

**Neopost SA
and
Ascom Holding AG**

A report on the proposed merger



COMPETITION COMMISSION

Neopost SA and Ascom Holding AG

A report on the proposed merger

**Presented to Parliament by the Secretary of State for
Trade and Industry by Command of Her Majesty
May 2002**

Members of the Competition Commission as at 24 April 2002


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Note by the Department of Trade and Industry

In accordance with section 83(3) and (3A) of the Fair Trading Act 1973, the Secretary of State has excluded from the copies of the report, as laid before Parliament and as published, certain matters, publication of which appears to the Secretary of State to be against the public interest, or which she considers would not be in the public interest to disclose and which, in her opinion, would seriously and prejudicially affect certain interests.

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Part I

Summary and Conclusions

1 Summary

1.1. We were asked to report on the acquisition by Neopost SA (Neopost), a French listed company, of Ascom Mailing Systems (AMS), which is currently owned by the Swiss company Ascom Holding AG (Ascom): see Appendix 1.1 for our terms of reference.

1.2. Neopost was created by a management buyout from Alcatel SA in 1992. It specializes in mailing equipment. In its financial year to 31 January 2002 it reported a consolidated turnover of €575 million (£357 million) and net income of €38 million (£24 million).

1.3. Ascom is a diversified group with interests in telecommunications networks, transport ticketing and power supply systems, as well as mailing equipment. In 2001, its consolidated turnover was CHF 3,143 million (£1,293 million), and it reported a net loss after exceptionals of CHF 396 million (£163 million). In 2000, AMS generated turnover of CHF 282 million (£110 million), of which 12 per cent was accounted for by its operations in the UK.

1.4. In August 2000, Ascom decided that AMS was not a core activity for the group and should be divested. Various possibilities for merging AMS with Francotyp Postalia AG & Co (Francotyp), a German mailing equipment company, were explored but these came to nothing, and in July 2001 Ascom initiated a private auction with a view to selling AMS. The highest indicative offer was made by a financial bidder interested in putting together a buyout with AMS's management team, with Neopost's offer the second highest. For several reasons, however, Ascom preferred the Neopost offer, and on 2 October 2001 the two companies signed an agreement for the sale of AMS to Neopost for €240 million (£149 million).

1.5. Ascom's original decision to divest AMS was taken for strategic reasons, but the group has subsequently got into financial difficulty and now has an urgent need to realize cash. On 28 February 2002, Ascom, having earlier received clearance from the US anti-trust authorities, sold to Neopost the distribution business of AMS in North America for a sum equivalent to [§] per cent of the total consideration which Ascom expects for AMS as a whole.

1.6. In order to establish the effects of the merger, we have to consider what would have been likely to happen if Neopost had not agreed to acquire AMS. We see two possibilities: that AMS would have merged with another franking machine manufacturer (probably Francotyp), and that AMS would have been acquired by someone from outside the franking machine industry.

1.7. The operations of Neopost and AMS overlap in the supply of certain categories of mailroom equipment. We determined that the markets principally affected are the UK market for franking machines, including after-sales service and certain related products, in which total annual sales are around £[§] million; and a worldwide market for folding and inserting machines valued at up to £21,000, including maintenance and repair services (UK sales of these machines in 2001 were worth some £[§] million).

1.8. In the UK franking machine market Neopost achieved 26 per cent of sales in 2001 and AMS 10 per cent. The market leader, the US company Pitney Bowes Inc (Pitney Bowes), had

52 per cent, and there were two other suppliers, Francotyp with 6 per cent and Frama with 4.5 per cent. The merger has three structural consequences for this market:

- (a) it reduces the number of suppliers from five to four and removes AMS as an independent source of competition;
- (b) it creates a market structure in which the top two suppliers will have over 85 per cent of this market between them; and
- (c) it strengthens the position of the number two supplier, Neopost, in relation to the market leader.

1.9. In relation to (a) we found that, while AMS has been and, to some extent, remains a beneficial force for competition in the UK franking machine market, it will be a declining force unless it merges with another franking machine supplier. In relation to (b), the prospects are that, at global level, the new market structure may be more competitive than the alternative possibilities. It does not necessarily follow, however, that this would be translated into behaviour in the UK market, where the two companies' positions are more symmetrical than elsewhere. (Globally, Pitney Bowes will still be two and a half times the size of the merged Neopost/AMS.) In the short run, we believe Neopost will have to compete on price because it lags behind Pitney Bowes in product development. In the longer term, we see some risk that the two companies would refrain from competing vigorously on price in the UK market. As regards (c), the merger would create a stronger global competitor to Pitney Bowes, which currently dominates the supply of franking machines worldwide and has great technological strength through an extensive portfolio of patents. The UK would be likely to benefit from the resulting effect on product development, and there might be a wider benefit from increased competition in the licensing of technology to smaller suppliers.

1.10. On balance, we do not expect the merger to lead to a significant reduction in competition in the supply of franking machines and related services.

1.11. In the supply of smaller folding and inserting machines in the UK, Neopost had 48 per cent of sales in 2001 and AMS 3 per cent. Worldwide their shares were 56 per cent and 2 per cent respectively. AMS does not manufacture folders/inserters, however, but sells machines sourced from PFE International Ltd (PFE) under its own name. PFE submitted that the merger would considerably harm its position, both in the UK and globally, because of the relationship it had built up with AMS affecting the distribution of its products. In our view, however, PFE has exaggerated the merger's effects in this regard and we find that the merger will not significantly lessen competition in the folders/inserters market.

1.12. We conclude that the merger may not be expected to operate against the public interest.

1.13. The supply of franking machines is a relatively small, niche market in which the supply side is highly concentrated and the demand side highly fragmented. There is a risk, stemming from the inherent characteristics of the market and not from the merger, that competition among suppliers will be muted. The market is currently undergoing a period of change because of the switch to digital technology and the liberalization of the postal services market. In these circumstances we propose that the Director General of Fair Trading should review the operation of the market within three to five years.