I. Introduction

The Federal Trade Commission (“Commission”) has accepted from Western Digital Corporation (“Western Digital”), subject to final approval, an Agreement Containing Consent Order (“Consent Agreement”), designed to remedy the likely anticompetitive effects resulting from Western Digital’s proposed acquisition of Viviti Technologies Ltd., formerly known as Hitachi Global Storage Technologies Ltd. (“HGST”), a wholly-owned subsidiary of Hitachi, Ltd. (“Hitachi”)

Pursuant to an agreement dated March 7, 2011, Western Digital intends to acquire HGST from Hitachi for approximately $4.5 billion in cash and Western Digital stock. The proposed merger would result in a merger to duopoly in the market for 3.5 inch hard disk drives used in desktop computers (“desktop HDDs”). The Commission’s Complaint alleges that the proposed Acquisition, if consummated, would violate Section 7 of the Clayton Act, as amended, 15 U.S.C. § 18, and Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. § 45, by lessening competition in the market for desktop HDDs.

The Consent Agreement remedies the alleged violation by replacing the lost competition in the desktop HDD market that would result from the proposed acquisition. Under the terms of the Consent Agreement, Western Digital will divest to Toshiba Corporation (“Toshiba”) all of the assets relating to the manufacture and sale of desktop HDDs necessary to replicate HGST’s position in the desktop HDD business. The Consent Agreement requires Western Digital to provide Toshiba with access to employees involved in the research, development, and production of desktop HDDs, cross license all intellectual property necessary to manufacture and sell desktop HDDs, and to supply Toshiba with up to 50 percent of certain critical components needed for the divested business. In addition, the Consent Agreement requires Western Digital to contract manufacture desktop HDDs for Toshiba at cost until Toshiba is able to manufacture these products on its own.

The Consent Agreement has been placed on the public record for 30 days to solicit comments from interested persons. Comments received during this period will become part of the public record. After 30 days, the Commission will again review the Consent Agreement and the comments received, and will decide whether it should withdraw from the Consent Agreement, modify it, or make final the accompanying Decision and Order.

II. The Products and Structure of the Market

HDDs are key inputs into computers and other electronic devices used to store and allow fast access to data. HDDs are used in various end-use applications including desktop and mobile computers, and in enterprise computing applications.
The relevant line of commerce in which to analyze the effects of the Acquisition is desktop HDDs. Desktop HDDs are utilized in non-portable desktop or tower personal computers. Consumers of these products demand HDDs with the highest available capacity at the lowest price per gigabyte. Desktop HDDs are the only HDDs that meet these specifications. As a result, customers would likely not switch to a different kind of HDD in response to a five to ten percent increase in the price of desktop HDDs in sufficient numbers to make that price increase unprofitable for a hypothetical monopolist.

The relevant geographic market for desktop HDDs is worldwide. Most HDDs, including desktop HDDs, are manufactured in Asia and are shipped to customers worldwide. Also, most large customers negotiate the purchase price of desktop HDDs at a global level.

The desktop HDD market is highly concentrated, with three manufacturers currently in the market. After Western Digital’s acquisition of HGST, Western Digital’s market share would increase to approximately 50 percent, and the number of suppliers of desktop HDDs would decrease from three to two.

III. Entry

Neither new entry nor repositioning and expansion sufficient to deter or counteract the likely anticompetitive effects of the proposed acquisition in the desktop HDD market is likely to occur. Deterrents to entry into the desktop HDD market include high capital expenditures and intellectual property barriers. Because the market for desktop HDDs is mature with limited growth potential, it is unlikely that a potential competitor would have the incentive to make the substantial investments necessary to enter this market.

IV. Effects of the Acquisition

The proposed acquisition likely would result in anticompetitive effects in the market for desktop HDDs. The structure and characteristics of this highly concentrated and mature market, where competitors sell largely homogenous products and have substantial insight into their competitors’ price and output levels, suggests that the two remaining firms in the market would likely find it possible and profitable to coordinate on pricing or output. In addition, HDD customers generally wish to have at least three suppliers available to them. The fact that customers have a strong desire to source their desktop HDD purchases from several suppliers simultaneously in order to obtain competitive pricing and adequate supply suggests that the transaction could result in unilateral effects as well.

V. The Consent Agreement

The Consent Agreement resolves the competitive concerns raised by Western Digital’s proposed acquisition of HGST by requiring the divestiture of HGST’s assets relating to the manufacture and sale of desktop HDDs to Toshiba. This divestiture must occur within fifteen days after the acquisition but may be extended an additional fifteen days, if necessary, to allow for regulatory approval in other jurisdictions.
Toshiba has the industry experience, reputation, and resources to replace HGST as an effective competitor in the desktop HDD market. Headquartered in Tokyo, Japan, Toshiba is a diversified manufacturer and marketer of advanced electronic and electrical products spanning digital consumer products, electronic devices and components, power systems, industrial and social infrastructure systems, and home appliances. Toshiba does not currently compete against Western Digital or HGST in the sale of desktop HDDs, but it does manufacture HDDs for use in mobile and enterprise applications. Because Toshiba has extensive experience manufacturing these other types of HDDs, and has a worldwide infrastructure for the research, development, and sale of desktop HDDs, Toshiba is well-positioned to replace the competition that will be eliminated as a result of the proposed transaction.

Pursuant to the Consent Agreement, Toshiba would receive all of the assets necessary to replicate HGST’s market position in the desktop HDD business, including sixteen desktop HDD production lines, representing the capacity to produce more than twenty million desktop HDD units per year, along with the product designs for HGST’s most recent and advanced desktop HDD products. The Consent Agreement further requires Western Digital to provide Toshiba with access to HGST and/or Western Digital employees involved in the research, development, and production of desktop HDDs. In addition, the Consent Agreement also requires Western Digital to cross license all intellectual property necessary to manufacture and sell desktop HDDs and to supply Toshiba with up to 50 percent of certain critical components needed for the divested business. The Consent Agreement also requires Western Digital to contract manufacture desktop HDDs for Toshiba at cost until Toshiba is able to manufacture these products on its own. A divestiture of HGST’s desktop HDD assets to Toshiba will enable Toshiba to compete immediately with the merged entity.

The Commission has appointed Phillip Comerford, Jr., Managing Director and Head of the Mergers & Acquisitions Group of ING Capital LLC, as Interim Monitor to oversee the divestiture of the desktop HDD assets. In order to ensure that the Commission remains informed about the status of the proposed divestiture, the Consent Agreement requires the parties to file periodic reports with the Commission until the divestiture is accomplished.

If, after the public comment period, the Commission determines that Toshiba is not an acceptable acquirer of the assets to be divested, or that the manner of the divestiture is not acceptable, Western Digital must unwind the divestiture and divest the assets within 180 days of the date the Order becomes final to another Commission-approved acquirer. If Western Digital fails to divest the assets within the 180 days, the Commission may appoint a trustee to divest the relevant assets.

The purpose of this analysis is to facilitate public comment on the Consent Agreement, and it is not intended to constitute an official interpretation of the Consent Agreement or to modify its terms in any way.