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Jos. A. Bank/Men's Wearhouse: According to Sources, FTC Focused on Promotional Strategy Incentives, Conducting Ongoing Investigational Hearings; Parties Request for a "Quick Look" Creates Substantial Timing Uncertainty

Conclusion

On March 11, 2014, Men's Wearhouse Inc. announced an agreement to acquire Jos. A. Bank Clothiers Inc., in a deal valued at about $1.8 billion. Multiple sources with familiarity of the deal have confirmed that Melissa Davenport of Mergers IV is leading the FTC's review, while Alexis Gilman is the Deputy Assistant Director in charge of the deal. During this week and next, the FTC is conducting investigational hearings with executives from both companies.

The Capitol Forum has also learned that the parties likely requested, and have already complied with, a truncated "quick look" alternative to the second request process. Under a quick look, the parties initially submit a limited subset of requested documents instead of substantially complying with the entire second request. If the FTC is satisfied, it will grant an early termination and close the investigation; if not, the parties must substantially comply with the entire second request. The FTC is primarily focused on establishing the impact that the merger would have on promotional practices (i.e., the combined firm's incentive to discontinue aggressive promotions).

Key points for stakeholders to consider include:

- **The parties' quick look request creates substantial timing uncertainty.** While the purpose of the quick look strategy is typically to speed up review, if the strategy backfires, it can have the opposite effect and create significant delays instead. Moreover, the FTC is more likely to be satisfied by a quick look review when the Commission, instead of the parties (as appears to be the case here), initiates the quick look request.

- **FTC's effects-focused quick look investigation likely to hone in on BOGOs and television advertising**. The FTC's focus on establishing the impact the merger would have on promotional practices means that the parties' buy-one get-one strategies (BOGO) and unique television advertising strategies would likely be featured in either a possible complaint or closing statement. To satisfy the FTC, the parties' quick look documents would likely need to show that the parties do not consider each other's pricing/promotions more of a constraint than those of other competitors.

- **FTC's inquiry into product market definition likely to take place after quick look phase, if investigation is not terminated.** If the FTC determines that the parties' evidence regarding promotional practices does not warrant closing the investigation, the parties must substantially comply with the second request. During that phase, the FTC would explore whether it can effectively plead a narrow product market consisting only of the merging parties. However, existing competition from department stores (as discussed in the FTC's Federated/May decision) might be an obstacle to an FTC challenge.

Key Points

A quick look at quick look reveals greater timing uncertainty than traditional second requests. If the FTC determines, upon a quick look, that the merger will not result in competitive harm, it will provide the parties with written notice that will allow them to immediately consummate the merger. On February 19, 2014, Men's Wearhouse entered into an agreement with the FTC modifying the scope of the Second Request, pursuant to which, among other things, Men's Wearhouse agreed that it would not consummate the acquisition of Jos. A. Bank until the earlier of (i) 30 days following substantial compliance with the Second Request or (ii) written notice from the FTC closing the investigation.

The ABA's Merger Review Process treatise provides a detailed description of how a quick look might operate: "Counsel for the parties and the agency reach an agreement identifying specific issue(s) that appear to be dispositive of the competitive concerns raise by the transaction, such as product/geographic market or entry. Although the full second request remains outstanding, the parties initially assemble documents and data only on the dispositive issues; responses to the remainder of the second request are held in abeyance."

Further, the treatise explains that a quick look is only appropriate in certain situations: "Only transactions in which one or two key issues can be isolated are effectively within the scope of a quick look review. … The issue most commonly examined under the quick look process has been ease of entry. Entry lends itself to a quick look, because it is a discrete issue that can be dispositive of the competitive analysis under the Horizontal Merger Guidelines and because information on entry often is readily available. Other potentially dispositive issues scrutinized under the quick look approach include product and geographic market definition, supply side substitution and the role of foreign producers. Some issues are rarely handled by the quick look procedure. For example, the likelihood of anticompetitive coordinated behavior among competitors after consummation of the transaction is simply too complex for quick look review in most cases."

Although the quick look review could hasten the deal's close, it could also backfire, resulting in a significantly extended FTC review. According to the treatise: "the staff may resolve the agreed-upon issue against the parties or conclude, in the end, that the issue was not entirely dispositive. In either of these cases, staff will require a complete response to the second request. The result could be significant additional delay, the need to go back to the same client personnel for additional documents and greater expense than if substantial compliance were pursued from the outset. In addition . . . under the quick look procedure, the waiting period does not recommence; theoretically, the staff can take as much time as desired to review the documents produced pursuant to the quick look."

Notably, the FTC is more likely to be satisfied by a quick look review when the Commission, instead of the parties (as appears to be the case here), initiates the quick look request.

FTC's competitive effects concerns likely honing in on BOGO promotions and television advertising strategies during the quick look phase. The FTC's focus in the quick look stage appears to be on what the parties' internal documents say about how they formulate their promotional strategies, particularly with respect to each other.

In a January 15th article for Slate, Matthew Yglesias indicated that "[t]here are plenty of companies out there selling men's clothing, so there's no question of antitrust violations or monopolies here." This statement highlights an outdated view of merger analysis that many who are monitoring the merger mistakenly share. Instead, the quick look inquiry will be keenly interested in Mr. Yglesias's observation that "in an environment without other marketing-heavy national chains focused on menswear, the merged firms might be able to charge higher prices."

For many years, the agencies have been paying closer attention to mergers' practical competitive effects and have been allowing the evidence of those effects to dictate market definition, instead of trying to first prove that a narrowly defined market exists without the benefit of such evidence. Since the agencies revised the Horizontal Merger Guidelines in 2010 to reflect this approach, the courts have adopted the new language when ruling in the agencies' favor in three litigated merger challenges: *US v H&R Block*, *FTC v St. Luke's* and *US v Bazaarvoice*.

The first aspect of the parties' common marketing practices is their use of BOGOs to drive customers to the store as opposed to department stores, which usually discount directly. According to some sources, the BOGO strategy might appeal more to a male consumer because it addresses the consumer's desire for price and convenience. Siam-Paul Regis, a men's fashion reporter/consultant in New York who runs the men's fashion blog Swagger New York, describes the mentality of the Jos. A. Bank and Men's Wearhouse consumer as, "let me buy three suits, get in, get out, a half hour and [I'm] done."

One issue that will be informative in the FTC's review is the question of how far in advance the two companies plan their promotions. Both retailers tend to advertise their promotions, which take place over weekends, only during the few days leading up to the event. Sales clerks at both stores indicate that they only find out about the promotions 24 to 48 hours in advance. Internal documents from the parties may show that these are in fact last minute promotions that are strategically timed to stay ahead of the other party.

On the other hand, it is possible that the parties do not consider each other's pricing/promotions more of a constraint than those of other competitors. An industry expert who favors the deal points out that department stores also run BOGO promotions, and the BOGO promotions that Men's Wearhouse runs are very different than Jos. A. Bank's promotions. Jos. A. Bank controls the retail price of its suits, which allows the company to mark up its prices and then offer buy one get two or three free promotions. Men's Wearhouse, however, cannot offer this type of "discount," because Men's Wearhouse carries brand name apparel instead of house label apparel. Consequently, Men's Wearhouse cannot realistically mark up the retail price of a particular suit to an amount substantially higher than the level at which the same suit is priced in department stores.

Perhaps the most important part of the BOGO promotions is how they are advertised. The television advertising campaigns that Men's Wearhouse and Jos. A. Bank run are unique, as most fashion companies do not advertise to men on television at all. According to Michael Williams, who runs a marketing agency, Paul & Williams, as well as the men's fashion blog A Continuous Lean: "A lot of these [fashion] companies don't have massive budgets to market." According to Mr. Williams, it makes sense for consumer packaged good companies like Gillette to invest heavily in advertising because the products do not change from year to year, while most fashion companies are constantly changing their product mix to keep up with trends. Fashion forward consumers, meanwhile, tend to seek out information in magazines or blogs. As Mr. Regis explained, "The Jos. A. Bank and Men's Wearhouse consumers are probably not going to the fashion blogs to find out the latest and hottest new things."

It makes sense for Men's Wearhouse and Jos. A. Bank to heavily invest in television advertising, because their consumers are less concerned with trends or self-expression, but rather more pragmatic factors like price and convenience. "It's probably cost effective to get numbers that way," Mr. Williams explained, "they don't want people that read magazines because they are not going after the connoisseur and it's harder to get critical mass."

Targeting men through television advertising commands a premium, according to Mr. Williams, as it requires paying for commercials during sporting events, which "are one of the few pieces broadcast entertainment that men watch live in big numbers."

The data supports Mr. Williams' view. According to Redbooks, both Men's Wearhouse and Jos. A. Bank had 2012 marketing budgets of around $60 million, 85-95% of which was allocated to TV and radio advertising. At the same time, the two companies spent almost nothing on Internet or print advertising. In fact, both companies decreased their Internet spends from 2011 to 2012 even though they increased their marketing budgets by 20-40%.

While the companies' success with BOGOs suggests that the parties' customers are responsive to price promotions, absent competition from each other, the companies might be able to charge more or promote less. Although neither Mr. Regis nor Mr. Williams, as fashion experts, expressed any interest shopping at either store, both recognize that Jos. A. Bank and Men's Wearhouse customers represent a significant demographic. "There's definitely a need for it," Mr. Williams explains, as the convenience-over-style preference is still shared by "the majority of men."

If the "quick look" documents reveal that the parties consider each other significantly more than they do other suit sellers in determining promotions, the FTC will require substantial compliance with the second request and turn its attention to market definition. Because the quick look review appears likely to focus on evidence of effects, the FTC will—at least for the moment—set aside concerns it might have with trying to prove that the relevant market can be defined narrowly to exclude other sellers of men's suits. Even in the Horizontal Merger Guidelines, the agencies acknowledge that, "evaluation of competitive alternatives available to customers is always necessary at some point in the analysis." If the FTC reaches that point, it will first turn its attention to broader evidence surrounding existing competition from department stores (similar to what was discussed in the FTC's Federated/May decision).

In 2005, the FTC cleared the $11 billion merger between Federated and May Department Stores even though the transaction created "by far the largest chain of so-called 'traditional' or 'conventional' department stores in the country," according to the FTC's closing statement. The consolidated group of department stores included Macy's, Bloomingdale's, Marshall Field's, Lord & Taylor, and Hecht's banners, among other leading conventional department stores that sold "mostly apparel, accessories, cosmetics and housewares."

Multiple antitrust lawyers have cited the Federated decision as the most relevant to the Jos. A. Bank/Men's Wearhouse deal, as the FTC found the product market must be "defined to include, at the very least, all department stores and specialty stores that collectively sell substantially similar products to those offered by Federated and May." But stakeholders should not interpret the FTC's conclusion that specialty and department stores competed with each other in a department store merger to mean that the FTC will necessarily find that they compete with each other in a specialty store merger, particularly not this specialty store merger.

The FTC's finding that specialty competes with department stores was based largely on the fact that department store shoppers will substitute between buying from department stores and specialty stores located in the same malls. The FTC found that the "overwhelming majority of department stores" are located in "enclosed suburban shopping malls," which "have largely replaced flagship downtown department stores as shopping destinations. And "although items have migrated away from department stores, shoppers can buy them in more specialized stores in the same shopping mall – a new kind of one-stop shopping. . . . In many respects, today's mall is itself a real competitor against traditional department stores."

Men's fashion experts believe that there are many male shoppers that want to avoid the department store and the mall. According to Mr. Williams, "men traditionally don't want to walk through a woman's clothing store to shop." A men's-only store provides a "safe environment" for those who "don't feel comfortable in a mixed environment." However, according to an industry expert who favors the deal, in surveys asking men where they are most likely to buy their next suit, a "department store" is the most common response.

The Federated decision may be helpful to the parties, however, to the extent that the econometric tools the agency used will be the same. According to the closing statement, staff found no evidence the merging parties "priced their goods strategically in relationship to each other. The absence of such pricing patterns provides the most compelling objective demonstration that these conventional department stores are not in a distinct product market."

The FTC also explained that "equally compelling is the fact that Federated and May, like other department store chains, set prices that are uniform over very broad geographic areas – typically, multi-state regions. These firms do not appear to vary local prices based on the number or identity of conventional department stores in malls or metropolitan areas."

According to an industry expert who favors the deal, Men's Wearhouse most likely checks its prices against department stores more frequently than against Jos. A. Bank, because department stores sell the same brands as Men's Wearhouse. Both Men's Wearhouse and department stores purchase branded products through brand aggregators like Peerless Clothing Group, which is one of the largest producers of branded tailored clothing, including products from Ralph Lauren, Calvin Klein, DKNY, Sean John, John Varvatos and Michael Kors.

Moreover, if the brand aggregators sell to the retailers at a suggested retail price, then it would be no accident that the price of a Calvin Klein suit at Macy's would be very close if not identical to the price of a Calvin Klein suit at Men's Wearhouse. In contrast, Jos. A. Bank sells its own private label of suits. The same source who favors the deal indicated that Men's Wearhouse appears to set its prices on a national basis, citing online pricing data as evidence that this is likely the case.