

## Determination

### **Oji Oceania Management (NZ) Limited and Carter Holt Harvey Limited [2014] NZCC 18**

**The Commission:** Dr Mark Berry  
Sue Begg  
Anna Rawlings

**Summary of application:** Oji Oceania Management (NZ) Limited seeks clearance to acquire up to 100% of the shares in Carter Holt Harvey Pulp & Paper Limited from Carter Holt Harvey Limited.

**Determination:** Under section 66(3)(a) of the Commerce Act 1986, the Commission gives clearance for Oji Oceania Management (NZ) Limited to acquire up to 100% of the shares in Carter Holt Harvey Pulp & Paper Limited from Carter Holt Harvey Limited.

**Date of determination:** 29 July 2014

Confidential material in this report has been removed. Its location in the document is denoted by [ ].

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## The proposed acquisition

1. On 16 May 2014, the Commerce Commission received an application from Oji Oceania Management (NZ) Limited (Oji), seeking clearance to acquire up to 100% of the shares in Carter Holt Harvey Pulp & Paper Limited (CHHPP) from Carter Holt Harvey Limited (CHH). The transaction forms part of a wider acquisition by a related company of Oji involving CHH's packaging interests in Australia.
2. CHHPP's existing New Zealand pulp and paper businesses includes the Kinleith pulp and paper mill and the Tasman pulp mill, both of which are located in the central North Island (CNI).<sup>1</sup>
3. Oji ultimately owns Pan Pac Forest Products Limited, which owns forests, a saw mill and a pulp mill, all of which are located in Hawke's Bay (in these reasons we refer to Pan Pac as Oji).
4. The acquisition will result in the aggregation of three pulp mills (Kinleith, Tasman and Oji's Napier mill) under Oji's ownership. The acquisition would harm competition if it gave Oji the ability to increase the prices it charges to its customers, or decrease the prices it pays to the suppliers of pulp logs and wood chips used in its pulp mills below competitive levels.

## The decision

5. The Commission gives clearance to the proposed acquisition as it is satisfied that the acquisition will not have, or would not be likely to have, the effect of substantially lessening competition in a market in New Zealand. That is, the Commission is satisfied that the acquisition would not be likely to give Oji the ability to increase the prices it charges to its customers, or decrease the prices it pays to the suppliers of pulp logs and wood chips it uses in its pulp mills below competitive levels.

## Our framework

6. Our approach to analysing the competition effects of the proposed acquisition is based on the principles set out in our Mergers and Acquisitions Guidelines.<sup>2</sup>

## The substantial lessening of competition test

7. As required by the Commerce Act 1986 (the Act), we assess whether the proposed merger is likely to result in a substantial lessening of competition.
8. We determine whether a merger is likely to substantially lessen competition in a market by comparing the likely state of competition if the merger proceeds (the scenario with the merger, often referred to as the factual), with the likely state of

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<sup>1</sup> CHHPP also includes the Penrose paper recycling mill; the Fullcircle waste paper collection and processing business; the Lodestar logistics and transport business; packaging operations, which consist of the corrugated case, speciality board and paper bag business units; and a facility to load wood chips at the port of Tauranga (which is not currently in use).

<sup>2</sup> Commerce Commission, *Mergers and Acquisitions Guidelines*, July 2013.

competition if the merger does not proceed (the scenario without the merger, often referred to as the counterfactual).<sup>3</sup>

9. A lessening of competition is generally the same as an increase in market power. Market power is the ability of supplier(s) to raise price above the price that would exist in a competitive market (the 'competitive price'), or reduce non-price factors such as quality or service below competitive levels.
10. Similar to a merger between competing suppliers, a merger between competing buyers may lessen competition by increasing the merged firm's ability, unilaterally or in coordination with other firms, to exercise market power when buying products. Buyer market power is the ability to profitably depress prices paid to suppliers to a level below the competitive price for a significant period of time. This can lead to the withdrawal of supply from the market.
11. Determining the scope of the relevant market or markets can be an important tool in determining whether a substantial lessening of competition is likely.
12. We define markets in the way that we consider best isolates the key competition issues that arise from the merger. In many cases this may not require us to precisely define the boundaries of a market. A relevant market is ultimately determined, in the words of the Act, as a matter of fact and commercial common sense.<sup>4</sup>

#### **When a lessening of competition is substantial**

13. Only a lessening of competition that is substantial is prohibited. A lessening of competition will be substantial if it is real, of substance, or more than nominal.<sup>5</sup> Some courts have used the word 'material' to describe a lessening of competition that is substantial.<sup>6</sup>
14. There is no bright line that separates a lessening of competition that is substantial from one that is not. What is substantial is a matter of judgement and depends on the facts of each case. Ultimately, we assess whether competition will be substantially lessened by asking whether consumers in the relevant market(s) are likely to be adversely affected in a material way.

#### **When a substantial lessening of competition is likely**

15. A substantial lessening of competition is 'likely' if there is a real and substantial risk, or a real chance, that it will occur. This requires that a substantial lessening of competition is more than a possibility, but does not mean that the effect needs to be more likely than not to occur.<sup>7</sup>

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<sup>3</sup> *Commerce Commission v Woolworths Limited* (2008) 12 TCLR 194 (CA) at [63].

<sup>4</sup> Section 3(1A). See also *Brambles v Commerce Commission* (2003) 10 TCLR 868 at [81].

<sup>5</sup> *Woolworths & Ors v Commerce Commission* (2008) 8 NZBLC 102,128 (HC) at [127].

<sup>6</sup> *Ibid* at [129].

<sup>7</sup> *Woolworths & Ors v Commerce Commission* (2008) 8 NZBLC 102,128 (HC) at [111].

## The clearance test

16. We must clear a merger if we are satisfied that the merger would not be likely to substantially lessen competition in any market.<sup>8</sup> If we are not satisfied – including if we are left in doubt – we must decline to clear the merger.<sup>9</sup>

## Key parties

### Oji

17. Oji is a wholly-owned subsidiary of JP NewCo, a company that at the time we received the Application was a wholly owned subsidiary of Oji Holdings Corporation (Oji Holdings), a Japanese-registered company. However, at the time the acquisition settles, it is intended that JP Newco will be owned 60% by Oji Holdings and 40% by Innovation Network Corporation of Japan (INCJ). INCJ is a corporation sponsored by the Japanese government and private enterprises aimed at promoting innovation and enhancing the value of businesses in Japan. INCJ has no existing investments in New Zealand.
18. Through its subsidiaries, Oji Holdings has global interests in the production of paper and packaging products.
19. As explained above, via its ultimate ownership of Pan Pac Forest Products Limited Oji owns forests, a saw mill and a pulp mill, all of which are located in Hawke's Bay.
20. Oji's pulp mill produces thermomechanical pulp (TMP) and a higher grade bleached chemi-thermomechanical pulp (BCTMP).
21. Pulp logs and wood chips are used in pulp manufacture. Oji acquires pulp logs for its pulp mill from its own forests as well as from third party log suppliers. It acquires wood chips from its own and other saw mills. Oji also exports wood chips through the port of Napier using a site that it leases from Port of Napier Limited.

### CHH/CHHPP

22. In contrast to Oji's TMP and BCTMP pulp, CHHPP manufactures kraft pulp at its Kinleith and Tasman mills.
23. CHHPP acquires pulp logs from various forest owners/managers, mainly in the CNI.<sup>10</sup> CHHPP also acquires wood chips from a number of saw mills, including its own mills and a number of third party saw mills. CHH mainly sources woodchips from the CNI.

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<sup>8</sup> Section 66(1).

<sup>9</sup> In *Commerce Commission v Woolworths Limited (CA)*, above n 2 at [98], the Court held that "the existence of a 'doubt' corresponds to a failure to exclude a real chance of a substantial lessening of competition". However, the Court also indicated at [97] that we should make factual assessments using the balance of probabilities.

<sup>10</sup> The CNI includes the Bay of Plenty region, the Waikato region and the central part of the North Island extending to the Taupo/Ruapehu region in the south.

## Other parties

### *Other pulp/paper mills*

24. There are two other pulp mills in the North Island apart from the CHHP and Oji pulp mills.
- 24.1 Winstone Pulp International Limited (Winstone) operates a pulp mill at Karioi (near Ohakune), producing BCTMP pulp. Winstone draws wood chips from its own sawmill at Tangiwai, pulp logs from its parent company's forests in the lower North Island, as well as logs and chips from third party suppliers in the lower North Island.
- 24.2 Norske Skog Tasman Limited (Norske Skog) operates an integrated mechanical pulp and newsprint paper mill at Kawerau. It acquires wood chips from the CNI.
25. In addition, Asaleo Care Limited (Asaleo), formerly SCA Hygiene Australasia Limited, manufactures a range of personal care and household tissue products at its mill in Kawerau. Asaleo uses pulp as an input into the manufacture of its tissue products.
26. [
- ]

### *Forest owners/managers*

27. There are a number of forest owners and managers supplying pulp logs to mills in the North Island. These include:
- 27.1 Hancock Natural Resource Group Inc (Hancock), which manages forests mainly in the CNI and Hawke's Bay, including on behalf of Ontario Teachers' Pension Plan (OTPP), Viking Global New Zealand Limited and The Tiaki Plantations Company;
- 27.2 Timberlands Limited, which manages forests in the CNI on behalf of Kaingaroa Timberlands and other clients;
- 27.3 PF Olsen Limited, which manages forests in the North Island, including in the CNI and Hawke's Bay/East Coast regions on behalf of various clients, such as farmers and government agencies; and
- 27.4 New Zealand Forest Managers Limited (NZFM), which manages a number of forests in the CNI, including those owned by The Lake Taupo Forest Trust.

### *Saw mills*

28. There are a number of saw mills in the North Island that produce wood chips as a by-product of the production of sawn timber. These include the mills operated by the following companies:

- 28.1 Red Stag Timber Limited, Rotorua, which is currently supplying wood chips [ ];
- 28.2 Tenon Limited, Taupo, which is supplying wood chips to [ ];
- 28.3 Sequal Lumber Limited, Kawerau, which is supplying wood chips to [ ]; and
- 28.4 a number of smaller sawmill operators located throughout the:
- 28.4.1 CNI, which supply wood chips predominantly to CHHPP and/or Norske Skog;
  - 28.4.2 Hawke's Bay/East Coast regions, which mainly supply to Oji; and
  - 28.4.3 lower North Island, which mainly supply to Winstone and/or Oji.

## Industry background

### Overview

29. At a high level the New Zealand pulp industry operates as follows.
- 29.1 Forests are planted and trees are harvested typically between 25 and 30 years of age.
  - 29.2 When a tree is felled it is cut into several sections. The most valuable part of the log is the saw log. The saw log is either exported, or provided to a domestic saw mill where it is processed into sawn timber and other wood products. Wood chips are produced as a by-product of the saw milling process.<sup>11</sup>
  - 29.3 The parts of the tree that are unsuitable for the production of sawn timber are called pulp logs.<sup>12</sup> These logs are either exported or sent to a pulp mill by the forest owner.
30. A flow chart is provided in Figure 1 showing each stage of the pulp production process from the harvesting of the logs to the production of the end product.

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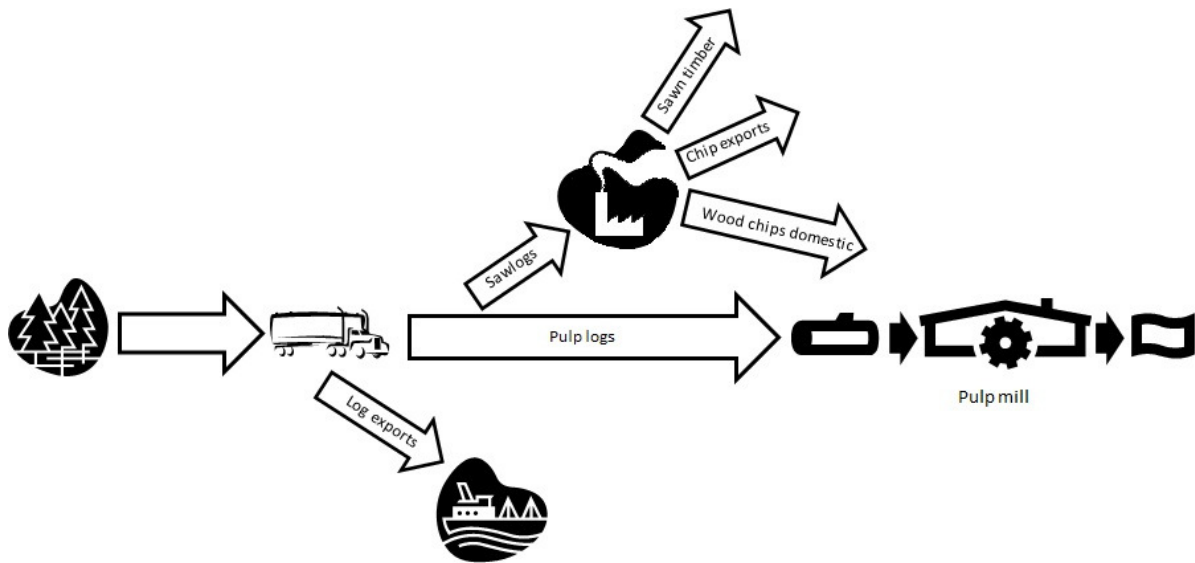
<sup>11</sup> On the basis of available information, the proportion of revenue earned from wood chips by saw mills compared to the revenue earned from saw logs varies between five and 15 per cent. For instance, [

]

<sup>12</sup> The pulp log is typically cut from the top of the tree. On the basis of information provided by forestry companies, pulp logs account for less than [ ] per cent of revenue for log producers but help to contribute towards harvesting costs.



**Figure 1: Flow chart of the pulp production process**



Source: Industry participants

31. Chips made from pulp logs and wood chips from a saw mill are used to produce pulp.<sup>13</sup> While all pulp is produced from the same base ingredients, there are two different ways that pulp can be produced in New Zealand:
  - 31.1 a chemical process, which produces what is known as kraft pulp; or
  - 31.2 a mechanical process, which produces what is known as mechanical pulp. TMP and BCTMP are types of mechanical pulp.
32. Kraft pulp and mechanical pulp are typically used to produce different types of paper and paper products. Paper products made from mechanical pulp include newsprint and other grades of paper typically used in magazines and advertising flyers. Such papers require good printability, but are only of limited strength and, compared to kraft pulp-based papers, relatively cheap. In contrast, kraft pulps tend to be used in applications where high brightness or high strength is needed, such as copy paper and liners for corrugated packaging.
33. As indicated above, CHHPP produces kraft pulp at its Kinleith and Tasman mills. Oji produces only mechanical pulp.<sup>14</sup> Winstone and Norske Skog also produce mechanical pulp.<sup>15</sup>

#### **With the acquisition**

34. With the acquisition, Oji would acquire up 100% of the shares in CHHPP.

<sup>13</sup> Wood chips are also used in the production of medium density fibreboard and particle board. However, neither of these end uses were identified as competitive alternatives by any of the parties we spoke to in the relevant markets. Therefore, we do not consider them further in these reasons.

<sup>14</sup> In 2012, Pan Pac upgraded its mill to enable it to produce a higher quality BCTMP mechanical pulp.

<sup>15</sup> Winstone produces BCTMP mechanical pulp, while Norske Skog produces TMP mechanical pulp.

### **Without the acquisition**

35. Without the acquisition, the status quo is likely to prevail [ ]

### **How the merger could substantially lessen competition**

36. The proposed merger has the potential to lessen competition in two ways:
- 36.1 through combining Oji and CHHPP as competitors in the manufacture and sale of pulp to customers; and
  - 36.2 through combining Oji and CHHPP as competing buyers for wood chips and pulp logs for use in their respective pulp mills.

### **Manufacture and sale of pulp to customers**

37. In this case there is little evidence that the kraft pulp manufactured and supplied by CHHPP competes with the mechanical pulp manufactured and sold by Oji. In previous decisions the Commission has found separate markets for each of kraft and mechanical pulps.<sup>16</sup> While those decisions were some time ago, current information does not provide any reason to change this approach when considering this acquisition. Mechanical and kraft pulps are purchased by different customers for different purposes, and on average the price of kraft pulp is higher than mechanical pulp.<sup>17</sup> Similarly, on the supply-side we have seen no evidence of actual or potential switching by the merging parties between the different types of pulp that they manufacture.
38. So, in the absence of any significant competition between Oji and CHHPP in the supply of pulp, we consider a substantial lessening of competition is unlikely. We do not therefore consider any further in these reasons the impact of this merger on the markets for the manufacture and supply of pulp to end users.

### **Purchase of wood chips and pulp logs**

39. Both merging parties use pulp logs and wood chips to manufacture pulp. This raises the prospect that the proposed acquisition could result in a substantial lessening of competition in the markets for the acquisition of pulp logs and wood chips by increasing Oji's ability and incentive to reduce the price it pays to pulp log and wood chip suppliers below competitive levels.
40. If this occurs, suppliers could no longer cover their supply costs and so would withdraw supply from the market, resulting in a lessening of competition.
41. Whether or not the merger would have this effect will depend on:

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<sup>16</sup> In *Fletcher Challenge Limited and NZ Forest Products Limited* (Commerce Commission Decision 213, 5 November 1987), the Commission concluded that mechanical pulps were not sufficiently close substitutes for kraft pulp. In *Carter Holt Harvey Limited and Norkse Skogindustrier ASA* (Commerce Commission Decision 424, 21 March 2001) the Commission again made a distinction between mechanical and kraft pulps for the purpose of defining one of the affected markets.

<sup>17</sup> Application at [105.4].

- 41.1 whether Oji and CHHPP compete to buy logs – that is, do pulp log or wood chip producers consider both Oji and CHHPP to be potential purchasers;
  - 41.2 whether affected pulp log and wood chip producers have other competitive alternatives to Oji and CHHPP;
  - 41.3 if any affected suppliers do not have such competitive alternatives, whether a decrease in price would lead them to reduce the quantity of pulp logs or wood chips they produce;
  - 41.4 if any suppliers were to decrease the quantity of pulp logs or wood chips they produce, whether Oji would be able to increase the price it charges its customers for pulp; and
  - 41.5 whether Oji would nonetheless find it profitable to reduce the price it pays for pulp logs and wood chips. This would potentially reduce the volume of pulp produced. However, this would be profitable for Oji if the resulting input cost savings on pulp logs and wood chips outweighed the reduced pulp revenues that result from decreased pulp output.
42. We have identified five parties ([ ] forest owners and [ ] saw mill operators) that could be affected by the proposed merger. However, none of these parties made any formal submissions or provided any evidence to show a substantial lessening of competition would likely result from the merger.

### **Market definition**

- 43. Market definition is a tool that can provide a framework to help identify and assess the close competitive constraints a merged firm would likely face. Determining the relevant market requires us to judge whether, for example, two products are sufficiently close substitutes as a matter of fact and commercial common sense to fall within the same market.<sup>18</sup>
- 44. We define markets in the way that best isolates the key competition issues that arise from the merger. There may not be a bright line that separates those products that are within a market from those outside that market. In reality, a product may compete more closely (ie, be a closer substitute) with some products than with others.
- 45. What matters is that we consider all relevant competitive constraints, and the extent of those constraints, on different products. For this reason, we may also consider products which fall outside the market but which may still impose some degree of competitive constraint on the merged firm.

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<sup>18</sup> Section 3(1A) of the Act.

### The relevant markets

46. As discussed, pulp mills obtain wood chips from two sources: pulp logs produced by forestry companies and chips produced by saw mills as a by-product of the production of sawn timber. Pulp mills (including those mills operated by the merging parties) use chips sourced from pulp logs and chip produced from saw mills, but the latter is generally preferred because of its higher density.<sup>19</sup> We separately consider whether the merger would result in a substantial lessening of competition in the purchase of both of these inputs.
47. In regard to the geographic dimensions of the markets, we considered whether any suppliers of pulp logs or wood chips could economically transport these products to both Oji and CHHPP such that there is competitive overlap in the (actual or potential) purchase of each of these inputs that would disappear post-merger. As explained below, we identified forests along the Napier/Taupo highway and certain saw mills in each of the lower North Island and East Coast regions that could consider supplying both merging parties.
48. Therefore, we consider that the markets most relevant to the consideration of this merger are the markets for:
- 48.1 the acquisition of pulp logs from forests along the Napier/Taupo highway; and
- 48.2 the acquisition of wood chips from certain saw mills in each of the lower North Island and East Coast regions.<sup>20</sup>

### Purchase of pulp logs and wood chips

49. In defining these markets a key question is whether Oji and CHHPP compete to buy pulp logs and wood chips. More precisely, we assess whether there are existing forest owners or saw mills that supply, or could supply, the merging parties' pulp mills and that may be indifferent to supplying either CHHPP or Oji. If so, this assists us to determine the relevant markets, which are defined around the location of those forests or saw mills.
50. We consider:
- 50.1 [ ] forestry companies along the Taupo/Napier highway could supply pulp logs to either of Oji or CHHPP; and
- 50.2 [ ] saw mill operators, [ ] could supply wood chip to either of Oji or CHHPP.
51. The remaining forestry and saw milling companies whom we spoke to do not consider that Oji and CHHPP are realistic alternative purchasers of pulp logs and

<sup>19</sup> Application at Appendix A, p.11.

<sup>20</sup> The relevant saw mills are the [ ].

wood chips because the location of their forests and saw mills prevents it being economically feasible for them to supply both Oji's and CHHPP's pulp mills.

#### *Purchase of pulp logs*

52. Pulp logs are bulky and therefore expensive to transport in relation to their price.<sup>21</sup> We have found that certain suppliers of pulp logs with forests approximately equidistant between CHHPP and Oji's pulp mills could economically supply both of the merging parties. These include those forests managed by [ ] that are located relatively close to the Napier/Taupo highway, the major road linking the CNI and Hawke's Bay.

#### *Purchase of wood chips*

53. Wood chips are expensive to transport relative to their value.<sup>22</sup> Therefore, most saw mills situated in the CNI, where CHHPP has its mills, could not economically supply Oji so there is no overlap in the acquisition of wood chips from these suppliers.
54. Similarly, the saw mills located close to Oji's mill would not normally consider supplying CHHPP in the CNI region as the transport cost differential between supplying the respective mills is too great.<sup>23</sup>
55. We have found [ ] saw mill owners supplying wood chips to Oji's mill in Hawke's Bay that consider they could supply CHHPP's pulp mills.<sup>24</sup>

55.1 [

]

55.2 [

].

### **Competition assessment**

56. We have considered separately the likely competitive impact of the merger on the buying markets for the acquisition of pulp logs and wood chips in each of the affected geographic locations.
57. For the reasons outlined below, we are satisfied that the merger is unlikely to result in a substantial lessening of competition in the markets for the acquisition of pulp

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<sup>21</sup> For instance, a report prepared for Oji by the New Zealand Forest Research Institute (trading as Scion), and which is attached as Appendix A to the Application, states that a pulp log ascribed a value of \$50 per tonne will incur a cost of \$15-16 per tonne to transport it 75 kilometres, which represents 30-32% of the delivered cost of the log.

<sup>22</sup> For instance, Tenon, which operates a sawmill at Taupo in the CNI, told us that the cost to transport wood chips to Oji's pulp mill in Hawke's Bay would be [ ] that to transport chips to its closest pulp mill, which is located at Kinleith.

<sup>23</sup> For instance, the owner of [ ] told us that the transport costs would make it uneconomic to send wood chips to CHHPP's pulp mills.

<sup>24</sup> Although neither parties have supplied CHHPP in the past, we consider these pulp mills to competitively constrain each other as CHHPP has been [ ].

logs as the quantity of pulp logs produced is determined in large part by the price of saw logs rather than the price of pulp logs. Therefore, even if the merging parties attempted to impose a substantial price decrease, this is unlikely to reduce the quantity of pulp logs supplied.

58. Similarly, we are satisfied that the merger is unlikely to result in a substantial lessening of competition in the markets for the acquisition of wood chips in the affected geographic markets for the following reasons.

58.1 Sourcing sufficient pulp logs and chips is critical for pulp production. Therefore, it is unlikely that Oji would depress the quantity pulp logs and wood chips supplied by paying below the competitive price for them. Pulp mills have high fixed costs and therefore aim to operate at close to capacity – wood chip from the [ ] saw mill operators in question is a large portion of Oji’s pulp mill inputs.

58.2 Oji would not likely be in a position to increase pulp prices if it were to decrease wood chip purchases, further decreasing the appeal of reducing wood chip purchases. In particular, [ ], which would limit Oji’s ability to raise pulp prices downstream.

#### **Increase in buyer power: pulp logs**

59. We do not consider that the merger is likely to result in a substantial lessening of competition in the acquisition of pulp logs from forests along the Napier/Taupo highway. This is because, while the merger could remove a competing buyer for suppliers of pulp logs, it is unlikely to have any significant impact on the output of pulp logs produced.

60. In addition, some of the pulp log producers located along the Napier/Taupo highway have alternative supply options, including export for some grades of pulp logs (see paragraph 63 for further details).<sup>25</sup>

#### **Forestry companies affected by the merger**

61. We identified [ ] forestry companies located along the Napier/Taupo highway who could face a decrease in the number of pulp log purchasers they supply as a result of the acquisition.

61.1 [ ] manages forests on behalf of clients in the CNI, some of which are equidistant between CHHPP and Oji’s mills. These forests are situated relatively close to the Napier/Taupo highway.

61.2 [ ] considered that while the acquisition would result in a loss of competitive choice in respect of the affected forests, it was unlikely to cause

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<sup>25</sup> For instance [ ], and which are close to the Napier/Taupo road, represent less than [ ] of [ ] forests.

concern because of the small area of overlap and because the affected forests only made up a small part of [ ] business.

61.3 [ ] has widely dispersed forests which it manages on behalf of a number of clients. This includes a small forest it manages on behalf of [ ] that is located close to the Napier/Taupo road. However, it stated that while the merger would result in a reduction of competitive choice for this forest, pulp logs make only a small marginal contribution to net harvest revenue, so even a price decrease of 10-20% would make little difference to the volume of pulp logs produced.

61.4 [ ] manages a number of forest plantations, the majority of which are located in the CNI. It stated that [ ] of its pulp logs (by volume) are currently sold to [ ] and the remainder to [ ]. While [ ] has sold pulp logs to Oji periodically these have been “one-offs” and only usually when CHHPP’s pulp mills have faced disruption.

62. All the forestry companies we spoke to considered that a key driver for the decision to harvest their forests is the price of the higher value saw log with the lower value pulp log being a by-product.

63. Further, all forest owners we spoke to, with the exception of [ ], told us they have the option of exporting some of their pulp logs, mainly to Asia where there is a demand for such logs to be converted into sawn timber. However, our assessment below is based on the presumption that these export alternatives do not provide sufficient competitive constraint for the forests in question.

#### *Competition assessment*

64. We are satisfied that any change in pricing is unlikely to result in a reduction in quantity. This is because the quantity of pulp logs produced is determined by the quantity of trees harvested. The harvesting of the forest is in turn determined by the age of the forest and the price of higher value saw logs. Pulp logs, once produced, must be sold and cannot be dumped because of the possible risk of blockage of waterways and other environmental concerns.<sup>26</sup>

#### **Increase in buyer power: wood chips**

65. We consider that the proposed merger could increase the ability of the merged entity to impose a quantity reducing price decrease on [ ] affected saw mill operators, as it may remove an alternative wood chip purchaser from the market and there are few remaining alternatives. However, we consider that the merged entity is unlikely to have the incentive to do so.

66. Our investigation identified [ ] saw mill operators who may face the potential loss of an alternative wood chip purchaser as a result of this merger, these being [ ].

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<sup>26</sup> Interview with Oji (12 June, 2014).

67. [ ]

68. [ ]

69. [ ]<sup>27</sup>

70. [ ]

71. [ ] has not raised any concerns about the acquisition. However, while it has not supplied CHHPP, we propose to include it as a saw mill operator that may be affected by the proposed merger given that [ ]  
].

*Competition assessment*

72. The merger may increase the ability of the merged entity to depress wood chip prices to these saw mills because:

72.1 Apart from the merging parties, the affected saw mills appear not to have economic alternative supply options in Norske Skog<sup>28</sup> or Winstone<sup>29</sup> as neither company appears to have the capacity to absorb additional wood chip supply.

72.2 The affected saw mills could likely decrease wood chip outputs in response to a substantial reduction in the price paid for wood chips.<sup>30</sup> Unlike pulp logs, wood chip quantities are, in part, dependent on the wood chip price. This is because a saw mill is commonly able to convert about 65-70% of the logs it purchases into sawn timber products, leaving 30-35% as chips.<sup>31</sup> So having an outlet for wood chips is important for a saw mill’s profitability and so is likely to be a key factor in their decision as to how many logs to purchase for the manufacture of sawn timber and wood chips. Dumping wood chips is not an economic alternative.

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<sup>27</sup> [ ]

<sup>28</sup> Norske Skog has decreased capacity in the last eighteen months and since it is not actively looking for new suppliers can no longer be regarded as a competitive alternative buyer of wood chips at this time.

<sup>29</sup> Winstone advised us that its pulp mill is [ ].  
Around [ ] of Winstone’s pulp fibre requirements are supplied from its parent company’s forests and its own saw mill.

<sup>30</sup> [ ]

<sup>31</sup> This is based on the conversion rates outlined on page 11 of the Scion report, which was attached as Appendix A to the Application.



73. However, we consider that the merged entity is unlikely to have the incentive to impose a price decrease that is so low as to induce saw mills to reduce the amount of wood chip they produce. This is because Oji would want to maintain its current level of wood chip purchases.
74. Pulp mills have high fixed costs and so there is a strong incentive to run them at capacity. [ ]<sup>32</sup> [ ]<sup>33</sup>
75. Oji sources approximately [ ] of its third party wood chips from the affected saw mills and is unlikely to reduce these quantities, as it requires this quantity of chips, not only for its current production needs, but also as buffer stock to maintain a constant supply at its pulp mill. As there can be times of high and low wood chip supply, Oji has an incentive to acquire all of the chip it can from its saw mill suppliers. This is the case even though Oji exports some of the chips it purchases.<sup>34</sup>
76. Further, were Oji to reduce its wood chip purchases from the affected saw mills, Oji is unlikely to make up for the deficit by increasing its purchases of pulp logs or wood chips from its own mills, or by reducing the amount of wood chip it exports.
- 76.1 Oji uses about [ ]% of pulp logs and [ ]% wood chip in its pulp mill. An increase in the portion of pulp logs used could affect the quality of the pulp produced. Therefore, Oji is unlikely to replace chip inputs for pulp logs.
- 76.2 Oji is unlikely to be able to increase the production of wood chips from its own saw mill. Oji advised us that its own saw mill is running at [ ]<sup>35</sup>
77. Moreover, even if Oji had an incentive to reduce its wood chip purchases, the consequent decrease in its pulp output would be unlikely to result in higher pulp prices. This is because Oji is a price taker for pulp exports [ ]<sup>36</sup> As such, Oji would obtain no benefit in the pulp market from decreasing wood chip purchases, making it more unlikely that Oji would reduce its wood chip purchases.
78. Some saw mills (and forestry companies)<sup>37</sup> expressed concern about their ability to export wood chips because export facilities are controlled by the merging parties. In this regard there is little history of export by third party saw mills from either Napier or Tauranga.<sup>38</sup> Moreover, we have received no evidence during the investigation to

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<sup>32</sup> Interview with Oji (12 June, 2014).

<sup>33</sup> Ibid.

<sup>34</sup> Oji is only able to process green or fresh chips with the remainder exported.

<sup>35</sup> Email from Chapman Tripp (16 July 2014).

<sup>36</sup> [ ]

<sup>37</sup> [ ]

<sup>38</sup> The merging parties each own wood chip loading facilities operated under lease at the ports of Tauranga and Napier, respectively. The terms of both parties' leases with the relevant port companies requires them to make these facilities available to third parties on competitive terms and when the facilities can

suggest that third parties have been denied access to these facilities. We consider that the merger would result in a bare transfer of the facility and as such, competition issues are unlikely to arise.

79. For these reasons, we do not consider that the merger is likely to result in a substantial lessening of competition in the acquisition of wood chips in any of the affected geographic markets.

### **Conclusion**

80. For the reasons provided above, we conclude that the proposed acquisition will not have, or would not be likely to have, the effect of substantially lessening competition in the affected markets.

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be reasonably used. However, our understanding is that no third party exports have been made from either facility for many years. In the case of the CNI, we have been told by industry participants that the demand for fibre by pulp mills in this region has been such that third party exports through the port of Tauranga have not been required since 2006. While chips have been exported through the port at Napier, all such exports have been made by Oji using its own loading facility.

**Determination on notice of clearance**

81. We are satisfied that the proposed acquisition will not have, or would not be likely to have, the effect of substantially lessening competition in a market in New Zealand.
82. Under section 66(3)(a) of the Act, the Commerce Commission determines to give clearance for Oji Oceania Management (NZ) Limited to acquire up to 100% of the shares in Carter Holt Harvey Pulp & Paper Limited from Carter Holt Harvey Limited.

Dated this 29<sup>th</sup> day of July 2014

Dr Mark Berry  
Chairman