

## Determination

### **Pact Group Holdings Limited and Flight Plastics Limited [2020] NZCC 27**

<b>The Commission:</b>	Anna Rawlings Dr Derek Johnston Vhari McWha Dr John Small
<b>Summary of application:</b>	An application from Pact Group Holdings Limited seeking clearance to acquire the assets and business of Flight Plastics Limited in New Zealand and the packaging-related assets of Flight Extruded Plastics LP in Adelaide.
<b>Determination:</b>	Under section 66(3)(a) of the Commerce Act 1986, the Commerce Commission gives clearance to the proposed acquisition.
<b>Date of determination:</b>	16 December 2020

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

## The Proposed Acquisition

1. On 25 August 2020, the Commerce Commission registered an application (the Application) from Pact Group Holdings Limited (Pact) to acquire the assets and business of Flight Plastics Limited in New Zealand and the packaging-related assets of Flight Extruded Plastics LP in Adelaide (together, Flight) (the Proposed Acquisition).

## Our decision

2. The Commission gives clearance to the Proposed Acquisition as it is satisfied it will not have, or would not be likely to have, the effect of substantially lessening competition in a market in New Zealand.
3. Pact and Flight (the Parties) are both major manufacturers of small rigid packaging made from polyethylene terephthalate (PET). PET is a commonly-used material for packaging foods such as meat and seafood, fresh fruit and baked goods. The focus of our investigation was on the impact of competition to supply plastic packaging for these applications.
4. In New Zealand (and globally) there has been an increasing trend towards more sustainable forms of plastic. PET is viewed as a sustainable type of packaging as it can be recycled repeatedly. PET that is new is referred to in this determination as ‘virgin PET’, and that which has been recycled as ‘RPET’. RPET can be sourced from both overseas and within New Zealand. At present, Flight is the only firm in New Zealand with the facilities to produce RPET (the main equipment required is known as a ‘wash plant’). New Zealand-produced RPET is referred to in this determination as NZ RPET.
5. One issue is whether it was appropriate to assess competition in respect of only NZ RPET, all RPET or all PET. The reason this mattered is that we considered whether Pact might build its own wash plant if the Proposed Acquisition did not go ahead. If it was, the Proposed Acquisition might have eliminated future competition between the Parties for the supply of NZ RPET packaging. However, on balance we concluded that there was not sufficient evidence to justify assessing packaging made from NZ RPET as constituting a separate market.<sup>1</sup>
  - 5.1 Several customers expressed an interest in NZ RPET but the evidence did not show they were prepared to pay more for it. Customers instead appeared to be satisfied with overseas-sourced RPET.
  - 5.2 Although our analysis is forward looking, the evidence did not suggest demand for NZ RPET was growing rapidly enough such that a separate market for NZ RPET would soon emerge.
6. We considered the Proposed Acquisition on a market including all PET (both virgin PET and RPET) packaging.<sup>2</sup> Post-acquisition, the merged entity will be the largest

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<sup>1</sup> [ ]

<sup>2</sup> Virgin PET and RPET were included in the same market as manufacturers of plastic packaging could easily switch between the two materials.

supplier of PET packaging for food applications in New Zealand. However, we consider that it will be constrained from raising prices by a combination of:

- 6.1 competition from existing suppliers, many of whom have spare capacity and can expand;
- 6.2 the threat of new suppliers entering the market;
- 6.3 the threat of some customers switching to alternative substrates; and
- 6.4 countervailing power, in the case of some larger customers.

## **Our framework**

- 7. Our approach to analysing the competition effects of the Proposed Acquisition is based on the principles set out in our Mergers and Acquisitions Guidelines (our guidelines).<sup>3</sup>

### **The substantial lessening of competition test**

- 8. As required by the Act, we assess mergers and acquisitions using the substantial lessening of competition test.
- 9. 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 competition if the merger does not proceed (the scenario without the merger, often referred to as the counterfactual).<sup>4</sup>
- 10. A lessening of competition is generally the same as an increase in market power. Market power is the ability to raise prices above the price that would exist in a competitive market (the 'competitive price'),<sup>5</sup> or reduce non-price factors such as quality or service below competitive levels.

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

- 11. 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>6</sup> Some courts have used the word 'material' to describe a lessening of competition that is substantial.<sup>7</sup>
- 12. As set out in our guidelines, there is no bright line that separates a lessening of competition that is substantial from one which is not. What is substantial is a matter of judgement and depends on the facts of each case.<sup>8</sup>

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<sup>3</sup> Commerce Commission, *Mergers and Acquisitions Guidelines* (July 2019).

<sup>4</sup> *Commerce Commission v Woolworths Limited* (2008) 12 TCLR 194 (CA) at [63].

<sup>5</sup> Or below competitive levels in a merger between buyers.

<sup>6</sup> *Woolworths & Ors v Commerce Commission* (2008) 8 NZBLC 102,128 (HC) at [127].

<sup>7</sup> *Ibid* at [129].

<sup>8</sup> *Mergers and Acquisitions Guidelines* above n3 at [2.23].

13. A lessening of competition or an increase in market power may manifest itself in a number of ways, including higher prices or reduced services.<sup>9</sup>
14. While we commonly assess competition effects over the short term (up to two years), the relevant timeframe for assessment depends on the circumstances. A longer timeframe will be appropriate if, on the evidence, competition effects are likely to arise in later years.<sup>10</sup>

#### **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>11</sup>

#### **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>12</sup> If we are not satisfied – including if we are left in doubt – we must decline to clear the merger.

#### **Background to the industry**

17. The Proposed Acquisition relates to small rigid plastic packaging, most commonly used to store food. In particular, both Pact and Flight use the ‘extrusion and thermoforming’ (E&T) process to make PET packaging.

#### **How PET packaging is manufactured**

##### *The E&T process*

18. The main steps in the E&T process for producing PET packaging are summarised below.
  - 18.1 Manufacturers of PET packaging purchase or produce raw PET material in flake form (‘PET flake’) (the source of PET flake is described below).
  - 18.2 In the ‘extrusion’ stage, flake is heated, mixed with other products such as colourants and then extruded into plastic sheets, which are rolled up (referred to as ‘roll stock’).
  - 18.3 In the ‘thermoforming’ stage, the roll stock is heated and stretched over a mould to form containers. Containers are then cut away from the sheet. Manufacturers that use thermoforming typically have a range of moulds that allow them to make different shapes and sizes of packaging.

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<sup>9</sup> Ibid at [2.21].

<sup>10</sup> *Woolworths & Ors v Commerce Commission* (2008) 8 NZBLC 102,128 (HC) at [131].

<sup>11</sup> Ibid at [111].

<sup>12</sup> Section 66(3)(a).

19. Packaging can be made from virgin PET flake or RPET flake. Virgin PET flake is normally imported from overseas. Some sources of RPET flake are as follows.
- 19.1 Collection recycling (from New Zealand or overseas).
- 19.1.1 PET containers used by consumers are collected for recycling, sorted, and formed into bales ('PET bales'). This is known as 'post-consumer PET'.
- 19.1.2 The PET bales are sent to a wash plant, which removes food and labels. The washed PET containers are then cut into flakes.
- 19.2 Thermoforming offcuts. The process of thermoforming produces offcuts, which can be granulated and extruded into new roll stock.
20. We understand that RPET flake from offcuts is clean and so can be extruded into new roll stock immediately. However, RPET flake that has come from collection recycling and that has been processed through a wash plant is not safe to use immediately with food. It can be used for food applications in two ways.
- 20.1 Flakes can be put through a decontamination plant before being extruded into roll stock. Such roll stock (and resulting packaging) is 100% RPET.
- 20.2 Flakes can be extruded between two sheets of virgin PET. This is referred to in the industry as 'A-B-A' extrusion (with the 'A' referring to the virgin PET and the 'B' referring to the RPET). Such roll stock (and resulting packaging) is less than 100% RPET due to the layers of virgin PET.
21. Flight's plant in Wellington means PET packaging can be used, collected, washed, decontaminated and then made again into plastic packaging all within New Zealand. This is known as 'closed loop' recycling, as PET packaging can be continually recycled within the country. The NZ RPET material that comes from this process is viewed as the most environmentally friendly form of PET packaging as it minimises the transportation of plastic and reduces the impact of producing virgin PET.

#### *How manufacturers use the E&T process*

22. Firms may be involved at different stages of the process for packaging manufacture. For example, only Flight conducts all steps in-house. Some manufacturers only have thermoformers and buy roll stock from other firms. For ease of reference we refer to all manufacturers as 'E&T packaging manufacturers', whether or not they carry out every stage of the process in-house.

#### *Other processes for making plastic packaging*

23. Another common way to make plastic packaging is through 'injection moulding' (IM). In this case, heated plastic material is injected into a mould. IM packaging is thicker, stronger, more microwave-resistant and more expensive to make than E&T

packaging. It is also more customisable (eg, for specifically designed shapes).<sup>13</sup> Examples of IM packaging include yoghurt pots and ice cream tubs.

### The trend towards sustainable packaging

24. Market participants have consistently told us there is a trend towards using sustainable products. This has led consumers and food suppliers (such as supermarkets, meat processors and fruit growers) to move towards plastics and materials that are easier to recycle or dispose of. RPET has been one form of recyclable packaging which has gained in popularity and its use has increased. However, users have also been innovating with other types of recyclable or compostable materials.
25. The Ministry for the Environment (MfE) has taken steps to support this trend in New Zealand both through phasing out hard-to-recycle plastics and through policies to encourage recycling. For example:
  - 25.1 MfE has set a target to phase out all PVC and polystyrene food and beverage containers (among other types of materials) by 2025.<sup>14</sup> These plastics have been targeted as they tend to be single use plastics. Some major international and local businesses have also committed to that target.
  - 25.2 MfE has provided subsidies to support building recycling facilities through the Waste Minimisation Fund (WMF).<sup>15</sup> For example, the MfE contributed \$4 million to help Flight build its wash plant in 2017.
  - 25.3 MfE has been looking at policies to increase the level of recycling.<sup>16</sup> This includes:
    - 25.3.1 A container return scheme (CRS) where customers must pay a deposit on a beverage container as part of the purchase price.<sup>17</sup> The customer gets the deposit back if they return the bottle to a designated drop-off point.
    - 25.3.2 Expanding and increasing the levy on waste sent to landfill, to encourage waste reduction and fund further investment in minimising waste.<sup>18</sup>

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<sup>13</sup> IM packaging can be made so that it closely resembles E&T packaging. For example, in the Application the Parties submitted that Bonson makes IM packaging that is identical in appearance and function to their E&T products. The Application at FN 5.

<sup>14</sup> See MfE “Reducing the impact of plastic on our environment” (August 2020) [www.mfe.govt.nz/reducing-impact-of-plastic-on-environment](http://www.mfe.govt.nz/reducing-impact-of-plastic-on-environment).

<sup>15</sup> See MfE “Waste Minimisation Fund” [www.mfe.govt.nz/more/funding/waste-minimisation-fund-funded-projects](http://www.mfe.govt.nz/more/funding/waste-minimisation-fund-funded-projects).

<sup>16</sup> See MfE “Reducing the impact of plastic on our environment” (August 2020) (<https://www.mfe.govt.nz/sites/default/files/media/Waste/Final-Reducing-the-impact-of-plastic-on-our-environment-December.pdf>).

<sup>17</sup> See <https://www.mfe.govt.nz/waste/container-return-scheme-option>.

<sup>18</sup> See <https://www.mfe.govt.nz/consultations/landfill-levy>.

## Key parties

### The merging parties

26. Pact describes itself as a packaging solutions business and has over 100 sites and 6000 employees worldwide.<sup>19</sup> Its primary focus is the manufacture and supply of rigid plastic packaging for customers in the food, beverage, chemical, industrial and agricultural sectors. In New Zealand, Pact manufactures and supplies plastic packaging products for a range of customers including supermarkets, meat processors and fruit growers.
27. In New Zealand, Pact operates E&T plants in Albany and Hastings. In July 2019 it was announced that Pact had successfully applied to the MfE for a grant to buy and install a decontamination unit.<sup>20</sup> This will enable it to extrude washed RPET flake into 100% RPET roll stock that is safe for food applications.<sup>21</sup> The new equipment is expected to be operational in [                      ]. Pact also operates injection moulding plants in New Zealand.
28. Flight is a manufacturer of plastic sheets and packaging in Australia and New Zealand, including for fruit and produce, bakery, meat and seafood, and nursery and horticulture. Flight is the only manufacturer in New Zealand that has a wash plant. It is located in Wellington. Its plant also has a decontamination unit, extruders and thermoformers. It is the only plant capable of end-to-end recycling and manufacture on a single site.

### Other suppliers of PET packaging

29. Other manufacturers of PET packaging in New Zealand include:
- 29.1 *Custom-Pak*. Custom-Pak has operations in Christchurch and Auckland and identifies its speciality as “thermo-formed ridged and semi-ridged PET packs for fruit and vegetables, cold take-out meals and salads, baked goods, and fresh meat and fish”.<sup>22</sup>
- 29.2 *Progressive Plastics*. Progressive Plastics is based in Dunedin and manufactures rigid and flexible plastic packaging for the domestic and export food industry.<sup>23</sup>
- 29.3 *Formrite Plastics*. Formrite is based in Christchurch and manufactures rigid plastic for bakery items, confectionery, produce and seedlings.<sup>24</sup>

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<sup>19</sup> See <https://pactgroup.com/>.

<sup>20</sup> Pact Group “Pact Group receive New Zealand Government funding to transition to 100% recycled PET in its food packaging range” (15 July 2019) <<https://pactgroup.com.au/news/pact-group-receive-government-funding-to-transition-to-100-recycled-rpet-in-its-food-packaging-range/>>.

<sup>21</sup> Ibid.

<sup>22</sup> Custom-Pak “About us” [www.custompak.co.nz](http://www.custompak.co.nz).

<sup>23</sup> Progressive Plastic [www.progressiveplastics.co.nz](http://www.progressiveplastics.co.nz).

<sup>24</sup> Formrite Plastics [www.formriteplastics.co.nz](http://www.formriteplastics.co.nz).

- 29.4 *PlusPac*. PlusPac is based in Auckland and manufactures packaging for industries including food, medical, horticulture and retail.<sup>25</sup>
30. Suppliers of PET packaging in NZ that do not have E&T manufacturing facilities in New Zealand but compete using imported packaging include:
- 30.1 *Linpac*. Linpac is part of Klöckner Pentaplast and operates a manufacturing plant in Melbourne, Australia.<sup>26</sup>
- 30.2 *Bonson*. Bonson is based in Auckland. It imports E&T PET products but has some IM facilities in New Zealand.<sup>27</sup>
- 30.3 *Jenkins Freshpac Systems ('JFS')*. JFS provides packaging solutions for New Zealand's fresh produce industry.<sup>28</sup>

### Customers that use PET packaging

31. Customers of the merging parties that use PET packaging include:
- 31.1 supermarkets (eg, containers/trays for inhouse bakery and meat/seafood products);
- 31.2 meat processors (meat trays);
- 31.3 fruit growers (eg, clamshells and punnets for strawberries and cherry tomatoes); and
- 31.4 bakeries (eg containers/trays for biscuits and cakes).

## How the Proposed Acquisition could substantially lessen competition

### Theories of harm that we consider in this determination

32. Pact and Flight are two of the largest manufacturers and suppliers in New Zealand of plastic packaging made from PET using the E&T method. As a result of the Proposed Acquisition any competition between the Parties for such packaging would be lost. We assessed whether the Proposed Acquisition might cause a substantial lessening of competition for the supply of plastic packaging due to:
- 32.1 unilateral effects (ie whether the merged entity could profitably raise prices or reduce quality or innovation by itself); and
- 32.2 coordinated effects (ie whether the merged entity and all or some of its remaining competitors could coordinate their behaviour so as to reduce output and/or raise prices).

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<sup>25</sup> PlusPac [www.pluspac.co.nz](http://www.pluspac.co.nz).

<sup>26</sup> Klöckner Pentaplast "Our locations" [www.kpfilms.com](http://www.kpfilms.com).

<sup>27</sup> Bonson "About us" [www.bonson-savpac.co.nz](http://www.bonson-savpac.co.nz).

<sup>28</sup> JFS "Who we are" [www.jenkinsfps.co.nz](http://www.jenkinsfps.co.nz).

33. We assess these issues in detail further below.

#### **Theories of harm that we do not consider further in this determination**

34. The Parties are potential competitors to buy PET offcuts which are inputs used to produce PET packaging. However, there are many other buyers for offcuts and so the Proposed Acquisition would not materially affect competition to buy them. We do not consider the issue of the loss of competition for the purchase of PET offcuts further.
35. We also considered whether any competing suppliers rely on the Parties to source inputs for making PET packaging, such as flake or roll stock, such that vertical effects could arise. However, we are satisfied that the Proposed Acquisition is unlikely to give rise to such concerns for the following reasons.
- 35.1 The Parties' competitors do not currently source roll stock from the Parties. Instead, they source roll stock (or flake if required) from overseas at a cost which does not appear to materially and adversely affect their competitiveness in supplying RPET packaging in the New Zealand market. The Proposed Acquisition is unlikely to affect this.
- 35.2 While the merged entity would be the only firm capable of supplying NZ RPET roll stock or flake, as discussed further below we do not consider that NZ RPET is, or is likely to become, a necessary input for the merged entity's competitors to compete.
36. We therefore do not consider this issue further in this determination.

#### **Market definition**

37. Market definition is a tool that helps identify and assess the competitive constraints the merged firm would 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.
38. We define markets in the way that we consider best isolates the key competition issues that arise from a merger. In many cases this may not require us to precisely define the boundaries of a market. What matters is that we consider all relevant competitive constraints, and the extent of those constraints. For that reason, we also consider products and services that fall outside the market, but which would still impose some degree of competitive constraint on the merged entity.
39. Given the changing dynamics of the industry, and in particular the trend towards the use of more environmentally sustainable packaging materials, we have considered the appropriate scope of relevant market(s) based not only on current conditions, but also in relation to how these conditions could evolve over time.

## The supply of plastic packaging

### *Product dimension*

40. In the Application, the Parties submitted that the Proposed Acquisition should primarily be assessed in a broad market that includes all small rigid packaging and alternatives (eg, rigid plastic, cardboard, corn starch).<sup>29</sup> The Parties submitted that customers can switch between different packaging types and materials,<sup>30</sup> and provided examples of products that can be stored in different packaging materials.<sup>31</sup>
41. In assessing product dimension, we considered whether the relevant market might be narrower than the market proposed by the Parties. In particular, we considered whether there might be separate markets for:
- 41.1 NZ RPET packaging (either currently, or emerging in the future);
  - 41.2 RPET packaging (including packaging made from NZ RPET or RPET sourced overseas); and
  - 41.3 PET packaging.
42. We concluded that, for the purpose of assessing this case, the relevant market includes all PET packaging. We explain our reasons for this in the sections below.

### Is there a separate market for NZ RPET packaging now?

43. One of our focuses during the investigation was whether there was a separate market for NZ RPET. This is because, if Pact was to build a wash plant in the counterfactual, then the Proposed Acquisition might have eliminated future competition between the Parties for the supply of NZ RPET packaging.
44. There is some evidence that demand is growing for NZ RPET packaging.
- 44.1 Some large buyers identified an interest in NZ RPET packaging.<sup>32</sup> Some manufacturers indicated plans to increase the supply of NZ RPET packaging to meet that growing interest.

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<sup>29</sup> The Application at [6.1]. In past cases ‘small’ has been defined as less than 5L. (See for example *TEC Projects/Tecpak* (Decision 702, 18 November 2010) at [23]). In this case we have not identified precisely where the cut-off for a ‘small’ package is but rather directly assessed the alternatives for each customer affected.

<sup>30</sup> The Application at [6.2].

<sup>31</sup> The Application at Appendix Four.

<sup>32</sup> For example: [ ] told us it would rather use NZ RPET if it can, as sustainability is a factor it considers (along with price). [ ] [ ] told us that it prefers to procure locally-sourced RPET. [ ] [ ] told us that large customers are asking about, and expressing a preference for, NZ RPET. [ ].

44.2 [ ]  
33].

45. However, we do not consider that there is a separate product market for NZ RPET packaging. Instead, the evidence suggests that packaging made from RPET sourced overseas or virgin PET are close substitutes for, and thus constrain, NZ RPET packaging in a broader product market.

45.1 Several customers told us they prefer NZ RPET packaging but were not prepared to pay more for it than for packaging manufactured from virgin PET or RPET sourced from overseas.<sup>34</sup>

45.2 Manufacturers indicated that although some customers have expressed an interest in NZ RPET, many were also satisfied with overseas RPET.<sup>35</sup>

45.3 [ ]

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46. We considered whether the merged entity could identify those customers that had strong preferences for NZ RPET and price discriminate against them. However, we consider that those customers that appeared to be most interested in NZ RPET had alternatives that the merged entity is likely to view as credible threats. For example, [ ]

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<sup>33</sup> [ ]

<sup>34</sup> For example: [ ] told us it is open to virgin PET and RPET but would only consider paying more for NZ RPET if the price difference was small. [ ]. [ ] told us that, while it prefers to procure locally-sourced RPET, it would not be willing to pay more for NZ RPET over RPET. [ ] [ ] told us it does not differentiate between PET and RPET. [ ]. [ ] told us [ ] that it would have found RPET acceptable but that it wanted to pursue NZ RPET. [ ]

<sup>35</sup> For example: [ ] told us that, in its experience, some customers prefer NZ RPET, but price is the most important factor. [ ]. [ ] told us most customers are happy with RPET. [ ].

<sup>36</sup> [

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Could a separate market for NZ RPET packaging emerge in the future?

47. Our analysis is forward-looking, and we considered whether a narrow market for NZ RPET could develop in future as customers are increasingly considering environmental impacts when selecting packaging. However, we did not consider there is sufficient evidence indicating that a market would be likely to emerge in the coming years.
48. While some customers prefer NZ RPET packaging, it seems unlikely that this preference will become strong enough such that other types of packaging are no longer close substitutes that constrain NZ RPET packaging. Even if customers are increasingly considering the environment when selecting packaging, this does not necessarily mean that a separate market for NZ RPET packaging will emerge. It is possible that customers will also view other materials that have sustainability credentials as close substitutes for NZ RPET. For example, strawberry growers are using cardboard.
49. As such, we consider the relevant market is likely to be wider than NZ RPET packaging in this case.

Is there a separate market for RPET packaging?

50. We next considered whether there is a separate market for all types of RPET packaging from both NZ and overseas, distinct from virgin PET packaging. Both RPET packaging and virgin PET packaging are likely to be in the same market because manufacturers can easily substitute between virgin PET and RPET roll stock. Transport costs are not prohibitive for firms seeking to import virgin PET and RPET. Manufacturers (whether based in New Zealand or overseas) can put either virgin PET or RPET through the same thermoforming process and supply it to customers. As the discussion of customer preferences above suggests, packaging made from RPET

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<sup>36</sup> [ ]

sourced from overseas, virgin PET and NZ RPET packaging appear to be close substitutes for one another.

51. As such we consider the market includes both RPET (including NZ RPET) and virgin PET packaging.

Does the product market include other materials?

52. We considered whether the product market should extend beyond packaging made using PET, as the Applicant argued.
53. Most of the customers we spoke to do not currently consider other materials to be a good alternative to PET for their needs. However, some customers did view other materials as substitutes. For example:
- 53.1 some suppliers of fresh produce such as cherry tomatoes, berries and kiwifruit use cardboard or fibre containers instead of PET; and
- 53.2 some suppliers of meat use alternatives to PET such as cardboard and soft plastic.<sup>37</sup>
54. It is possible the market could be defined more widely than PET packaging.<sup>38</sup> However, we did not need to conclude on this as we consider the Proposed Acquisition would not cause a substantial lessening of competition on a PET packaging market. To the extent other materials are likely to act as constraints on the merged entity, we have taken this into account in our competitive effects analysis.

Conclusion on product dimension

55. For the purposes of our analysis we consider the relevant product market is for PET packaging (including NZ RPET, RPET from overseas, and virgin PET).

*Geographic dimension*

56. We consider the geographic dimension of the relevant market is national because:
- 56.1 the Parties' competing products are supplied throughout NZ; and
- 56.2 competitive conditions do not appear to change significantly depending on the location of domestic buyers and sellers of PET packaging.

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<sup>37</sup> For example Silver Fern Farms packs many of its products in a vacuum packed plastic with cardboard. See <https://www.silverfernfarms.com/for-home/>. Bostock Brothers packs its chicken breasts in vacuum packed plastic bags. See <https://bostocksorganic.co.nz/>

<sup>38</sup> We also considered whether we could define narrower markets, eg, for specific products such as packaging for meat. However, we do not consider it necessary to analyse different product categories in separate markets because: there did not appear to be significant barriers to making moulds for different categories; and, to the extent there were any differences in who is competing in each category, we were able to take this into account within a PET market.

57. Although we use a national market for the purposes of the competition analysis, as we explain below, overseas suppliers do impose a competitive constraint for some customers.

### **With and without scenarios**

58. To assess whether a merger is likely to substantially lessen competition in a market, we compare 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 competition if the merger does not proceed (the scenario without the merger, often referred to as the counterfactual).<sup>39</sup>

### **Scenario with the Proposed Acquisition**

59. The Proposed Acquisition will mean Flight's assets, including the wash plant, will come under the control of Pact Group.

### **Scenario without the Proposed Acquisition**

60. The Applicant submitted that the relevant counterfactual is the status quo. Pact further submitted that, if it does not buy Flight, it would consider [ ].
61. Given the evidence of a trend towards sustainability and growing interest in NZ RPET, we assessed whether Pact or any other suppliers would be likely to build a wash plant in the counterfactual.<sup>40</sup> While this matter was relevant to our assessment of the counterfactual scenario, and is described here for that reason, it is not pivotal to our clearance decision since (as discussed above) NZ RPET packaging is constrained by other forms of PET and we consider it to be in the same product market as other forms of PET.

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62.2.1

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<sup>39</sup> *Mergers and Acquisitions Guidelines*, above n 3, at [2.29].

<sup>40</sup> Pact is likely to require fewer investments than other rivals to establish a closed loop system. Pact has a decontamination plant, extruders and thermoformers. Most other rivals (aside from Flight) only have thermoformers.

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65. We therefore consider the counterfactual against which to assess the Proposed Acquisition is the status quo.

### **Unilateral effects in the market for supply of PET packaging**

66. The Proposed Acquisition would mean that any competition between Pact and Flight to supply PET packaging would be lost. We have therefore assessed whether the merged entity would be able to raise prices or reduce service quality in the New Zealand market for the supply of PET packaging. In conducting our assessment, we considered:

66.1 how closely Pact and Flight compete to supply PET packaging;

66.2 the strength of existing competitors (including suppliers of non-PET packaging, where relevant);

66.3 the extent to which the merged entity would be constrained by potential entry and expansion; and

66.4 the extent to which customers of PET packaging could resist or prevent price increases or decreases in quality.

### **Closeness of competition between Pact and Flight**

67. In the Application, the Parties submitted they are not each other's closest competitors in any given product category where PET packaging is used (for example, meat and seafood trays, or punnets for fruit).<sup>43</sup> In a later submission, Pact and Flight argued that they each compete more closely with different competitors (than with each other) in the product categories where they focus.<sup>44</sup>

68. The evidence we viewed indicated that the Parties are close competitors. Although at present they tend to have high shares in different categories, both have the tooling to compete in all of the major categories. Also, across categories, they are two major suppliers of PET packaging in New Zealand in terms of sales and capacity.<sup>45</sup> At times they appear to compete for the same customers and contracts

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<sup>43</sup> The Application at [7.4].

<sup>44</sup> Pact and Flight, Response to Statement of Issues (20 November 2020), at [28(a)].

<sup>45</sup> The Application at 24-25.

and are likely to see each other as a major threat.<sup>46</sup> This is consistent with [ ].<sup>47</sup>

69. As such, we assessed the Proposed Acquisition on the basis that it would be likely to remove a significant competitive constraint from the market.

### **Constraint from existing competition**

70. We assessed the level of competitive constraint from other suppliers of PET packaging. This includes those suppliers that:

70.1 manufacture locally, such as Custom-Pak, Progressive Plastics, and Formrite; and

70.2 compete by importing finished products made overseas, such as Linpac, Bonson, and other companies that supply plastic packaging in New Zealand.

71. We have also assessed the competitive constraint posed by suppliers of packaging made from materials other than PET, such as cardboard, fibre, and corn starch.

### *Constraint from other local suppliers of PET packaging*

72. Market enquiries revealed that there are several local manufacturers [ ]. These include:

72.1 Custom-Pak: Custom-Pak is the [ ] local supplier of PET packaging, and has manufacturing facilities in both Auckland and Christchurch which it uses to make PET punnets and trays for storing fresh produce, baked goods and meat. Based on our estimates, Custom-Pak's capacity is about [ ].<sup>48</sup>;

72.2 Progressive Plastics: Progressive Plastics makes trays to service local meat processors [ ]. It told us that [ ];<sup>49</sup> and

72.3 Other local suppliers include Formrite and PlusPac, both of which have indicated they [ ].<sup>50</sup>

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<sup>46</sup> For example, both Parties competed to supply [ ], [ ], and [ ]. Both Parties also supply [ ]. Finally, [ ] told us that Pact and Flight are the only suppliers that can meet its requirements [ ].

<sup>47</sup> [ ]

<sup>48</sup> [ ]

<sup>49</sup> [ ]

<sup>50</sup> [ ]

73. Some of the competitors listed are much smaller than the Parties and may not be large enough to be able to meet the requirements for some large customers without further investment. However, we consider the merged entity would likely see these rivals as genuine threats for many customers, because the merged entity may be uncertain about rivals' spare capacity. These firms have moulds suitable for the main applications and [ ].

*Constraint from importers*

74. The Parties submitted that there is a significant and increasing competitive constraint from suppliers that import PET packaging from overseas.<sup>51</sup> The Parties submitted that:
- 74.1 imports have a manufacturing price advantage due to lower labour costs (eg, in Asia) and economies of scale;<sup>52</sup> and
- 74.2 imports make up a large proportion of all PET packaging sold to New Zealand customers, and importers continue to win major contracts.<sup>53</sup>
75. The evidence we have viewed suggests that importers provide some competitive constraint, although not all customers viewed importers as a good alternative. The main concerns that customers raised over using importers rather than local producers were:
- 75.1 buying from local suppliers is more reliable and involves shorter lead times (particularly due to the supply disruptions that COVID-19 has caused);<sup>54,55</sup>
- 75.2 it is more sustainable to buy product from local suppliers than to freight product over longer distances; and
- 75.3 imported product tends to be more generic with less customisation available due to the need to make bulk orders.
76. Despite this, importers appear to have been effective competitors for some customers, [ ]. For example:
- 76.1 [ ]; and

<sup>51</sup> The Application at [1.3(b)].

<sup>52</sup> The Application at [7.9(b)(i)-(ii)].

<sup>53</sup> The Application at 7.9(a)]. Examples include: Linpac winning a significant share of PET packaging following its entry into New Zealand in 2016; and, [ ] winning [ ] units of PET punnets [ ] by sourcing product from [ ].

<sup>54</sup> [ ].

<sup>55</sup> [ ].

76.2 [ ] viewed importers as a good alternative to local suppliers.<sup>56</sup>

77. While we are aware that some customers are unlikely to source imported products, we consider that the merged entity may find it difficult to identify those customers. This is because the choice to use a local supplier or imports appears to mostly come down to customer preferences over factors such as price and supply chain risks, which may be hard to observe. Therefore the merged entity is likely to view importers as a constraint for many customers.

*Constraint from packaging manufactured using other materials*

78. As noted in the Market Definition section above, many customers do not consider alternative materials to be good substitutes for PET. However, there are some customers in certain categories that use alternatives to PET. For example:

78.1 some suppliers of fresh produce such as cherry tomatoes, berries and kiwifruit use punnets made from cardboard or fibre; and

78.2 as noted above, some customers choose to store their meat in packaging made from cardboard and soft plastic.

79. Accordingly, the merged entity is likely to perceive some risk that customers may switch to alternative packaging in response to price increases for PET packaging. It would be unlikely to know with certainty which customers are captive to PET packaging, which will make it difficult to raise prices to those customers and others.

**Constraint from new entry and expansion**

80. The Parties submitted that entry and expansion is easy, arguing that:

80.1 there are no long-term customer contracts; and

80.2 thermoforming equipment is relatively inexpensive while being quick to install and to bring online.

81. Market enquiries suggest that the merged entity will face some constraint from entry and/or expansion. The evidence broadly confirms that it is not difficult or time-consuming to invest in thermoforming equipment.<sup>57</sup> New entrants would also need to buy flake or rollstock, although this does not appear to be a major barrier to entry. Consistent with this, [ ] has said that it is planning to invest in thermoforming

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<sup>56</sup>

[ ]

<sup>57</sup> Firms do not need to have extruders or wash plants to compete in the PET market, as they can buy roll stock directly, eg, from overseas suppliers.

equipment, [ ], and expects to start manufacturing in [ ].<sup>58</sup>

82. Such entry (and the threat of entry) is likely to impose some constraint on the merged entity. However, it is unclear that entry would be at a scale that would impose a strong constraint on the merged entity for customers with high volume requirements. Imports may be a viable alternative for some of these customers.

### **Countervailing power**

83. Countervailing power arises where a customer possesses special characteristics that give it the ability to exert substantial influence on negotiations.<sup>59</sup> For example, this might apply if a customer is large enough to sponsor entry or is able to self-supply.
84. The evidence before us indicates that certain larger customers may have some countervailing power, but that there may be limits to this.
- 84.1 [ ] told us that it could support the entry of a smaller firm but that, in its experience, it can be difficult to arrive at suitable long-term arrangements that suit both parties.
- 84.2 [ ] told us that it is a large company and has “sway” but that it still needed some alternatives to be able to switch to avail itself of that power.
85. Overall, we consider that certain larger customers have some ability to exercise countervailing power. However, it is unclear that smaller customers would benefit from the countervailing power exercised by larger customers. An exception might be where a large customer sponsored the expansion of a smaller E&T rival.

### **Conclusion on horizontal effects in the market for the supply of PET packaging**

86. Post-acquisition, Pact would be a large PET packaging manufacturer in terms of sales and capacity. However, we consider that there are constraints that the merged entity would continue to face. These include:
- 86.1 competition from existing suppliers, many of whom have spare capacity and can expand;
- 86.2 the threat of new suppliers entering the market;
- 86.3 the threat of some customers switching to alternative substrates; and
- 86.4 countervailing power, in the case of some larger customers.
87. Customer size and requirements are diverse and accordingly the degree of each constraint listed differs for each customer. However, we were satisfied that the constraints in combination mean that the Proposed Acquisition will not have, or

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<sup>58</sup> [ ].

<sup>59</sup> *Mergers and Acquisitions Guidelines* above n3 at 31.

would not be likely to have, the effect of substantially lessening competition in a market in New Zealand due to horizontal effects.

### **Coordinated effects in the market for supply of PET packaging**

88. Coordinated effects can occur when a merger or acquisition makes it significantly more likely that the merged entity and one or more of the remaining firms can coordinate their behaviour so as to increase prices (or reduce quality).
89. We assessed whether the Proposed Acquisition would make coordination more likely, more complete or more sustainable in the market for the supply of PET packaging by considering:
- 89.1 whether the market for supply of PET packaging has features that would facilitate (or hinder) attempts by firms to coordinate on price, volume, or alternatively allocate customers between them;<sup>60</sup> and
- 89.2 whether the Proposed Acquisition would make coordination significantly more likely by removing Flight as an independent competitor.
90. We identified some features of the market that might facilitate coordination. For example, there are a small number of large suppliers that all supply similar PET packaging.
91. However, we consider there are factors that may increase the difficulty of coordination and reduce the likelihood of coordinated effects:
- 91.1 prices and volumes are not easily observable, which would make it hard for suppliers to find a focal point for coordination. Another possible means to coordinate could be for the firms to allocate the types of packaging (for example, meat, fruit) between them, although other factors listed below may make this difficult;
- 91.2 there is significant asymmetry between suppliers, who have different business models, specialisations and cost structures. Accordingly, suppliers may find it difficult to agree on prices or a market split that would be mutually satisfactory. The transaction will increase the asymmetry between the firms as Pact and Flight together will be larger (and more vertically integrated) than other suppliers;
- 91.3 in relation to smaller customers, it may be difficult to coordinate on volume or price because jobs are usually ad-hoc (come up irregularly when customers need more stock), and prices vary by job. It would also be difficult for suppliers that specialise in different types of packaging to allocate numerous small customers with different requirements; and
- 91.4 for larger customers that procure PET packaging by tender, contracts differ in size, come up irregularly and tend to be for several years. We consider it

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<sup>60</sup> See *Mergers and Acquisitions Guidelines* above n4 at [3.89].

unlikely that suppliers would easily agree on a mutually satisfactory allocation. There would also be a strong temptation to “cheat” on the agreement in order to win one of the large contracts.

92. On balance, we conclude that the Proposed Acquisition is unlikely to make coordination more likely, complete and/or sustainable. In particular, the transaction is unlikely to increase most coordination factors and will increase the asymmetry between remaining players.
93. As such, we consider it unlikely that the Proposed Acquisition would substantially lessen competition due to coordinated effects.

### **Overall conclusion – no likely substantial lessening of competition**

94. We are satisfied that the Proposed Acquisition will not have, or would not be likely to have, the effect of substantially lessening competition in any of the relevant markets.

### **Determination on notice of clearance**

95. Pursuant to section 66(3)(a) of the Act, the Commerce Commission determines to give clearance to Pact to acquire the assets and business of Flight.