



## COMMERCE COMMISSION

### Decision No. 530

Determination pursuant to the Commerce Act 1986 in the matter of an application for clearance of an asset acquisition involving:

**BONDOR NEW ZEALAND LIMITED**  
**and**  
**LONG INTERNATIONAL LIMITED**

**The Commission:** Paula Rebstock  
David Caygill  
Peter Taylor

**Summary of Application:** The acquisition by Bondor New Zealand Limited (“Bondor” or “Applicant”) of the business assets of the insulated panel business of Long International Limited (“Long International”).

**Determination:** Pursuant to section 66(3) (a)/(b) of the Commerce Act 1986, the Commission determines to decline clearance to the proposed acquisition.

**Date of Determination:** 22 July 2004

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## **EXECUTIVE SUMMARY**

### **The Proposal**

1. A notice pursuant to s 66(1) of the Commerce Act (the Act) was registered on 3 May 2004. The notice sought clearance for the acquisition by Bondor New Zealand Limited (“Bondor” or “Applicant”) of the business assets of the insulated panel business of Long International Limited (“Long International”).

### **Market Definition**

2. The Commission concludes that the relevant product markets are:
  - the New Zealand market for the manufacture and wholesale supply of exterior claddings for industrial, commercial and residential buildings (the national cladding market); and
  - the North and South Island markets for the manufacture and wholesale supply of insulated polystyrene panel for the construction of controlled temperature industrial and commercial buildings (North and South Island insulated polystyrene panel markets).

### **Counterfactual**

3. The Commission considers that the relevant counterfactual is the sale of Long International’s assets to another purchaser. The Commission assumes that the assets would most likely be retained in the South Island and used to establish a competing polystyrene panel operation to Bondor. As such, competition would continue similarly to the status quo, albeit with Long International’s assets under different ownership.

### **Competition Analysis**

#### *Existing Competition*

4. Minimal aggregation would occur in the national cladding market as a result of the acquisition and it is considered the combined entity would continue to face competition from a range of different industry participants producing a range of different products.
5. Competition in the North Island insulated polystyrene panels market is unaffected as no aggregation would take place as a result of the acquisition.
6. In the South Island insulated polystyrene panel market the acquisition would result in a reduction of competitors in the South Island insulated polystyrene panels market to one significant competitor with the combined entity holding a market share in excess of [ ]. The Commission considers that post-acquisition Bondor is likely to face a very limited degree of constraint from Glenroy which is considered to be a niche panel producer and that North Island suppliers only provide a limited constraint due to the difficulty in competitively supplying panels of a thickness of 100mm and above to the South Island (sizes generally required for temperature controlled applications). The Commission, therefore, concludes that the level of existing competition in the

South Island insulated polystyrene panel market would be substantially lower in the factual than in the counterfactual.

### *Potential Competition*

7. The Commission has considered the relevant structural and strategic entry considerations with respect to entry into the market for the manufacture and supply of insulated polystyrene panel. The Commission is of the view that the sunk costs related to entry in this case are moderate but are increased in the factual compared to the counterfactual. The Commission is also of the view that certain strategic considerations would be of particular concern to a new entrant including the potentially more difficult route-to-market in the factual, uncertainty over the future of the market, the excess capacity that would be held by the incumbent and the increased potential for an incumbent response to entry. The combination of these factors leads the Commission to conclude that the barriers to entry into the market for insulated polystyrene panels are significant and that entry is unlikely in the factual.

### **Overall Conclusion**

8. The Commission is required to give clearance to an Application under section 66(3) of the Act if it is satisfied that the acquisition will not lead to a substantial lessening of competition in a market or decline clearance where the Commission is not satisfied that the acquisition will not lead to a substantial lessening of competition in a market.
9. The Commission is satisfied that the proposed acquisition would not have, nor would be likely to have, the effect of substantially lessening competition, in:
  - the national cladding market due to the presence of existing competition; and
  - the North Island insulated polystyrene panel market as no aggregation occurs as a result of the acquisition within the North Island.
10. In this case the Commission has identified a number of issues regarding aggregation of market share and potential entry in the factual scenario in the South Island insulated polystyrene panel market. The acquisition would result in a reduction of competitors in the South Island insulated polystyrene panels market to one significant producer with the combined entity holding a market share in excess of [ ]. The Commission is of the view that the size of the sunk costs required to enter the insulated polystyrene panel market increase in the factual vis-à-vis the counterfactual. The Commission also considers that there are strategic barriers to entry in the factual that increase the overall barriers to entry and make entry in the factual unlikely. These factors include the potentially more difficult route-to-market in the factual scenario, uncertainty over the future of the market, the excess capacity that would be held by the incumbent and the increased potential for an incumbent response to entry.
11. Whilst each factor on its own is not determinative, the combination of these factors results in the Commission not being satisfied, on the balance of probabilities, that the acquisition would not be likely to lead to a substantial lessening of competition in the South Island market for insulated polystyrene panel.

12. Pursuant to section 66(3) (a) of the Commerce Act 1986, the Commission determines to decline clearance for the proposed acquisition by Bondor New Zealand Limited of the business assets of the insulated panel business of Long International Limited.



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## PROCEDURE

18. Section 66(3) of the Act requires the Commission either to clear or to decline to clear a notice given under s 66(1) within 10 working days, unless the Commission and the person who gave notice agree to a longer period. An extension of time was agreed between the Commission and the Applicant. Accordingly, a decision on the Application was required by 22 July 2004.
19. The Applicant sought confidentiality for specific aspects of the Application. A confidentiality order was made in respect of the information for up to 20 working days from the Commission's determination notice. When that order expires, the provisions of the Official Information Act 1982 will apply.
20. The Commission's approach to analysing this proposed acquisition is based on principles set out in the Commission's Merger and Acquisition Guidelines.

## STATUTORY FRAMEWORK

21. Under s 66 of the Act, the Commission is required to grant clearance to an Application, made in accordance with s66(1) of the Act, for an acquisition where it is satisfied that the proposed acquisition would not have, or would not be likely to have, the effect of substantially lessening competition in a market. The standard of proof that the Commission must apply in making its determination is the civil standard of the balance of probabilities.<sup>1</sup>
22. The Commission considers that it is necessary to identify a real lessening of competition that is not minimal.<sup>2</sup> Competition must be lessened in a considerable and sustainable way. For the purposes of its analysis, the Commission is of the view that a lessening of competition and creation, enhancement or facilitation of the exercise of market power may be taken as being equivalent.<sup>3</sup>
23. When the impact of market power is expected to be predominantly upon price, for the lessening, or likely lessening, of competition to be regarded as substantial, the anticipated price increase relative to what would otherwise have occurred in the market has to be both material, and able to be sustained for a period of at least two years.

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<sup>1</sup> *Foodstuffs (Wellington) Cooperative Society Limited v Commerce Commission* (1992) 4 TCLR 713-722.

<sup>2</sup> See *Fisher & Paykel Limited v Commerce Commission* (1996) 2 NZLR 731, 758 and also *Port Nelson Limited v Commerce Commission* (1996) 3 NZLR 554.

<sup>3</sup> See *Queensland Co-Op Milling Assn Ltd* (1976) 25 FLR 169, 515.

24. Similarly, when the impact of market power is felt in terms of the non-price dimensions of competition such as reduced service, quality or innovation, for there to be a substantial lessening, or likely substantial lessening, of competition, these also have to be both material and sustainable for at least two years.

## **ANALYTICAL FRAMEWORK**

25. The Commission applies a consistent analytical framework to all its clearance decisions. The first step the Commission takes is to determine the relevant market or markets. As acquisitions considered under s 66 are prospective, the Commission uses a forward-looking analysis to assess whether a lessening of competition is likely in the defined market(s). Hence, an important subsequent step is to establish the appropriate hypothetical future with and without scenarios, defined as the situations expected:
- with the acquisition in question (the factual); and
  - in the absence of the acquisition (the counterfactual).
26. The impact of the acquisition on competition is then viewed as the prospective difference in the extent of competition in the market between those two scenarios. The Commission analyses the extent of competition in each relevant market for both the factual and counterfactual scenarios, in terms of:
- existing competition;
  - potential competition; and
  - other competition factors, such as the countervailing market power of buyers or suppliers.

## **THE PARTIES**

### **Key Parties**

#### ***Bondor New Zealand Limited ('Bondor')***

27. Bondor, owned by Austral Comnia Holdings Pty Limited in Australia, began operating in 2003 after acquiring the assets of James Hardie Building Systems Limited in 2003. It is involved in both the manufacture and supply of panel, and in the installation of panel by way of tendering and project work.
28. Bondor is the only New Zealand panel manufacturer currently producing panel both in the North Island (Auckland) and the South Island (Christchurch).
29. Bondor produces a range of panels and related materials that are used in both general construction and temperature controlled construction.
30. Bondor is the largest producer of insulated polystyrene panel in the industry with a production of [ ] of panel nationwide for the calendar year 2003. Bondor also



produces an architectural wall and roofing product that is manufactured using pre-profiled steel.

***Long International Limited ('Long International')***

31. Long International began operating in 1974 as a manufacturer of insulated polystyrene panel and related materials in Christchurch. Long International entered the market in Auckland late in 2002 where it operated as a panel manufacturer until exiting in January 2004. Long International sourced its polystyrene from an independent polystyrene manufacturer for its Auckland operation.
32. Long International is, at present, the only company with the ability to produce roll formed roofing and wall cladding panels without the need to use pre-profiled steel. This is done using an attachment to their panel machine which profiles the steel as it is fed through the machine.
33. Long International ceased its project and installation operations in 2001. Since then it has operated as a supply-only business. Contract Coolstores Canterbury Limited and Apollo Projects Limited were formed by Long International employees in 2001 to carry out installation tendering work and project work respectively, though operating as separate companies.
34. The majority shareholder in Long International is Arrow Capital Limited, which is in turn owned by the Arrow International Group Limited (discussed below).
35. Long International is the [ ] largest producer of insulated polystyrene panel in New Zealand producing [ ] of panel in the year ended 31 March 04.

**Other Relevant Parties**

***Lanwood Industries Limited ('Lanwoods')***

36. Lanwoods is a polystyrene panel manufacturer situated in Palmerston North which has been operating since 1968. It produces both a standard polystyrene panel (Styrolock™), and a profiled roofing panel (Styreroof™), that is manufactured using pre-profiled steel.
37. Lanwoods is the [ ] largest panel producer in the country producing [ ] of panel in the 2003 calendar year.
38. Lanwoods manufactures a range of other products including toilet partitions, kitset rooms, polystyrene block and a number of pre-formed polystyrene products.
39. Lanwoods also holds the distributorship rights for Eurobond Laminates Limited (Eurobond) products such as PIR and mineral wool which are imported from Europe.

***The Insulation Panel and Door Company Limited ('IPDL')***

40. IPDL is owned and operated by Phil Julian (a former employee of Lanwood Industries). IPDL commenced operating in Palmerston North in 1997 and is the [ ] largest producer of panel in the country producing [ ] of panel in the year to 31 March 2004.

41. IPDL produces a standard panel product and a roofing panel using pre-profiled steel as well as a number of other products and materials such as raw polystyrene block.

***Glenroy Polystyrene Limited ('Glenroy')***

42. Glenroy is a company located in Blenheim that produces small quantities of polystyrene panel predominately for the construction of its own hireable portable buildings.
43. Glenroy is the smallest producer of panel in the country, producing a total of approximately [ ] of panel annually.

***Apollo Projects Limited ('Apollo Projects')***

44. Apollo Projects undertakes controlled (temperature/air etc) building construction projects that in most cases involve insulated polystyrene panel products or similar products. Apollo Projects also performs supply and installation services of insulated panels through the tendering process.
45. Apollo Projects was formed when Long International ceased its project and installation work in 2001. The current Chief Executive of Apollo Projects (Paul Lloyd) was formerly the Chief Executive of Long International.
46. The majority shareholder in Apollo Projects is Capital Lease Limited, which in turn is wholly-owned by family trusts of the two Directors of Arrow International Group. As such Apollo Projects is deemed to be interconnected with Arrow International Group. [

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47. Long International is the preferred supplier of Apollo Projects given the relationship with Arrow International Group. However, no formal arrangement exists.
48. Apollo Projects also has the distributorship for Kingspan Group Plc ('Kingspan') PIR (polyisocyanurate) and mineral wool products which are imported into New Zealand.

***Arrow International Group Limited ('Arrow International Group')***

49. Arrow International Group was established in 1984 and is involved in construction work in various sectors and industries, in both the North and South Islands.
50. Specifically, Arrow International Group performs strategy management work, involving concept design, construction and management of actual project and construction work.
51. Arrow International owns 100% of the shares in Arrow Capital Limited, which in turn owns 100% of the shares in Long International.

***Pre-formed polystyrene product manufacturers***

52. A number of producers of pre-formed polystyrene products exist that manufacture items such as chilli-bins and the cores of bicycle helmets. Two of these manufacturers are Long Plastics Limited ('Long Plastics') and Poly Profiles Cutting Limited ('Poly Profiles'). Long Plastics in Christchurch [
- ].

53. These two companies were both interviewed in respect of their ability and willingness to supply polystyrene to a new entrant in the insulated panels market and, in the case of Poly Profiles, its ability to source polystyrene block from the North Island.

***Composite Insulation Limited ('Composite Insulation')***

54. Established in Christchurch in 1992, Composite Insulation produces the Thermomass system (described in paragraph 91) for the New Zealand market. Composite Insulation has sold roughly [ ] of its concrete based product into the market in the last year.

***PIR manufacturers***

55. PIR is currently manufactured in Europe by a number of companies, of which Kingspan and Eurobond are two of the larger. Both companies produce a range of PIR products with varying thicknesses and steel profiles. They also produce mineral wool products.
56. Kingspan and Eurobond products are currently imported from Europe and distributed by Apollo Projects and Lanwoods respectively.
57. An Australasian affiliate of Eurobond known as Eurobond Pacific is on the verge of establishing itself in Australia with PIR manufacturing technology. [

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58. Bondor Australia Limited, owned by Metecno Pty Limited ('Metecno'), has also informed the Commission that it intends to start manufacturing PIR panel in Australia within the next 12 months.

***Panel Installers***

59. Panel installers tender for work requiring panel construction and purchase their panel from a panel manufacturer.
60. These panel installers include: Contract Coolstores Canterbury Limited, Contract Coolstores Dunedin Limited, Hi-Tech Building Systems, Supermac Holdings Limited, and Harold Wunderink (an independent installer).
61. Metelcraft Industries Limited are panel installers who also have the right to distribute Metecno products in New Zealand (being owned by Metecno in Australia), including mineral wool panel.

***Insulation blanket providers***

62. A number of companies provide fibreglass insulation blanket, which is used as an insulating material in many construction jobs. Two of these companies are Forman Insulation Limited and Potter Interior Systems Limited.

***Insurers***

63. Many companies who trade internationally or have international interests require international insurance. Two of the larger international insurers are Munich Reinsurance Company Australasia ('Munich RE') and FM Insurance Company

Limited ('FM Global'). A list of approved products is published by FM Global which indicates the different products they have rated and approved.

64. The Commission also interviewed various New Zealand insurance providers including New Zealand Insurance Limited, IAG New Zealand Limited and State Insurance Limited.
65. A representative of the New Zealand Insurance Council was also interviewed about the current state of the New Zealand insurance industry with respect to attitudes towards polystyrene panel and alternative core panels.

***Australian Panel manufacturers and installers***

66. Panel manufacturers in Australia operate in the same fashion as panel manufacturers in New Zealand. The Commission spoke to Australian Urethane and Styrene Limited, PanelTech Industries Australia Pty Limited and Bondor Australia Limited (Metecno) during the investigation.

***Sprinkler Installers***

67. The Commission interviewed several companies in the business of installing and maintaining sprinkler systems in commercial and industrial buildings, to understand the installation and related costs of sprinkler systems. These companies included Fire Security Systems Limited and Compliance Fire Systems Limited.

***End users***

68. A number of companies were interviewed in relation to their attitudes towards differing construction materials, particularly for temperature controlled applications. Parties interviewed included [

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**PREVIOUS DECISIONS**

69. The Commission previously cleared (Decision 412, 15 December 2000) a proposed acquisition of the assets of Long International by James Hardie New Zealand Limited through one of its divisions, James Hardie Building Systems. Bondor New Zealand Limited entered the New Zealand market in 2003 through the acquisition of James Hardie Building Systems.
70. In that case the Commission determined that James Hardie would not face a significant degree of constraint from existing competition, but that potential entry into the market was likely and sustainable, sufficient in extent and timely so as to satisfy the Commission that the acquisition would not result in the strengthening of a dominant position, despite the high aggregation involved. This acquisition did not proceed.
71. The Application in that case was determined under the 'dominance test' that was the threshold at the time under s47 of the Commerce Act. The section was subsequently amended in 2001 to a test of whether the acquisition would be likely to result in a substantial lessening of competition.

72. As will be discussed in later sections, the market and factual situation has also changed since Decision 412, particularly in respect of the emergence of several new alternative core insulation products.

## **INDUSTRY BACKGROUND**

73. Bondor and Long International are two of the five polystyrene panel producers nationwide that have the manufacture and supply of insulated polystyrene-based panel as their core business activity. The other New Zealand polystyrene-based panel manufacturers are Lanwoods, IPDL and Glenroy.
74. The raw material used for the manufacture of expanded polystyrene is imported into New Zealand as grains approximately the size of common domestic sugar. The raw material, in grain form, as imported, has a much higher density than expanded polystyrene and this reduces transport costs per unit of volume. Expansion of the grains into polystyrene beads of various sizes and densities, by the addition of heat, occurs at several manufacturing plants throughout New Zealand. Expanded polystyrene has a low value per unit of volume (its volume is mostly air).
75. Subsequent addition of more heat and pressure to the previously expanded polystyrene beads, within moulds in block and profile moulding machines, allows the production of large blocks of polystyrene and polystyrene shapes for various applications.
76. Polystyrene sheets laminated on both sides with steel sheets of various profiles find use in the construction of controlled temperature buildings. The panels are suitable for this application because of their insulating properties, their high strength to weight ratio and their relatively low cost. The panels are manufactured using a panel machine and raw materials of expanded polystyrene, steel and glue. The steel used in the manufacture of panels is purchased, typically from NZ Steel, in coils that are 1200mm wide and .59mm thick. A total of approximately [ ] of panel was produced in 2003 with roughly [ ] of that being produced in the South Island.
77. The insulated panels are manufactured in a continuous process machine whereby polystyrene sheets are sandwiched between two sheets of steel which are continuously glued to the polystyrene sheets as they pass through the machine. The panel is then cut to the desired length.
78. The thickness of the final panel produced depends on the temperature difference against which the panels are required to insulate, and the strength required from the panels as load-bearing walls of controlled temperature buildings. Freezer panels are typically 250 millimetres thick, while cool store panels may be only 100 millimetres thick. Panel of varying thicknesses can be produced relatively easily by varying the size of the polystyrene block, which in turn is cut from a larger block using a wire cutting table. At present panel is produced in New Zealand at thicknesses that range from 25mm to 300mm.
79. Polystyrene panels are also used commonly as an architectural cladding and structural building material for commercial buildings. This application, which is largely independent of polystyrene panels' traditional insulation role, relies on the panel's

weather resistance, light weight per square metre and, in some circumstances cost advantage, and competes with other more traditional exterior claddings and structural building materials. The fact that it is also a good insulating material is a further consideration.

80. Whilst it is manufactured as a steel laminated panel in the same process, polystyrene architectural panel differs from insulated wall panel in that it is commonly of a lesser thickness and is often coloured. Long International's panel machine can produce architectural panel with substantial corrugations allowing its product to be used for "architectural" type roofing. A comparable product can be produced with a standard panel machine using pre-profiled steel which is fed manually through the panel machine and laminated to the polystyrene block although the steel corrugations are not filled with polystyrene as with Long's product.
81. With the exception of the insulated panels manufactured by Glenroy, only minor differences exist in respect of the size and shape of the panels, the profiles of the steel laminations and in the jointing arrangements between individual panels. Glenroy produces panels which are joined together in construction through the use of a connecting bolt that is 'H' shaped. Other panel producers produce panel that is interlocking through what is called an 'S' lock. The 'S' lock system is the preferred system amongst panel installers as it is simpler and less labour intensive in the construction process.
82. Although its structure and ownership has changed, both Long International and Bondor have participated in the market for approximately 30 years, as has Lanwoods in Palmerston North. IPDL is the most recent entrant into the market, setting up a competing operation in Palmerston North in 1997.
83. Long International expanded its operations in December 2002 by entering the North Island with a panel manufacturing operation. Long International closed that operation after approximately 13 months and now operates solely from Christchurch.
84. Since the Commission's determination in Decision 412 the global industry has changed somewhat with the emergence of several new insulation alternatives, and increased concerns, particularly from a fire and insurance perspective, about the use of polystyrene panel. Most industry participants attribute the emergence of these alternatives to a number of recent fires, and to the more conservative attitude of insurers since the events of 11 September 2001.
85. Rigorous fire safety testing is now carried out for most construction materials such as polystyrene panel, the most common of which is a 'corner test'. A corner test is a simulated environment in which pallets are ignited next to two walls and a roof of panel that are joined to form a 'corner'. The purpose is to test whether the walls and roof will self-propagate the fire and destroy the test building. Polystyrene panel does not meet the standards set by FM Global though the Commission has been informed that polystyrene only narrowly misses FM Global's criteria when correctly installed.
86. It is commonly accepted that for insurance purposes sprinkler systems need to be installed in all polystyrene buildings larger than 200m<sup>2</sup>. The Commission has been

informed by a number of risk assessors that sprinklers are also required in PIR buildings of a similar size in order to protect both the building and the stock.

87. Other insulation materials, including several 'alternative core' based sandwich panels are currently available that include: Thermomass; polyisocyanurate (PIR) panel; polyurethane panel; mineral wool panel; Polyphen and fibreglass insulation blanket.
88. PIR, polyurethane and mineral wool panels are all similar to polystyrene panel in design. These different materials form the insulation core of the sandwich panel which is laminated between sheet metal as is polystyrene panel. The panel is made in varying thicknesses to cater for the varying applications of the panel.
89. PIR panel is currently imported from Europe into the New Zealand market by Lanwoods (which distributes Eurobond products) and Apollo Projects (which distributes Kingspan products). The key selling feature of PIR panel is that the core is a thermosetting plastic that will char and form a protective seal when exposed to heat. This ultimately means that there is a much reduced fire risk with the product when compared to polystyrene panel. PIR panel also appears to have marginally better insulation characteristics than polystyrene panel.
90. Mineral wool panel has a rock fibre insulation core that does not burn. It is heavier than an equivalent PIR or polystyrene panel and is not suitable for applications requiring a controlled temperature of below five degrees Celsius.
91. Thermomass is constructed using a fibre composite connector rod to sandwich a sheet of Styrofoam between two slabs of concrete. The connector rods are made from a low conductivity material that helps to avoid any loss in insulation value. The concrete slabs are resilient against weathering and prevent all water penetration or vapour transmission. Construction of the Thermomass product is relatively labour intensive as the concrete slabs are mixed and poured onsite. Thermomass is completely fire proof when installed correctly. Thermomass is also a very durable construction material due to its concrete exterior.
92. Thermomass has been used in wineries, prisons, small commercial buildings and in many other applications. However, due to its cost (around \$240/m<sup>2</sup> compared to roughly \$40/m<sup>2</sup> to \$50/m<sup>2</sup> for polystyrene panel) it finds limited value as a general structural material. It also cannot be used as a roof spanning product due to its weight.
93. Polyphen is a newly developed product that is made from a phenolic foam (phenol formaldehyde foam) and sandwiched between sheet metal. It has recently been given the best FM Global fire rating as a result of it only charring when exposed to heat. It also appears that Polyphen panel can be produced using existing polystyrene panel machine technology. XFlam is a very similar product and purports to have good fire resistance, low thermal conductivity, good mechanical strength and a low production cost.
94. Fibreglass blanket is another building material that is used to provide insulation. It is usually encased in timber cladding, or with wire mesh for roofing applications. It is not suitable for low temperature applications but is often preferred in other instances

because it can be used with most exterior wall claddings, such as timber, which may be preferred for aesthetic reasons.

95. Panel is usually installed either by the panel manufacturer through its own or sub-contracted labour, or by specialist panel installers. Depending on the intended use of the panel, other materials such as doors, door handles and aluminium flashings are also purchased at the same time from the panel manufacturer.
96. Long International is, at present, the only panel manufacturer that operates on a supply-only basis. It has developed relationships with many independent panel installers, such as Contract Coolstores Canterbury and Hi-Tech Building Systems, in the South Island.

## MARKET DEFINITION

97. The Act defines a market as:

“... a market in New Zealand for goods or services as well as other goods or services that, as a matter of fact and commercial common sense, are substitutable for them.”<sup>4</sup>

98. For competition purposes, a market is defined to include all those suppliers, and all those buyers, between whom there is close competition, and to exclude all other suppliers and buyers. The focus is upon those goods or services that are close substitutes in the eyes of buyers, and upon those suppliers who produce, or could easily switch to produce, those goods or services. Within that broad approach, the Commission defines relevant markets in a way that best assists the analysis of the competitive impact of the acquisition under consideration, bearing in mind the need for a commonsense, pragmatic approach to market definition.<sup>5</sup>
99. For the purpose of competition analysis, the internationally accepted approach is to assume the relevant market is the smallest space within which a hypothetical, profit-maximising, sole supplier of a good or service, not constrained by the threat of entry, would be able to impose at least a small yet significant and non-transitory increase in price, assuming all other terms of sale remain constant (the SSNIP test). The smallest space in which such market power may be exercised is defined in terms of the three dimensions (product, functional and geographic) of the market discussed below. The temporal and customer dimensions are not relevant to the analysis in this case. The Commission generally considers a SSNIP to involve a five to ten percent increase in price that is sustained for a period of one year.

### Product Market

100. Initially, markets are defined for each product supplied by two or more of the parties to an acquisition. For each initial market so defined, the Commission considers whether the imposition of a SSNIP would be likely to be profitable for the

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<sup>4</sup> s 3(1A) New Zealand Commerce Act 1986.

<sup>5</sup> Australian Trade Practices Tribunal, *Re Queensland Co-operative Milling Association*, above note 10; *Telecom Corporation of NZ Ltd v Commerce Commission & Ors* (1991) 3 NZBLC 102,340 (reversed on other grounds).



hypothetical monopolist. If it were, then all of the relevant substitutes must be incorporated in the market.

101. The greater the extent to which one good or service is substitutable for another, on either the demand-side or supply-side, the greater the likelihood that they are bought and supplied in the same market. The degree of demand-side substitutability is influenced by the extent of product differentiation.
102. Close substitute products on the demand-side are those between which at least a significant proportion of buyers would switch when given an incentive to do so by a small change in their relative prices.
103. Close substitute products on the supply-side are those between which suppliers can easily shift production, using largely unchanged production facilities and little or no additional investment in sunk costs, when they are given a profit incentive to do so by a small change in their relative prices.
104. The Applicant has submitted that two product markets are relevant to the determination, namely:
  - the market for exterior architectural claddings for industrial, commercial and domestic residential buildings (architectural cladding market); and
  - the market for insulated panels and blankets (or, alternatively, polystyrene-based and “alternative core” insulated panels and blankets) for the construction of controlled temperature commercial and industrial buildings (insulated panel market).

#### **Architectural cladding market**

105. The Applicant has submitted that it agrees with the Commission’s approach to the architectural cladding market in Decision 412 in defining a New Zealand market for the manufacture and supply of exterior architectural claddings for industrial, commercial and domestic residential buildings.
106. In Decision 412 the Commission considered that polystyrene panels used as an exterior wall cladding formed part of a broader market that included a range of differentiated alternatives embodying different qualities at different prices, including fibre cement products, brick veneer, steel, timber, concrete slabs and blocks, etc. Polystyrene panels are used in this market for their weather resistance, ease of construction and other characteristics, rather than their insulating properties. Here the choice of the particular material depends on the preferences of the architect and his/her client.
107. In many instances polystyrene panels used for a structural or cladding purpose have profiled steel exteriors which make them more suitable functionally and aesthetically for exterior wall and roof applications than a standard insulated panel. Long International’s panel machine is capable of profiling the steel as it is fed through the panel machine and laminated to the polystyrene block. Other panel manufacturers have the ability to feed pre-profiled steel into their panel machine in order to produce a comparable product.

108. As determined in Decision 412, polystyrene panel is preferred in some instances for its lightness, ease of construction and self-supporting qualities, particularly for high span roofs where, as one industry participant has said, the cost of construction is greatly reduced due to the reduced need for steel support structures. One example of such construction is the ‘Aquagym’ swimming pool in Christchurch, which was designed and built by Armitage Williams Construction. However the Commission is of the view that for similar applications, alternative structural and cladding products are often preferred for other reasons. One example of this is the recent approach by [
- ]
109. Polystyrene panel, used for a cladding purpose, is usually of a thickness of below 100mm. The thickness used will ultimately vary with the specifics of the individual case but in general the end use of panel as a cladding material is not wholly reliant on its insulating properties and thus thicker panel sizes are not necessarily required.
110. The Commission is of the view that although polystyrene panel may be preferred as a structural or cladding material in some applications, other products, including those listed above, may be preferred in other applications. In general the Commission considers that there is a range of substitutable alternatives for the bulk of construction projects in terms of the structural or cladding product used.
111. The Commission therefore concludes that it is appropriate to define a product market consisting of a range of cladding products used in the construction of industrial, commercial and residential buildings.

### **Insulated panel market**

112. In Decision 412 the Commission was of the view that there was a distinct product market for polystyrene insulated panels for the construction of controlled temperature commercial and industrial buildings.
113. Typical applications of insulated panels are for stand-alone cold stores, cool rooms within supermarkets, freezers for the freezing and storage of primary produce, wineries for the low temperature storage of wine, facilities for the processing of meat and chicken products and controlled temperature warehouses.
114. It is generally the case that thicker panel sizes of above 100mm are used for temperature controlled applications of polystyrene panel. The Commission has been informed that for sub-zero applications of the panel a thickness of 250mm to 300mm is required.
115. The Applicant has submitted that this market should include a range of alternative core panel products including PIR, mineral wool, Polyphen, Polyurethane and Thermomass, as well as other materials used for insulation purposes such as fibreglass insulation blanket. Some of these products have only recently been introduced into New Zealand (PIR and mineral wool), whilst XFlam has only recently been introduced globally.

116. Each product, as explained in the industry background section, has differing characteristics in terms of insulation qualities, weight, fire rating, ease of construction and price.
117. These alternative core products suggested by the Applicant were not considered in Decision 412 as they were not commercially produced at the time.

PIR panel

118. The Commission has identified that there is a significant cost differential between polystyrene and PIR, PIR being in the vicinity of 70% to 100% more expensive depending on the thickness of panel. Polystyrene panel ranges in price from around \$35 to \$55/m<sup>2</sup> whereas PIR panel would cost roughly \$70 to \$90/m<sup>2</sup> for an equivalent panel.
119. The Applicant has submitted that the cost of polystyrene panel should be compared with the cost of PIR panel based on the value of a complete construction job, which involves many more costs than the panel itself. The Applicant claims that whilst PIR panels are considerably more expensive, the total building cost in using PIR panels in comparison to polystyrene panels means they are effectively only 25% more expensive.
120. Bondor informed the Commission that sprinkler systems are often required by insurance companies where polystyrene panels are used and further submitted, as a way of illustrating the potential cost of such an installation, that the cost of installing a sprinkler system in Bondor's Auckland factory was around [ ]. Hence, it was submitted that the higher related costs (insurance and sprinkler fitting costs, etc.) associated with the use of polystyrene panel ultimately make PIR and polystyrene panels more comparable in price.
121. Whilst it is true that sprinkler systems are required in the majority of cases where insurance is sought for a polystyrene panel-constructed building, the Commission has also been informed by a number of insurance risk assessors, including Peter Matheson, of Ace Risk Management Services, that sprinkler systems are also invariably required to be installed in a building constructed from PIR.
122. Most insurers spoken to during the course of the investigation said that the insurance industry's primary focus is on the structure, design and risk in the individual case, rather than purely on the material with which the building is constructed. Peter Matheson stated that sprinklers mitigate the risk associated with insurance as they protect the stock held within the plant as well as the building itself. As the building itself usually forms a very small part of the business as a whole, the need for sprinklers, even in a PIR building, becomes more of a factor.
123. Stuart Warden, of FM Global, stated that FM Global requires sprinklers only in polystyrene buildings that are larger than 200m<sup>2</sup>, which would automatically exclude most coolstore and temperature-controlled applications of the panel.
124. The Commission was informed that despite the fire risk associated with polystyrene panel, it does not represent a significant fire risk when effectively protected. Peter Matheson told the Commission that he was unaware of any polystyrene panel building protected by sprinklers that had burnt down, and that the use of polystyrene

panel combined with an effective sprinkler system was currently acceptable to most insurers in New Zealand.

125. The Applicant also submitted that the cost differential is somewhat mitigated through lower insurance premiums in respect of PIR due to its greater fire resistance. However, Neil Gravestock, Fire Engineering Consultant, informed the Commission that, at the moment, the insurance premiums for a polystyrene building with sprinklers are in general a lot lower than premiums for an unprotected PIR building and that there is little difference between a protected polystyrene building and a protected PIR building. He said that this was often the case because in a sprinkler protected building there is very little chance of either type of building being destroyed.
126. Bob Oldnall of Munich RE stated that it is generally the case that PIR is looked on more favourably than polystyrene panel on a straight panel comparison, but the risk is always assessed on a case-by-case basis. He also confirmed that sprinklers will mitigate risk, regardless of the building material used.
127. The Commission is aware of the imminent arrival of PIR plants in Australia, which is expected to reduce the cost of PIR panel to New Zealand due to the decreased freight costs. Stuart Warden, of FM Global Insurance, stated that with the imminent entry of Eurobond Pacific and Bondor Australia into the Australian market as manufacturers of alternative core products, polystyrene panel is likely to come under 'heavy pricing attacks'. Eurobond Pacific estimated that the panel would still be considerably more expensive (twice the price) than polystyrene, but the cost to the end user in NZ may be as much as [ ] less than what it would cost to import from the United Kingdom due to the reduction in freight costs. [ ] Even making allowance for a potential decrease in the price of PIR panel in the near future the Commission considers that a hypothetical, profit-maximising monopolist would not be constrained by the threat of substitution away from polystyrene panel such that it would be unable to profitably impose a 5% to 10% SSNIP to the price of polystyrene panel.
128. Even taking into account the full costs of using both types of panel, and the likely decrease in the costs of PIR panel, due to the opening of Australian production facilities, the Commission is of the view that the relative prices of polystyrene panel and alternative core panels are still likely to be of a degree that a 5% to 10% SSNIP applied to the price of polystyrene panel would be likely to cause very little substitution away from polystyrene panel to alternative core panels.
129. The delineation of separate markets for PIR panel and polystyrene panel also reflects the view of the majority of industry participants interviewed during the investigation. This view was generally based on the relative cost of PIR panel and the current attitude of New Zealand insurance companies.
130. The balancing of these considerations and the price differentials involved leads the Commission to conclude that it is appropriate in this case to consider that PIR does not fall within the same market as polystyrene insulated panels in the period of relevance.

### Mineral wool

131. Mineral wool panel is another product that has started to be imported into New Zealand by a number of industry participants. Mineral wool, again, has differing properties and accordingly is more suited to some particular applications. In particular, it does not burn and has a much better fire performance than polystyrene. On the other hand it is even more expensive than PIR panel, being more than double the price of polystyrene panel on a square metre comparison.
132. The Commission has been informed by several industry participants that mineral wool panel is not suited to some particular applications due to the nature of the core material. It has been suggested that mineral wool is not suitable for temperatures below five degrees Celsius and thus cannot be used in the construction of freezers or coolstores for which low temperatures are required. The Commission has further been informed that mineral wool panel is not desirable for applications involving primary produce due to the risk of contamination from wool fibres should the integrity of the panel surface or structure be damaged in any way. Very small quantities of mineral wool panel have been supplied into the New Zealand market to date.
133. The Commission is of the view that, as with PIR panel, mineral wool panel may be used in limited quantities for specific applications where a non-flammable product is essential. However, the Commission considers that the market penetration of mineral wool, due to the factors identified above, is likely to be minimal, and given its significant price differential does not fall in the same market as polystyrene panel.

### Polyphen/Xflam/polyurethane

134. The Commission is also of the view that the other alternative core products suggested by the Applicant do not fall within the same market as polystyrene panel. Polyphen (or XFlam) is not currently being supplied into New Zealand, having only recently been introduced to the United Kingdom market, and thus is not considered as forming part of the market at this point in time. Similarly, polyurethane panel appears to be obsolete in the New Zealand market and no longer a substitution possibility for all but a very limited number of applications. The Commission is not aware of any manufacturers currently producing polyurethane panel in New Zealand.
135. Accordingly a SSNIP applied to the price of polystyrene panel would not induce a switch to these alternatives due to their unavailability.

### Thermomass and fibreglass insulation blanket

136. Thermomass also differs substantially from polystyrene panel in that it is manufactured at the construction site and consists of two concrete slabs, making it a considerably more heavy-weight product. As such it is unsuitable for many applications such as roofing. Thermomass is also considerably more expensive than both polystyrene and PIR panel, costing up to 300% more than polystyrene panel.
137. Alan Freeman of Composite Insulation Limited stated that Thermomass does not compete with the lighter-weight products such as polystyrene. He stated that the primary point of difference for Thermomass was the physical mass and durability of a

concrete based product, which would make the product attractive for some customers in limited circumstances.

138. Fibreglass insulation blanket installed in timber or steel wall framing is also not considered to be a substitution possibility such that it should be included in the same market as polystyrene panel. Brian Bamforth, of Potter Interiors (a supplier of such insulation materials), stated that circumstances will dictate which product is the most suitable to use, and that it is rare for blanket to compete for a job for which panel is being considered as an alternative. Although the use of fibreglass blanket will provide a degree of insulation, it appears that for low temperature applications (below five degrees Celsius) fibreglass blanket is not a substitution possibility. The installation of a blanket insulation system is also much more labour intensive, as the blanket does not come laminated between steel, and a high degree of care is needed to insure that the integrity of the insulation is not compromised in the installation of the product. This issue is largely avoided with the installation of an interlocking panel system.
139. It appears that Thermomass and fibreglass-based insulation systems will be used in particular circumstances based on the preferences of the architect and the client. There is also little evidence of actual or potential substitution between these products and standard steel-based panel products.

#### Conclusion on product market

140. The Commission concludes that for the reasons outlined above the product market should be limited to polystyrene panel only. There appears to be no substitution alternative for which demand would increase, upon the application of a 5% to 10% SSNIP to polystyrene panel, to such an extent as to make the application of that SSNIP unprofitable for a hypothetical monopolist manufacturing polystyrene panel. The Commission has also considered a number of non-price comparisons and differing product characteristics in reaching this conclusion. While the Commission recognises that there are advantages provided by differences in product characteristics (in particular fire properties), current and likely future climate with respect to insurers' attitudes towards the product are likely to result in slow uptake of PIR over the next few years, with PIR likely to be the product of choice only in limited situations.
141. The Commission has also found that insulated panels are used primarily in the construction of industrial and commercial buildings rather than domestic residential buildings. Insulated panel is used primarily for the construction of cool-stores, chillers, freezers and storerooms requiring an insulated quality. Invariably these uses are in the industrial and commercial setting. This finding is consistent with the finding in Decision 412.
142. Accordingly the Commission concludes that the appropriate product dimension is the market for insulated polystyrene panels for the construction of controlled temperature commercial and industrial buildings.

### **Functional Markets**

143. The production, distribution and sale of a product typically occurs through a series of functional levels, conventionally arranged vertically in descending order. Generally, the Commission identifies separate relevant markets at each functional level affected by an acquisition, and assesses the impact of the acquisition on each.
144. Both Bondor and Long International manufacture polystyrene panel and supply it into the market. Accordingly the Applicant has submitted that the relevant functional level is that for manufacture and supply. The Commission is of the view that the manufacture and wholesale supply is the correct functional definition in this case.
145. Bondor is also involved in the installation of panel in the New Zealand market. Many South Island installers of panel (who purchased until very recently from Long International) expressed concern to the Commission that in the counterfactual they will need to purchase their panel from Bondor with which they will also be competing at the installation functional level. The Commission is of the view, however, that any effect that may occur as a result of the acquisition in this market will be a flow on effect from the state of competition in the manufacture and wholesale supply market. As such the identification of a distinct installation market is not necessary for the purposes of the analysis as the effect, if any, will be adequately captured in analysing the upstream manufacture and wholesale supply market.

### **Geographic Markets**

146. The Commission defines the geographic dimension of a market to include all of the relevant, spatially dispersed sources of supply to which buyers would turn should the prices of local sources of supply be raised.

#### **Architectural cladding market**

147. The Applicant has submitted that this market should be national in extent as determined in Decision 412. It also appears that panel with profiled steel is more expensive per cubic metre than regular panel and thus freight costs are proportionally less as a proportion of the delivered price of the panel. This results in a greater degree of competition being possible between the North and South Island in respect of these products. Other cladding and building products are available from a multitude of suppliers all over the country, many of which have national offices.
148. The Commission, therefore, concludes that it is appropriate for the purposes of the analysis to consider the market for architectural cladding as being national in scope.

#### **Insulated polystyrene panel market**

149. The Applicant has submitted that the market for insulated polystyrene panels is national in extent. The Applicant states that it believes competition between the Islands has increased since the determination in Decision 412. The Applicant also states in its Application that it believes transportation costs are significantly lower than those the Commission considered in Decision 412. The Applicant submitted that

transportation costs are as low as NZ\$20 per cubic metre between Christchurch and Auckland, which could be as low as 4% to 5% of the total cost of supply.

150. Stephen Gale, of Castalia Strategic Advisors, submitted to the Commission on behalf of the Applicants that South to North shipping of panels appears to cost around \$2.4/m<sup>2</sup>, which he suggests is not so high as to make panel from the North Island uncompetitive as the freight charge is below the level of a SSNIP that the Commission would apply to South Island prices (as it equates to less than 5% of the panel cost). He suggests that separating the markets into distinct North to South markets would require freight to be about twice this level.
151. The Commission's findings do not support this assessment. The \$2.4/m<sup>2</sup> cost submitted by Stephen Gale appears to be based on 100mm thick panel (derived from a cubic metreage rate). This cost estimate would double for 200mm thick panel for transportation of the same square metreage. As panel thickness increases, the square metreage of panel able to be transported in a given volume decreases. This results in freight rates being proportionately higher for thicker panels which makes it difficult for such panel to be competitively supplied into the South Island.
152. The Commission has been informed by a number of industry participants that the cost of freight from North to South is considerably more expensive than that indicated in the application and more expensive than the 'backhauling' freight rates that apply to freighting from the South to North Island. Ian Smith from Owens Transport stated that the cost of freighting insulated polystyrene panel from Palmerston North to Christchurch is approximately [ ], and that to Dunedin or Invercargill the price is approximately [ ]. These rates equate to a cost of roughly [ ] for 100mm panel and [ ] for 200mm panel. The Commission notes that Owens has occasionally transported panel to the South Island from Palmerston North in the past.
153. The Applicant has submitted that Lanwoods and IPDL compete within the South Island by supplying panel from their Palmerston North based operations. Lanwoods informed the Commission that they have supplied panel to [ ] jobs in the South Island this year and [ ].
154. There has also been an indication that panel has been supplied between the Islands primarily to fulfil national contracts or upon specific request by an installer of panel following unsatisfactory dealings with local panel suppliers. [ ]
155. The Commission considered average price data which, while inconclusive, seemed to suggest that a distinction based on panel thickness may be appropriate. The cost of freighting between the Islands suggests a SSNIP may be profitable for the combined entity on panel sizes of 100mm and above. Similarly, many industry participants informed the Commission that sourcing 200mm panel from the North Island for a job in the South Island is not economic as the applicable freight cost is prohibitive. John Lockwood of Lanwood Industries informed the Commission that the price would



have to increase a further [ ] in the South Island before 200mm polystyrene panel from the North Island would become an economic option. The Commission has conducted its own analysis of this claim and found that this is a fair approximation.

156. The Commission received differing opinions as to which panel thicknesses could be competitively ‘imported’ from the North Island into the South Island. However, most parties considered that at least for the thinner panels, North Island suppliers were an option, particularly for larger jobs.
157. The Applicant pointed out to the Commission that around 70% of the total panel produced is of a thickness of less than 100mm and that this should weigh more heavily when defining the geographic market. However, the Commission has been informed by various industry participants that in the market for controlled temperature application of panel, the majority of panel used is of a thickness of 100mm and above. As such the Commission is of the view that the competition effect in terms of the thicker sizes of panel should be given at least an equal if not greater weight in considering the geographic market dimension in this case.
158. Bondor also suggested that the ability of Poly Profiles to source 600mm polystyrene block from Palmerston North is an indication that freight costs are not prohibitively expensive. However, the Commission found that the potential polystyrene block suppliers to Poly Profiles in the South Island (Bondor and Long Plastics) both have a competing polystyrene profiling businesses, and thus may have a limited incentive to provide raw materials at low costs to their competitors. It is also evident that [

]. As such, the Commission is of the view that this example does not provide a close indication of the transportation possibilities for insulated polystyrene panel.

159. Chris Bissett, of Contract Coolstores Dunedin, informed the Commission that it is often difficult to source panel from the North Island due to the time delays and logistics involved. Whilst the Commission considers that any time lag (based on the total length of the construction process) is likely to be minimal, the problem of replacement panel if required is particularly relevant. If a panel shipped from the North Island to the South is damaged in transit, or needs to be replaced for another reason, difficulties may arise in replacing the panel at an efficient cost.
160. Despite the ability of thinner polystyrene panel thicknesses to compete on more of a national basis the Commission is of the view that, on balance, the conservative and most appropriate approach in this instance is to define separate North Island/South Island markets due to:
  - the freight rates that apply to panel transported between the Islands particularly in respect to thicker panel sizes;
  - the limited frequency with which panel has been transported between islands; and
  - the views of the majority of industry participants.
161. Any differing competitive effects relating to panel thickness can be accounted for in the competition analysis.

## Conclusion on Market Definition

162. The Commission, therefore, concludes that the relevant product markets are:
- the New Zealand market for the manufacture and wholesale supply of exterior claddings for industrial, commercial and residential buildings (the national cladding market); and
  - the North and South Island markets for the manufacture and wholesale supply of insulated polystyrene panel for the construction of controlled temperature industrial and commercial buildings (North and South Island insulated polystyrene panel markets).

## FACTUAL AND COUNTERFACTUAL

163. In reaching a conclusion about whether an acquisition is likely to lead to a substantial lessening of competition, the Commission makes a “with” and “without” comparison rather than a “before” and “after” comparison. The comparison is between two hypothetical future situations, one with the acquisition (the factual) and one without (the counterfactual).<sup>6</sup> The difference in competition between these two scenarios is then able to be attributed to the impact of the acquisition.

### The Factual

164. The Applicant has submitted that the rationale for the acquisition is [

] The  
Commission notes that [

]

165. The acquisition involves the transfer of assets involved in the manufacture of polystyrene panel, including intellectual property rights and goodwill in respect of the panel business. The transfer specifically includes the “Metric Roof” and “Metric Wall” roll-forming assets of Long International. The transfer does not include Long International’s polystyrene machine which, Long International has informed the Commission, will most likely be sold to Long Plastics in Christchurch.
166. The acquisition will result in aggregation in respect of the manufacture and wholesale supply of polystyrene panel. No aggregation takes place in respect of polystyrene production machinery. Similarly no aggregation takes place in respect of the “Metric Roof” or “Metric Wall” roll-forming assets as Bondor is currently not producing these products.

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<sup>6</sup> Commerce Commission, *Decision 410: Ruapehu Alpine Lifts Ltd/Turoa Ski Resorts Ltd (in receivership)*, 14 November 2000, paragraph 240, p 44.

## **The Counterfactual**

167. Long International informed the Commission that [

]

168. Whilst this Application has been under consideration, Long International has ceased its panel-making operations. The Commission has been informed that [

]

169. Bondor has subsequently submitted to the Commission that [

] The Commission has considered these points and concluded that it is not appropriate to amend the counterfactual in this case.

170. The Commission has [

].

171. The Commission, therefore, is of the view that the relevant counterfactual is the sale of Long International's assets to another purchaser. The Commission assumes that the assets would most likely be retained in the South Island and used to establish a competing polystyrene panel operation to Bondor. As such, competition would continue similarly to the recent past, albeit with Long International's panel manufacturing assets under different ownership.

## **COMPETITION ANALYSIS**

### **Existing Competition**

172. Existing competition occurs between those businesses in the market that already supply the product, and those that could readily do so by adjusting their product-mix (near competitors). Supply-side substitution by near competitors arises either from redeployment of existing capacity, or from expansion involving minimal investment, in both cases involving a delay of no more than one year.

173. An examination of concentration in a market can provide a useful indication of the competitive constraints that market participants may place upon each other, providing there is not significant product differentiation. Moreover, the increase in seller concentration caused by a reduction in the number of competitors in a market by an

acquisition is an indicator of the extent to which competition in the market might be lessened.

174. The Commission estimates market shares for all significant participants in the relevant market. Market shares can be measured in terms of revenues, volumes of goods sold, production capacities or inputs (such as labour or capital) used. For the purposes of this analysis the Commission concludes it is appropriate to define market shares on the volumes of panel (m<sup>2</sup>) supplied to the market as panels are largely undifferentiated.
175. An aggregation that would result in a very small change in the level of market concentration is unlikely to be associated with a substantial lessening of competition in a market. On this basis, indicative safe harbours may be specified.
176. A business acquisition is considered unlikely to substantially lessen competition in a market where, after the proposed acquisition, either of the following situations exist:
  - where the three-firm concentration ratio (with individual firms' market shares including any interconnected or associated persons) in the relevant market is below 70%, the combined entity (including any interconnected or associated persons) has less than in the order of a 40% share; or
  - where the three-firm concentration ratio (with individual firms' market shares including any interconnected or associated persons) in the relevant market is above 70%, the market share of the combined entity is less than in the order of 20%.
177. The Commission recognises that concentration is only one of a number of factors to be considered in the assessment of competition in a market. In order to understand the impact of the acquisition on competition, and having identified the level of concentration in a market, the Commission considers the behaviour of the businesses in the market. Specifically, the Commission seeks to understand the dynamics of the competition that would exist between the remaining firms in the market, compared to what would exist in the absence of the merger.

#### **National cladding market**

178. The Applicant has submitted that in respect of the national cladding market the aggregation that results as a consequence of the acquisition falls well within the Commission's safe harbour guidelines, amounting to less than 5% of the total market.
179. The Commission is of the view that a variety of construction options are available and the type chosen will depend on the preference for the particular characteristics of each cladding material. The range of substitutable alternatives makes the calculation of market share information difficult. However, the Commission considers that the aggregation that would result from the proposed acquisition is minimal and unlikely to raise any competition concern in respect of this market. Polystyrene panel is one of a range of possible options in this market such as timber, brick and steel, all produced nationally in large quantities. Cladding and structural building materials can be purchased from a range of producers including Carter Holt Harvey, Benchmark, Carters, Parapine and a number of others, many of which are large and

well established in the New Zealand market. As such, this market will not be considered further.

#### **North Island insulated polystyrene panel market**

180. The delineation of distinct North and South Island markets for the manufacture and wholesale supply of insulated panel results in no aggregation occurring in the North Island as a result of the proposed acquisition. The Commission considers that competition in this market would continue post-acquisition, as under the status quo, between Bondor, IPDL and Lanwoods. Consequently, this market will not be considered further.

#### **South Island insulated polystyrene panel market**

181. In the factual, the acquisition will reduce the number of polystyrene panel producers in the South Island from three to two, leaving only Bondor and Glenroy (a small company in Blenheim with the ability to produce a slightly different form of panel) in the market.
182. Glenroy is considered to be a niche player in the market. Terry Mischefski, owner of Glenroy, informed the Commission that panel production is only a very small part of Glenroy's business, and that it is produced primarily as an input into the manufacture of small portable buildings and toilets. Terry Mischefski also informed the Commission that Glenroy [
- ]. Glenroy also produces a slightly different panel through the use of an 'H' bolt joiner, rather than the 'S' lock system used by other panel producers in the market, which is viewed as not lending itself as easily to larger production and installation jobs. Glenroy also informed the Commission that it does not take a large role in the tender market, and produces much of its panel for its own building and construction projects. For these reasons Glenroy is considered to be a niche player, not significantly competing with Long International or Bondor.
183. Glenroy has informed the Commission that [

]

184. The Applicant has submitted that post-acquisition the combined entity would continue to face competition in the South Island from Lanwoods and IPDL (North Island panel manufacturers), Glenroy, Apollo Projects (importers of PIR) and Composite Insulation Limited (Thermomass manufacturers). The Commission, however, in defining a distinct South Island market for insulated polystyrene panel, considers that the North Island polystyrene panel manufacturers do not actively compete for jobs in the South Island, and hence are not considered as existing competitors in the South Island.
185. Apollo Projects (importers of PIR) and Composite Insulation (which produces the Thermomass product) are not seen as existing competitors in this market for the

reasons outlined in the market definition. Both products are seen as providing only a very limited constraint on a few specific applications of polystyrene panel.

186. The analysis, therefore, suggests there will be a reduction in competitors in the South Island market to one substantial producer and one small niche producer. Table 1 represents approximate market share figures based on production (in m<sup>2</sup>) of panel.

**Table 1: Market shares for polystyrene panel manufacturers in the South Island<sup>7</sup>**

<b>Manufacturer</b>	<b>Panel produced</b>	<b>Market Share</b>
Bondor	[ ]	[ ]
Long International	[ ]	[ ]
<i>Combined entity</i>	[ ]	[ ]
Glenroy	[ ]	[ ]
Total	[ ]	100%

187. The Commission does, however, acknowledge that at some price point the North Island companies would be able to be more competitive in the South Island particularly in respect of thinner panel, where it appears that even a small price increase would enable them to become somewhat competitive after including the relevant freight costs. However, the Commission notes that it has found little evidence of North Island companies historically supplying panel to the South Island, despite a higher panel price existing in the South Island compared to the North. As such, the Commission is of the view that while the potential to import the thinner sizes of panel (100mm and below) appears to impose some degree of competitive constraint on the actions of the combined entity post-acquisition, this constraint is limited to thin panel only.
188. However, for thicker sizes of panel this competition effect is much weaker as freight costs proportionally increase with the size of the panel freighted as discussed in the geographic market definition.
189. The Commission has evidence that would suggest that [ ] of Long International's production of standard panel is of a thickness of 100mm or less, whilst approximately [ ] of their entire panel production (including architectural panels) is of a thickness 100mm or less. Bondor also informed the Commission that approximately [ ] of their panel production was of a thickness 100mm and below based on m<sup>2</sup> of total panel produced. While this implies that for a substantial number of primarily cladding applications in the South Island the combined entity may be constrained by North Island suppliers, the Commission considers that most temperature controlled applications of panel require a panel thickness that is greater than 100mm as explained in the market definition section. It appears that in respect of thicker sizes of panel there is little or no constraint provided by North Island manufacturers.

<sup>7</sup> Figures include insulated panel produced for an industrial cladding purpose.

### *Conclusion on Existing Competition*

190. In the South Island insulated polystyrene panel market the acquisition would result in a reduction of competitors to one significant competitor with the combined entity holding a market share in excess of [ ]. The Commission considers that post-acquisition Bondor is likely to face a very limited degree of constraint from Glenroy which is considered to be a niche panel producer and that North Island suppliers only provide a limited constraint due to the difficulty in competitively supplying panels of a thickness of 100mm and above to the South Island (sizes generally required for temperature controlled applications). The Commission, therefore, concludes that the level of existing competition in the South Island insulated polystyrene panel market would be substantially lower in the factual than in the counterfactual.

### **Potential Competition**

191. An acquisition is unlikely to result in a substantial lessening of competition in a market if the businesses in that market continue to be subject to real constraints from the threat of market entry.
192. The Commission's focus is on whether businesses would be able or would be likely to be able to enter the market and thereafter expand should they be given an inducement to do so, and the extent of any barriers they might encounter should they try. Where barriers to entry and expansion in a market are clearly low, it may be unnecessary for the Commission to identify specific businesses that might enter. In other markets, where barriers are higher, the Commission may seek to identify possible new entrants as a way of testing the assessed entry and expansion barriers.

### *Barriers to Entry and Expansion*

193. The likely effectiveness of the threat of new entry and expansion in preventing a substantial lessening of competition in a market following an acquisition is determined by the nature and effect of the aggregate barriers to entry into that market. The Commission is of the view that a barrier to entry is best defined as anything that amounts to a cost or disadvantage that a business has to face to enter a market that an established incumbent does not face.

### Structural barriers to entry

194. In Decision 412 the Commission received information from IPDL that estimated the cost of entry into the market, depending on whether second-hand or new machinery was used, would be [ ]. At the time the Commission considered that that cost did not amount to a high barrier to entry into the market.
195. Stephen Gale, on behalf of the Applicant, has submitted to the Commission that sunk costs are the only relevant barrier to entry into this market and that expertise, intellectual property, customer switching costs or access to the primary raw materials are not barriers.
196. The Commission considers that entry into the manufacture of polystyrene panel would require the entrant to purchase a panel machine. The cost of a panel machine would vary depending on whether a second-hand or new machine were purchased.

The Applicant submitted in the application that a second-hand panel machine could be purchased for \$100,000. The Applicant also provided a quote for a new Hilleng machine from Australia for [ ]. Stephen Gale for the Applicants submitted that panel machines from China range between \$100,000 and \$160,000 depending on whether the machine is second-hand or new. Long International informed the Commission that their Auckland panel machine was purchased for [ ] and required a further [ ] in terms of commissioning. IPDL stated that the machine with which it entered the market eight years ago cost [ ] second-hand, and that a new machine from the same manufacturers would now cost [ ], excluding freight and installation costs. Robert Zahara, of Bondor Australia, informed the Commission that it is currently looking to dispose of a second-hand machine, and would be willing to sell it for [ ].

197. Stephen Gale, in his submission to the Commission, suggested that of this cost a conservative estimate would be that only 50% of it would amount to a sunk cost. It appears that there is an international market for second-hand panel machines, and the ability to produce mineral wool panel using these machines adds weight to the fact that there will continue to be a demand for them in the future, even if a shift from polystyrene to alternative core panels were to occur. The Commission understands that Long International intended to sell their Auckland panel machine prior to it forming part of this acquisition for [ ] The Commission has tested this submission on sunk costs and accepts that a conservative and appropriate approach is to assume that 50% of the cost of the investment in a panel machine would be sunk due to the existence of a strong second-hand market.

198. [

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199. The Commission is of the view that there is no reason to suppose that a new entrant could not use a second-hand machine to enter this market, whilst acknowledging that allowances may have to be made for inspection, assessment and re-commissioning of the machine. Second-hand machinery has been used previously to enter this market, with Long International's entry into the Auckland market and IPDL's entry in Palmerston North. In any event it appears that the cost of new machinery is not excessively more than a second-hand machine inclusive of a re-commissioning allowance. The Commission acknowledges, however, that there is an increased risk and potential cost through re-tooling and set up in entering in the factual with unknown second-hand machinery compared to the counterfactual where entry would be through the acquisition of the Long International machinery which has a reputation as a good machine.
200. The Commission is, therefore, of the view that a panel machine would be required to enter this market, and could be sourced (second-hand) at a cost of approximately \$250,000 to \$400,000 (inclusive of an allowance for shipping and re-commissioning)



for a second-hand machine and \$500,000 for a new machine, of which the Commission assumes \$125,000 to \$250,000 to be a sunk cost.

201. The Commission is of the view that a polystyrene block moulder may also be required in order to produce the polystyrene sheets required to manufacture polystyrene panels rather than purchasing the polystyrene sheets from a third party. Long International in 2002 entered the Auckland market by externally sourcing polystyrene. [

]. The Commission notes that all polystyrene panel manufacturers currently in operation have their own polystyrene plant.

202. The Commission was informed by [

] However, most industry participants spoken to were of the view that a polystyrene plant would be required, as to externally source polystyrene would add an additional element of cost to the production of panel such that it might not be viable. The Commission considers that due to the fact that polystyrene would otherwise have to be sourced externally, which may compromise the profitability of a panel manufacturer, it is appropriate to take a conservative view in this case by assuming that a polystyrene plant would be required in order to manufacture insulated polystyrene panels.

203. Phil Julian of IPDL stated that the cost of IPDL's new polystyrene plant, expander, moulder, crusher, ducting, silos, boiler, accumulator, pipework and associated machines involved in preparing polystyrene sheets for panel manufacture was [ ].

204. The Commission has also contacted [ ], who were suggested by [ ] as the likely purchaser of the Long International polystyrene plant, which does not form part of this acquisition. The Commission further understands that [ ] has informed the Commission that the value of that polystyrene machine would be approximately [ ].

205. Various other industry participants informed the Commission that a second-hand polystyrene block moulder and related equipment would cost in the vicinity of \$500,000 to \$750,000, depending on the age and specification of the desired machinery.

206. The Commission is of the view that it would be possible to source a second-hand polystyrene plant for around \$500,000 to \$750,000, which again includes an allowance for some re-commissioning of the machinery if necessary. It has been submitted to the Commission and the Commission accepts that a conservative estimate would be to assume that 50% of this investment would amount to a sunk investment for the same reasons as those discussed in relation to panel machines.

207. Accordingly the Commission considers that a sunk investment in polystyrene machinery of approximately \$250,000 to \$375,000 would be required to enter into the insulated polystyrene panel market.
208. The Applicant and other industry participants also suggested that various other pieces of machinery such as forklifts, trolleys, trucks, panel cutting tables, an air compressor, various hand-tools and a degree of working capital would be necessary in order to start producing panel. Some of these items, it seems, could be purchased or leased at a low initial cost and with a low sunk cost component. However, other expenses, such as the costs of establishing a business plan, arranging finance, advertising and other administrative costs all amount to sunk costs. [ ] explained to the Commission that there would also be costs involved in trial runs of panel which would be a sunk investment. [ ] said that these costs could range in the vicinity of [ ]. Whilst the Commission considers these estimates to be high, as much of the required machinery could be leased or purchased second-hand, it conservatively assumes that these additional expenses could amount to in the vicinity of \$200,000 to \$300,000. Again, for the same reasons, the Commission assumes no more than 50% of this cost to be sunk.
209. Ultimately, it appears that entry would be likely to require a capital investment in the vicinity of \$900,000 to \$1.3m, of which the sunk cost component is assumed to be between \$450,000 and \$650,000. When viewed against the annual total value of the South Island polystyrene panel market approximately [ ] of which a new entrant might optimistically look to capture 40%, the sunk costs are considered to represent a moderate barrier to entry. The Commission also notes that the most likely market entrants are panel installers or small businesses to whom this may amount to a large investment.
210. The Commission has been informed by [ ] that the cost of entry in the counterfactual may be [ ] through the acquisition by tender of the Long International polystyrene panel machine, polystyrene block moulder and related equipment. The Commission considers that this estimate is appropriate given the reduced need for shipping and re-commissioning costs, etc. Using the same approximation used above of the sunk component of this cost (50%) it appears that entry could be achieved, in the counterfactual, for a sunk cost of around [ ].
211. Most industry participants interviewed were also of the view that a degree of technical knowledge and expertise would be required in order to enter the market. The Commission accepts that some degree of knowledge in respect of the panel market would be an advantage in establishing a new panel business, but that there are a number of industry participants, in particular various installers of panel, who have the sufficient degree of expertise due to having a working knowledge of panel manufacture and machinery. [ ] As such, the Commission considers that there are sufficient industry participants with the required knowledge and expertise for it not to be considered a significant barrier to entry in this case.

212. The Commission is of the view that, overall, the structural barriers to entry are moderate due to the relatively modest level of the sunk costs involved in entering the market through the acquisition of second-hand machinery, which appear to be more costly in the factual compared to the counterfactual.

Strategic barriers to entry

Market Contraction

213. The Commission considered whether any uncertainty over the future of the polystyrene panel industry may cause some hesitation over entry into the market. This uncertainty was raised by a few parties interviewed, who suggested that the imminent entry and expansion of PIR and mineral wool panel might have some bearing on a firm's entry assessment from a strategic perspective.
214. [ ], stated that 12 months ago it seemed that PIR was going to make major inroads into the New Zealand panel market. He stated that this had not happened to the extent that he expected due to the attitudes of New Zealand insurers, who seem happy to accept polystyrene buildings as long as they are suitably protected. [ ] said that he would predict that polystyrene would continue to have 80% of the market in the future, though nothing is entirely certain.
215. [ ] all informed the Commission that the future of the market with respect to the entry of alternative core panels had very little impact on their entry considerations. They each said that there will always be a strong market for polystyrene panel, with PIR and other alternative core panels providing, at best, some competition for specific applications.
216. Bob Oldnall of Munich RE informed the Commission that the insurance market has peaked in 'hardness', and in the next 12 months is likely to become 'softer', which he clarified as being more favourable to polystyrene panel construction. He continued by saying that an uninsurable building 12 months ago may well be insurable now or in the next 12 months.
217. John Lockwood, of Lanwood Industries (importer of PIR), said that [ ] . He stated that he is hoping to sell up to [ ] of PIR panel per year by 2006/7 ([ ] of the total panel used annually in NZ). This estimate was consistent with the views of other industry participants, particularly panel installers, who said that given the current attitudes of insurers and the relative cost of PIR panel, PIR is unlikely to gain more than 10% to 20% of the market in the next 24 to 36 months. [ ] was of the view that future demand for PIR panel is likely to be for quite specific uses (rooms that have an extremely high fire risk) within buildings otherwise constructed of polystyrene.
218. Paul Lloyd of Apollo Projects in Christchurch commented on the likely future market uptake of PIR panel. Mr Lloyd stated that particularly in situations where a company is required to insure internationally, PIR is becoming the most attractive product. Apollo Projects has currently supplied [ ] of PIR into the market, and informed the Commission that it anticipates providing in excess of [ ] of PIR panel into the market in the next 12 months [ ]. Apollo Projects

considers that it competes with Bondor and Long International on some jobs. Apollo provided the Commission with contact details of companies which now had policies not to use polystyrene panel, and so were considered likely future customers for PIR panel. Amongst these were [

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219. The Commission also considered the experience in Europe where PIR is now the predominant insulated panel product supplied into the market. There is some indication, however, that the switch to PIR panel in Europe has been accelerated by the emergence of several PIR manufacturing plants in the United Kingdom, making the price of PIR panel less expensive than in New Zealand. Neil Gravestock informed the Commission that UK insurers have taken a harder line (compared to New Zealand insurers) on the use of polystyrene panel, which has further encouraged the uptake of PIR.
220. Tony Groth of Australian Urethane and Styrene, said that PIR has had a steady uptake in Australia due to several large fires (including a particularly bad one at the Fairfield Tip Top bakery in New South Wales in 2002) that have changed the attitude of Australian insurers, more so than New Zealand insurers.
221. Having considered the various factors, the Commission is of the view that the experience in Australia and the United Kingdom with respect to PIR and polystyrene is not necessarily what is likely to occur in the New Zealand market due to the different attitudes of insurers. It also appears that New Zealand does not have a population base that could sustain the manufacturing of PIR panel onshore. Bondor told the Commission that PIR plants do not work well economically if they are not run for long periods at a time and that the demand available in New Zealand would not be sufficient to enable such a plant to run properly. This has been confirmed by a number of parties interviewed by the Commission including Robert Zahara of Bondor Australia who stated that it was a close call as to whether there would be enough demand in Australasia to justify the establishment of a PIR plant. Based on the evidence and discussion above the Commission considers that the uptake of PIR in New Zealand is likely to be measured and involve only limited substitution for polystyrene panel, at least in the next two years (the time period relevant to the Commission's determination).
222. The Commission considers that based on the current approach adopted by New Zealand insurers and risk assessors (as discussed in the market definition section) PIR is unlikely to be used in any significant quantities in the next two years. However, while PIR's impact is likely to be minimal within the Commission's timeframe a business contemplating entry may consider a longer timeframe in developing its business case. In such an extended timeframe there is greater uncertainty regarding PIR's impact.
223. It is also important to note that a polystyrene panel machine can be used to produce mineral wool panel with little alteration needed. Thus, production could potentially be switched to alternative core products if a shift away from polystyrene panel were to

occur. Such possible applications would also maintain, to some extent, the resale value of the machine if the entrant decided to exit.

224. On balance the Commission considers that uncertainty over the future of polystyrene panel may amount to a low barrier to entry into the market.

#### Excess capacity and incumbent response

225. During its investigation the Commission also encountered a perception amongst some industry players that the recent exit of Long International in Auckland (January 2004) was caused by highly competitive pricing by Bondor and that this may deter a potential competitor from contemplating entry in the South Island. It was suggested that entering to compete against an entrenched incumbent with a large existing operation may elicit an incumbent response that would challenge the viability of the new operation.

226. The Commission has not discovered any evidence that incumbent response was a factor in the decision of Long International to exit the Auckland market. [

]. However, the Commission acknowledges that a perception may still exist that this was the case.

227. Bondor has submitted to the Commission that it [

] However, the Commission is of the view that its investment through this acquisition would signal a commitment to the market, particularly in light of the fact that, post-acquisition, Bondor would possess four panel machines, which would be enough to supply the entire New Zealand demand for panel several times over. This further investment would indicate to a new entrant (yet to incur any costs) a possible intention to defend market share in the face of entry through the strategic use of this excess capacity. This is likely to be a significant consideration for a new entrant who would be required, in the factual, to add to the capacity that already exists in the market (in the hands of one large incumbent) in order to enter the market.

228. Further, an incumbent response would not necessarily require pricing below average variable cost (the level commonly accepted as the benchmark of predatory pricing) on every job as the ability would exist for the incumbent to selectively compete with the new entrant through matching or undercutting an entrant on particular contracts, and as a result discourage entry and expansion in the factual scenario. Such a response is likely to be less successful in the counterfactual as there is likely to be at least one other party with capacity to compete.
229. The Commission considers that it is reasonable, in the factual, for a potential entrant to take account of the potential for there to be a strong competitive response to entry by the incumbent especially considering the excess capacity Bondor will have post acquisition.

#### Conclusion on strategic barriers to entry

230. The Commission is of the view that the strategic barriers to entry are moderately high due to the excess capacity held by the incumbent and increased potential for an incumbent response in the factual vis-à-vis the counterfactual.

Conclusion on Barriers to Entry

231. The Commission has considered the relevant structural and strategic entry considerations with respect to entry into the market for the manufacture and supply of insulated polystyrene panel. The Commission is of the view that the sunk costs related to entry in this case are moderate and are increased in the factual compared to the counterfactual. The Commission is also of the view that certain strategic considerations would be of particular concern to a new entrant including uncertainty over the future of the market, excess capacity that would be held by the incumbent and the increased potential for an incumbent response. The combination of these factors leads the Commission to conclude that the barriers to entry into the market for insulated polystyrene panels market are significant.

*The “LET” Test*

232. In order for market entry to be a sufficient constraint, entry of new participants in response to a price increase or other manifestation of market power must be Likely, sufficient in Extent and Timely (the LET test).
233. The mere possibility of entry is, in the Commission’s view, an insufficient constraint on the exercise of market power, and would not alleviate concerns about a substantial lessening of competition. In order to be a constraint on market participants, entry must be likely in commercial terms. An economically rational business would be unlikely to enter a market unless it had a reasonable prospect of achieving a satisfactory return on its investment, including allowance for any risks involved.
234. If it is to constrain market participants, the threat of entry must be at a level and spread of sales that is likely to cause market participants to react in a significant manner.
235. If it is to alleviate concerns about a substantial lessening of competition, entry must be feasible within a reasonably short timeframe, considered to be two years, from the point at which market power is first exercised.

Likelihood

236. Stephen Gale, for the Applicant, has submitted to the Commission that Glenroy, under new ownership, is a likely entrant into polystyrene panel production through the purchase of a new panel machine. Terry Mischefski informed the Commission that [

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237. The Commission has identified [ ], who have all indicated that they are interested in acquiring the assets of Long International in the counterfactual. [

] They were each of the view that acquiring the assets in the counterfactual would cost approximately [ ], and that production could be commenced within [ ] of purchasing the equipment.

238. [

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239. [

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240. [

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241. [ ] also said that if the acquisition did go through then it is likely that they would not be able to stay in business (as installers) as they would need to then purchase their panel from Bondor with whom they would be competing with in the installation market. The Commission has been further informed by [

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242. [ ] stated that the option of becoming a contracted installer for Bondor or sourcing thinner panel sizes from the North Island would not secure them enough business for their operations to remain viable. They said that the risk that they might have to exit the industry as installers was further heightened in the factual given the increased time it would take a new entrant to establish a competing operation to Bondor due to the need to source and relocate machinery internationally.]

243. The Commission is of the view that this may be of concern to a potential entrant as the independent installers represent a route-to-market that could be used in setting up a competing operation. The Commission considers that the longer it would take for a competing manufacturing operation to establish itself, the greater the risk that this route-to-market would not be an option (as the installers may have ceased operating).

244. The Applicant submitted that it would not be unreasonable to expect new entry to occur within 3½ months, illustrating this point with the example of IPDL, which was able to enter the market within this time period.

245. Most parties spoken to were of the opinion that six to eight months would be a more realistic estimate of the time required to enter the market in the factual. [ ] stated that it would take at least six months to enter this market from scratch. Likewise [ ] stated that entry in the factual would probably take at least six months compared to one month in the counterfactual. [ ] were of the view that entry in the counterfactual would take very little time at all as the machinery was position locally and in good condition.

246. The Commission considers that there is an increased risk in the factual that independent installers will cease operating due to the time required for a new manufacturing operation to establish itself. As a result there is an increased risk, in

the factual compared to the counterfactual, that the route-to-market for a new insulated polystyrene panel producer will be more difficult.

247. The Commission has been informed by [ ] that it would not consider entering the South Island insulated polystyrene panel market regardless of what might occur. A similar response was given by [ ]
248. The Commission considers that the size of the sunk costs involved in entry and the increased potential for incumbent response to entry in the factual are factors that a hypothetical entrant will consider seriously in contemplating entering the market in the factual. The ability to align itself with independent installers of panel would be an attractive option for a new entrant looking to secure business after its initiation. However, as evidenced this may not be likely in the factual scenario.
249. The Commission acknowledges that the market power of the combined entity in the factual may not be as great in respect of panel sizes below 100mm and that a potential entrant may be able to supply some thinner panel into the North Island. However, the Commission considers that supply from the South Island to the North Island would be of an insufficient frequency given the current competitive environment in the North Island and the freight rates that would apply, for such a consideration to be given great weight in the entry considerations of a potential competitor. Further, the Commission is of the view that this factor is outweighed by other considerations such as the level of sunk costs and the potential for incumbent response in the South Island.
250. The Commission is, therefore, not satisfied that entry into the manufacture and wholesale supply of polystyrene panel is likely to occur in the factual. Accordingly it is not necessary for the Commission to consider the extent or timeliness elements of the 'LET' test.

#### *Conclusion on Potential Competition*

251. The Commission has considered the relevant structural and strategic entry considerations with respect to entry into the market for the manufacture and supply of insulated polystyrene panel. The Commission is of the view that the sunk costs related to entry in this case are moderate but are increased in the factual compared to the counterfactual. The Commission is also of the view that certain strategic considerations would be of particular concern to a new entrant including the potentially more difficult route-to-market in the factual, uncertainty over the future of the market, the excess capacity that would be held by the incumbent and the increased potential for an incumbent response to entry. The combination of these factors leads the Commission to conclude that the barriers to entry into the market for insulated polystyrene panels market are significant and that entry is unlikely in the factual.

#### **Other Competition Factors**

252. The potential for a firm to wield market power may be constrained by countervailing power in the hands of its customers, or alternatively, when considering buyer



(oligopsony or monopsony) market power, its suppliers. In some circumstances, it is possible that this constraint may be sufficient to eliminate concerns that a business acquisition may lead to a substantial lessening of competition.

253. Where a combined entity would face a purchaser or supplier with a substantial degree of market power in a market affected by the acquisition, the Commission will consider whether that situation is such as to constrain market participants to such an extent that competition is not substantially lessened.
254. Although the various panel installers in the South Island are repeat purchasers sales are often of a low frequency. The high aggregation in the factual and the lack of alternatives for sourcing panel mitigates any potential power they might possess in this market. Accordingly the Commission is of the view that no purchaser holds a degree of countervailing power sufficient to prevent a substantial lessening of competition in the South Island market for insulated panels.

## **OVERALL CONCLUSION**

255. The Commission is required to give clearance to a clearance Application under section 66(3) of the Act if it is satisfied that the acquisition will not lead to a substantial lessening of competition in a market or decline clearance where the Commission is not satisfied that the acquisition will not lead to a substantial lessening of competition in a market.
256. The Commission has considered the probable nature and extent of competition that would exist in the counterfactual in the following markets:
  - the New Zealand market for the manufacture and wholesale supply of exterior claddings for industrial, commercial and residential buildings (the national cladding market); and
  - the North and South Island markets for the manufacture and wholesale supply of insulated polystyrene panel for the construction of controlled temperature industrial and commercial buildings (the North and South Island insulated polystyrene panel markets).
257. The Commission considers that the appropriate counterfactual is the sale of Long International's assets to a third party and the retention and operation of their manufacturing capacity in the South Island.
258. The Commission is satisfied that the proposed acquisition would not have, nor would be likely to have, the effect of substantially lessening competition, in:
  - the national cladding market due to the presence of existing competition; and
  - the North Island insulated polystyrene panel market as no aggregation occurs as a result of the acquisition within the North Island.
259. The Commission has identified a number of issues regarding aggregation of market share and potential entry in the factual scenario in the South Island insulated polystyrene panel market. The acquisition would result in a reduction of competitors in the South Island insulated polystyrene panels market to one significant producer

with the combined entity holding a market share in excess of [ ]. The Commission is of the view that the size of the sunk costs required to enter the insulated polystyrene panel market increase in the factual vis-à-vis the counterfactual. The Commission also considers that there are certain strategic barriers to entry in the factual that increase the overall barriers to entry and makes entry in the factual unlikely. These factors include the potentially more difficult route-to-market in the factual scenario, uncertainty over the future of the market, the excess capacity that would be held by the incumbent and the increased potential for an incumbent response to entry.

260. Whilst each factor on its own is not determinative, the combination of these factors results in the Commission not being satisfied, on the balance of probabilities, that the acquisition would not be likely to lead to a substantial lessening of competition in the South Island market for insulated polystyrene panel.
261. Pursuant to section 66(3) (a) of the Commerce Act 1986, determines to decline clearance for the proposed acquisition by Bondor New Zealand Limited, of the business assets of the insulated panel business of Long International Limited.

**DETERMINATION ON NOTICE OF CLEARANCE**

262. Pursuant to section 66(3) (a) of the Commerce Act 1986, the Commission determines to decline clearance for the proposed acquisition by Bondor New Zealand Limited of the business assets of the insulated panel business of Long International Limited.

Dated this 22nd day of July 2004

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Paula Rebstock  
Chair  
Commerce Commission