Notice seeking clearance for the applicants to merge their operations pursuant to section 66 of the Commerce Act 1986

Given by	Heyden Farms Limited, Henergy Cage-Free Limited Rasmusens Poultry Farms Limited
To	The Registrar Mergers and Acquisitions Commerce Commission registrar@comcom.govt.nz

Executive Summary

Heyden Farms Limited (**Heyden Farms**), Henergy Cage-Free Limited (**Henergy**) and Rasmusens Poultry Farms Limited (**Rasmusens**) seek clearance to merge their egg production and wholesale operations through the sale and purchase of shares or assets. The proposed merger will provide the merged entity with scale, balance sheet strength and access to cost-effective production, allowing the merged entity to invest and innovate in ways that drive efficiencies into its business. Over time, the benefits of these investments and efficiency gains can be shared with consumers through lower prices.

The proposed merger will result in aggregation in national egg production and wholesale supply markets. The applicants consider that the egg production and wholesale supply market should be analysed as a single product market, in which case the level of aggregation resulting from the merger will at best be modest. However, if the Commission is minded to define separate product markets for cage eggs, barn-laid eggs and free-range eggs, then the most significant area of concentration will be in the barn-laid egg market.

Regardless of how the relevant markets are defined, there is unlikely to be any substantial lessening of competition relative to the counterfactual. A number of factors point to the current competitive dynamic in the market continuing (whether or not barn-laid eggs are analysed in a separate market). These are:

- supply and demand dynamics which mean egg producers are effectively price-takers and cannot sustain price increases over time;
- the exit of traditional caged eggs from the market due to regulatory changes and the phase out of colony eggs by major supermarkets. These two factors have accelerated trends towards commoditisation of barn-laid and free-range eggs (formerly seen as premium products), meaning additional pressure from customers to reduce prices;
- a range of competitors operate in the market utilising different business models and production methods, giving customers sufficient options should the merged entity seek to raise prices or reduce quantity;
- significant expansion in the market by competitors is imminent, both mitigating any comparative scale benefits resulting from the proposed merger and demonstrating that barriers to further entry and expansion are able to be overcome;
- major customers (particularly supermarkets, but also food service) have significant countervailing power, and actively structure their relationships with suppliers to harness competition among suppliers and constrain any upwards pressure on prices.

For these reasons, the applicants consider that there is no realistic prospect that the proposed merger will result in a substantial lessening of competition. The applicants therefore request that the Commission grant clearance for the proposed merger.

The Parties to the Proposed Merger

Heyden Farms Limited

1. Heyden Farms Limited (**Heyden Farms**) farms caged, barn-laid and free-range eggs, which it supplies to wholesale and retail customers. It has production facilities located in Waikato and Bay of Plenty, and a feedmill facility in Tuakau. It currently sells under the Morning Harvest, Sure as Eggs, and New Day Free Range brands, which are owned by the Independent Egg Producers Co-operative (**IEP Co-op**). Heyden Farms also produces liquid eggs. More information on Heyden Farms can be found at heydenfarms.co.nz.

2. Heyden Farms is currently a member of the IEP Co-op, and its supply arrangements are determined through its membership to the co-operative. Heyden Farms and its sister company, Sunny Bay Eggs Limited, has a 31.06% shareholding in Independent Egg Producers Co-operative Limited. Heyden Farms is in the process of leaving the IEP Co-op, and will transfer its shareholding to facilitate this exit in order to give effect to the proposed merger.

3. Other interests in the IEP Co-op include Northern Eggs Limited, Hessells Poultry Farm Limited, Craigs Poultry Limited, Ewing Poultry Limited, Spray-Free Holdings Limited, Quail Valley Free Range Limited, Portadown Farming Limited, Braemar Poultry Farm Limited and Gizzy Eggs Limited. Directors of the IEP Co-op are elected by these shareholding interests in the usual way.

4. Heyden Farms is ultimately owned by members of the van der Heyden family.

5. Heyden Farms' contact details are:

   Gareth van der Heyden
   C/- Graham Brown & Co Ltd
   45-49 Tirau Street
   Putaruru

   Email: Gareth@heydenfarms.co.nz

Henergy Cage-Free Limited

6. Henergy Cage-Free Limited (Henergy) farms barn-laid eggs and buys in free-range eggs, which it supplies to wholesale and retail customers. It has a production facility located in Masterton. Its sells primarily under its Henergy Cage-Free brand, and also supplies eggs for the Pams and Select private labels. More information on Henergy can be found at henergy.co.nz.

7. Henergy is ultimately owned by a range of interests.

8. Henergy's contact details are:

Mike Fleming
C/- Southey Sayer Limited
110 Dixon Street
Masterton 5810

Email: mike@visionag.co.nz

Rasmusens Poultry Farms Limited

9. Rasmusens Poultry Farms Limited (**Rasmusens**) farms caged colony and free-range eggs, which it supplies to wholesale and retail customers. It has a production facility located in Whanganui. Its sells under the Morning Harvest and New Day brands as part of the IEP Co-op, as well as the Rasmusens free-range brand. Rasmusens is also involved in the commercial sale of pullets. More information on Rasmusens can be found at rasmusenseggfarm.co.nz.

10. Rasmusens is currently a member of the IEP Co-op, and its supply arrangements are determined through its membership to the co-operative. As part of its membership, Rasmusens has a 6.80% shareholding in Independent Egg Producers Co-operative Limited. Rasmusens is in the process of leaving the IEP Co-op, and will sell its shareholding to facilitate this exit to give effect to the proposed merger.

11. Rasmusens is 100% owned by Aaron Rasmusen.

12. Rasmusens' contact details are:

Janette Rasmusen
C/- Markhams Wanganui Limited
249 Wicksteed Street
Whanganui, 4500

Email: janette@rasmusenseggfarm.co.nz

Correspondence and notices

13. The applicants request that all correspondence and notices in respect of this application be directed in the first instance to:

Phil Taylor / Edward Willis
Partner / Consultant
Tompkins Wake
Level 8
430 Victoria Street
Hamilton 3204

Email: Phil.Taylor@tompkinswake.co.nz

The Proposed Transaction

Overview

14. There is currently no common ownership between any parties to the proposed merger (although both Heyden Farms and Rasmusens are members of the IEP Co-op, and so are not strictly competitors because wholesale supply arrangements are determined by the co-operative). Under the proposed merger, the parties intend to merge the entirety of their current operations into a single entity. This will be achieved through a series of share swaps from the current entities to a new holding company. Simply put, a new company will be formed called “Better Eggs Limited”. The shareholders of the merging entities will transfer their shares in the merging entities to “Better Eggs Limited”. As a result, each of the current businesses operated by Heyden Farms, Henergy and Rasmusens will be 100% owned by a holding company. The current shareholders of Heyden Farms, Henergy and Rasmusens will then acquire a shareholding in the “Better Eggs Limited” holding company. It is this acquisition of shares in “Better Eggs Limited” by each of the applicants for which the applicants seek clearance pursuant to section 66 of the Commerce Act. In addition, some physical assets owned by the applicant businesses will be sold directly to the new holding company. The applicants are also considering the development of new brands post-merger, which may be operated separately under the new holding company (that is, as part of a stand-alone subsidiary rather than any of the existing companies involved in the share swap).

15. The transaction came about organically as the applicants realised they have common interests and ambitions. The initial impetus came indirectly as a result of Henergy seeking investment capital in 2019. Heyden Farms initially expressed interest in participating in the capital raise, but ultimately declined to do so. Through that initial contact Heyden Farms and certain interests in Henergy discussed various opportunities. However, it quickly became apparent that Heyden Farms’ strategy of supply chain integration meant that it would only be interested in full acquisition or a merger. Quite separately, Rasmusens was known to Heyden Farms through their mutual association with the IEP Co-op, and they shared a belief in the vertical integration strategy. [ ]. The discussions between the applicants only began in earnest in mid-March, and a confidentiality agreement was signed at that stage.[1] The parties signed the transaction documents to give effect to the share swap on 29 June 2020. The transaction is conditional on receipt of a clearance for the proposed merger from the Commerce Commission. There are no ancillary agreements that the parties are aware of that might bear on this proposed merger.

16. A diagram of the proposed structure resulting from the proposed merger is set out in Appendix 1.

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1 Prior to that time discussions were formative and organic, and Henergy and Rasmusens were not even aware of the identity of the other. There is, accordingly, no clear evidential record of those discussions.

Commercial rationale

17. The parties have identified the merger as an attractive opportunity to combine:

    (a) Henergy's scale in egg production, national distribution and expertise in cage-free egg production;

    (b) Heyden Farms' scale, knowledge and experience of supply chain integration and production processes, which lower production and supply costs; and

    (c) Rasmusens' strong balance sheet and knowledge and experience of egg farming.

18. The merged entity would be in a position to drive cost-efficiencies in order to maintain competitive prices, and continue to invest in innovation and production over the long-term. All three applicants are long-term shareholders, and are committed to investing for the long term. Over time, consumers are likely to benefit from these cost-efficiencies and investment through sustainably lower prices.

Notification to other competition agencies

19. The proposed transaction only impacts competition with domestic markets in New Zealand. Accordingly, no other competition agencies are being notified regarding the proposed merger.

Counterfactual

20. From Heyden Farms' perspective, if the proposed merger does not occur, it is likely that it will [

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21. From Henergy's perspective, if the proposed merger does not occur, it is likely that it will [

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22. From Rasmusen's perspective, if the proposed merger does not occur, it is likely that it will [

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23. This is an opportunistic merger rather than a scenario where one or more of the parties would be held out for sale if the merger does not proceed. Further, the two largest parties to the transaction have a primary strategy of [ ]if the proposed merger does not occur. Accordingly, the applicant considers that the *status quo* serves as the relevant counterfactual, except that [ ]. The applicants have framed this application for clearance against that counterfactual scenario.

Wider Industry Context

General background

24. The New Zealand egg production industry is currently very competitive. There are a number of producers operating in the market, with around 3,900,000 laying birds based on around 160 egg farms across New Zealand. The competitive nature of the market is reflected in the available market share data, which shows material fluctuations in response to competitive pressures.

25. Eggs can be farmed in several different ways:

    (a) cage-farmed eggs, which place a small number of laying birds in small, confined cages and includes ‘colony farming’ where larger numbers of laying birds in larger cages providing more space per bird and greater enrichment;

    (b) barn-laid eggs, which do not make use of cages but instead confine laying birds in an enclosed facility; and

    (c) free-range eggs, which allows laying birds freedom to move around in outdoor areas.

26. While eggs are shelf-stable for a period of time (indeed, are sufficiently so that they can be transported nation-wide), they are perishable which means that producers are price-takers. Any attempt to sustain prices above the level where the market clears would result in lower volumes of sales. This would in turn require greater volumes to be sold through the market at a lower price in the short term. This market dynamic, where demand relative to supply is the key determinant of price, effectively prevents any egg producers from raising prices above competitive levels over the medium-to-long term.

27. In addition, supermarkets represent the major wholesale purchasers of eggs. The applicants estimate that sales to supermarkets represent approximately 60% of the market, a figure we have cross-checked with the Egg Producers Federation of New Zealand. The dominance of the major supermarket brands in the retail supply chain means that they effectively set the prices as buyers of the producers’ product. Further, as we explain below, supermarkets are active in ensuring that they leverage their buying power into lower wholesale prices. The other major customer segment is food service, where again there is significant countervailing power and egg producers engage in the market as price-takers.

28. The egg production sector is represented by the Egg Producers Federation of New Zealand. More information on the sector can be found at eggfarmers.org.nz.

Changing market conditions

29. The egg production and wholesale market is currently undergoing significant change. Regulatory changes have meant that traditional cage-farmed eggs are exiting the market in the short-to-medium term (by 2022). In addition, major supermarket customers, which represent approximately 60% of the market on the buyer's side, have indicated that they will not be stocking colony farmed eggs in the future (Progressive as a target date of 2024/25, while Foodstuffs has a target date of 2028). This is likely to facilitate the increasing commoditisation of eggs that were previously viewed as premium in the marketplace (barn-laid and free-range eggs). While non-price dimensions such as certainty of supply will continue to influence the market, the commoditisation of non-cage eggs means that price is increasingly the most important dimension of competition. The proposed merger will have no impact on these prevailing trends.

30. The applicants have included historical retail pricing information at Appendix 2. The Commission will note the increase in retail prices towards the end of the 2018 calendar year. This reflects a reduction in supply in the market, as the first wave of conventional cages exited. This trend has since reversed. With COVID-19 there is currently a reduction in demand, reflecting impacts on the hospitality sector in particular. These trends demonstrate that the forces of supply and demand effectively dictate the market price for eggs, and that producers (including the merged entity) have little if any influence over prices. This is not a dynamic that will change post-merger.

31. In addition, there is significant expansion currently being undertaken. We understand that a major competitor to the merged entity, Zeagold/Mainland, is bringing major barn-laid and free-range facilities online in the next 12 months, which will make it the number one supplier by volume in both free-range and barn-laid market segments. This new investment is likely due in part to the phase out of traditional cage-farmed eggs. Zeagold/Mainland is already the market leader in the free-range category, and represents a strong competitor. Other competitors in the cage-farmed market segments are likely to follow suit with their own production facility conversions where they are able to do so. While the applicants do not have any insight into their competitors plans, the Egg Producer's Federation estimates that 40% of current production is carried out in conventional cages that are due to be phased out. While some suppliers will find conversion of production methods to be cost-prohibitive,[2] if half of that figure is converted to barn production then this would represent substantial entry into that market segment.

2 Older cage sheds are often not suitable for conversion to barn, requiring a complete rebuild. Newer sheds can be converted more cheaply and easily.

Detailed Competition Assessment

Relevant markets

32. The applicants consider that the relevant market for the purposes of competition analysis is a single national market for the production and wholesale supply of eggs. That market is highly competitive, and would remain so if the proposed merger were to proceed. The applicants estimate that their combined market share of the national market for the production and wholesale supply of eggs is only [ ]%. As a result, the proposed merger would be very unlikely to raise any competition concerns. This is especially so in light of the other competition factors that are discussed below.

Product markets

33. That said, the applicants recognise that the Commission may wish to distinguish between various egg product markets. In particular, the Commission may wish to assess the competitive impact of the proposed merger in respect of the following markets:

    (a) the national market for the wholesale supply of barn-laid eggs;

    (b) the national market for the wholesale supply of free-range eggs;

    (c) the national market for the wholesale supply of cage-farmed eggs; and

    (d) the national market for the supply of liquid eggs.

34. To be clear, the applicants have differentiated between wholesale supply of barn-laid and free-range eggs in particular out of an abundance of caution. There are good reasons to consider that barn-laid and free-range eggs represent close points on a broader spectrum of substitutable products (which includes traditional cage-farmed eggs, colony-farmed eggs, barn-laid eggs, free-range eggs and organic eggs),[3] and are therefore part of the same product market. The primary distinction is between premium and commodity eggs, driven in large part by a consumer preference for cage-free eggs over caged eggs. This distinction is becoming less important from a market analysis perspective as market trends lead towards premium eggs becoming more and more commoditised.

35. However, the applicants also acknowledge that there are a number of factors that point to barn-laid eggs and free-range eggs possibly being separate product markets. These factors include:

    (a) on the production side of the market, free-range and barn-laid eggs are not substitutable;

    (b) the available retail market data is broken down by barn-laid eggs and free-range eggs categories, suggesting that suppliers and major customers in the market understand these to be separate markets;

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3 This is sometimes referred to as a “chain of substitution” in the relevant literature.

(c) free-range eggs do command a premium price to the end-consumer, at least under current market conditions; and

(d) there is some overseas precedent that suggests that competition authorities place free-range eggs in a separate product market.[4]

36. As far as the applicants are aware, the Commission has not previously reached a considered public view on the appropriate market definition for the supply of eggs. We anticipate that the Commission may elect to take a conservative approach that places cage-farmed, barn-laid and free-range eggs in separate product markets. Even in this case, the applicants consider that the proposed merger will not result in a substantial lessening of competition.

37. Accordingly, we conduct the competition assessment below on the basis of a single, overall egg product market, as well as the cage-farmed, barn-laid and free-range market segments separately. Detailed market share estimates for each market segment are set out in Appendix 4. Our focus is on the barn-laid egg segment of the market in particular, on the assumption that this has the potential to reveal the greatest risk of a reduction in competition between the proposed merger and the counterfactual. We note, however, that outside of market share and concentration indicators the competition factors falling for analysis are largely similar. Therefore, if there is no substantial lessening of competition with respect to barn-laid eggs (where market concentration post-merger would be at its highest) then there is no realistic prospect of a substantial lessening of competition in any other affected markets however defined.

Geographic market

38. The applicants also consider that there is a single national geographic market for wholesale supply across New Zealand, given that:[5]

(a) major customers procure eggs on a nationwide basis from centralised locations;

(b) the applicants and their competitors supply customers throughout New Zealand, as the location of production facilities do not dictate the reach of a supplier;[6] and

(c) in respect of smaller customers who may be located only in a single region, eggs supplied from neighbouring regions throughout the country are substitutable for each other.

39. There are some 160 egg farms located across New Zealand,[7] indicating a spread of production facilities nationally. The large number of facilities itself, combined with the ability to transport eggs across regions, means that the Commission's

4 See the 2007 Deans Food Group/Stonegate merger in the United Kingdom.

5 While eggs are perishable produce, they are sufficiently shelf stable that they can be transported across the country to meet demand.

6 As we explain further below, this includes across the North Island and South Island.

7 This figure has been supplied by the Egg Producers Federation.

competition assessment is unlikely to be assisted by a focus narrow, regional markets.[8] The applicants' production facilities are all located in different regions in the North Island (Waikato/Bay of Plenty, Masterton, Whanganui). If regional markets were adopted for the purposes of analysis, there would be no aggregation in any single geographic market as a result of the proposed merger.

40. We understand that the Commission may wish to investigate the possibility of separate North Island and South Island geographic markets, particularly as the applicants' production facilities are all located in the North Island. In particular, there may be a concern that freight costs between New Zealand's major islands represent a barrier to establishing a single national market.[9] We note that those freight costs are not currently acting as a meaningful barrier. The applicants' major competitor, Zeagold/Mainland, has its production based in the South Island and is active in North Island wholesale supply markets. Henergy also supplies to the South Island from the North Island.[10] The applicants understand that other producers are also active in both markets, although they do not have any real transparency over their competitors' operations. The applicants therefore do not consider that defining a separate North Island market would materially change the competition analysis.

Upstream markets

41. The applicants also note for completeness that Rasmusens is involved in the commercial sale of pullets, although this is not a major part of its business. Pullets are a necessary input for egg producers where they have elected not to invest in their own rearing facilities. Although precise figures are not available, it is common for egg producers to supply pullets in addition to their core business. Given Rasmusens small bird numbers overall, its supply of pullets is likely to be extremely modest in terms of the overall market.

42. Both Henergy and Heyden Farms rear their own chicks, which are supplied by one of two national producers. As such, they do not participate in the supply of pullets. None of the applicants in active in the commercial supply of other inputs, and so the proposed merger will not result in any concentration in upstream markets.

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8 Commission staff have requested that the applicants provide a map indicating the location of production facilities. The large number of facilities and the applicants' lack of knowledge of their competitors' operations makes this infeasible, and in any event we do not consider that it assists with the substantive analysis.

9 Indicative freight costs are included at Appendix 5.

10 [

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SINGLE EGG PRODUCTION MARKET: COMPETITION ASSESSMENT

Market shares and concentration

43. If the proposed merger were to proceed, the merged entity would hold a market share of approximately [ ]%. This estimate is the aggregate of:[11]

    (a) Heyden Farms [ ] laying birds, which represents [ ]% of the market;

    (b) Henergy's [ ] laying birds, which represents [ ]% of the market; and

    (c) Rasmusen's [ ] laying birds, which represents [ ]% of the market.

44. A more complete market share table is included at Appendix 4. In the context of a number of competitors in the market holding a similar or greater market share, this does not come within an area of concern according to the Commission's market concentration indicators. The applicants therefore consider that there is no realistic prospect of the proposed merger resulting in a substantial lessening of competition.

Other competition factors

45. We do not exhaustively repeat the full assessment of competition law factors here which are set out below with respect to the barn-laid segment of the market. We do note in particular that:

    (a) Zeagold/Mainland is a powerful and effective competitor that is currently undertaking an aggressive programme of market expansion. Zeagold/Mainland is already the largest competitor in the market with approximately [ ]% market share. In addition, it has two additional production facilities currently in development — the first a barn-laid production facility of 300,000 laying birds due to be commissioned by 2021, and the second a free-range production facility of similar bird numbers. This would bring Zeagold's market share to approximately [ ]% of that segment of the market. The merged entity has very little opportunity to engage in dominant behaviour in the market based on the existence of such a significant competitor.

    (b) Supermarkets, who represent the majority of the buyer's side of the market, do have market power and exercise this to ensure that wholesale prices remain low. Supermarkets refuse to enter into supply contracts (other than for private label supply), and retain complete discretion to accept or reject supply. This effectively creates a kind of spot market for egg supply each day, which gives supermarkets (either at the national or regional level) significant influence over the wholesale price. It is always an option for supermarkets to prefer a competitor's price, or simply to refuse to accept supply altogether. This market

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11 Sales data is not available in respect of the combined egg market. These figures are based off the latest information available from the Egg Producers Federation, who estimate that the total number of birds of laying age nation-wide is 3,900,000.

dynamic will prevent the merged entity from raising its prices or otherwise lessening competition.

(c) The other major customer segment, food service, also exhibits evidence of countervailing buyer power. Food service businesses are major businesses who are able to play producers off against each other in order to secure a favourable price. Egg producers are price takers in this market, a dynamic that will only continue post-merger.

46. As set out above, a single, combined market for the supply of eggs, regardless of method of production, is the applicants' preferred lens for assessing the state of competition. If reveals the market reality where there is significant pressure from competitors and wholesale customers. However, if the Commission is minded to define separate product markets for caged-farmed, barn-laid and free-range eggs, then the most significant area of concentration will be in the barn-laid egg market. We therefore undertake a more comprehensive assessment of the competition factors relevant to the barn-laid segment of the market below.

BARN-LAID EGGS: COMPETITION ASSESSMENT

Market shares and concentration

47. If the proposed merger were to proceed, the merged entity would hold a market share of up to approximately [ ]% of the barn-laid segment of the market. This is the aggregate of:[12]

(a) Henergy's current market share, including private label contracts, of approximately [ ]%; and

(b) Heyden Farms' and Rasmusens' estimated combined market share of [ ]% (in the North Island only), which is derived from an assumption of a combined [ ]% contribution to the IEP Co-op's current market share.

48. A more complete market share table is included at Appendix 4.

49. The applicants acknowledge that, if the Commission is minded to define a separate market for barn-laid eggs, the headline market share indicators fall well outside the nominal 'safe harbour' market share indicators set out in the Commission's Merger and Acquisition Guidelines. However, in this particular market context, the applicants submit that:

(a) The increase in market concentration as a result of the proposed merger would be incremental in nature, rather than creating a new competitive dynamic in the market. As a result, there is no realistic opportunity for the merged entity to unilaterally exercise market power in a new way that is not available to Henergy as the largest of the merging parties.

12 Where available, market share data is taken from Aztec, which is included in this application as Appendix 3.

(b) As set out below, there are a number of other factors in the competition analysis that strongly suggest that there is no realistic prospect of the proposed merger resulting in a substantial lessening of competition. There are existing and emerging constraints in the market that prevent any ability to exercise unilateral market power in a sustained way.

Existing competition

50. If the proposed merger were to proceed, there would be three credible competitors in the nation-wide barn-laid egg market:

Competitor	Approx market share (%)
Wholesome NZ	[ ]%
Zeagold	[ ]%
IEP Co-operative	[ ]%

51. Each of these competitors is of a sufficient size (in terms of volume of production) that they would offer competitive constraint on the merged entity. The applicants also understand that each of these competitors operates nationally (including in both the North Island and the South Island). Customers would continue to have the ability to seek alternative supply if the merged entity sought to increase prices above competitive levels. In particular, and to the best of the applicants' knowledge, the IEP Co-op will continue to be a competitive presence in the market, and will not face any additional competitive barriers due to the loss of Heyden Farms and Rasmusens. The applicants do not have any particular insight into IEP Co-op's likely strategy if the merger proceeds, but it will continue to have sufficient scale and the relevant market contacts to compete for supply contracts (in particular supply of supermarket private label contracts).

52. The applicants also note that:

(a) After the proposed merger has been completed, the IEP Co-op may appear to be in a weaker competitive position as the result of losing scale with the exit of Heyden Farms and Rasmusens. However, a [ ]% reduction in market share is a crude estimate based on production capacity. Given the IEP Co-op's existing wholesale relationships and supply networks it will likely have a greater market share in terms of sales then the merged entity. In any case, the relevance of the IEP Co-op's reduction in market share as the result of Heyden Farms and Rasmusens choosing to exit the co-operative for the purposes of competition assessment needs to be kept in mind. [

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(b) In any case, IEP Co-op has greater influence over the market than the raw market data suggests. IEP Co-op holds private label supply contracts with Foodstuffs. There is no reason to believe that IEP Co-op will not have sufficient scale to continue to supply its current arrangements, but in any case these contracts are likely to be sufficiently valuable to justify further investment in production scale if necessary, and if the merged entity is to seek to become a private label supplier to Foodstuffs, it must compete on its own merits against an effective incumbent.

(c) Current market shares are not stable, and can fluctuate by +/- 5% according to the available market sales data.[13] This suggests an ability to increase production where necessary and win or hold market share from an incumbent.

53. These factors suggest that the existing competition in the market is likely to be sufficient to constrain the merged entity if the proposed merger were to proceed.

Entry and expansion

54. Over and above incremental expansion from increasing hen numbers, new entry and expansion is dependent on the ability to bring new production facilities online. Outside of securing the necessary investment capital, the barriers to entry are relatively low.

55. The primary barriers to entry in this case are:

(a) land availability; and

(b) regulatory restrictions and costs (primarily Resource Management Act consents).

56. Neither of these barriers is significant. In terms of land availability, existing blocks of land (for example, dairy farms) can readily be purchased and converted to barn-laying or free-range production facilities. In terms of resource consent, noise and odour permissions are usually necessary. Processing times for consents can vary, with some regional councils able to process these applications quickly. Others can take up to a year or more. However, the economic potential of egg production facilities means that these are usually processed and granted without any genuine concern provided that the facilities are not located close to a population centre.

57. Once land and consents are secured, physical plant is installed (although this may also begin while the consenting process is still in train). This plant includes concrete floors, frames and panelling, and production equipment: feeders, boxers, conveyers, perch bars, and so on. Production equipment is not bespoke and is readily available and can be bought off the shelf. Pullets can be purchased for immediate production. If the facility rears its own chicks, these can begin laying after around 18 weeks, Accordingly, lead in times are relatively modest and these potential barriers can readily be overcome by a sufficiently motivated competitor. In most cases, a sufficiently motivated competitor can commission a new barn-laying production facility in a total of 12-18 months.

58. The market evidence suggests that these barriers do not represent a material barrier to new entry or expansion. Zeagold is currently completing a 300,000 bird facility in

13 This is evidenced in the Aztec retail market data, set out in Appendix 3.

the Waikato area, due to be in production in early 2021. This is a 100% barn-laid egg facility, and so once this occurs, Zeagold will become the number one competitor in the market based on production volumes and market share. This not only demonstrates the ability of competitors to expand in the market, and at scale, but will significantly reshape competitive dynamics with the merged entity's estimated market share in the barn-laid egg market dropping to approximately [ ]%.

59. It is likely that further new entry or expansion will occur as non-colony cage-farmed eggs are phased out of the market until 2022. Producers currently operating in these market segments are likely to invest in barn-laid egg production in order to maintain their viability. Although the applicants do not have a close understanding of their competitors' plans, the general understanding within the industry is that this can and is occurring. This conversion of production method can be eased by a willingness to undertake capital investment, or if sheds housing conventional cages are newer and able to be directly converted rather than replaced. Estimates available from the Egg Producer's Federation suggest that around 40% of the production market currently uses convention cages that are being phased out. If only around half of this production was converted to barn, it would represent a significant shift in production volumes and potentially market share. If the Commission's preferred approach is that market analysis is conducted on the basis of different production methods, there is a strong likelihood of new entry and expansion occurring independently of the proposed merger. The market reality is that more and more competition is likely to be brought to bear in the barn-laid egg segment of the market, and the very real prospect of such changes in market dynamics will constrain the merged entity considerably.

Market contraction and exit

60. The wholesale supply market is governed by supply and demand dynamics. Where there is a drop in demand, there is an immediate drop in prices that supplies can secure. This can result in eggs being sold at lower prices. If suppliers cannot secure supply contracts (supermarket private label being the key example), then they do have the option of redirecting stock through their own retail brands. However, these brands are still subject to price competition at the wholesale level, with wholesale customers effectively able to set the price for supply.

61. If there is a sustained surplus of supply relative to demand in the market, then some sort of supply response can be anticipated. Suppliers may be required to write off stock in the first instance, incurring temporary losses. If there is continued over-capacity the only option for some producers may be to cull bird numbers to bring these down to more sustainable levels. If this occurs, it obviously results in capacity exiting the market. The smallest suppliers may not be able to sustain the resulting losses, and so may exit the market altogether. However, for most suppliers this situation will by no means be permanent and if prices stabilise produces can replenish their laying stock.

62. Current market dynamics are in a state of flux. With the phase out of conventional cage farming beginning in 2018, and its replacement with barn and other production methods, supply in the market overall (that is, regardless of production method) can vary month to month. How balanced levels of supply and demand are at the end of the phase out period in 2022 is not yet known. After that stage, the risk of market

exit is unlikely to be less acute. If there is sufficient demand at that time, there is no real barrier to further market entry or expansion.

Countervailing buying power

63. Supermarkets are major customers for egg producers. The applicants understand that publicly available estimates indicate that sales to supermarket customers account for approximately 60% of the market.

64. Supermarkets have significant buying power, and have significant influence over the price that egg producers can receive for their eggs. This will not change if the proposed merger proceeds. Accordingly, the countervailing power of supermarket customers will keep downwards pressure on wholesale prices both with or without the proposed merger proceeding.

65. Supermarkets actively structure their relationships with suppliers to harness competition among suppliers and constrain any upwards pressure on prices. The primary means by which they achieve this is through the refusal to enter into supply contracts, even over the short-term. This has the effect of creating a kind of spot market for the supply of eggs each day, with supermarkets holding the power to prefer a competitor's wholesale price that day or simply refuse any supply at all. This market dynamic, which is driven completely by the supermarkets' buying power in the market, places significant downwards pressure on prices. The merged entity would not be in a position to alter this market dynamic in any way.

66. Even if the merged entity's high market share in the barn-laid segment was of concern to its supermarket customers, there are steps that those customers could take to actively facilitate the development of competition in upstream supply markets. This could include sponsoring new entry or expansion through contractual arrangements if this was to bring further competition to the market in a way that would benefit customers (such as through lower prices). Supermarkets collectively represent approximately 60% of the market, and so have the scale to achieve these types of outcomes if necessary.

67. In short, any attempt by the merged entity to raise prices post-merger would readily be defeated by the supermarkets switching promotional slots or shelf space away from the merged entity and to competitors. Supermarkets control access to these aspects of the retail supply chain, who recognise the value of ongoing competition between their suppliers.

68. Importantly, the proposed merger will not result in consolidation of supply contracts with the merged entity (which exist in respect of supermarket private label brands). Instead:

(a) while Heyden Farms and Rasmusens both currently supply supermarkets through the IEP Co-op, and would be forced to give up the Pam's free range supply arrangements in order to pursue the merger as these supply arrangements are currently held by the IEP Co-op; and

(b) while Henergy does have private label supply contracts with both major supermarket chains, these arrangements are generally short-term and can be terminated largely at the supermarket's discretion for poor performance which is strictly (reflecting their market power as major customers).[14]

69. Countdown tenders to the market at least every three years for its private label supply. While Foodstuffs has not re-tendered barn-laid egg supply for its private label brands for some time, [ ]. The merged entity will need to compete on its merits to win or retain any private label supply contracts. The applicants estimate that private label supply in total represents only about [ ]% of the market. This suggests that while private label supply arrangements can help guarantee volume, they are not a major feature of the market in any case.

70. In any case, there is no realistic prospect that the market for the supply of major customers will be subject to any lessening of the competition as a result of the proposed merger. Only Henergy supply arrangements will be retained, and so there is no consolidation when compared to the counterfactual.

71. Retailer customers outside of the major supermarkets are also likely to continue to enjoy competitive wholesale prices. Smaller retail suppliers (dairies, butcheries and independent produce stores) compete in the retail market with supermarkets. While retail prices may be higher, there is a ceiling because supermarkets want to attract customers to buy from them. This in turn forces the wholesale price down to competitive levels across the market.

72. The other major customer segment is food service wholesalers. Food service businesses are major businesses who buy from producers and on-sell to hospitality and other clients. These food service wholesalers, such as Bid Food, Service Foods, ECLY, Produce Company and Food Chain, each have sufficient buying power that they are able to play producers off against each other in order to secure a favourable price in much the same way as supermarkets. Egg producers are effectively price takers with respect to supply of these customers, a dynamic that will only continue post-merger. Much like with supermarkets, there are no standing contracts or supply arrangement to guarantee volumes for producers, and a kind of spot market operates with respect to supply of these customers. Any attempt to raise prices to these customers will result in a loss of business.

FREE-RANGE EGGS: COMPETITION ASSESSMENT

Market shares and concentration

73. The market share of the merged entity post-merger is not significant enough to cause competition concerns in the free-range egg market. Henergy currently has approximately [ ]% market share. IEP has approximately [ ]% market share, putting Heyden Farms and Rasmusen's at approximately [ ]%. This puts the market share of the merged entity at around [ ]% of the market. In the context of a number of competitors in the market holding a similar or greater market share, including Zeagold with a market share of approximately [ ]% (which can be seen in the Aztec market data included as Appendix 3), this does not come within an area of

14 Example contractual terms are set out in Appendix 6.

concern according to the Commission's market concentration indicators. Accordingly, the proposed merger is unlikely to substantially reduce competition.

Other competition factors

74. In addition, the prevailing market dynamics in the barn laid egg market that suggest a lack of a substantial lessening of competition post-merger are largely present in the free-range egg market as well. This includes:

    (a) Actual and potential entry and expansion in the free-range egg market, including significant new entry by Zeagold. The applicants understand that Zeagold is currently in the advanced stages of securing land for a significant new free-range production facility in the upper North Island.This demonstrates the lack of genuine barriers to entry also applies with respect to the free-range segment of the market.

    (b) The very real countervailing buying power of supermarkets as major customers, which we have already demonstrated at length.

75. This provides a strong degree of comfort that the free-range egg market will remain competitive post-merger.

CAGED-FARMED EGGS: COMPETITION ASSESSMENT

76. Traditional caged-farmed eggs are more likely to be properly considered a separate product market category then barn-laid and free-range eggs. Of the parties to the proposed merger, Heyden Farms and Rasmusens currently produce and supply caged-farmed eggs. While we do not have access to reliable, independent market share data on the cage-farmed segment of the market, we estimate based on the total number of cage-farmed birds provided by the Egg Producers Federation that Heydon Farms currently has approximately [ ]% market share and Rasmusen's currently has approximately [ ]%. This puts the market share of the merged entity at around [ ]% of the market. This represents at best modest aggregation in this segment of the market and falls outside of the Commission's standard market concentration indicators.

77. In addition the competitor factors discussed above, including competitor pressure and countervailing buyer power, also apply in respect of the cage-farmed segment of the market. Accordingly, there is no substantial lessening of competition relative to the counterfactual.

LIQUID EGGS: COMPETITION ASSESSMENT

78. Liquid eggs are a distinct product, which are used in commercial cooking and food processing. Of the parties to the proposed merger, Heyden Farms and Rasmusens currently supply liquid eggs, but only in very small volumes.

79. Accordingly, there will only be very limited aggregation in the market for the supply of liquid eggs as a result of the proposed merger, and so no substantial lessening of

competition relative to the counterfactual. The applicants estimate that Zeagold/Mainland have an approximate market share of 99% of the pasteurised liquid egg market. In that market context there is no real prospect of any change in competitive dynamics.

Coordination and Vertical Effects of the Proposed Merger

Coordinated effects

80. No coordinated effects are likely to arise within the egg production industry, and in particular the wholesale supply of eggs, that would result in a lessening of competition.

81. While eggs may be treated as a commodity product:

    (a) there are a number of competitors in the relevant markets;

    (b) there are different business models, including co-operative structures;

    (c) there are different cost-structures, stemming from different approaches to upstream (supply chain) investment and integration;

    (d) the market is dynamic, with competitors gaining and losing market share in material volumes;

    (e) wholesale pricing transparency is low, as these are negotiated confidentially with major customers; and

    (f) the significant countervailing power of supermarkets as major customers would inhibit any attempt to co-ordinate on prices.

Vertical effects

82. The proposed merger would not result in the merged entity having any ability or incentive to:

    (a) foreclose to its competitors in upstream markets from being able to sell eggs to retail customers; and

    (b) foreclose to its competitors the supply of an input.

83. As discussed above, the only relevant aspect in terms of input markets is Rasmusens commercial supply of pullets, which is modest in scope and will not be the subject of any market consolidation. Accordingly, there is no risk of vertical anti-competitive effects arising out of the proposed merger.

Summary and conclusion

84. For the reasons explained in detail in this application for clearance, the proposed merger will not substantially lessen competition in any market (and however the relevant markets are defined).

85. Post-merger, the merged entity will face constraint from existing competitors, expansion and the risk of further new entry, and will be subject to the constraint of the buying power of major customers. The applicants therefore request that the Commission grant clearance for the proposed merger.

Confidentiality

Information provided in confidence

86. Confidentiality is sought in respect of the information in this application that is contained in square brackets and highlighted. Yellow highlight indicates information that is confidential to Heyden Farms. Green highlight indicates information that is confidential to Henergy. Pink highlight indicates information that is confidential to Rasmusens. Aqua highlight indicates information that is confidential to two or more of the applicants. This information is commercially sensitive to the parties to the proposed merger and is provided to the Commission in confidence.

Request for confidentiality under the Official Information Act

87. Confidentiality is sought in respect of the information referred to in the previous paragraph for the purposes of section 9(2)(b) for the Official Information Act 1982 on the grounds that:

    (a) the information is commercially sensitive and valuable information that is confidential to the parties to the merger transaction; and

    (b) disclosure would be likely to unreasonably prejudice that commercial position of the parties to the proposed merger, as the entities providing the information.

88. The parties request that they are notified of any request made to the Commission under the Official Information Act for release of confidential information, and that the Commission seek and consider the views of the parties as to whether the information remains confidential and commercially sensitive at the time responses are being considered.

Declarations

Declaration on behalf of Heyden Farms:

I, Gareth van der Heyden, have prepared, or supervised the preparation of, this notice seeking clearance.

To the best of my knowledge I confirm that:

- all the information specified by the Commission has been supplied;
- if the information has not been supplied, reasons have been included as to why the information has not been supplied;
- all information known to me that is relevant to the consideration of this notice has been supplied; and
- all information supplied is correct as at the date of this notice.

I undertake to advise the Commission immediately of any material change in circumstances relating to the notice.

I understand that it is an offence under the Commerce Act to attempt to deceive or knowingly mislead the Commission in respect of any matter before the Commission, including these documents.

I am a director/officer of the company and am duly authorised to submit this notice.

Gareth van der Heyden
Director

Signature	**Date**

Declaration on behalf of Henergy:

I, Mike Fleming, have prepared, or supervised the preparation of, this notice seeking clearance.

To the best of my knowledge I confirm that:

- all the information specified by the Commission has been supplied;
- if the information has not been supplied, reasons have been included as to why the information has not been supplied;
- all information known to me that is relevant to the consideration of this notice has been supplied; and
- all information supplied is correct as at the date of this notice.

I undertake to advise the Commission immediately of any material change in circumstances relating to the notice.

I understand that it is an offence under the Commerce Act to attempt to deceive or knowingly mislead the Commission in respect of any matter before the Commission, including these documents.

I am a director/officer of the company and am duly authorised to submit this notice.

Mike Fleming
Director

Signature	**Date**

Declaration on behalf of Rasmusen's:

I, Janette Rasmusen, have prepared, or supervised the preparation of, this notice seeking clearance.

To the best of my knowledge I confirm that:

- all the information specified by the Commission has been supplied;
- if the information has not been supplied, reasons have been included as to why the information has not been supplied;
- all information known to me that is relevant to the consideration of this notice has been supplied; and
- all information supplied is correct as at the date of this notice.

I undertake to advise the Commission immediately of any material change in circumstances relating to the notice.

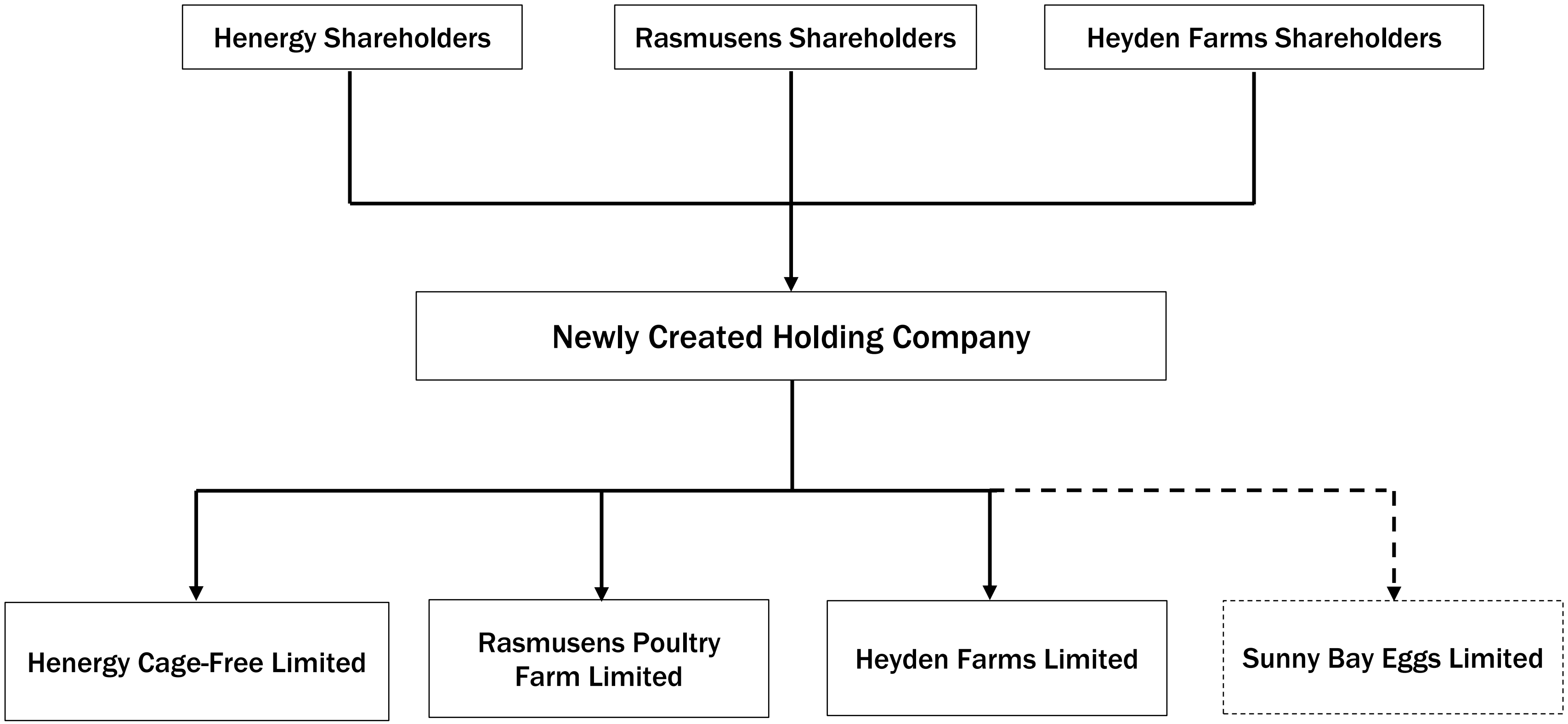
I understand that it is an offence under the Commerce Act to attempt to deceive or knowingly mislead the Commission in respect of any matter before the Commission, including these documents.

I am a director/officer of the company and am duly authorised to submit this notice.

Janette Rasmusen
Director

Signature	**Date**

Appendix 1: Merged entity proposed structure



Appendix 2: Pricing trends (see separate file)

Appendix 3: Aztec market data (see separate file)

Appendix 4: Market share tables (see separate file)

Note on quality of market share estimates: The applicants have only limited market share data available, especially in relation to smaller competitors. We have constructed market share tables representing the applicants' best guess of actual market share information at the Commerce Commission's request. While we anticipate that the Commission's own cross-checking with other industry sources will demonstrate that our estimates are reasonably accurate in 'big picture' terms, it is also likely to show some variance in the detail of our estimates.

Commission staff have also requested market share analysis on the basis of market value. The applicants simply have insufficient data to provide any meaningful estimates. While there are public statements suggesting the value of sector overall is $285 million per annum, there is no breakdown by production method.

Appendix 5: Freight costs (see separate file)

Appendix 6: Private label terms of supply (see separate file)

Appendix 7: Market contacts

Party	Contact details
Foodstuffs	[ ] [ ]
Progressive	[ ] [ ]
Bid Food	[ ] [ ]
Produce Company	[ ] [ ]
Andy Lucas Director of The Coffee Club	[ ] [ ]
Finest Foods	[ ] [ ]
Zeagold/Mainland	The applicants understand that the Commission will already have this information on file from previous market inquiries.
Otaika Valley	[ ]
Wholesome NZ	[ ] [ ]
Independent Egg Producers Co-operative	[ ] [ ]
Egg Producers Federation	[ ] [ ]

Appendix 8: Transaction documentation (see separate file)

Appendix 9: Additional documentation (see separate files)

9A: Henergy board papers assessing merger proposition

9B: Henergy competitor analysis

9C: Pre-transaction documents

Appendix 10: Schedule of confidential information (see separate file)