

UNITED STATES DISTRICT COURT
FOR THE MIDDLE DISTRICT OF FLORIDA
JACKSONVILLE DIVISION

UNITED STATES OF AMERICA,)	
)	
Plaintiff,)	
)	Civil No. 81-1232-Civ-J-M
v.)	
)	
AMERICAN MAIZE-PRODUCTS)	COMPETITIVE IMPACT
COMPANY and BAYUK CIGARS,)	STATEMENT
INC.,)	
)	Filed: February 12, 1982
Defendants.)	

This competitive impact statement, relating to the proposed consent judgment submitted for entry in this civil antitrust proceeding, is filed by the United States pursuant to Section 2(b) of the Antitrust Procedures and Penalties Act, 15 U.S.C. § 16(b).

I. THE NATURE AND PURPOSE OF THE PROCEEDING

This is an action brought under Section 7 of the Clayton Act, 15 U.S.C. § 18, seeking to enjoin one cigar manufacturer from acquiring another. The defendants are American Maize-Products Company ("American Maize"), a Maine corporation with principal offices in Stamford, Connecticut, and Bayuk Cigars Incorporated ("Bayuk"), a Maryland corporation located in Fort Lauderdale, Florida.

Jno. H. Swisher & Son, Inc. ("Swisher"), a wholly-owned subsidiary of American Maize located in Jacksonville, Florida, is the second largest manufacturer of cigars in the United States by unit volume of sales and the third largest by dollar volume of sales. Its principal brands are King Edward and Swisher Sweets.

Bayuk is the fourth largest manufacturer of cigars in the United States by unit volume of sales and the fifth largest by dollar volume of sales. Its principal brands are Phillies and Garcia y Vega.

On December 21, 1981, the shareholders of Bayuk approved a plan for the complete liquidation of the company, to be completed within one year. As part of its plan of liquidation Bayuk agreed to sell substantially all of its cigar business assets to Swisher (or to another company formed by American Maize for the purpose of acquiring the Bayuk assets) for approximately \$14.5 million. Bayuk's plan of liquidation provides for the sale of the company's cigar business assets to another buyer if the sale to Swisher is not consummated.

On December 22, 1981, the government filed a complaint alleging that the proposed acquisition by Swisher of Bayuk's cigar business assets would substantially lessen competition in the manufacture and sale of cigars in violation of Section 7 of the Clayton Act and asking that the acquisition be preliminarily and permanently enjoined. The defendants subsequently agreed to postpone the closing of the transaction pending a hearing on the government's application for a preliminary injunction. The parties reached an agreement settling the case before a hearing could be held on the application.

II. THE NATURE OF THE ALLEGED VIOLATION

The complaint alleges that the appropriate market within which to assess the proposed acquisition's effect on competition is the manufacture (including importation) and sale of cigars throughout the United States. A cigar is defined as any roll of tobacco wrapped in tobacco leaf or reconstituted tobacco and weighing more than three pounds per thousand.

The government relied on market shares calculated both in units (individual cigars) and in dollars. Because cigars vary widely in price, and the proportion of cigars sold at each price level varies from one manufacturer to the next, a firm's share of the market may be very different as computed by these two methods. Although we believe units are generally the more reliable measure of competitive strength in this industry, the most complete and accurate picture of the industry's structure is obtained by using a combination of the two.

In unit sales, Swisher's market share for 1980 was 19.55%. Bayuk's market share was 7.67%. In dollars, the comparable figures are 10.54% for Swisher and 6.64% for Bayuk. The top four firms, as measured by unit sales, have approximately 69.8% of the market, the top eight 86.1%. Measured in dollar sales, the four-firm concentration ratio is 59.9%, and the eight-firm concentration ratio is 76.4%. The combined shares of Swisher and Bayuk amount to 27.22% in units and 17.18% in dollars, and would have resulted in post-acquisition four-firm and eight-firm concentration ratios of 76.9% and 87.7% in units and 66.6% and 79.1% in dollars.

The government believes that an increase of this magnitude in the level of concentration in the cigar industry would have resulted in a substantial lessening of competition in the manufacture and sale of cigars. Among the important factors supporting this conclusion are the companies' extensive overlap in the low-priced segment of the market, the steady decline in demand for cigars, the low probability of new entry, and the impracticality of increased importation of inexpensive cigars.

III. THE PROPOSAL FOR A CONSENT JUDGMENT AND ITS ANTICIPATED EFFECT ON COMPETITION

The proposed consent decree by which the parties would settle this case permits Bayuk to sell its cigar business assets and complete its liquidation, but it minimizes the potential increase in concentration in the cigar industry by limiting the buyers to whom Bayuk may sell. Section IV(A) of the proposed decree prohibits Bayuk from selling or transferring any trade name or manufacturing facility used in its cigar business to any of the largest cigar manufacturers -- Consolidated Cigar Company, American Maize, Culbro Corporation, or American Brands, Inc. -- without prior approval from the Department of Justice. Section IV(A) contains an exception for Bayuk's Garcia y Vega brand and related assets, which may be sold to any cigar manufacturer other than the largest, Consolidated Cigar Company. The decree is to remain in effect

for five years and will bind the purchasers of Bayuk's cigar business assets during that period.

In effect, the defendants have agreed that they will not go forward with the acquisition as it was originally structured. Bayuk will be allowed under the decree to attempt to negotiate a sale of its Garcia y Vega brand to Swisher, but failing that it will be free to sell that brand to any cigar manufacturer other than Consolidated. Bayuk's Phillies brand cannot be sold to any of the largest cigar manufacturers without the consent of the Department of Justice.

The government relied on several factors in assessing the proposed decree's probable effect on competition and in concluding that it represented reasonable and adequate relief:

(1) The maximum increase in concentration in the cigar industry permitted under the decree is much smaller than would have occurred if the acquisition had gone forward in its original form. Given the characteristics of the market and the companies involved, it is unlikely to lead to a substantial lessening of competition.

(2) Phillies will be preserved as a competitive entity independent of the other major manufacturers.

(3) Continued litigation would not be a satisfactory alternative if Bayuk and Swisher voluntarily limited the transaction to Garcia y Vega.

A. Increase in Concentration

The Garcia y Vega brand accounts for approximately one-third of Bayuk's unit sales and one-half of its dollar sales. Standing alone, its 1980 market share would have been 2.57% in units and 3.34% in dollars. The comparable figures for Phillies would have been 5.10% in units and 3.14% in dollars. The market shares of the four largest manufacturers, excluding Bayuk, are as follows:

<u>Manufacturer</u>	<u>1980 Market Share (Units)</u>	<u>1980 Market Share (Dollars)</u>
Consolidated Cigar	24.82%	26.56%
Swisher	19.55	10.54
General Cigar (Culbro)	17.74	13.98
American Cigar (American Brands)	7.14	8.86

No other firm has as much as 4% of the market on either basis, and most of the remaining firms are significantly smaller on one dimension (units or dollars) than on the other.

A useful means of comparing the increases in concentration that would result from various dispositions of the Bayuk cigar business assets is the Hirschman-Herfindahl index, a measure of the level of concentration in a market calculated by adding the squares of the market shares of all companies in the market. The Hirschman-Herfindahl index for the cigar industry in 1980 was at least .1464 in units and .1190 in dollars. The original proposed acquisition would have increased these figures by .0300 and .0140, respectively. By comparison, Swisher's acquisition of Garcia y Vega would yield an increase of .0100 in units and .0070 in dollars. The comparable figures for Garcia y Vega and Culbro are .0091 in units and .0093 in dollars. A sale to American Brands would increase the index by .0037 in units and .0059 in dollars. The maximum increase resulting from a sale of Phillies to one of the smaller manufacturers would be .0039 in units and .0018 in dollars, or .0023 in dollars and .0013 in units. An increase of .0100 in a moderately concentrated industry ordinarily would be considered significant.

Even in combination, the possible sales of Garcia y Vega and Phillies pursuant to the decree will produce a much smaller increase in concentration than the original transaction, and this assumes that Bayuk will in fact sell each brand to one of the largest manufacturers permitted under the decree. Alternative purchasers, either from outside the industry or

from among the very small cigar manufacturers, would further lessen or even eliminate the increase in concentration.

This does not mean that increases in concentration of the magnitude possible under the decree are necessarily competitively benign. In another industry, or in other circumstances, the Department of Justice might oppose the acquisition of a company the size of Garcia y Vega by a competitor the size of Swisher or Culbro. Here, however, we believe that the risk of anticompetitive effect is acceptably low, in part because Garcia y Vega and Swisher compete primarily in different segments of the market.

There is general recognition that within the broader cigar market not all cigars compete equally with one another. Cigars of a particular size and price compete most directly with other cigars of similar size and price. The degree of substitutability, and hence of competition, decreases as the price differential between cigars increases.

Despite the wide range of prices for cigars, it would be difficult and possibly misleading to define discrete submarkets on this basis. There are no clear dividing lines between different price categories, and variations of size and shape affect patterns of substitutability in ways that may counteract apparent differences in price. Arbitrarily defined submarkets might obscure the meaningful competition that does exist between cigars in different price categories. Nevertheless, it is important in analyzing the broader cigar market to take account of the tendency for similarly-priced cigars to compete more vigorously with each other than with cigars selling for a substantially higher or lower price.

As originally structured, the acquisition would have combined Phillies, one of the largest-selling brands of inexpensive cigars, with Swisher, which produces only inexpensive cigars and is the largest seller in that segment of the market. The effect on competition, because of this direct overlap, would have been particularly acute.

Garcia y Vega cigars are generally more expensive than Phillies or the cigars sold by Swisher. The latter sell for thirteen cents each or less at retail. Suggested retail prices for Garcia y Vega run from seven cents to seventy-five cents, with most selling for more than fifteen cents each.

Although the Garcia y Vega brand does compete with the brands sold by Swisher, they compete less directly than brands in the same price range, and the significance of their combined shares in the overall market should be weighed accordingly. If Swisher is able to negotiate a purchase of only Garcia y Vega, it will thereby expand its production into the medium-priced segment of the market in which it is not now represented.

This analysis is applicable to Culbro, which has its greatest strength in the low-priced and premium segments of the market, though to a lesser degree, as it does have medium-priced brands. American Cigar is a strong competitor in the medium-priced segment but has a much smaller share of the overall market.

B. Preservation of Phillies
as a Competitive Entity

A principal concern of the government in this lawsuit was that the number of significant competitors not be reduced because of Bayuk's desire to leave the industry. At present, the five largest cigar manufacturers control 76.9% of unit sales and 66.6% of dollar sales in the domestic market. The remainder is split among a multitude of small firms, many of which have limited product lines, regional or local sales territories, or both.

If Bayuk's cigar business and market share went entirely to one or more of the major manufacturers, the top five would have become the top four, and the market would be left with one less significant competitor. The resulting increase in concentration would almost certainly portend a loss of competitive vigor. Conversely, by insuring that the Phillies brand and manufacturing facilities are not sold to one of the major

manufacturers, the decree guarantees that it will remain an independent and important presence in the market. If Phillies is sold to one of the smaller manufacturers, it will project that company into the top five in the industry, essentially replacing Bayuk as a major competitor. If sold to a new entrant or otherwise maintained as a separate entity, Phillies will still be large enough to have a meaningful impact on the market.

This assumes, of course, that Phillies would be independently viable (if not sold to an existing manufacturer) and that Bayuk will sell or maintain it as a going business. Bayuk currently manufactures its cigars in two plants. The entire Phillies line can be produced efficiently in a single plant, which we expect will be offered to the buyer of the Phillies brand. Obtaining additional manufacturing facilities in any event would not be difficult. The government is aware of no special impediments or disadvantages that would prevent Phillies' survival as a separate company.

The government believes that Bayuk's financial interest in maintaining Phillies as a valuable, saleable property is sufficient to guarantee that it will not be operated or disposed of in a way that would injure its standing as a viable competitor and thereby diminish its worth.

C. Alternatives to the Proposed Decree

If the government had rejected the proposed settlement, it is likely that Bayuk would have proceeded unilaterally to restructure its transaction with Swisher to cover only Garcia y Vega. The government's options then would have been to continue this case, challenging only the narrower acquisition, or to dismiss the original action and await the sale of Phillies before deciding if one or both of the transactions should be the subject of further litigation. Even if we believed that Swisher's acquisition of Garcia y Vega itself was substantially anticompetitive, a case brought on that basis

would be much more difficult to win than the present case and would require a greater commitment of resources.

The alternative of waiting for Bayuk to complete the sale of its cigar business assets, however, was even less satisfactory. Without the decree there would be no guarantee concerning the future disposition of Phillies. If Phillies subsequently were sold to one of the major manufacturers, the net effect, when considered with a sale of Garcia y Vega to Swisher, would have been very close to that of the original transaction. At that point, however, the sale to Swisher would have been consummated, and attacking the two acquisitions collectively would have been far more difficult.

On balance, therefore, the government believes the proposed decree represents a reasonable resolution of the case, one that minimizes the probability that Bayuk's liquidation will adversely affect the quality of competition in the cigar industry. The five-year term of the decree was deemed sufficient in light of the steady decline in demand for cigars and the industry's uncertain future.

IV. REMEDIES AVAILABLE TO PRIVATE PARTIES

Entry of the proposed consent judgment will have no effect on the rights of persons who may have been injured by the alleged violation. Private plaintiffs may sue for money damages or any other legal or equitable remedy. However, this judgment may not be used as prima facie evidence in private litigation pursuant to Section 5(a) of the Clayton Act, 15 U.S.C. § 16(a).

V. PROCEDURES AVAILABLE FOR MODIFICATION OF THE PROPOSED CONSENT JUDGMENT

For a period of 60 days following the filing of the proposed consent judgment and its publication in the Federal Register, interested persons may submit written comments concerning the proposed judgment to Alan L. Marx, Acting Chief, General Litigation Section, Antitrust Division, United States

Department of Justice, Washington, D.C. 20530. These comments and the government's response to each will be filed with the Court and published in the Federal Register. The government will carefully consider all comments to determine if there is any reason for withdrawing its consent to the proposed judgment, which it may do at any time before the decree is entered by the Court. The Court will retain jurisdiction over the judgment following its entry so as to permit any of the parties to apply for orders nullifying or enforcing the decree.

VI. ALTERNATIVES ACTUALLY CONSIDERED

The complaint filed in this action requested that American Maize be enjoined from acquiring any interest in Bayuk's other business assets. This was the only other form of relief actually considered by the United States.

VII. DETERMINATIVE DOCUMENTS AND MATERIALS

There are no documents or materials that the government considered determinative in formulating the proposed judgment.

Respectfully submitted,

DATE:

/s/ Steven C. Douse
STEVEN C. DOUSE

/s/ Richard W. Pierce
RICHARD W. PIERCE

/s/ David S. Moynihan
DAVID S. MOYNIHAN

/s/ Philip M. Eisenstat
PHILIP M. EISENSTAT

Attorneys
United States Department
of Justice
Antitrust Division
Washington, D.C. 20530
(202) 724-6485