself to amount to countervailing power.

7 Application at [126].

13.1 the retail supply of optical products and services (including prescription glasses, contact lenses and sunglasses); and

13.2 the wholesale supply of finished prescription lenses.

14. As part of our investigation, we will consider whether these are the only relevant product markets or whether there may be other affected product markets (for example, a narrower market at the retail level for the retail supply of finished prescription lenses and frames). We will also consider whether there may be other affected functional markets within the relevant supply chain (for example, separate functional markets relating to lens manufacturing, lens importation and lens processing/finishing).

Preliminary issues

15. We will investigate whether the proposed merger is likely to substantially lessen competition in the relevant markets by looking at the unilateral, vertical and conglomerate effects that might result from the merger. The questions that we will be focusing on are:

15.1 unilateral effects: would the merged entity be able to raise prices or reduce quality by itself?

15.2 vertical and conglomerate effects: would the merged entity be able to engage in behaviour that either forecloses rivals or otherwise renders them less able to compete?

Unilateral effects: would the merged entity be able to raise prices by itself?

16. Where two suppliers compete in the same market, a merger could remove a competitor that would otherwise provide a competitive constraint, allowing the merged entity to raise prices. A merger could also reduce competition if the target was a potential or emerging competitor. In such a case, a merger could result in higher prices compared to the scenario without the merger.[8]

17. In their application, Essilor and Luxottica submitted that there is no or limited horizontal overlap between them in the relevant markets, because:

17.1 Essilor is not a genuine competitor in the wholesale supply of prescription frames;[9]

17.2 while Luxottica holds a 30% share in Eyebiz (a joint venture with Essilor), it is not active in the wholesale supply of finished prescription lenses;[10] and

17.3 Essilor is active only to a very limited extent in the retail supply of optical products and services through its online store clearly.co.nz.[11]

---

8 Commerce Commission, *Mergers and Acquisitions Guidelines*, July 2013 at [3.62-3.63].

9 Application at [132.3].

10 Ibid at [135].

18. Although there may be limited horizontal overlap between Essilor and Luxottica, we will consider whether the parties would become more meaningful competitors without the merger. For example, we will consider whether, without the merger, either party might start to compete directly with the other. If such expansion would be likely without the merger, then any potential competitive constraint from this would be lost as a result of the proposed merger. This could result in higher prices or decreased service levels relative to the without the merger scenario.

19. To assess whether the loss of potential competition is likely to be material, we will consider:

    19.1 whether Essilor or Luxottica would be likely, without the merger, to launch any products or services that would be in competition with one another;

    19.2 whether existing competition in the markets in which any new Essilor or Luxottica services would be launched without the merger is currently weak (such that potential competition would impose an important constraint); and

    19.3 whether Essilor or Luxottica are uniquely positioned to be the potential entrant that would impose constraint on incumbents in the relevant markets without the merger.

20. We note that many of the factors mentioned above are also relevant to vertical and conglomerate effects, which we discuss below.

Vertical and conglomerate effects: would the merged entity be able to foreclose rivals?

21. A merger between suppliers who are not direct competitors and operate in related markets is less likely to result in unilateral effects. However, such a merger can result in a substantial lessening of competition due to vertical or conglomerate effects. This can occur where a merger gives the merged entity a greater ability or incentive to engage in conduct that prevents or hinders rivals from competing effectively.[12] [13]

    21.1 A vertical merger is a merger between firms operating at different levels of a supply chain (eg, a wholesaler and a retailer). Vertical mergers can increase a merged entity's ability or incentive to foreclose its competitors. Foreclosure can either be:

        21.1.1 input foreclosure – where the merged entity refuses to supply an input to a downstream competitor or raises the price of the input; or

        21.1.2 customer foreclosure – where the merged entity disadvantages an upstream competitor in the sale of that competitor's products by limiting access to customers.

---

11 Ibid at [162].

12 Commerce Commission, *Mergers and Acquisitions Guidelines*, July 2013 at [5.2].

13 When we refer to foreclosure, this includes behavior that either forecloses rivals or otherwise renders a competitor less competitively effective.

21.2 A conglomerate merger is a merger between firms that supply products that may relate to each other (eg, complementary products). Foreclosure can arise in the case of conglomerate mergers due to:

21.2.1 bundling – where the merged entity provides bundled discounts to customers that buy the merging parties' products together rather than separately; or

21.2.2 tying – where the merged entity refuses to sell one of the merging parties' products unless customers also buy the other party's product.

22. In their application, Essilor and Luxottica submitted that there is no realistic prospect of input or customer foreclosure because:[14]

22.1 Essilor has no ability to foreclose optical retailers from obtaining supplies of finished prescription lenses, who have a range of alternative suppliers available to them and have substantial countervailing buyer power; and

22.2 Luxottica's demand for finished prescription lenses is not so significant that (even if its demand was to become contestable, which is not currently the case) foreclosing access to Luxottica would affect the competitive viability of competing lens wholesalers.

23. The proposed merger brings together a supplier of prescription lenses (Essilor) with a supplier of prescription frames and sunglasses (Luxottica). As the parties themselves stated when they announced the proposed merger, the merger will create a global integrated player in the eyewear industry.[15] The proposed merger potentially raises both vertical and conglomerate effects.

24. We will consider whether the proposed merger would give the merged entity the ability and incentive to engage in behaviour that might foreclose rivals in the relevant markets or otherwise render them less competitively effective and result in a substantial lessening of competition in a relevant market.

Next steps in our investigation

25. The Commission is currently scheduled to make a decision on whether or not to give clearance to the merger by **6 September 2017**. This date may change as the investigation progresses.[16] In particular, if we need to consider the issues identified above further, the decision date is likely to extend.

26. As part of our investigation, we will be identifying and contacting parties we consider will be able to help us assess the preliminary issues identified above.

---

[14] Application at 2-3.

[15] Essilor and Luxottica media release (16 January 2017).

[16] The Commission maintains a clearance register on our website where we update any changes to our deadlines and provide relevant documents: http://www.comcom.govt.nz/clearances-register/

Making a submission

27. If you wish to make a submission on this merger, please send it to us at registrar@comcom.govt.nz with the reference "Essilor/Luxottica" in the subject line, or by mail to The Registrar, PO Box 2351, Wellington 6140. Please do so by close of business on **16 August 2017.**

28. Please clearly identify any confidential information contained in your submission and provide both a confidential and a public version. We will be publishing the public versions of all submissions on the Commission's website.

29. All information we receive is subject to the Official Information Act 1982 (OIA), under which there is a principle of availability. We recognise, however, that there may be good reason to withhold certain information contained in a submission under the OIA. For example, if disclosure would unreasonably prejudice the supplier or subject of the information. In assessing the confidentiality of information contained in submissions for the purposes of publication on our website, we intend to apply an approach that is consistent with the OIA.