# COMMERCE ACT 1986: BUSINESS ACQUISITION

# SECTION 66: NOTICE SEEKING CLEARANCE

Date: 18 December 2002

The Registrar
Business Acquisitions and Authorisations
Commerce Commission
PO Box 2351
WELLINGTON

Pursuant to s66(1) of the Commerce Act 1986 notice is hereby given seeking **clearance** of a proposed business acquisition.

## PART I: TRANSACTION DETAILS

1. **What is the business acquisition for which clearance is sought?**

Clearance is sought for the proposed acquisition by Burns Philp & Company Limited (**Burns Philp**), or an interconnected body corporate of Burns Philp, of up to 100% of the ordinary issued share capital of Goodman Fielder Limited (**Goodman Fielder**) and, subject to disclosure to Burns Philp of the terms of Goodman Fielder's existing options, to the proposed acquisition of those options and any ordinary issued shares that may be issued pursuant to those options (the **Acquisition**).

Burns Philp acquired an initial tranche of 14.9% of the ordinary issued share capital of Goodman Fielder on-market on 12 December 2002. Burns Philp has given notice of a takeover bid for all the ordinary issued share capital of Goodman Fielder not already owned by Burns Philp. Attached as Appendix A are the announcements to the Australian Stock Exchange on 13 December 2002 relative to the acquisition of the initial tranche of shares in Goodman Fielder and the intention to make a conditional, off-market, cash takeover bid for the remaining issued ordinary share capital of Goodman Fielder.

2. **The Person Giving Notice**

This notice is given by Burns Philp.

Burns Philp requests that all correspondence and notices in respect of this application be directed in the first instance to:

Bell Gully
Royal & SunAlliance Centre
48 Shortland Street
P O Box 4199
Auckland

Telephone: 09 916 8800
Facsimile: 09 916 8801

Attention: Phil Taylor/Belinda Bagge
Email: phil.taylor@bellgully.com/belinda.bagge@bellgully.com

## 3. Confidentiality

Confidentiality is not sought for the fact of the proposed acquisition.

Confidentiality is sought for information contained in square brackets in this notice for the earlier of a period of two years from the date of this application or until Burns Philp advises the Commission that it may disclose the information.

The information that has been deleted is commercially sensitive and valuable information that is confidential to Burns Philp. Disclosure of that information could result in material financial loss and prejudice to the competitive position of Burns Philp and its interconnected bodies corporate. In this respect, Burns Philp relies on section 9(2)(b) of the Official Information Act 1982. The foregoing applies equally in respect of all additional information (expressed to be confidential) that Burns Philp may provide in relation to this application.

## 4. Details of the Participants

The participants are Burns Philp and Goodman Fielder.

The contact details for Burns Philp are as follows:

Burns Philp
Level 2, 44 Martin Place
Sydney NSW 2000
GPO Box 543

Sydney
NSW 2001
Australia

Telephone: 0061 2 9227 9371
Facsimile: 0061 2 9223 1234

Attention: Helen Golding, Company Secretary and Group Legal Counsel
Email: helen.golding@burnsphilp.com

The contact details for Goodman Fielder are as follows:

Goodman Fielder Limited
75 Talavera Road
Macquarie Park
NSW 2113
Australia

Telephone: 0061 2 8874 6000
Facsimile: 0061 2 8874 6099

Attention: Ian Gilmour, Company Secretary

## 5. Interconnected/associated bodies

### 5.1 *Acquirer group/associates*

Burns Philp is listed on the Australian and New Zealand stock exchanges.

A copy of Burns Philp's 2002 Annual Report is available at www.burnsphilp.com.

The only operating subsidiary in the Burns Philp group in New Zealand is New Zealand Food Industries Limited (**NZFI**) (100%). There are three other New Zealand subsidiaries (one holding and two non-operating).

Rank Group, through subsidiary companies, owns, on a fully diluted basis, 57.58% of the voting share capital of Burns Philp. It is the largest individual shareholder in Burns Philp. All other significant shareholdings belong to institutional investors. Rank Group is an interconnected body corporate of Burns Philp under the Commerce Act 1986.

Rank Group, through subsidiary companies, owns 100% of the shares in New Zealand Dairy Foods Limited (**NZDF**).

5.2 *Target Company/Goodman Fielder*

Goodman Fielder is listed on the Australian and New Zealand stock exchanges. Goodman Fielder's 2002 Concise Annual Report is available at www.goodmanfielder.com.au. Burns Philp is unaware of all of the relevant subsidiaries of Goodman Fielder.

Burns Philp is undertaking a full takeover bid for all the share capital of Goodman Fielder. No other company will own more than 10% of the shares in Goodman Fielder post acquisition. The takeover bid by Burns Philp is conditional on it obtaining at least 90% acceptances.

## 6. Pre-existing interest or entitlements or shares

Except in respect of the 14.9% of the issued ordinary share capital of Goodman Fielder already acquired by Burns Philp, no participant, or any interconnected body corporate thereof, already has a beneficial interest in, or is beneficially entitled to, any shares or other pecuniary interest in another participant.

## 7. Links between any participant/s including interconnected bodies corporate and other persons identified at paragraph 5 and its/their existing competitors in each market.

Rank Group, through subsidiary companies, owns 100% of the issued share capital of NZDF. NZDF distributes butter, butter-based products and olive oil-based spreads in New Zealand. Rank Group owns 57.58% of the issued share capital of Burns Philp (on a fully diluted basis). Burns Philp manufactures and distributes food ingredients and branded food products. Included in "food ingredients" is yeast (in both fresh and dry forms). Burns Philp manufactures yeast in both Australia and through NZFI in New Zealand.

Burns Philp, through its wholly owned subsidiary NZFI, makes bakery ingredient products (bread improvers & additives, muffin and other pastrycook premixes). NZFI estimates it has less than 8% market share in these products. These products or similar are available through Bakels New Zealand, George Weston Foods Limited (**Westons**), Goodman Fielder, Rivermill & Manildra Flour via JC Sherratts.

## 8. Common Directorships

Graeme Hart, the Deputy Chairman of Burns Philp, is also a director of NZDF.

## 9. Business activities of each participant

### 9.1 *Acquirer/Burns Philp*

Burns Philp is a global yeast and natural food ingredients manufacturer. Burns Philp has operations in over 20 countries and consumers in over 60 countries. Burns Philp manufacturers the following products:

- yeast (bakers' yeast, yeast extracts and speciality yeast products such as wine/brewers' yeast);
- bakery ingredients; and
- herbs and spices.

Burns Philp, through its wholly owned subsidiary NZFI, owns and operates a fresh yeast manufacturing plant in Auckland, which is the only yeast manufacturing plant in New Zealand. Currently, Burns Philp supplies all the fresh yeast utilised by the baking industry in New Zealand. No competition issues arise in respect of Burns Philp's bakery ingredients business (since Burns Philp only has a small market share) or its herbs and spices business (since there is no aggregation). Burns Philp has recently divested its vinegar business.

NZDF manufactures or supplies a range of dairy products for export and domestic consumption. NZDF manufactures Anchor and other branded products, specifically milk, creams, cheeses, yoghurt and dairy products. It acquires and distributes in New Zealand butters (plan, unsalted, light, spreadable, garlic, clarified and blended) from Fonterra under a long-term supply contract and distributes olive oil-based margarine.

### 9.2 *Target/Goodman Fielder*

Goodman Fielder is an Australian owned retail branded food company with operations in Australia, New Zealand and the Asia-Pacific region.

Goodman Fielder manufactures many of Australia's and New Zealand's well-known brands:

- Baking (e.g. Quality Bakers, Vogel's, Freya's and Ernest Adams);
- Edible oils (e.g. Meadow Lea, Sunrise, Olivani and Gold 'N' Canola); and
- Cereals and snacks (e.g. Uncle Toby's, White Wings and Bluebird)

10. **Reasons for the proposal and the intentions in respect of the acquired or merged business**

The proposed acquisition is to further Burns Philp's ongoing strategy of expanding its core business activities through selective acquisitions.

Burns Philp considers that a number of compelling strategic and financial benefits will arise from the proposed acquisition of Goodman Fielder. Burns Philp and Goodman Fielder will form a highly complementary merged entity.

Both companies operate in a broad spectrum of the supply of food products, selling both to food processors in the sale of ingredients and to retailers to whom branded consumer products are sold. Burns Philp sees the acquisition as an opportunity to consolidate both companies' strengths in all facets of food supply.

The proposed acquisition will substantially increase Burns Philp's revenue, facilitating future acquisitions. Burns Philp considers the proposed acquisition will provide it with a platform for broader participation in the consumer branded food and non-alcoholic beverages industries in Australasia.

Burns Philp believes that the proposed acquisition represents an opportunity for the performance of the existing Goodman Fielder businesses to be improved. Goodman Fielder's board has recognised the need to focus on productivity. Burns Philp considers that Goodman Fielder can benefit from Burns Philp's track record of achieving profitable growth through Burns Philp's disciplined strategic management approach.

Burns Philp's intentions for the Goodman Fielder business will be set out in detail in its Bidder's Statement, which will be provided to the Commission once lodged with the Australian Securities and Investments Commission. In summary, however, Burns Philp does not intend to dispose of any of the Goodman Fielder businesses or assets, and expects minimal rationalisation across business divisions (other than in respect of elimination of any duplicated head office functions), which would continue to operate independently on a day-to-day basis, with strategic direction provided by the Burns Philp board. On completion of the acquisition, Burns Philp will implement an immediate, broad-based, general review of Goodman Fielder's structure and operations, which it expects will identify opportunities to enhance the performance of the existing Goodman Fielder businesses, through a wide range of measures.

## PART II: IDENTIFICATION OF MARKETS AFFECTED

### Horizontal Aggregation

11. **Are there any markets in which there would be an aggregation of business activities as a result of the proposed acquisition? Please identify for each market the product, functional, geographic and time dimensions, the specific parties involved and the relationship of those parties to the acquirer or target.**

*Yellow spreads*

Goodman Fielder manufactures and distributes margarine and olive oil-based margarines in New Zealand. It is understood that most, if not all, Goodman Fielder margarine brands are manufactured in New Zealand. Burns Philp, through its interconnected body corporate NZDF, distributes butter, butter/margarine blends and olive oil-based margarine in New Zealand. Burns Philp considers that it competes with Goodman Fielder in the market for the distribution of yellow spreads in New Zealand.

Commerce Commission (**Commission**) precedent supports a market definition for the manufacture and distribution of yellow spreads in New Zealand, described in different decisions as yellow table spreads[1] and consumer spreads.[2] A market for yellow spreads includes butter, margarine, olive oil-based spreads, and butter/margarine blends.

In the *NewCo* Draft Determination (27 August 1999), the Commission referred to a variety of resources that concluded that butter and margarine are close substitutes. This conclusion is supported by the Commission's comments in various staff reports.[3] The

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1 Decision No. 156 *Fielder Gillespie Davis Limited*

2 Draft Determination – Proposed Dairy Co-operative Merger dated 27 August 1999.

3 Mainland Products/Kiwi Co-operative Dairies and Aspak Foods Limited/Abels Division and Unilever New Zealand Limited

adoption of a market for the supply of yellow spreads is also consistent with the approach taken by the Australian Competition and Consumer Commission (**ACCC**). When deciding not to intervene in the proposed merger of Bonlac Foods Limited and the New Zealand Dairy Board in 2000, the ACCC commented that there would be no major overlap in the market for dairy spreads and margarine.

The geographic market is national.

This application adopts a market definition that is consistent with Commission precedent, namely *a market for the supply of yellow spreads in New Zealand.*

However, Burns Philp notes that if the Commission adopted a narrower market definition and examined separate markets for the supply of butter and for the supply of margarine, the acquisition would not raise competition concerns.  If a narrower definition was adopted, the acquisition would result in only de minimus aggregation in respect of olive oil-based spreads (well within the Commission's safe harbour guidelines) and no aggregation in respect of separate markets for each of butter and margarine.

**Differentiated product markets**

12. **Are the products in each market identified in question 11  standardised or differentiated?**

Products in the yellow spreads market are differentiated by reference to whether they comprise:

- margarine;
- butter;
- olive oil; or
- butter/margarine blends.

The products in the market are also differentiated by branding.

13. **Characteristics of differentiated products**

While butter and margarine are substitutable, they are different products and have different promotional points.  For example, margarines emphasise softness.  While both butter and margarine are generally utilised for the same purposes, their manufacturing processes and cost bases are entirely different resulting in a clear differentiation. This differentiation helps competitors to compete by reference to those differentiation points. However, butter and margarine remain close substitutes.

**Vertical Integration**

14. **Will the proposal result in vertical integration between firms involved at different functional levels?**

The Acquisition raises a potential vertical integration issue in respect of Burns Philp's yeast manufacturing business and Goodman Fielder's bread baking business.

Vertical Integration itself is not a barrier to competition. However it may cause competition problems if market strength in one functional level of the market is extended or strengthened into another functional level because of the vertical integration. The Commission's Practice Note identifies the four main competition concerns that may be raised by vertical integration:

- facilitation of co-ordination effects;
- foreclosure of entry into one or other of the vertical levels affected;
- increase of entry barriers; and
- access concerns.

In Burns Philp's view, the potential vertical aggregation issue arising from the Acquisition will not have the effect of substantially lessening competition in a market because:

- of the real constraint imposed by the threat of imports;
- of the countervailing power exercised by trans-Tasman bakeries in respect of their purchases of fresh yeast in Australia;
- of the ability of users of fresh yeast to switch to dry yeast; and
- it would not be profit-maximising behaviour to selectively increase the price of fresh yeast to users given the limited cost that yeast comprises in a loaf of bread against the economic detriment of the risk of loss of volume sales.

Burns Philp is the sole New Zealand manufacturer and distributor of fresh yeast and one of a number of distributors of imported dry yeast. That market position will not change as a result of the Acquisition. Yeast is an essential input in bread baking.Goodman Fielder participates in the market for manufacture and distribution of bread and other bakery products and is a significant industrial consumer of fresh yeast in relation to that business. Burns Philp understands that Goodman Fielder does not use dry yeast within New Zealand.

Goodman Fielder is one of the three large industrial bakers in New Zealand. Yarrows (The Bakers) Limited (**Yarrows**) is based in New Plymouth, Taranaki and Australian baking company, Westons, through subsidiary companies, has a large industrial bakery in Auckland and smaller bakeries nationwide. Goodman Fielder also competes with Rivermill, supermarket in-store bakeries, franchise groups (such as Bakers Delight) and other small bakeries and hot bread shops.

*Fresh and Dry Yeast*

Yeast is a living organism of the fungi family grown through a fermentation process beginning with a small quantity of yeast and key inputs of molasses, oxygen and other nutrients. Commercial quantities are produced over one to two days. Excess water is then removed to produce different forms of yeast.

Bakers yeast is produced in fresh (also known as “wet” yeast) and dry forms. Fresh yeast has a short life of approximately 2 to 4 weeks. During transportation, fresh yeast needs to be refrigerated. Dry yeast has a considerably longer life of up to 2 years.

Cream yeast, in a liquid form, is sold in 10,000 litre truckloads and is used by larger, automated bakeries. In New Zealand, Goodman Fielder, Westons and Yarrows are the only bakeries large enough to accept cream yeast. Goodman Fielder and Westons are located in Auckland and Yarrows in Taranaki.

Stabilised cream yeast is created by adding a stabilising gum and is sold in 1,000 litre vats to smaller industrial bakers. There are currently ten bakeries using stabilised cream yeast - six are owned by, or associated with, Goodman Fielder, three are owned by, or associated with, Westons and one is owned by an independent.

Compressed yeast, also called crumbled or block yeast, is created by the removal of water from cream yeast. It is usually sold in 18 kg cartons of 1 kg blocks and is generally used by smaller bakeries.

Dry yeast (created by an additional drying process) is more concentrated than fresh yeast and provides approximately 3 times the leavening for bread and bakery products as the same quantity in weight of fresh yeast. By weight, fresh yeast consists of up to 70% water, whereas the water in dry yeast can be as little as 8% of its weight. This results in a higher activity level for dry yeast. In this application dry yeast volumes are given as a fresh yeast equivalent (**Y30 Equiv**.) so that proper comparisons can be made between fresh and dry yeast.

**Table 1**

**NZFI Fresh and Dry (Bakers) Yeast Sale Volumes (Year Ending June 2002)**

| **Product** | | **Tonnes (at Y30 Equiv.)** |
|---|---|---|
| Fresh | Cream | 1,688 |
| | Stabilised Cream | 1,419 |
| | Compressed | 1,824 |
| | **Total** | **4,931** |
| Dry Bakers | Imported Dry | 171 |
| | ADY, Surebake, Supabake | 260 |
| | **Total** | **431** |

Based upon NZFI sales to June 2002 and current import statistics, the total market for fresh and dry bakers yeast by end users is estimated below.

**Table 2**

**Total Market for Fresh and Dry Yeast by End Users**

| All volumes Y30 Equiv tonnes | **Fresh Bakers Yeast** | | | | Dry Yeast (Y30 Equiv) | Total |
|---|---|---|---|---|---|---|
| | Liquid Cream | Stabilized Cream | Compressed | Sub Total | | |
| Goodman Fielder * | [ ]<br>[ ]% | [ ]<br>[ ]% | [ ]<br>[ ]% | 2,023<br>41% | | 2,023<br>34% |
| George Weston Foods | [ ]<br>[ ]% | [ ]<br>[ ]% | [ ]<br>[ ]% | 892<br>18% | | 892<br>15% |
| Yarrows | [ ]<br>[ ]% | | [ ]<br>[ ]% | 645<br>13% | | 645<br>11% |
| Other Independents, Supermarkets & Other Hot Bread Shops | | 241<br>17% | 1,130<br>62% | 1,371<br>28% | 678<br>72% | 2,049<br>35% |
| Retail dry yeast supplied by NZFI | | | | | 260<br>28% | 260<br>4% |
| | 1,688<br>100% | 1,418<br>100% | 1,824<br>100% | 4,931<br>100% | 938<br>100% | 5,869<br>100% |

Goodman Fielder's volumes include purchases by the 4 contracted bread manufacturers – Northern Bakeries, Breadcraft, Walter Findlay and Findlays Gisborne. These manufacturers produce bread under Goodman Fielder brands.

*Market Definition*

In Decision 201A[4], the Commission concluded that dry yeast did not "provide discipline upon wet [fresh] yeast". Burns Philp note that:

- although dry yeast is more expensive than wet yeast, this can be explained by its higher activity levels; and
- dry yeast is used more extensively by bakeries now than it was in 1987. For example, Progressive Enterprise's supermarkets now use dry yeast in their in-house bakeries instead of fresh yeast.

For these reasons, Burns Philp is of the view that fresh and dry yeast are readily substitutable and therefore compete with each other in a market for the supply of yeast.

*Yeast Pricing*

Because of the higher activity of dry yeast, dry yeast prices per unit of weight are approximately 3 times those of fresh yeast. Average end user prices for fresh yeast in New Zealand (Australian comparative prices are added in brackets) currently range between $[ ] to $2.20 per kilogram (AU$[ ] to AU$1.45) and for dry yeast range between $[ ] to $6.00 per kilogram (AU$[ ] to AU$4.40). Broken down by segment, prices (per kilogram) are:

- cream yeast NZ$[ ] - NZ$[ ];
- stabilised cream yeast NZ$[ ] – NZ$[ ];
- compressed yeast NZ$[ ] – NZ$2.20; and
- dry yeast NZ$[ ] – NZ$6.00.

*Fresh Yeast Market*

Currently, Burns Philp is the sole manufacturer and distributor of fresh yeast in New Zealand through its subsidiary NZFI. Presently, no fresh yeast of any form is imported into New Zealand.

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4 Goodman Fielder Limited and Wattie Industries Limited, 14 May 1987

Compressed yeast users and stabilised cream yeast users can readily interchange between those products and dry yeast, which is readily available and priced competitively relative to fresh yeast (for further details relating to dry yeast see discussion later in this section). While stabilised cream yeast offers some handling advantages to bakeries, pricing of the product is constrained by the acquirer's ability to switch to dry or compressed yeast.

De Novo entry into the fresh yeast market is unlikely. Burns Philp considers there is only a low possibility of a firm opening a competing fresh yeast manufacturing plant in New Zealand.

In Decision 201A[5] the Commission found, based on the market conditions that then existed, that "[i]mports of [fresh] yeast are not feasible as the product[s] is bulky and expensive to transport relative to its value". Burns Philp believes that as a result of changes in market and transportation conditions, it is now feasible and practical to import fresh yeast (both cream and compressed) from Australia into New Zealand on a competitive basis.

*Changes in market conditions*

Since Decision 201A in 1987, three significant changes have occurred in Australasia:

- Importantly, in 1994 Bakels-Lesaffre Yeast Pty Limited (**Bakels** or **BLY**), a joint venture owned by Societe Industrielle Lesaffre (a French company, one of the largest yeast manufacturers in the world and a global competitor of Burns Philp) and Australian Bakels Pty Limited, entered the Australian fresh yeast market. The joint venture has a modern and efficient fresh yeast manufacturing plant in Melbourne. Bakels now have 50% of the fresh yeast market in Australia. When the plant opened it had a capacity of 26,000 tonnes and its current spare capacity is estimated as sufficient to supply twice the total New Zealand market. In Australia, it supplies cream yeast to large bakeries in Perth (Western Australia) by train from its Melbourne plant. Both Bakels and Burns Philp supply compressed yeast to Perth (Burns Philp from its Sydney plant). The distance between Melbourne and Perth is greater than the distance between Melbourne and Auckland. Since 1994 when Bakels entered the Australian market, cream yeast prices have decreased over 20% in nominal terms and by even more in real terms. This has increased the price differential between

5 14 May 1987 *Goodman Fielder Limited And Wattie Industries Limited*

Australia and New Zealand for fresh yeast but because of the decrease in price, prices have not increased in New Zealand in the last 4 years.

- Generally, shipping costs between Australia and New Zealand have reduced since 1987 due to reduced union power and the introduction of greater competition. There have been reductions of up to 50% in the cost of dry container shipping since 1987. Additionally, within the last 5 years the “Flexitank” concept has evolved from New Zealand whereby a bladder is used inside a refrigerated container to ship food grade liquid products. This concept is much cheaper than the dedicated stainless steel refrigerated tanks. Therefore, shipping rates are much lower and shipping options are more flexible and cheaper.

  Burns Philp currently and successfully exports fresh compressed yeast from Vietnam to Thailand. Since starting production in Vietnam in July 2000, Burns Philp has become the market leader for compressed yeast in that country and sends over 350 tonnes of compressed yeast per annum via refrigerated containers on ships to Thailand from Vietnam. The product has a 4 week shelf life and shipping takes approximately 5 days from factory to market. Burns Philp has also shipped fresh cream yeast using refrigerated tank containers from China to Japan.

- Tariffs on yeast, which the Commission said in Decision 201A averaged 10% in 1987, no longer exist.

*Importation of Fresh Yeast into New Zealand*

To supply cream yeast into New Zealand from Australia, Bakels would need to provide a cream yeast holding station in Auckland. The purpose of such a station is to receive the imported yeast transported from Australia in 20,000 litre tanks (similar in size to a 20 foot container), put the cream yeast into the holding tank and then deliver it to end users as required. Bakels already use holding stations in Perth and Sydney. Burns Philp estimates that a holding station would involve a capital investment of NZ$360,000 with an annual operating cost of NZ$150,000 including depreciation.

Assuming Bakels would supply Westons and Yarrows based on pricing ex-factory in Australia (similar to other large users in the Australian market), and based on the price differential between New Zealand and Australia, Bakels could supply cream yeast and compressed yeast at a competitive price to NZFI. Attached as Appendix B is a detailed calculation of this import option including a shipping quotation and a breakdown of the costs associated with a cream yeast holding station.

Also attached as part of Appendix B is the same calculation but based totally on supply to Yarrows.

Compressed yeast has a shelf life of up to four weeks. Burns Philp considers it feasible and practical to transport compressed yeast by refrigerated container from Melbourne to Auckland and Christchurch for supply New Zealand-wide.

Based on pricing for large compressed yeast users in Australia (AU$0.96 per kilogram or NZ$1.06), Bakels can ship compressed yeast to New Zealand and supply existing users at current market prices. Bakels would achieve similar profit margins ex-factory as it achieves in Australia (see Appendix B). Bakels' prices in Australia are lower than prices in New Zealand due to a number of factors, including lower input cost (molasses) and a more efficient, modern manufacturing plant.

As NZFI is based in Auckland and has no plant elsewhere in New Zealand, internal distribution costs associated with transportation of fresh yeast supplied by Bakels would be the same as the costs applying to NZFI product.

*Importation is a current constraint*

The ability for Bakels to import cream yeast into New Zealand has been enhanced by the increase in price differentials between Australia and New Zealand and by modern transportation impacts. Indeed, in June 2001, Goodman Fielder negotiated a price reduction with NZFI of 3% based on the "threat" of Goodman Fielder importing fresh yeast from Bakels in Australia. Goodman Fielder ensured that the New Zealand price for fresh yeast was effectively capped at the cost of buying fresh yeast in Australia and shipping it to New Zealand. This negotiation indicates that importation of fresh yeast has been a real constraint on NZFI's pricing for some time. As stated previously the impact of falling fresh yeast prices in Australia since 1994 has led to flat prices for fresh yeast in New Zealand for at least the last 4 years.

For the first time in four years, Burns Philp is seeking increases for fresh yeast in New Zealand.

Goodman Fielder's competitors in the bread baking market are principally Westons (throughout New Zealand) and Yarrows (Taranaki). Other competition derives from independent bakers, supermarket in-house bakeries and hot bread franchises and shops.

Baker's yeast represents less than 4% of the cost of a loaf of bread and therefore has only a minor impact on the overall pricing of bread in the market place. The key ingredient with the largest impact on cost is flour. NZFI is an independent, profitable business but with material fixed costs. Its profit-maximising incentive is to continue supplying the New Zealand market on an even-handed basis. There are no incentives to differentiate between bakers, regardless of ownership. Indeed there is a disincentive as such activity is likely to encourage the entry of imports from Bakels. As Appendix B indicates, any increase in price of about 5% is likely to see entry by Bakels. Further, because the price of yeast per loaf of bread is so small, there can be no incentive to give a price advantage relative to the purchase of yeast to Goodman Fielder. Such an advantage would not provide Goodman Fielder with a pricing edge over its baking competitors.

*Countervailing Power*

In any event, if Burns Philp were to discriminate against Westons in the New Zealand market for supply of fresh yeast, Westons, which is a major customer of Burns Philp in Australia, would use that relationship (and the threat to switch to Bakels) to discipline Burns Philp in New Zealand. In Australia, Westons purchases over 4 times the volume of fresh yeast from Burns Philp than it purchases in New Zealand.

*Dry Yeast*

In Decision 201A in 1987 the Commission found, based on the market at the time, that "dry yeast has been used by three bakers only in New Zealand". Today the picture is much different with many smaller bakers using dry yeast including supermarket in-house bakeries. NZFI estimates that dry yeast accounts for 40% of the yeast used in New Zealand after excluding the fresh yeast used by Goodman Fielder, Westons and Yarrows, the three large industrial bakers.

Dry yeast supplied for baking in New Zealand by NZFI is principally imported from Burns Philp factories in Vietnam and Australia. NZFI manufactures limited quantities of dry yeast in the form of active dry yeast, Surebake and Supabake. Active dry yeast and Surebake is sold to Goodman Fielder (Bluebird) for repacking for retail sale for use in home baking and Supabake is wholesaled to other customers for the same purpose. NZFI also markets some other dry yeast products principally sold to industrial customers for food flavouring.

NZFI has 100% of the bakers fresh yeast segment and 91% of the overall yeast market.

Following is a table setting out the countries exporting dry yeast to New Zealand in the 12 months to October 2002. In this table, NZFI imports are those from Australia and Vietnam. Imports from France are sourced from Societe Industrielle Lesaffre, a global dry yeast supplier, which is distributed in New Zealand by Bakels New Zealand under the Bake Safe brand. Bakels New Zealand have a Penrose, Auckland based bakery ingredients operation. Imports from the Netherlands are sourced from DSM Bakery Ingredients (**DSM**), which is also a global dry yeast supplier. This yeast is distributed in New Zealand by Champion Flour Mills, a division of Goodman Fielder.

**Table 3**

**Importation of Dry Yeast by Country of Origin Year to October 2002**

| Origin | Dry Yeast Tonnes (Y30 Equiv) |
|---|---|
| Australia | 75 |
| France | 144 |
| Netherlands | 318 |
| Vietnam | 99 |
| Others | 42 |
| | 678 |

Attached as Appendix C is a table of dry yeast imports into New Zealand sourced from Statistics New Zealand. This table confirms the increasing importation of dry yeast into New Zealand by DSM. Imports by NZFI are identified on the right-hand side of the table.

Dry yeast usage in New Zealand has been reasonably stable at around 650 tonnes (Y30 Equiv) for the last three years. It is NZFI's opinion that the formal import statistics for the prior years 2001 and 2002, are incomplete as they do not include certain imports for NZFI from Australia in those years. When adjusting the figures in Appendix C for this, the imports have been reasonably stable.

While imports have been stable, NZFI imports have fallen since 1999 as the Woolworths in-store bakery business was transferred from dry yeast imported by NZFI to NZFI compressed yeast during 1999. On the other hand, the imports by DSM have increased due to the switch of Progressive Enterprises' in-store bakeries from NZFI compressed yeast to DSM dry yeast in early 2000. These two changes by the major supermarket groups tend to net out in the total figures. Burns Philp considers it likely that DSM will appoint an alternative distributor of its product as a result of the Acquisition. In Australia, DSM dry yeast is distributed by Weston Milling, part of the George Weston Group.

The impact of dry yeast as a price controller on compressed yeast can be seen in a recent 4% price reduction given to Progressive's Woolworths chain as they are currently giving consideration to switching to imported dry yeast from DSM.

*Baking ingredients*

Bakery ingredients makes up a diverse group of food ingredients used in the baking industry. It includes yeast, which is discussed separately above.

In respect of the remainder of the bakery ingredients market, Burns Philp believes that it has an estimated 8% of that market in New Zealand and estimates that Goodman Fielder would have in the region of 30% of that market. Of the balance, it believes Bakels New Zealand would also have in the region of 30%, with the remainder being held by a diverse number of participants.

Because is it not a significant participant in the bakery ingredients market, Burns Philp does not have certain knowledge of market share details or of all of the participants. From the information it does have, it believes that the market is an unconcentrated market and that accordingly the combination of Burns Philp and Goodman Fielder would fall within the Commission's safe harbour guidelines. On that basis, Burns Philp makes no further submissions, but is happy to answer questions put to it by the Commission.

15. **Acquisitions of assets of a business or shares involving either participant in the last three years (whether or not notified to the Commission).**

In 2002 National Foods Limited applied to the Commission for clearance to acquire NZDF. Clearance was declined. Rank Group purchased NZDF. Subsequently, the Commission reversed its findings relative to the issue of "associated persons".[6]

Burns Philp is unaware of any other acquisition, whether notified to the Commission or not, that is relevant to the Application.

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[6] Decisions 459 and 459A

## PART III: CONSTRAINTS ON MARKET POWER BY EXISTING COMPETITION

**The Market for the Supply of Yellow spreads in New Zealand**

### Existing Competitors

16. **In the market or markets, who are the suppliers of competing products, including imports?**

In terms of supply of yellow spreads in New Zealand, as noted above, Burns Philp is interconnected with NZDF. NZDF distributes Anchor and other branded butter products that are manufactured under contract by Fonterra, including:

- Anchor Butter;
- Anchor Unsalted Butter;
- Anchor Lite;
- Anchor Spreadable;
- Anchor Garlic Butter;
- Anchor Clarified Butter;
- Fernleaf Butter; and
- Fernleaf Semisoft Butter.

The following products are manufactured for NZDF by Bakels Edible Oils:

- Anchor Country Soft;
- Anchor Country Soft Lite; and
- Avezzo Margarine.

Goodman Fielder manufactures and markets the following yellow spreads (all being margarines):

- Meadow Lea ;

- Sunrise;
- Olivani;
- Gold 'N' Canola;
- Choice;
- Slimarine; and
- Logicol.

Direct competitors in terms of the supply of yellow spreads include:

(a) Mainland, which is owned by Fonterra. Mainland manufactures and supplies butter and butter/margarine blend products.

(b) Unilever plc, which is an international public company based in London and Rotterdam. Unilever's most significant yellow spreads brand is Flora margarine, which is recognised as driving price in the margarine segment of the yellow spreads market. Unilever also supplies Olivio and I Can't Believe it's Not Butter.

(c) Bonland, which is a joint venture between Mainland and Bonlac, the latter being an international company. Bonland supplies Bonlac Dairy Smooth Blend (butter/margarine blend) which is manufactured in Australia.

(d) Universal Foods, which distributes butter primarily to Foodstuffs in the lower North Island.

(e) Dairymaid which distributes butter primarily to Pak N Save in Wellington.

Of the foregoing both Unilever and Fonterra are massive global competitors having major financial resources, skill and market knowledge. Alone, they would totally constrain the merged entity.

The market shares of the key participants in the consumer spreads market, based on volume and value of sales, is set out in Table 4.

**Table 4**

**Yellow Spreads Market Shares**

| | **Total Yellow Spreads** | | **Total Yellow Spreads** | |
|---|---|---|---|---|
| | **Value of Sales ($)** | **%** | **Volume of Sales (kilograms)** | **%** |
| Burns Philp (NZDF) | 29,409,109 | 20.3 | 5,735,609 | 19.1 |
| Goodman Fielder | 40,323,050 | 27.9 | 8,102,837 | 27.0 |
| Mainland | 13,971,027 | 9.7 | 3,025,991 | 10.1 |
| Unilever | 25,345,849 | 17.5 | 4,268,507 | 14.2 |
| House Brands | 30,989,000 | 21.4 | 7,884,100 | 26.2 |
| Universal Foods | 2,570,878 | 1.8 | 648,213 | 2.2 |
| Dairymaid | 878,464 | 0.6 | 231,075 | 0.8 |
| Bonlac | 433,468 | 0.3 | 79,938, | 0.3 |
| **Total** | 144,602,637 | 100 | 30,040,736 | 100 |

While 100% of the butter house brands are supplied by NZDF, Burns Philp can only estimate the supplies of margarine based house brands. Burns Philp believes that Goodman Fielder supplies approximately 25% of the margarine based house brands (Foodstuffs Auckland). It is unclear as to the supplier of the remaining margarine based house brands.

The market share information is based on A C Nielsen data provided by NZDF. This data includes grocery key accounts only (excludes oil, food services and route channels).

In addition to suppliers, Bakels Edible Oils Limited (a subsidiary of the Bakels Group) manufactures olive oil-based margarine and the butter/margarine blends for NZDF. Burns Philp is unable to establish what other brands Bakels Edible Oils currently toll manufactures, however it believes Bakels Edible Oils Limited may manufacture some housebrands.

Margarine, and to a lesser extent butter, are imported into New Zealand. Unilever currently imports all of its margarine products. Accordingly, at least 14.2% of the volume, and 17.5% of the value, of the yellow spreads sold to key grocery accounts is imported. These figures exceed the 10% threshold specified by the ACCC as sufficient to render a substantial lessening of competition unlikely.[7]

Bonland also imports its products, including Western Star Butter, from Australia. Small quantities of butter are imported into New Zealand by others such as Lurpak (5,860 kilograms at a total of $94,253). Certain house brands may also be imported to New Zealand. These imports are not included in the above figure.

Burns Philp does not believe that there are any material restrictions on imports increasing in response to increased demand.

**Conditions of Expansion**

17. **Market conditions**

The Court of Appeal *in Commerce Commission v The Southern Cross Medical Care Society*[8] noted that:

> "[w]hatever the size of the merged entity's market share, it is elementary that its market power will not be insufficiently [*sic:* sufficiently] constrained unless there are barriers to entry or expansion which protect it from effective rivalrous reaction to the exercise of its market power."

and:

> "What level of market power a firm has, as a result of its market share, will depend substantially on the level of barriers to entry and expansion which apply to the market. If the barriers are low, a high market share is unlikely to result in an insufficiently constrained level of market power."

Burns Philp is of the firm view there are few, if any, entry or expansion conditions, taking into account the ability to import, that would hinder new entry or further expansion by local or overseas butter or margarine suppliers. More importantly, many of the participants in the yellow spreads market are major firms, some of them international in

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7 ACCC Merger Guidelines para 5.111.

8 Court of Appeal 21 December 2001 CA 89/91 at page 39

nature (including Fonterra) with the ability and capacity to expand their supply in or into the New Zealand market in accordance with demand. While the combined market share of Burns Philp and Goodman Fielder will be relatively high, any attempt to impose a *ssnip* would meet with an immediate response from incumbents.

Fonterra exports significant quantities of yellow spreads, some of which could be easily diverted to the domestic market if Burns Philp attempted to impose a *ssnip* post-acquisition. The constraint imposed by such an "export diversion strategy" was accepted by the Commission as recently as August 2002[9].

18. **Please name any business which already supplies the market – including overseas firms – which you consider could increase supply of the product concerned in the geographic market by diverting production into the market, increasing utilisation of existing capacity and/or expanding of existing capacity.**

All of the participants in the market identified in Table 4 above have the ability to increase supply to meet demand including, as discussed above, Fonterra, by diverting exports into the domestic market.

19. **Of the conditions of expansion listed above, which do you consider would influence the business decision in each case to increase supply?**

Nil.

20. **How long would you expect it to take for supply to increase in each case?**

No appreciable delay - the period of manufacture and transportation following receipt of an order.

21. **In your opinion, to what extent would the possible competitive response of existing suppliers constrain the merged entity?**

Competitive response would be an absolute constraint upon the merged entity.

22. **Looked at overall, and bearing in mind the increase in market concentration that would be brought about by the acquisition, to what extent do you consider that the**

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9 Decision 468, Fletcher Challenge Forests/Central North Island Forest Partnership at para 261.

**merged entity would be constrained in its actions by the conduct of existing competitors in the markets affected?**

See answer to previous question 21 above.

**Co-ordinated Market Power**

23. **Identify the various characteristics of the market that, post-acquisition, you consider would either facilitate or impede co-ordination effects.**

The following key factors impede co-ordination in the market for the supply of yellow spreads:

- the market is characterised by differentiated products and therefore it is more difficult for participants to agree on a price. The different cost structures for margarine and butter emphasise this feature;
- new firms, through importation, and locally (see Dairymaid as an example), can enter the market relatively quickly;
- there are a significant number of fringe competitors , such as Universal Foods (2.2%), Dairymaid (0.8%) and Bonlac (0.3%) which could expand their distribution of New Zealand products and importation of competing products with minimal delay – defeating any attempt to tacitly increase price;
- there is no record of the industry price-fixing or undertaking other forms of collusion. The former Dairy Board Act provided the Dairy Board with the power to control price for butter in domestic New Zealand.

On balance, from the factors discussed above, the Acquisition is unlikely to materially enhance the scope for co-ordinated behaviour.

24. **Identify the various characteristics of the market that, post-acquisition, you consider would facilitate or impede the monitoring and enforcement of co-ordinated behaviour by market participants.**

The following characteristics of the yellow spreads market impede the ability of firms to monitor and punish deviations from a hypothetical collusive arrangement between the participants:

- the costs of firms differ, especially in relation to the manufacture of butter compared to margarine; and
- vertical integration exists in relation to Fonterra.

Burns Philp considers the different cost structures and inputs of market participants (particularly taking into account imports) makes it difficult to monitor and punish deviations from a hypothetical collusive arrangement.

25. **Indicate whether the markets identified in paragraph 9 above show any evidence of price co-ordination, price matching or price following by market participants.**

The yellow spreads market is very competitive and participants react to competitors' prices. To Burns Philp's knowledge, there is no evidence of price co-ordination, price matching or price following by market participants that would suggest the existence of tacit collusion.

26. **Please state the reasons why, in your opinion, the transaction will not increase the risk of co-ordinated behaviour in the relevant market(s).**

The market characteristics identified in response to question 23 of this application prevent the Acquisition from increasing the risk of co-ordinated behaviour in the relevant markets. Market participants, because of the presence of imported products, are unlikely to reach a collusive arrangement or understanding. Even if they were able to do so, they would be unlikely to maintain the internal discipline that would be needed to keep the understanding intact, particularly given the threat of new entry and the ease of expansion. Moreover, approximately 95% of the retail sales of yellow spreads are made through supermarket chains with major countervailing power.

## PART IV: CONSTRAINTS ON MARKET POWER BY POTENTIAL COMPETITION

27. **Which conditions do you consider would be likely to act as a barrier to entry of new competitors**

See 29 below.

28. **Please name any businesses which do not currently supply the market but which you consider could supply the relevant market.**

See 29 below.

29. **What conditions of entry do you consider would most influence the business decisions to enter in each case?**

See responses to questions in Part III above. Any of the global manufacturers or suppliers of yellow spreads could enter the market with minimal delay in response to supra-competitive pricing by the merged entity. The following key Australian manufacturers of butter and margarine could begin supplying yellow spreads in New Zealand:

- Peerless (industrial producers of margarine). Peerless manufactures Tablelands as its branded margarine.They have indicated they have the ability/capacity to produce “house brand” margarine;
- Dairy Farmers, (large industrial manufacturer of butter);
- Norca (NSW) (butter manufacturer);
- Tatura Milk Industries (butter manufacturer);
- Warrnambool Cheese and Butter Factory (manufactures Sungold butter); and
- Murray Goulburn – Devondale is their key brand (butter manufacturer).

Approximately 95% of the total yellow spreads market is sold through supermarket chains which have major countervailing power with the ability to encourage alternative supply arrangements with incumbents and/or potential entrants.

**Likelihood, Sufficiency and Timeliness of Entry**

30. **How long would you expect it to take for entry to occur, and for market supply to increase, in respect of each of the potential business entrants named above?**

No appreciable delay.

31. **Given the assessed entry conditions, and the costs that these might impose upon an entrant, is it likely that a potential entrant would consider entry profitable at pre-acquisition prices?**

If Burns Philp increased prices pre-acquisition an entrant would consider entry profitable, particularly if encouraged by the offer of a supermarket contract.

32. **Would the threat of entry be at a level and spread of sales that it is likely to cause market participants to react in a significant manner?**

Yes, particularly in response to a contract offered by a large supermarket chain.

33. **What conditions of entry do you consider would influence the business decision to enter the market by setting up from scratch, i.e. de novo entry?**

The ability to import products without constraint and at competitive prices renders discussion of conditions of entry inapplicable in this market.

34. **How long would you expect it to take for de novo entry to occur?**

De novo entry has occurred recently in the market for supply of yellow spreads. Niche players Universal Foods and Dairymaid have been able to source and supply butter to supermarkets such as Pak N Save in Wellington and lower North Island Foodstuffs outlets.

35. **In your opinion, to what extent would the possibility of de novo entry constrain the merged entity?**

Given existing incumbent restraint and the countervailing power of supermarkets, it is anticipated that de novo entry is not a major constraint, although it could possibly become so if market conditions changed.

## PART V: OTHER POTENTIAL CONSTRAINTS

### Constraints on Market Power by the Conduct of Suppliers

36. **Who would be the suppliers of goods or services to the merged entity in the relevant market?**

The conduct of suppliers is unlikely to constrain Burns Philp and Goodman Fielder post-Acquisition.

37. **Who owns them?**

Not applicable.

38. **To what extent would the conduct of suppliers constrain the merged entity?**

Not applicable.

### Constraints on Market Power by the Conduct of Acquirers

39. **Who would be the acquirers of goods or services supplied by the merged entity in each of the markets identified in questions 11 and/or 14?**

Acquirers included supermarket chains, oil companies and route trade.

40. **Who owns them (where appropriate)? Please list as follows.**

All of the principal supermarket chains and oil companies are well known to the Commission. See also response to question 41.

41. **In your opinion to what extent would the conduct of acquirers of goods or services to the merged entity constrain the merged entity in each affected market? How would this happen?**

The Commission has considered the countervailing market power of supermarkets in previous Decisions[10]. In Decision 390, which concerned the acquisition by Polarcup (NZ) Limited of the plastic packaging business of Carter Holt Harvey Limited, in respect of the foam tray market the Commission stated:

> "138. The main buyers of the foam trays are the supermarket chains, which include those operated by Progressive Enterprises, Woolworths Ltd, and the Foodstuffs Group. These purchasers account for between 80% and 90% of all purchases of food trays. By virtue of their size, these supermarket chains would have countervailing power and could provide some constraint on the behaviour of the merged entity if it attempted to exercise market power.
>
> 139. It has been noted that supermarkets operate in a very competitive low margin, high volume environment, so are not necessarily loyal to suppliers. As such, their profitability is sensitive to their input costs. Price is an important factor in their decision to purchase. They are apparently prone to shifting with any changes in price, assuming they have a suitable product to change to."

In Decision 401, which concerned the acquisition by Montana Group (NZ) Ltd of up to 100% of Corban Wines Ltd, in respect of the national markets for the:

- production or importation of white wine for distribution;
- production or importation of red wine for distribution;

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10 Decisions 390, 401, 406, 418 and 459 (amongst others).

- production or importation of sparkling wine for distribution; and
- distribution of wine,

the Commission concluded that supermarkets were likely to exert significant countervailing power because:

- supermarkets were a very important distribution channel for suppliers to these markets;
- purchasers in the supermarket distribution channel were highly concentrated;
- the costs of switching supply were low; and
- alternative supply was readily available.

In this case, approximately 95% of the total volume of yellow spreads sales are conducted through supermarket chains. Accordingly, by virtue of the size of their demand, supermarkets do and will continue to exercise considerable countervailing power over suppliers.

Supermarkets are also able to exercise considerable countervailing power through their house brands. 26.2% of all yellow spreads by volume is sold under house brand labels. Supermarkets are able to drive down the price of yellow spreads through competitive pricing of their house brands compared with other products. They are in a strong position to obtain competitive pricing from suppliers of house brands due to the presence of a large number of incumbents and potential suppliers.

THIS NOTICE is given by Helen Golding, Company Secretary and Group Legal Counsel, Burns Philp & Company Limited

I hereby confirm that:

* all information specified by the Commission has been supplied;
* all information known to Burns Philp & Company Limited which is relevant to the consideration of this notice has been supplied;
* 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 application/notice.

Dated this 18th day of December 2002.

Signed by Burns Philp & Company Limited:

______________________________________

Helen Golding

Company Secretary and Group Legal Counsel

I am an officer of the company and am duly authorised to make this notice.

# Appendix A

## Announcements to the Australian Stock Exchange

# Appendix B

## Calculation of Price of Imported Fresh Yeast

# Appendix C

## Dry Yeast Imports