

31 August 2012

Notice under s 66 of the Commerce Act

CSR Building Products (NZ) Limited and Brickworks
Building Products (NZ) Pty Limited (**Applicants**)

Commerce Act 1986: Business Acquisition Section 66: Notice Seeking Clearance

31 August 2012

By email: registrar@comcom.govt.nz
The Registrar
Market Structure Group
Commerce Commission
PO Box 2351
WELLINGTON

Pursuant to s 66 (1) of the Commerce Act 1986 notice is hereby given seeking clearance of a proposed business acquisition.

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APPENDICES

Part 1: Overview

CSR and Brickworks propose to establish a JV to supply clay bricks

1. In this application CSR Building Products (NZ) Limited (**CSR NZ**) and Brickworks Building Products (NZ) Limited (**Brickworks NZ**) (together the **Applicants**) seek clearance to establish a joint venture to supply clay bricks in New Zealand (**Proposal**).
2. The Proposal would reduce the number of major clay brick suppliers in New Zealand from three to two. However, brick is only one of a number of choices for exterior cladding. Numerous other cladding suppliers would remain, as would clay brick suppliers Midland Brick (Boral's New Zealand distributor),¹ Canterbury Clay and Clay Bricks.

The Proposal raises no competition concerns

3. The Applicants are taking the conservative approach of filing this application as they are aware that the Commission is interested in the building industry. The Applicants consider that the Proposal does not raise competition concerns and that clearance should be granted:
 - (a) **The acquisition falls in the highly competitive market** for the supply of *exterior architectural claddings for industrial, commercial and residential buildings*, the market definition twice adopted previously by the Commerce Commission.² The Commission stated that the market included fibre cement, brick veneer, steel, timber, concrete slabs and blocks, and polystyrene sheet.
 - (b) **There are numerous substantial suppliers of external cladding** in New Zealand. They include leading building industry players such as James Hardie (supplying fibre cement), Fletcher Building group (concrete brick and block, and fibre cement) and Carter Holt Harvey (timber weatherboard). Post-merger, the Applicants estimate that the three-firm concentration ratio would be approximately [] with the merged entity's share being approximately [], which is well within the Commission's safe harbours.
 - (c) **Boral will remain incentivised to compete aggressively** in New Zealand via its distributor in order to utilise excess capacity, having recently lost significant market share in Australia. Landed costs for brick in New Zealand from Australia are comparable to that of the Applicants.
 - (d) **There are a number of Australian and Asian-based cladding manufacturers who could supply into New Zealand** if incentivised including brick manufacturers such as BGC (Australia) Pty Ltd, Selkirk, and Clay Bricks & Tiles Sdn Bhd.
 - (e) **There is a material level of countervailing buyer power**, due to the role of influencers, such as builders and architects, who will either influence the end-users' choice of type of external cladding (including the mix of cladding), or make that decision for them.
 - (f) The competitiveness of the market is evidenced by brick suppliers having to absorb recent cost increases rather than pass them on. The status quo is likely unsustainable.

¹ Midland Bricks is the trading name of NZ Brick & Stone Limited.

² See Decision 412: *James Hardie / Long International*, 15 December 2000 and Decision 530: *Bondor New Zealand / Long International*, 22 July 2004.

Part 2: Transaction Details

1. Person giving this notice

1.1 This notice is given by:

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1.2 Correspondence and inquiries should in the first instance be directed to:

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1.3 Correspondence and inquiries specifically relating to Brickworks Building Products (NZ) Pty Limited should be directed to:

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2. Details of other merger parties

2.1 The merging parties are the Applicants set out in paragraph 1.1 above.

3. List of companies relevant to merger parties

3.1 CSR Building Products (NZ) Limited (CSR NZ):

- (a) Rivarol Pty Limited
- (b) CSR Building Products Limited
- (c) CSR Limited (CSR Australia)

3.2 Brickworks Building Products (NZ) Pty Limited (Brickworks NZ):

- (a) Brickworks Building Products Pty Limited
- (b) Brickworks Limited

3.3 Shareholder structure diagrams for CSR NZ and Brickworks NZ are appended to this application as **Appendices 1 and 2** respectively.

4. Details on what is to be acquired

4.1 Clearance is sought by CSR Building Products (NZ) Limited (trading as Monier Bricks & Roofing) or any interconnected bodies corporate of CSR Building Products (NZ) Limited, and by Brickworks Building Products (NZ) Pty Limited (trading as Austral Bricks) or any interconnected bodies corporate of Brickworks Building Products (NZ) Pty Limited (together, the **Applicants**) to acquire up to 100% of the assets of the Applicants' respective New Zealand brick businesses (except CSR NZ's manufacturing plant located at New Lynn, Auckland) (**Proposal**).

4.2 The structure of the joint venture arrangements between the parties is yet to be finalised. It is currently proposed that:

- (a) CSR NZ and Brickworks NZ would each acquire:
 - (i) partnership interests in a proposed 50/50 joint venture limited partnership (**JV Co**); and
 - (ii) shares in a proposed 50/50 New Zealand limited liability company which will be the sole general partner of JV Co; and
- (b) JV Co would acquire the assets of the New Zealand brick businesses of CSR NZ (except CSR NZ's manufacturing plant located at New Lynn, Auckland) and Brickworks NZ.

4.3 JV Co will carry out and operate the brick businesses which CSR NZ and Brickworks NZ currently undertake in New Zealand, excluding CSR NZ's manufacturing plant at New Lynn, Auckland (**New Lynn Plant**).

4.4 The Applicants' New Zealand brick businesses comprise supply, customer and related services contracts, plant and equipment, inventory, office hardware, intellectual property, employees, owned property, and leases of real property.

4.5 JV Co is likely to initially source its brick and related materials 50% from CSR NZ (or its related parties) and 50% from Brickworks NZ (or its related parties), on terms to be agreed.

5. Explanation of commercial rationale for proposed acquisition

5.1 Record low building consents have resulted in a significant decrease in the demand for brick.

- 5.2 While demand has plummeted the Applicants have faced increased costs of supply and continued to incur the costs of their manufacturing facilities, front office and retail divisions.
- 5.3 The Applicants consider that the synergies created by the Proposal will enable JV Co to more effectively and sustainably compete in the cladding market. The Applicants have identified annual savings of [] as a result of the Proposal, comprising both fixed and variable cost savings.
- 5.4 These cost savings will stem primarily from rationalising freight, display centre premises, and merging sales and administrative teams. Rationalising transport costs is expected to achieve variable cost savings in the order of [] per annum. [].
- 5.5 The Proposal represents the most efficient means for realising sufficient synergies. Brick's current share of supply is expected to face further challenges from alternative cladding, especially fibre cement. A combined CSR NZ and Brickworks NZ supplier will be better equipped to develop strategies to meet this challenge. As such, the Proposal represents the most sensible commercial option in the current circumstances.
- 5.6 Given that both Applicants have excess manufacturing capacity, it is logistically easier to have joint supply rather than entering into complicated arrangements as to which party is to supply JV Co. A single consolidated manufacturing plant could generally only produce a limited product range and therefore would not be able to supply the full range of products sought by customers in New Zealand.
6. **Copies of final/most recent version of documents bringing about the proposed merger**
- 6.1 A copy of the Heads of Agreement entered into by the Applicants is appended to this application in **Confidential Appendix 3**.
7. **List of competition agencies in any other jurisdictions which have been notified of the proposed merger**
- 7.1 Not applicable.

Part 3: The Industry

8. Description of relevant goods or services supplied by the merger parties

- 8.1 The Applicants each manufacture and supply clay bricks (referred to in the remainder of this application as **bricks**). The Applicants both supply bricks of varying colours, sizes and cosmetic appearances, eg bricks that cater to a heritage or contemporary aesthetics. While bricks are manufactured in varying sizes New Zealand has traditionally built using brick measuring 230mm x 76mm x 70mm (length x height x width).
- 8.2 Bricks are made from clay, shale and selected minerals such as manganese. CSR NZ sources the majority of its clay for the New Lynn Plant from the Huntly region, with the balance of the materials being sourced from Port Waikato, Clevedon and Kumeu. The materials are combined and the resulting mixture is extruded to form a continuous brick ‘column’ which subsequently passes through a wire cutter to achieve the final brick shape and size. The bricks are then dried and fired in a continuous tunnel kiln at temperatures up to 1200°C for a period of time in excess of 70 hours. The relevant ingredients and the high firing ensure a brick that is durable and will not lose its colour.
- 8.3 Brick suppliers keep a reasonable level of stock for each brick type but manufacturing is primarily driven by large orders. All New Zealand brick suppliers have manufacturing and/or storage facilities in New Zealand.
- 8.4 Bricks are divided into two main product groups:
- (a) Common Brick: commodity product which can be left unfinished or can be rendered or painted; and
 - (b) Face Products: customised products differentiated by texture, colour and finish.
- 8.5 Face Products are more expensive than Common Bricks as they are a customised option.
- 8.6 Bricks are generally used in the construction of residential properties (up to two to three stories) and some small non-residential buildings such as schools, churches and town halls.
- 8.7 Historically bricks were used as both a building’s internal structure and external cladding. The external (and internal) brick walls were an integral part of the building’s structural integrity and designed to carry the weight of the building including its ceiling(s) and roof. This construction technique often required a building to have double (or triple) brick walls with a cavity in between the inner, (middle) and outer brick walls.
- 8.8 However, for most modern brick buildings the bricks do not perform a primary structural role. Rather the bricks are applied as an exterior weather-tight cladding to an internal timber (or steel) frame which is designed as the building’s primary load bearing structure. For additional structural integrity the brick cladding is tied using metal brackets to the building’s internal frame. The external cladding industry often refers to the modern use of bricks as “brick veneer”, not to be mistaken with fake brick veneer sheets which were common in the 1970s.

CSR NZ

- 8.9 CSR NZ is ultimately owned by CSR Australia. The CSR group manufactures and supplies various building products including insulation, processed glass, concrete products, plasterboard, fibre cement, and roof tiles. CSR Australia also has interests in aluminium and property. The CSR group operates in New Zealand, Australia and Asia.

- 8.10 CSR NZ supplies bricks manufactured at its New Lynn plant and imported from CSR Australia's manufacturing facilities. CSR NZ supplies bricks through:
- (a) its Monier Bricks and Roofing display centres in Auckland, Canterbury (Christchurch), Waikato (Hamilton) and Bay of Plenty (Tauranga); and
 - (b) independent distributors in Northland (Whangarei), Auckland, Hawkes Bay, Wellington (Lower Hutt), Nelson-Marlborough (Richmond), Canterbury (Christchurch), Otago (Dunedin), and Southland (Waikiwi).
- 8.11 CSR NZ is also an indirect wholly-owned subsidiary of Australian-based CSR Building Products Limited. CSR Building Products Limited manufactures the Hebel aerated concrete product in Australia. Hebel is supplied in New Zealand by a third party distributor.
- 8.12 For further information on CSR Limited's New Zealand operations see www.csr.co.nz.

Brickworks NZ

- 8.13 Brickworks NZ is ultimately owned by Australian based Brickworks Limited. The Brickworks group manufactures and supplies various building products including Schist, pavers, concrete products, concrete and terracotta roof tiles, timber and terracotta cladding. The Brickworks group has manufacturing operations in New South Wales, Victoria, Tasmania, South Australia, Western Australia and Queensland.
- 8.14 Brickworks NZ supplies bricks imported from the Brickworks group's Australian manufacturing facilities through:
- (a) its Australbricks sales offices and design centres in Auckland, Tauranga, Porirua, and Christchurch; and
 - (b) independent distributors in Canterbury (Christchurch), Otago (Dunedin), and Southland (Waikiwi).
- 8.15 For further information on Brickworks NZ see www.australbricks.com/nz.

9. Description of industry

- 9.1 Bricks are a form of external cladding (**cladding** in the remainder of this application). Cladding can be manufactured from clay (eg bricks), concrete (ie block, brick and precast)³, timber (eg pine weatherboard, cedar shingle, and plywood), stone (eg schist, Oamaru stone), mud (eg bricks), aluminium (eg extruded weatherboard), iron (eg corrugated), cement (eg fibre cement weatherboard and sheeting), and exterior insulation and finishing systems (EIFS). Cladding manufactured from all these materials is widely available in New Zealand.
- 9.2 Similar to many building material industries, the cladding industry is made up of a variety of participants supplying products manufactured from various materials but which have the same functional characteristics. Essentially, for any given building project there are likely to be a number of different competing cladding solutions. Pricing will usually be a major factor in relation to the choice of cladding. The relevant environment and the decision makers' perceptions in relation to various claddings will also play a role in the decision process.
- 9.3 EIFS cladding is a type of monolithic cladding consisting of polystyrene boards, planks, sheets or panels that are fixed to framing and reinforced with a plaster and paint coating to finish. EIFS cladding has been in use in New Zealand since the 1980s. Most EIFS cladding systems in New

³ The Applicants note that concrete products are also used for structural, in addition to cladding, purposes.

Zealand are installed directly over timber framing, although they can be installed over masonry structures.

- 9.4 Fibre cement is a composite cladding material that is made up of sand, cement and cellulose fibres. Fibre cement cladding comes in a variety of forms but is generally installed in sheets or horizontal boards. Fibre cement was originally developed as an alternative to asbestos-based building cement products.
- 9.5 The cladding industry is comprised of both independent and well-resourced multinational players and is highly competitive. Cladding manufacturers may either supply their cladding direct to the market, appoint distributors/agents or a combination of both.
- 9.6 The cladding industry employs a range of marketing media to reach its potential customers. Most players will have well developed websites, comprehensive high quality brochures and committed sales teams. Some players have dedicated display stores and showhomes which enable customers to visually experience the product in a real build. Others players produce high cost television commercials, as James Hardie has done to persuade customers as to the benefits of fibre cement.
- 9.7 Emphasising a particular cladding's positive characteristics is typical in the cladding market. James Hardie sets out the following benefits associated with its Linea fibre cement product:

“Attractive finishes in five different styles, including Smooth Weatherboard, Rusticated Weatherboard, Styleline™ Weatherboard and Frontier Weatherboard profiles.

Cost effective weatherboard option.

Lightweight, easy to handle and install.

Easy installation gives a professional finish.

Low maintenance.

Pre-primed, and easily finished with acrylic paint or stain.

James Hardie Weatherboards are resistant to fire and damage from moisture and rotting when installed and maintained correctly.

Product warranty of 15 years.”⁴

- 9.8 Midland Brick notes:

“Bricks work

Take a fresh look at bricks for the ultimate expression of individuality and timeless appeal.

Texture is the key feature in house design today and it is easily achieved through a balance of finishes and surfaces that contrast and complement.

Nothing competes with the alluring textures on offer from natural clay brick.

The choice is yours”⁵

- 9.9 Exterior cladding suppliers generally deal with the following three customer groups:

- (a) New/renovating homeowners (**Homeowners**), accounting for approximately 25% of customers.

⁴ <http://www.jameshardie.co.nz/product/James-Hardie-Weatherboards?i=3>

⁵ <http://www.midlandbrick.co.nz/>

- (b) Builders – managers, building franchise owners, large and small contract and speculation home builders (**Builders**), accounting for approximately 70% of customers.
- (c) Specifiers – architects and architectural designers and colour consultants (**Specifiers**), accounting for approximately 5% of customers.

The Homeowner's cladding decision process

- 9.10 Homeowners typically go through the following **five-stage decision making process** when building a new residential property or renovating an existing property. The Homeowner:
- (i) decides to buy brand new or renovate;
 - (ii) develops a portfolio of wants and desires;
 - (iii) decides on a design;
 - (iv) chooses a builder; and
 - (v) chooses colours and fittings.
- 9.11 Specifiers generally get involved at stage (iii), the design stage. If an independent specifier is not being used, stages (iii) and (iv) are combined (ie design and choosing a builder). While many of the larger Builders will have standard house plans many will also have their own in-house designers who custom-design standard plans for Homeowners. In the Applicants' experience unless the house is already completed, Homeowners will make changes to Builders' standard plans, which may include the plan's cladding.
- 9.12 Specifiers and colour consultants may have some influence as to the type of material used, depending on their relationship with the Builder and Homeowner and at what stage they are brought into the process. In the Applicants' experience many Builders are now using colour consultants to help their clients in the choice of materials. Specifiers place greater importance on product information and technical support while for Builders service is important.
- 9.13 But ultimately it is the Homeowner and Builder who have the greatest influence in selecting the type of cladding. Homeowners will come with their own preferences and preconceptions in relation to cladding but will be given options and recommendations by the Builder and conduct their own research. Such research typically includes driving around new subdivisions, visiting showhomes, homeshows and home idea centres, reviewing magazines and brochures, and searching the internet. Advice will also be invariably offered by family and friends.
- 9.14 In addition to overall price, the most important factors when choosing a cladding are the look, the site location and the quality and durability of the cladding. For the Homeowner brand perceptions drive the initial inclusion of products at stage (ii) and then provide assurance at stages (ii) and (iii). However, for brick the brand is often less important than colour as brick is seen as a trusted and generic material which does not require the comfort of an established brand.
- 9.15 Participants in the cladding industry typically transact with Builders rather than Homeowners or Specifiers. Builders will often align themselves with particular players and negotiate supply terms including volume rebates. Builders often carry out projects on the basis of a fixed price plus cost for customised aspects, so they are incentivised to promote cladding that allows for a greater margin. Builders tend to have an allegiance to a brand of bricks based around service.
- 9.16 To the best of the Applicants' knowledge, there are no Builders in New Zealand who build solely in brick. Most, if not all, New Zealand Builders build in a variety of cladding materials. As such the Applicants do not have any exclusive cladding arrangements with Builders. For example, GJ Gardiner has extensive lightweight cladding solutions as does Golden Homes who directly

imports a lightweight concrete panel. Platinum Homes, while historically concentrating on brick cladding has in recent times moved to lightweight solutions due to changing preferences.

Higher infrastructure costs in New Zealand

- 9.17 There are structural difficulties to efficiently supplying cladding in New Zealand. In relation to brick for example, supply in New Zealand incurs considerably higher costs than supplying brick in Australia. New Zealand has a greater number of customers (Builders) relative to its population size. While Australia is dominated by very large building companies, New Zealand tends to have a far greater number of smaller independent Builders. What is considered to be a large building company in New Zealand would be considered a small-medium company in Australia. For example, Fletcher Building's Residential Construction division builds approximately 200 houses annually in New Zealand. In Australia, a company building 200 houses per year would be considered a small-medium Builder. A large Builder in Australia will build between 200 and 2000 houses annually.
- 9.18 Due to the scale differences in Builders the average New Zealand brick order is approximately half that of the average Australian order. Servicing the many independent Builders and their many small orders requires greater resources including the number of sales staff.
- 9.19 A far greater percentage of Homeowners in New Zealand build using independent builders rather than large building companies. Servicing these Homeowners, who play a primary role in sourcing the required materials compared to dealing with large building companies, requires greater investment in display centres which allow the Homeowner to conduct their research.

10. Current industry trends and developments

- 10.1 The global recession and downturn in the building industry has been detrimental to the cladding industry. Predicted increases in demand have been significantly counteracted by the downturn in the building industries with new housing starts at historically low levels.⁶ Suppliers now compete for fewer projects while continuing to endure fixed costs.
- 10.2 Following the GFC, weak demand and excess capacity has led to several plant closures as suppliers seek to improve productive efficiencies. In relation to bricks
- (a) Boral recently closed its 60 million piece per annum clay brick plant in Brisbane. The plant required significant investment in order to continue operating. Boral made the decision that the required investment was not economically justified and ultimately closed the plant.
 - (b) CSR closed its brick plant in Cooroy, Queensland in June 2010.
 - (c) Brickworks has closed two plants in Western Australia and three sites in Victoria since 2007.
- 10.3 As coastal shipping and land transport costs continue to increase, imports from Australia and Asia are becoming more cost effective. Offshore manufacturers have the benefit of lower per unit production costs due to scale advantages. In addition, Trans-Tasman shipping costs are often comparable to or better than transport costs from domestic manufacturing facilities. By way of example, Midland Brick is thought to account for [] of the supply of brick in the South Island.
- 10.4 Glass is an example of a cladding material that has become more attractive as cost of production has reduced in Asia. There is a trend towards using glass as a facade or cladding, particularly in the commercial segment.

⁶ http://www.fletcherbuilding.com/media/11/Fletcher-Building-First-Quarter-Trading-Update_259

Inability to recover increases in costs

- 10.5 The Applicants have been unable to increase their prices to fully cover the increased costs of production and supply for a number of years. This is due to the threat of losing market share to competing cladding materials, in particular fibre cement. Many costs including electricity and fuel have increased well above the CPI rate. Due to its bulky nature, transport cost increases have particularly impacted total supply costs of bricks. The Applicants have been unable to recover these increased costs due to the threat of customers substituting brick for alternative cladding.

[

]

- 10.6 Traditionally brick was viewed as a natural, low maintenance, trusted material that worked well with other claddings. [

]

- 10.7 In the Applicants' recent experience, while some Homeowners wanted to have homes similar to what they had seen, there is a definite trend to show some individuality. It is this motivator that has steered Homeowners away from traditional brick and tile. Builders are reporting that Homeowners are increasingly requesting products such as James Hardie's Linea board having seen Linea advertised on TV.

Demand patterns changed as a result of the leaky home phenomena

- 10.8 While the leaky home phenomena has helped create a preference for more durable and 'real' products, including timber, concrete, schist, stone and plaster over brick or concrete block rather than EIFS, the "boring" subdivision factor has developed as a consequence of that preference.
- 10.9 Historically around 25% of houses were clad in brick. As a direct result of the leaky home phenomena that share spiked to around 45%, but there is no evidence to suggest that this share of supply is permanent. The Applicants believe that it is the manifestation of a shift that will dissipate over time as confidence in EIFS returns and the preference for Linea type products grows. With the new E2 regulations now in place in relation to EIFS, architects in particular are now confident enough to specify such systems again.
- 10.10 A trend towards higher-density multi-unit dwellings has also increased the substitution from brick to alternative materials such as concrete panels and glass.⁷

There is greater use of multiple cladding types

- 10.11 There is also a greater use of multiple cladding types in a single building. For example, a building may incorporate weatherboards, EIFS, and schist. This trend ties in with the "boring" subdivision factor as the use of multiple cladding types allows Homeowners to create their "individual" house with greater ease. The use of multiple claddings allows greater flexibility for Homeowners to vary the use of a particular cladding during the design and building process if prices change.

There is a preference for monopitch roofs rather than gable and hip

- 10.12 There has also been a move from gable and hip to monopitch roofs.⁸ This shift has led to a preference for long-run roofing (ie corrugated iron sheets) as monopitch roofs are not suited to tiles. This trend impacts the choice of cladding used as long-run is not usually aesthetically compatible with brick. James Hardie products and timber weatherboard are more likely to be used to clad buildings with monopitch roofs.

⁷ IBISWorld Industry Report C2621, Clay Brick Manufacturing in Australia, November 2011, page 11.

⁸ For images of different roof designs see <http://houseplans.co.nz/house-designs>.

[]

10.13 [

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Canterbury and the aftermath of the earthquakes

10.14 Brick had been the most common cladding in Canterbury post-WW2 as the region was not widely identified as being at a high risk of earthquakes. Prior to the series of earthquakes (starting in September 2010), it was not unusual for a Christchurch Builder to be involved in building 5 or 6 houses during a given year which were all clad in brick (or plaster over brick).

10.15 [

] Buildings

in earthquake zones also typically have light-weight roofing. Long-run is light and suited for earthquake zones. As mentioned, long-run and brick are generally not selected as a combination.

The costs of Auckland congestion

10.16 In addition to the introduction of the Emissions Trading Scheme, traffic congestion in Auckland has had a significant impact on CSR NZ's New Lynn Plant. Previously a delivery truck could complete three round trips between the Plant and the Huntly clay site during a shift. Now only two round trips can be achieved due to congestion. Such inefficiencies have led to productivity losses.

11. Any relevant mergers that have taken place over last three years

11.1 Neither Applicant has acquired assets or shares in relation to external cladding businesses in New Zealand within the last three years.

Part 4: Market Definition

Horizontal aggregation

12. Market definition

Product market

Previous consideration by the Commission

- 12.1 The Proposal will lead to aggregation in relation to the supply of bricks. As noted, the most common use for bricks is as a cladding material attached to the support structure of a building. Cladding serves an aesthetic and weather-resistance purpose.
- 12.2 The Commission considered cladding in Decision 412: *James Hardie / Long International*, 15 December 2000 and Decision 530: *Bondor New Zealand / Long International*, 22 July 2004. In both instances, cladding was considered in the context of proposed aggregation in the supply of polystyrene panels (a type of EIFS system). The Commission defined the relevant product market as one for the supply of “*exterior architectural claddings for industrial, commercial and domestic residential buildings*” (including “*fibre cement products from various manufacturers, brick veneer, stiel (sic), timber, concrete slabs and blocks, and polystyrene sheet*”).⁹
- 12.3 In *Bondor / Long International*, the Commission noted that “[i]n general the Commission considers there is a range of suitable alternatives for the bulk of construction projects in terms of the structural or cladding product used”¹⁰ and “[p]olystyrene panel is one of a range of possible options in this market such as timber, brick and steel, all produced nationally in large quantities.”¹¹
- 12.4 Similarly, in *James Hardie / Long International*, the Commission commented that “*Long International stated that in this market, orders flowed from competitive tenders and it had to be price competitive against other types of architectural cladding if it was to win tenders.*”¹² The Commission noted Monier, Dimond, Firth and Steel and Tube as suppliers in the architectural cladding market.¹³ The Commission did not consider the architectural cladding market in detail “*given that there are at least 12 competitors in the market, with no participant having more than 20% market share.*”¹⁴ That market structure remains largely unchanged.
- 12.5 The Applicants agree with the Commission’s approach in *James Hardie / Long International* and *Bondor / Long International* that the relevant product market is one for the supply of cladding for industrial, commercial and residential buildings.

Substitutability and industry views

- 12.6 A cladding market is consistent with the high degree of substitutability between different cladding products and the way that market participants and industry bodies view the day-to-day operations of the market.
- 12.7 There is strong competition between suppliers of different cladding products. The threat of losing market share to other cladding materials has been the dominant factor preventing the Applicants from increasing prices to a level that would cover their increased unit costs.

⁹ *James Hardie / Long International*, paras 50, 53. *Bondor / Long International*, paras 105-111.

¹⁰ *Bondor / Long International*, para 110.

¹¹ *Ibid*, para 179.

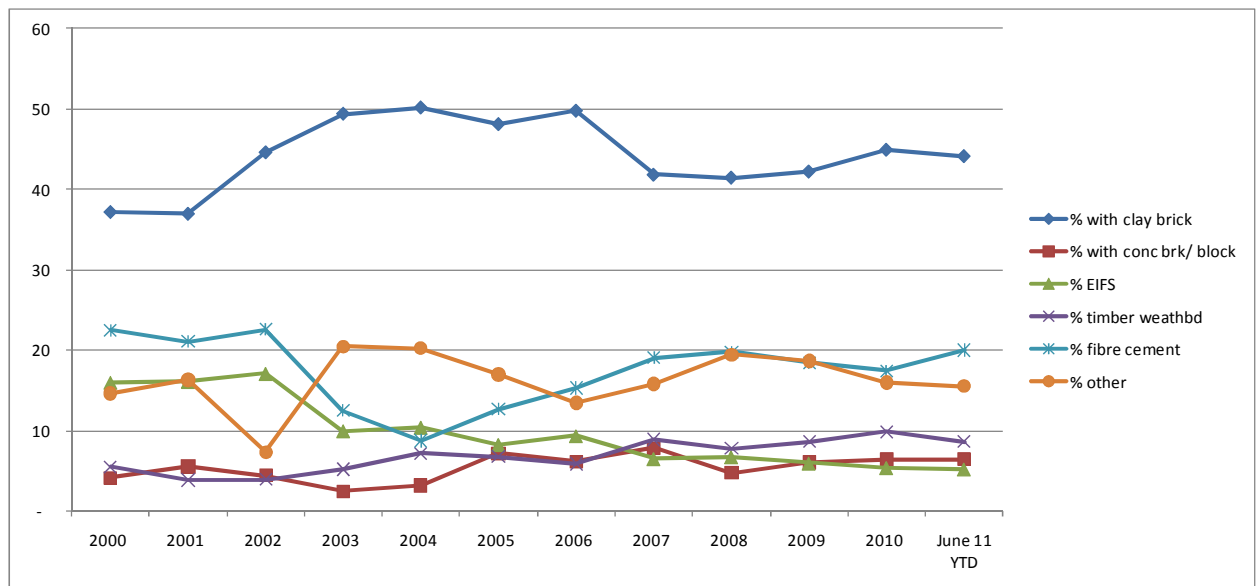
¹² *James Hardie / Long International*, para 53.

¹³ *Ibid*, para 69.

¹⁴ *Ibid*, para 79.

- 12.8 Data collected by the Building Research Association of New Zealand (**BRANZ**) and construction consultancy firm Rawlinsons also analyse a cladding market. An industry report into clay brick manufacturing in Australia by IBISWorld notes “[c]ompetition from other wood product manufacturing” and “[c]ompetition from building boards, bricks and other concrete product manufacturing” as two of the five key external drivers for the clay brick manufacturing industry.¹⁵ The report also noted “the declining clay brick share of the total construction materials market”.¹⁶
- 12.9 The diagram below illustrates the substitutability particularly between bricks and fibre cement and to a lesser degree between bricks and concrete and other cladding.

External Cladding Market - % by wall area



Source: CSR presentation dated 20 September 2011 based on data collated by Statistics NZ and BRANZ

- 12.10 Other industry participants also appear to set targets and track performance within a cladding market:

- (a) NZ Wood stated in 2011 that “in the latest survey of timber use conducted for NZ Wood by BRANZ...In terms of cladding, timber weatherboard has staged a comeback since 2005, now accounting for 13.5% of claddings, up from 8.9 percent. Brick cladding still takes almost half of the market.”¹⁷
- (b) James Hardie’s 2011 Annual Report noted that “A key strategy for the company is to maximise its market share growth/retention of the exterior cladding market for new housing starts and for repair and remodel segments, which it does by growing fibre cement’s share of the exterior siding market and by maintaining the company’s share of the fibre cement category.”¹⁸
- (c) Aluminium cladding supplier Nu-Wall had stated in 2008 that “Given the work we have done in development of the product and the resources to support it, I believe we can now realistically aim to secure 10 percent of the exterior cladding market in the next three to five years.”¹⁹

¹⁵ IBISWorld Industry Report C2621, Clay Brick Manufacturing in Australia, November 2011, page 3.

¹⁶ Ibid, page 13.

¹⁷ [http://www.pine.net.nz/resources/newsletter/Issue%20153%20\(April%202011\).pdf](http://www.pine.net.nz/resources/newsletter/Issue%20153%20(April%202011).pdf)

¹⁸ James Hardie, Annual Report 2011, page 46.

¹⁹ <http://www.scoop.co.nz/stories/BU0803/S00459.htm>

(d) PSL's website notes that EIFS systems represent "*approximately 5% of New Zealand cladding market*"²⁰.

- 12.11 While different cladding materials have different characteristics and advantages, the Applicants do not consider that any of those differences represent a barrier to switching from brick to other cladding materials.
- 12.12 As noted, even when using a Builder's standard plans, Homeowners will usually have the ability to choose the type of cladding they wish to use based on their own preferences.
- 12.13 A number of cladding suppliers promote their products by emphasising the benefits of a particular type of cladding (as opposed to the benefits of the particular brand).²¹ Such claims support the Commission's approach to market definition as a cladding's individual characteristics are clearly viewed by manufacturers as being capable of influencing a buyer's choice of cladding.
- 12.14 Further, CSR NZ has commissioned market research analysing customer behaviour in relation to cladding and the factors influencing customers' choice of cladding material. CSR NZ invested in understanding customers' processes for selecting the type of cladding so that they would be better placed to win market share from alternative cladding material suppliers.
- 12.15 The Applicants consider that there would be sufficient switching away from brick to other cladding materials in response to a SSNIP such that the product market should be defined as the cladding market.

Other applications

- 12.16 As noted, brick can also be used for other applications such as fencing, paving, edging, and fireplaces. As brick competes against a number of other materials for those applications, the Applicants do not propose analysing those markets further.

Functional Level

- 12.17 The Applicants manufacture or import cladding in order to supply to merchants, Builders, Specifiers, and directly to Homeowners.
- 12.18 The Applicants submit that the relevant functional level is the manufacturing/import and wholesale/retail supply of cladding products.

Geographic Area

- 12.19 The Applicants agree with the Commission's approach in *James Hardie / Long International* and *Bondor / Long International* where it concluded that the geographic dimension of the architectural cladding market was national.²²

Customer dimension and timeframe

- 12.20 Cladding tends to be priced on a volume basis. The Applicants therefore consider that the Proposal will not disproportionately impact on any particular groups of customers. The Applicants submit that there are no distinct customer or temporal dimensions to the market.

Conclusion on market definition

²⁰ <http://www.plastersystems.co.nz/CPD/EIFS/cavity1.html>

²¹ See examples at paras 9.7 and 9.8 above.

²² *James Hardie / Long International*, paras 69-70. *Bondor / Long International*, paras 147-148.

12.21 The Applicants submit that the relevant market is the *national market for the manufacture or import and wholesale or retail supply of external cladding products* (which the Applicants will refer to as the “**cladding market**”).

13. **Explanation of how products or services are differentiated within the market(s)**

13.1 As the Commission concluded in *Bondor / Long International*, the cladding market is made up of a range of differentiated alternatives embodying different qualities.²³ Purchasing decisions are made on the basis of product characteristics, service and price.

13.2 Cladding materials can be differentiated based on aesthetic appeal, ease of construction, degree of maintenance required, weight, insulation, durability, (perceived and actual) weathertightness and price.

13.3 Suppliers of cladding materials also differentiate themselves based on the quality of their product and quality of service including promptness of delivery, warranties, and level of advice and technical support.

Vertical Integration

14. **Details of any creation or strengthening of vertical integration that would result from the proposed merger**

14.1 Both Applicants manufacture and import and participate in the wholesale and retail supply of cladding. In this respect, the Proposal may be viewed as strengthening the existing level of vertical integration. But the relevant functional levels of the exterior cladding market will remain competitive post-merger.

²³ Decision 530: *Bondor New Zealand / Long International*, 22 July 2004, para 106.

Part 5: Counterfactual

15. **Description of what is likely to happen to the business operations of the merger parties and the market/industry in the event that the proposed merger does not take place**
- 15.1 Current losses indicate that the status quo is unsustainable. In the absence of the Proposal proceeding, there is a reasonable chance that one or both of the Applicants could exit the New Zealand market.

Part 6: Competition Analysis

Existing Competitors

16. Identities of all relevant competitors in the market(s) and how they all compete in the market(s)

16.1 The major competitors in the cladding market are:

- (a) **NZ Brick & Stone Limited** (trading as **Midland Brick**): supplies a wide range of bricks and pavers sourced from Boral's plants in Australia. Midland Brick is owned and operated by Brent Whalan who originally founded Midland Brick over 17 years ago before selling the Midland business to Boral. According to Mr Whalan he "*bring[s] a wealth of knowledge and experience to the [Midland Brick business]*".²⁴ Midland Brick has a storage yard and display centre in Auckland and distributors in Christchurch, Tauranga, Napier, Paraparaumu and Blenheim (see www.midlandbrick.co.nz).

Midland Brick's supplier **Boral Limited** claims to be Australia's largest building and construction materials supplier. It also has significant operations in the United States and Asia and claims to be the largest brick manufacturer in the United States.²⁵

- (b) **James Hardie New Zealand Ltd (James Hardie)**: According to James Hardie it is a leading international building materials company and a global leader in fibre cement. It claims that fibre cement is one of the world's fastest growing building products. James Hardie states that it has major operations in New Zealand, Australia, Asia, Europe and the United States, employs over 2,500 people and generates annual revenue of more than AU\$1.55 billion. Specific cladding products include Titan® Facade Panel, James Hardie Weatherboards, Shingleside® Panel, James Hardie light-weight Scyon® Axent™ Fascia (cement), Scyon® Linea® Weatherboard (cement), Hardiebacker® Substrate (plaster) (see www.jameshardie.co.nz).
- (c) **Fletcher Building Group (Fletchers)**: The Fletchers group supply a range of building products including concrete masonry veneers and masonry blocks manufactured by Firth, Dimond metal cladding, and ColorCote cladding supplied by Pacific Coilcoaters. Fletchers recently became the largest building materials company in Australasia with total annual revenues of nearly \$10 billion and total employees of 20,000.²⁶ The Fletchers group also has a strong building and construction division and retail presence through Placemakers (see <http://www.fletcherbuilding.com/>).

Firth was established 80 years ago. It is the largest and only national manufacturer offering a complete range of concrete products, systems and solutions.

There are five products in the Firth concrete brick veneer range: Focus® Bricks are the size of traditional bricks and are stated to have smooth, clean lines that are ideal to create a contemporary effect. Pioneer® Bricks are the size of traditional bricks and are rumbled to give an established, 'heritage' appearance. Devonstone™ Bricks have a natural look that suits many building styles. Manorstone® Bricks have a larger format and resemble natural stone. Summit Stone® have a rough-hewn face and bolstered edges giving them the look of natural, handcrafted stone.

²⁴ Letter dated 4 May 2012 addressed to customers of Midland Brick signed by Brent Whalan, Managing Director of NZ Brick & Stone Ltd.

²⁵ http://www.boral.com.au/corporate/organisational_structure.asp and http://www.boral.com.au/Boral_Companies/CI_Boral_USA.asp

²⁶ http://www.fletcherbuilding.com/cms/files/report_pdfs/FBL2011AnnualReview.pdf

According to Firth it employs about 650 people and has 65 plant sites throughout New Zealand. Firth claims that the Firth brand is one of New Zealand's best known, most trusted and most enduring trade names. Firth distributes its products through Placemakers, Mitre 10, ITM Building Centres, Carters, BuildLink, and Bunnings Warehouse (see www.firth.co.nz).

Dimond, a division of Fletcher Steel Limited, is the leading supplier of New Zealand metal roofing, cladding, structural and rainwater products. Dimond supplies three different metal cladding products: Corrugate, DimondClad and Baby Corrugate – the main difference being the span of the corrugate sheets. Dimond's cladding comes in a range of different colours.

Pacific Coilcoaters produces ColorCote®, one of New Zealand's leading brands of pre-painted, steel and aluminium roofing and cladding products. ColorCote® comes in a wide range of colours and its colours and coatings are specifically designed for New Zealand's unique climate. ColorCote® offers a six-tier range of pre-painted metal roofing and cladding products. All of the products either have a steel (with a corrosion-resistant zinc coating) or aluminium substrate and each product has a different level of primer and type of top-coat depending on the environment in which it is to be used.

- (d) **W.D. Boyes & Sons Limited (Canterbury Clay)**: According to Canterbury Clay it was established 45 years ago and is the only local manufacturer of kiln fired bricks in the region. It supplies 25 varieties of brick under its classic and heritage ranges and render grade. Canterbury Clay predominately supplies the greater Canterbury region but will also supply as far north as Nelson and as far south as Invercargill (see www.clay-bricks.co.nz).
- (e) **Carter Holt Harvey (CHH)**: CHH products include CHH Profiles™ which represent a wide range of weatherboards, fascia and mouldings manufactured from timber or MDF. Other products include Shadowclad™ plywood panels which according to CHH provide a beautiful, natural wood exterior cladding that is well suited to most architectural styles; adding street appeal to any project whether used alone or accented with other building materials (see www.chhwoodproducts.co.nz).
- (f) **Clay Bricks Limited (Clay Bricks)**: Clay Bricks is based in Huntly. According to Clay Bricks it offers a quality service, allowing potential customers to choose their own pallets of bricks from the factory, to ensure complete customer satisfaction. Clay Bricks predominately supplies in the greater Waikato and Bay of Plenty regions but it has been known to supply Auckland (see www.claybricksltd.co.nz).
- (g) **Jenkin Timber Ltd (Jenkin)**: According to Jenkin it designs and manufactures quality, horizontal wooden wall cladding products including weatherboards, (see www.jenkin.co.nz).
- (h) **Pukepine Sawmills and PurePine Mouldings Ltd (PurePine)**: PurePine claims to produce a pine weatherboard cladding system from sustainable trusted timber and state of the art SmartSeal for maximum stability. PurePine considers its product to have a superior finish to any other weatherboard (see www.smartclad.co.nz).
- (i) **Ullrich Aluminium Company Ltd (Ullrich)**. Ullrich claims that its Wintec Ulltraclad® is a new innovation in aluminium cladding and has been designed to overcome the leaky building syndrome. Ullrich views its product as an ideal exterior cladding as it still has the look of traditional weatherboards but without the maintenance and problems associated with a timber cladding (see www.ulltraclad.co.nz).
- (j) **BGC**: BGC Duraplank™ is a general-purpose fibre cement cladding for external applications. It is manufactured as a plank, which is reminiscent of traditional weatherboards both in appearance and installation methods. BGC Stonesheet is a purpose

designed fibre cement sheet for external application. It is recommended as a backing board for stone slip substrates on timber frame buildings (see www.bgcplaster.com).

- (k) **Nuplex** – plaster systems division (PSL). PSL claims to be New Zealand's largest provider of residential and commercial proprietary plastering systems and materials and is one of the key companies in Nuplex's diverse Construction Products Group. According to Nuplex, PSL currently exports to a number of countries including the South Pacific, Australia, Canada and South Africa. Products include, ENDURON AAC and Graphex System (see www.plastersystems.co.nz).
- (l) **Rockcote Systems (NZ) Ltd (Rockcote)**: According to Rockcote it specialises in the manufacture and distribution of an extensive range of premium plaster cladding systems and coatings solutions to the construction industry. In July 2002 Rockcote joined the Resene Paints Limited Group, New Zealand's largest privately owned and operated paint manufacturing company (see www.rockcote.co.nz).
- (m) **Nu-Wall Aluminium Cladding Limited 2010 (Nu-Wall)**: Nu-Wall is a locally designed and developed aluminium weatherboard system. Nu-wall claims to supply its weatherboard system to construction projects throughout Australasia and around the world (see www.nu-wall.co.nz).
- (n) **Kaneba Limited (Kaneba)**: Kaneba is the regional support centre for the popular Alucobond aluminium composite panel manufactured by Alcan Composites. Kaneba claims that *“With more than 90 million m² sold since 1969, ALUCOBOND® is one of the most successful materials worldwide.”*²⁷
- (o) Other participants include:

Timber weatherboard	<ul style="list-style-type: none"> • Access Pacific Limited www.accesspacific.co.nz/ • Beechmark (NZ) Limited http://www.beechmark.co.nz/ • Cedar Products Limited http://www.cedarproducts.co.nz/ • Gunnensen Pty Limited http://www.gunnersens.co.nz/ • Herman Pacific Limited http://www.hermipac.co.nz/ • J Scott and Company Limited t/a <i>JSC Timber</i> http://www.jsctimber.co.nz/ • Plytech International Limited http://www.plytech.co.nz/ • Rosenfeld Kidson & Co Limited t/a <i>The Timber Source</i> http://www.thetimbersource.co.nz/ • Stuart Timber Company Limited http://www.stuarttimber.co.nz/ • Tenon Manufacturing Limited http://tenon.co.nz/ • Triclad Limited http://triclad.co.nz/ • Weathertex Pty Limited http://www.weathertex.co.nz/
Concrete block	<ul style="list-style-type: none"> • Celco New Zealand Limited t/a <i>euroblock</i> http://euroblock.co.nz/ • Celcrete Cladding Solutions (2008) Limited http://celcretecladding.co.nz/ • Omni Block Group http://www.omniblock.com/ • Stoanz Limited

²⁷ <http://kaneba.co.nz/index.html>

	<ul style="list-style-type: none"> http://www.sto.co.nz/ Thomson Concrete 2007 Limited http://www.thomsonconcrete.co.nz/ Trenwyth Industries http://www.trenwyth.com/
EIFS	<ul style="list-style-type: none"> Insulform New Zealand Limited http://www.insulform.co.nz/ Kingspan Limited http://www.kingspanpanels.co.nz/ Masons Plastabrick Limited http://www.masonsplastabrick.co.nz/ Mineral Plaster Technologies (NZ) Limited http://www.mineralplaster.co.nz/ Styrobeck Limited t/a <i>PPG Styrobeck Plastics</i> www.styrobeck.co.nz/
Fibre cement	<ul style="list-style-type: none"> Evonik Industries Degussa AG http://corporate.evonik.com PBS Group http://www.pbs.co.nz/
Other	<ul style="list-style-type: none"> Calder Stewart Roofing Limited (steel) http://www.calderstewart.co.nz/ Classic Stone Limited (stone) http://www.classicstone.co.nz/ Craftstone NZ Limited (stone) http://www.craftstone.co.nz/ D.Hitchcock Stonemasonry (stone) http://www.stonemasonry.co.nz/ Designer Stone and Schist Products Limited (stone) www.designaschist.co.nz/ Dynex Extrusions Limited (plastic weatherboard) http://www.palliside.co.nz/ GeoTech Systems Limited (sheet piles) http://www.geotechsystems.co.nz/ Hydestone Limited (stone) http://www.hydestone.co.nz/ Moda Pietra Global Stone Limited (granite) http://www.modapietra.co.nz/exterior.html Mulford Plastics (NZ) Limited (plastic weatherboard) http://www.mulfordplastics.com/ Sandstone Developments Limited t/a <i>Muriwai Earth Bricks</i> (mud bricks) Solid Earth Limited (mud bricks) http://www.solidearth.co.nz/ Steel & Tube Holdings Limited (steel) http://www.steelandtube.co.nz/ Stratco (N.Z.) Limited (steel) http://stratco.co.nz/ Symonite New Zealand Limited (aluminium) http://symonite.co.nz/ The Architectural Roofing Company Limited t/a <i>Architectural Cladding</i> (aluminium) http://www.architecturalcladding.co.nz/

16.2 All of the above players compete, to varying degrees, in the cladding market. Players' individual market shares will vary as trends develop, peak and fade and new technologies and techniques are evolving. The cladding market is highly competitive and will remain so post merger.

16.3 For a single-storied house, brick is likely to be 3-4% cheaper than the other types of building materials. Brick is more expensive in multi-story construction due to requirements for scaffolding and other equipment. Fibre-cement is likely to be the cheapest option for a multi-storied dwelling.

Table 1: Costs of a selection of cladding materials installed per square metre by year

Cladding	2007 (\$ per m2 installed)*	2008 (\$ per m2 installed)	2009 (\$ per m2 installed)	2010 (\$ per m2 installed)
Brick (Monier)	87 - 128	87 - 141	121 - 141	147
Concrete Block	100 - 116	111 - 124	123	127
Insulclad 60mm (type of EIFS)	115 - 140	115 - 140	114 - 140	112
Plywood	135 - 174	119 - 160	147 - 161	165
Pallisade (type of fibre cement)	143 - 155	143 - 150	188 - 197	200
FJ Pre-primed Weatherboard	145 - 169	145 - 159	215 - 230	238
Presto Plastered Brick	145 - 180	160 - 184	160 - 184	227
Cedar	168 - 195	166 - 180	275 - 285	286
Linea (James Hardie)	146 - 161	179 - 188	210 - 215	215
Schist	320 - 375	320 - 375	320 - 375	343

Data sourced from Rawlinsons

17. **Outline of the estimated market shares in terms of sales, and where relevant, volume and productive capacity, of the merger parties and competitors identified above**

17.1 In the tables below, the Applicants have estimated market shares for the cladding market.

17.2 The Applicants estimate that the total value of the New Zealand cladding market is approximately \$85 million for the product only. The installed value of the products is estimated to be over \$350 million.

Table 2: Estimated market shares for the cladding market by competitor

Rank	Competitors	Estimated Revenue (\$m)	Estimated % of Market Share by Revenue
[]	CSR NZ	[]	[]
[]	Brickworks NZ	[]	[]
[]	Hebel	[]	[]
	<i>Merged Entity</i>	[]	[]
[]	James Hardie	[]	[]
[]	Boral (Midland Brick)	[]	[]
[]	Fletchers	[]	[]

[]	CHH	[]	[]
	Others	[]	[]

Applicants' estimates. Revenues are estimated for each competitors' cladding products only, ie installation costs are excluded. Market shares and revenues are calculated based on sales by manufacturer/importer rather than by distribution channel.

Table 3: Estimated market shares for the cladding market by cladding material

Rank	Cladding Material	Estimated % of Market Share by Volume
1	Brick	45.1%
2	Fibre cement	19.0%
3	Timber weatherboard	9.8%
4	Concrete block	4.7%
5	EIFS	6.4%
6	Other	15.1%

Based on data collected by Statistics NZ and BRANZ. Market share is an average of the four quarters in 2011.

18. **The extent to which the merged entity would be constrained in its actions by the conduct of existing competitors in the markets affected**
- 18.1 Based on the Applicants' estimates, the three firm concentration ratio post-merger would be approximately [] with the merged entity having approximately [] market share, which is well within the Commission's safe harbours.
- 18.2 Post-merger, the merged entity can be expected to continue to compete vigorously in the supply of cladding. The Applicants view the formation of JV Co as resulting in a stronger brick supplier which has the capabilities and internal cost structure to compete better against other cladding, especially fibre cement.
- 18.3 In addition to Midland Brick, Canterbury Clay and Clay Bricks, a number of large and well-resourced cladding suppliers including James Hardie, Fletchers and CHH will continue to supply and constrain the cladding market. The prospect of losing market share to alternative cladding materials has forced brick suppliers to absorb increased costs rather than recover those costs through price increases. As noted at 12.10, suppliers of alternative cladding materials are actively looking to grow their share of the cladding market. Given the scope of those constraints, JV Co would be expected to lose sufficient business to make any material price increase unsuccessful.
- 18.4 James Hardie is a well-established supplier of cladding and has had particular success with its Linea product. James Hardie introduced Linea in New Zealand in 2002²⁸ and Linea has secured nearly [] of the cladding market in that short space of time. Linea and brick are particularly strong substitutes. Large scale marketing campaigns have ensured that Homeowners are familiar with Linea and its attributes. Linea houses have won awards including Registered Master Builder's House of Year Awards²⁹ providing the product with additional profile.
- 18.5 According to James Hardie "*fibre cement is one of the world's fastest growing building products*". James Hardie have driven consumer demand through heavily advertising their Linea product. This consumer awareness has created pull through when the customer meets the Builder

²⁸ *Cladding Revolution*, The Press, 6 May 2002, Edition 2, page 21.

²⁹ http://www.tvshowhomes.co.nz/index.php/ps_pagename/showhome/pi_articleid/18

during the selection process. The Applicants do not expect Linea's success to abate in the foreseeable future. The Applicants understand that the manufacturing cost of fibre cement is generally lower than that for brick, giving suppliers such as James Hardie a cost advantage and the ability to gain market share through lower prices. Thus James Hardie's offerings will materially constrain JV Co.

- 18.6 Fletchers and CHH are trusted names in the industry by Builders and Homeowners alike and their range of cladding is tried and true. Both Applicants have the resources to exploit opportunities in the market and promote their cladding to a wide audience. Having a strong retail dimension to its business in the form of Placemakers as well as a building and construction division also provides Fletchers with a direct pulse on the changing trends in the industry, especially at the residential end. Should JV Co attempt to materially increase prices Homeowners would be expected to sufficiently (fully or partially) substitute JV Co's brick for Fletchers' and CHH's wood, concrete and metal alternatives rendering any increases ineffectual.
- 18.7 As noted, there are no switching barriers. Builders readily switch allegiances between cladding suppliers if incentivised and Homeowners' preferences will dictate where a particular cladding is sourced in any event.

A well connected Midland Brick will continue to compete strongly

- 18.8 Boral's sale of its Midland Brick business to NZ Brick & Stone Limited has not and will not impact Midland Brick's ability to aggressively compete. In fact, Midland Brick is likely to become a more effective and aggressive competitor.
- 18.9 Midland Brick traditionally sourced bricks from Boral's Queensland and New South Wales plants. The recent closure of Boral's Queensland plant may have limited the volumes that Boral could supply to its New Zealand operations. However, any such limit is clearly no longer an issue following the recent entry of BGC in Western Australia. This took market share from Boral, leaving Boral with significant excess capacity at its Western Australia plant. Boral will therefore be seeking to utilise that excess capacity through supplying higher volumes to Midland Brick in New Zealand. The Applicants expect importing from Western Australia to be cost-effective due to significantly lower unit production costs.
- 18.10 NZ Brick & Stone Limited is owned by Brent Whalan who originally founded Midland Brick before selling the business to Boral. The Midland Brick business will continue to operate from and use the same premises and distributors. Midland Brick has also retained key staff.
- 18.11 Given Boral's desire for increased volumes and Mr Whalan's industry knowledge and relationship with Boral, Midland would be expected to continue to compete strongly. It is unlikely to be content with simply retaining existing customers and market share (estimated to be [] of the cladding market and [] of the supply of brick respectively). It incurs lower distribution costs relative to the Applicants as it has only a single storage yard and display premise on the North Shore of Auckland. The Applicants expect Midland will compete aggressively for new custom by continuing to present the market with competitive rates. Such conduct will constrain JV Co and other participants in the cladding market.
- 18.12 Midland Brick's share of the supply of brick in the South Island is estimated to be []. This level of supply supports the view that it can readily increase its share of supply in the North Island whether incentivised or not.

Canterbury Clay and Clay Bricks will also continue to compete

- 18.13 Combined Canterbury Clay and Clay Bricks account for around [] of the cladding market and [] of the supply of brick respectively. Both players would be expected to continue to compete in the cladding market, particularly in regions within a close proximity to their respective plants.

- 18.14 The conduct of both Canterbury Clay and Clay Bricks will add to the constraint on JV Co and other participants in the cladding market.

Further, nothing prevents Midland Brick, Canterbury Clay and Clay Bricks expanding their respective operations

- 18.15 There are no barriers preventing Midland Brick, Canterbury Clay and Clay Bricks from expanding their brick operations if incentivised to do so. Midland Brick has so far carried out a low cost operation focused on higher-end commercial projects such as churches, schools and retirement villages. Midland Brick could easily expand its display centres and distribution network if incentivised and seek to expand supply to residential Builders. As noted, Boral has existing capacity so there are no concerns in relation to a consistent supply of brick from Boral's Australian plants. Shipping costs from Australia are often comparable to domestic shipping costs.
- 18.16 Canterbury Clay and Clay Bricks could also easily expand their respective operations and supply to the South Island and North Island. This could be achieved in a number of ways. For example, by collaborating with a larger Builder (as this would provide an assured customer base), seeking private equity or pursuing a model of cherry picking high margin projects. Any additional investment by Canterbury Clay would put it in an even stronger position to serve any increase in demand resulting from the Christchurch rebuild.

Other suppliers could also supply cladding to New Zealand

- 18.17 Further, distribution channels are open enabling access by other Australian and Asian suppliers of cladding. For example, an Australian cladding supplier such as BGC or Selkirk, could sponsor entry for a distributor or enter joint venture arrangements with an existing participant in the wider building industry. Supply and distribution agreements can be set up with relative ease. Sustainability of such arrangements will be driven by achieving a relative price point to other claddings.
- 18.18 Companies including Selkirk, the largest privately owned brick manufacturer in Australia, could easily supply into New Zealand on a marginal cost basis. Such supply allows manufacturers to fill voids in manufacturing capacity. Selkirk was established in 1883 and claims that its *“drive to innovate has led to the introduction of Australian and World first manufacturing technology, and working proactively with customers to develop value adding solutions”*.³⁰
- 18.19 Similarly, BGC commenced production at its Brikmakers plant in Perth in 2009. BGC claims that the plant is *“the largest greenfields clay brick plant ever built in Australia”* and it *“operates at industry best-practice with state-of-the-art steel-lined kilns which consumes less energy per tonne of product manufactured than those of older kilns in generation”*.³¹ BGC also states that it owns reserves of clay in Western Australia sufficient to meet its needs for the next 20 years. The Applicants understand that BGC has excess capacity to produce another 100 million standard brick units per year.

Expanding imports will continue to constrain the markets

- 18.20 By virtue of their scale advantages, Australian and Asian cladding manufacturers enjoy significantly lower manufacturing costs. In addition, shipping costs from Australia are often comparable to if not better than domestic shipping costs (depending on the relative locations of the customer and manufacturing facilities). The costs of landed imported materials are therefore generally highly competitive.
- 18.21 There are no barriers preventing existing or potential importers from expanding or entering the New Zealand cladding markets.

³⁰ <http://www.selkirk.com.au/about/about-selkirk>

³¹ http://www.bgc.com.au/s_08/BGC_corporate_profile.pdf, page 15.

Potential Competition

Conditions of Entry

19. **The requirements for new entry and/or importers in the relevant market(s)**
- 19.1 There are very few barriers to new importers entering the cladding market in New Zealand.
- 19.2 Requirements will vary depending on the type of cladding and distribution model. Requirements may include obtaining BRANZ approval for a particular product (not a necessary requirement, but preferred by many Builders) and the costs of establishing a display centre. The Applicants are not familiar with the costs required to set up a distribution channel in New Zealand for other cladding products, but the Applicants considers that the costs for setting up a smaller version of Midland Brick’s operation to be minimal – approximately \$50,000 plus working capital.
20. **Factors that could impede entry, and what might prompt new entry post-merger**
- 20.1 The Applicants consider that existing competition will provide more than sufficient competitive constraint on the cladding market. The recent low number of building consents means that entry may not be attractive at present. However, there are no factors that would impede entry if market conditions are conducive and there were perceived profits to be made.
- 20.2 As noted by the Commission in *Fletcher Building Australia (PTY) Limited and Crane Group Limited*, Decision No 719, 24 February 2011:³²

*“While the requirements of entry are straightforward, industry participants informed the Commission that due to the adverse economic climate and the significant excess capacity in the market, entry is unlikely in the short term. Despite this, the Commission considers **should the excess capacity in the market be fully utilised in the future, the threat of entry would be likely to constrain the merged entity in the factual.**”* (emphasis added)

Likelihood, Extent and Timeliness of Entry (the LET test)

21. **Likely businesses that do not currently supply the market but which the applicant considers could supply each of the relevant markets**
- 21.1 As noted, companies including Selkirk, BGC or Malaysian based Clay Bricks & Tiles Sdn Bhd could easily supply New Zealand customers through a distributor if market conditions were conducive. If incentivised, those parties could export to New Zealand on a marginal cost basis in order to fill excess capacity during downturns in local demand.
- 21.2 Those parties do not currently produce bricks with dimensions traditionally sold in New Zealand. Bricks with alternative dimensions would be more expensive to install in New Zealand building projects but the Applicants consider that the likes of Selkirk or BGC could supply alternative dimension bricks to New Zealand at a lower price if they were not willing to invest in machinery to produce bricks with traditional New Zealand dimensions.
- 21.3 In any event, the Applicants understand that BGC’s new factory in Western Australia has the flexibility to be converted to produce 70mm bricks suitable for the New Zealand market.

³² *Fletcher Building Australia (PTY) Limited and Crane Group Limited*, para 126.

22. **The extent to which the applicant considers that potential entry would be sufficient to constrain the merged entity in the markets affected**

22.1 The Applicants consider that a new entrant could effectively constrain the cladding market with the establishment of a single distribution point. For example, Midland Brick has been able to obtain a [] share of the cladding market with only one display premise on the North Shore at Auckland.

23. **How long the applicant would expect it to take for entry to occur, and for market supply to increase, in respect of the potential entrants named in question 21 above**

23.1 The Applicants consider that an Australian or Asian manufacturer of cladding could set up a distribution arrangement to supply New Zealand customers within a matter of months.

23.2 Overseas manufacturers could also supply direct to Builders for specific projects on an ad hoc basis. The Applicants are aware that Boral is manufacturing a range of bricks from its plant in Western Australia that have been specified directly by Builders for a range of projects in New Zealand, including South Island retirement villages.

Countervailing power of buyers

24. **The extent to which the applicant considers that the merged entity would be constrained in its action by the conduct of buyers in the markets affected**

24.1 In the current climate, building industry participants are under even greater pressure to complete projects at the lowest cost. Builders will seek lower price alternatives for cladding to minimise their project costs and add to their margin.

24.2 Builders will often undertake projects on a fixed price basis (plus cost for any additional customised aspects), incentivising Builders to obtain prices that will give them the greatest margin.

24.3 Large home building companies could sponsor entry once conditions are conducive. The loss of a large Builder's account represents a significant loss of business for a cladding company.

25. **Identities of the top five buyers by sales and/or volume in the relevant markets**

25.1 Customer information for CSR NZ and Brickworks NZ will be provided separately.

Coordinated market power

26. **The various characteristics of the market that, post-merger, the applicant considers would either facilitate or impede co-ordination**

26.1 There is no scope for collusion in the cladding market following the Commission's Guidelines:

- (a) there is a high degree of competition between existing suppliers. There are a number of large market participants and fringe competitors in the industry along with a number of potential participants. Neither of the Applicants could be described as "mavericks";

- (b) cladding is differentiated as cost structures vary due to different raw materials and production processes and the finished products have different features such as aesthetics and ease of construction and maintenance;
- (c) new entry (via a distribution channel) can occur relatively quickly;
- (d) the Applicants are not aware of any history of price coordination in the industry; and
- (e) there are no barriers preventing Builders and Homeowners from switching between participants.

26.2 The Applicants consider that there is no material difference between the likelihood of coordinated effects under the factual compared to any relevant counterfactual.

Efficiencies

27. Description of the efficiencies that the applicant believes the acquisition could bring

27.1 The Proposal is driven by the efficiencies that would be obtained, enabling JV Co to compete more effectively and sustainably in the cladding market.

27.2 The Applicants estimate that consolidating and rationalising the Applicants' New Zealand operations will deliver savings of approximately [] per annum, comprising both fixed and variable cost savings:

- (a) The Proposal will enable the Applicants to rationalise transportation by minimising duplication from separately supplying similar products to the same geographic areas. The Applicants estimate that rationalising transportation will lead to almost [] per year of variable cost savings.
- (b) []
- (c) []
- (d) Operating costs are estimated to reduce by [] per year. This includes sharing of administration support, marketing, software, insurance and maintenance.

27.3 The Applicants consider that the above savings would be realised within 6-12 months and it would not be possible to achieve the same degree of cost savings without the Proposal.

27.4 The efficiencies achieved will enable JV Co to remain price competitive against alternative cladding suppliers but also make an economic return, enabling the Applicants to sustain their presence in the market.

Other Factors

28. Description of other features of the market(s) that should be taken into account in considering the effect of the proposed merger

28.1 Not applicable.

Part 7: Further Information & Supporting Documentation

29. Contact details of the relevant competitors, buyers, suppliers and any other relevant market participants

Table 4:

	Name of Company: <i>Both legal and trading names</i>	Contact Details: <i>Postal and physical address, telephone & fax, website</i>	Relevant Contact Person: <i>Name, position and contact details including telephone phone, fax email</i>
Competitors	James Hardie New Zealand Limited	PO Box 12-070 Penrose Auckland 50 O'Rorke Road Penrose Auckland T: 09 579 9919 F: 09 525 4810 http://www.jameshardie.co.nz/	info@jameshardie.co.nz
	Carter Holt Harvey Limited <i>Carter Holt Harvey Wood Products New Zealand</i>	Private Bag 92106 Victoria Street West Auckland 1142 CHH Woodproducts NZ Head Office 173 Captain Springs Road Onehunga Auckland 1061 T: 09 636 7016 F: 0800 746 400 http://www.chhwoodproducts.co.nz	
	NZ Brick & Stone Limited <i>Midland Brick NZ</i>	8 Cowley Place Albany North Shore Auckland T: 09 414 1075 http://www.midlandbrick.co.nz	info@midlandbrick.co.nz

Fletcher Building Group	Private Bag 92 114 Auckland 1142 810 Great South Road Penrose Auckland 1061 T: 09 525 9000 http://www.fletcherbuilding.com	Marion Clements T: 09 525 9248 F: 09 525 9032 marion.clements@fb.co.nz http://www.fletcherbuilding.com
W.D. Boyes & Sons Limited <i>Canterbury Clay</i>	1-7 Horndon Street Darfield Canterbury T: 03 341 5036 F: 03 341 5378 http://www.clay-bricks.co.nz	info@clay-bricks.co.nz
Clay Bricks Limited	50 Tregoweth Lane Huntly Waikato 3700 T: 07 828 9919 F: 07 828 9913 http://www.claybrickslimited.co.nz	
BGC (Australia) Pty Limited	BGC Corporate 6th Floor 18 Mount Street Perth WA 6000 Australia PO Box 7223 Cloisters Square WA 6850 Australia T: +61 8 92611800 F: +61 8 92611737 http://www.bgc.com.au/	corporate@bgc.com.au
Rockcote Systems (NZ) Limited	Christchurch PO Box 39108 Harewood Christchurch 8545 10b Abros Place Burnside Christchurch T: 03 338 6328	

F: 03 338 6819

Auckland

PO Box 58317

Botany

Manakau 2163

4 Te Apunga Place

Mount Wellington

Auckland

T: 09 259 2732

F: 09 259 2713

Wellington

PO Box 30 219

Lower Hutt 5040

1st Floor Horlor Street

NaeNae

Lower Hutt

T: 04 567 3576

F: 04 567 3578

<http://www.rockcote.co.nz>

Jenkin Timber Limited	55 The Concourse Henderson Waitakere City Auckland	info@jenkin.co.nz
	PO Box 21 702 Henderson Waitakere 0650	
	T: 09 836 8462 F: 09 836 8463	
	http://www.jenkin.co.nz/	

Pukepine Sawmills (1998) Limited	PO Box 41 Te Puke	
PurePine Mouldings Limited	T: 07 573 9161	
	http://www.purepine.co.nz/	

Ullrich Aluminium Co Limited	PO Box 98843 SAMC Manukau City	alkalum@uacl.co.nz
	T: 09 262 6262 F: 09 262 6265	
	http://www.ullrich.co.nz	

	/		
	Nuplex Industries Limited	12 Industry Road Penrose Auckland 1061 T: 09 579 2029 F: 09 571 0542 http://www.nuplex.com/	
	Nu-Wall Aluminium Cladding Limited	750B Great South Road Penrose Auckland 1061 PO Box 74280 Greenlane Auckland 1546 T: 09 582 0040 F: 09 579 5649 http://www.nu-wall.co.nz/	Dave Hopkinson Director (Sales and Marketing) T: 09 582 0663 daveh@aluminium.co.nz z
	Kaneba Limited	9-11 Rothwell Avenue Rosedale Auckland 0632 PO Box 303 388 North Harbour Auckland 0751 T: 09 926 2297 F: 09 926 1444 http://www.kaneba.co.nz/ z/	
Buyers	The Applicants will separately advise the Commission.		
Suppliers	The Applicants have not listed any suppliers as there are a wide range of suppliers and the Applicants consider that they are not particularly relevant for this application. The Applicants are happy to provide contact information at the Commission's request.		
Trade Associations	Clay Brick and Paver Manufacturers Association (NZ) Incorporated <i>Think Brick New Zealand</i>	Private Bag 92066 Victoria Street West Auckland 1142	info@thinkbrick.co.nz

30. **Copies of the most recent annual report (or audited financial statements if no annual report available) for each of the merger parties**
- 30.1 Copies of the most recent annual reports of each of the merger parties are appended to this application as Confidential Appendices 4 and 5 respectively.

Part 8: Confidentiality

31. **Request for specific information contained in or attached to the notice to be confidential and the reasons for this request in terms of the criteria set out in the Official Information Act 1982**
- 31.1 Confidentiality is not claimed for the fact of the proposed acquisition.
- 31.2 Confidentiality is sought for:
- (a) the information contained in **Confidential Appendices 3-5** to the confidential version of this application;
 - (b) the information contained in bold square brackets in the confidential version of this application (i.e. []).
- 31.3 Confidentiality is sought until the relevant applicant confirms in writing to the Commission that the particular information is no longer confidential.
- 31.4 This request is made because the information is commercially sensitive and valuable information which is confidential to the participants, and disclosure of it would be likely to unreasonably prejudice the commercial position of the participants. Confidentiality is requested for the purposes of section 9(2)(b) of the Official Information Act 1982.
- 31.5 The applicant requests that it be notified of any request made to the Commission under the Official Information Act 1982 for release of confidential information, and that the Commission seeks its views as to whether the information remains confidential and commercially sensitive, at the time a response to such a request is being considered.
- 31.6 Paragraphs 31.1 – 31.5 of this application also apply in respect of any additional information provided, whether orally or in written form, to the Commission where it has been expressed to be confidential or it is implicit by the nature of that information.

THIS NOTICE is given by CSR Building Products (NZ) Limited and Brickworks Building Products (NZ) Pty Limited.

We hereby confirm that:

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

We undertake to advise the Commission immediately of any material change in circumstances relating to the application/notice.

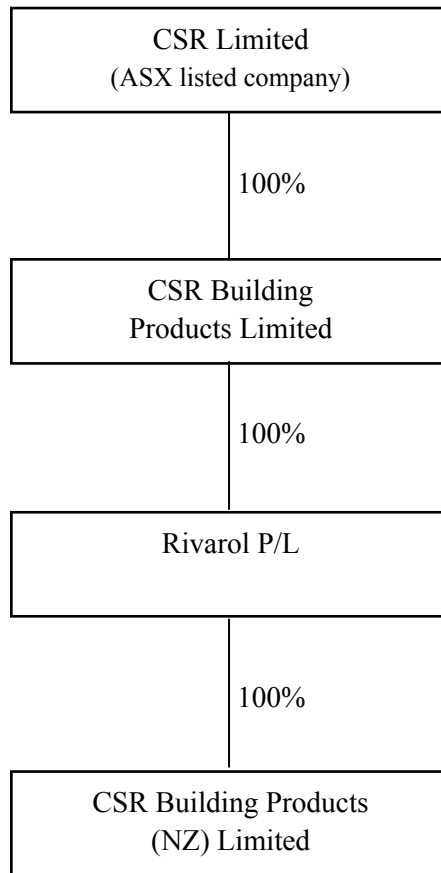
Dated this 31st day of August 2012

Nick Pezet, Director

I am a director of CSR Building Products (NZ) Limited and am duly authorised to make this application/notice on behalf of the Applicants.

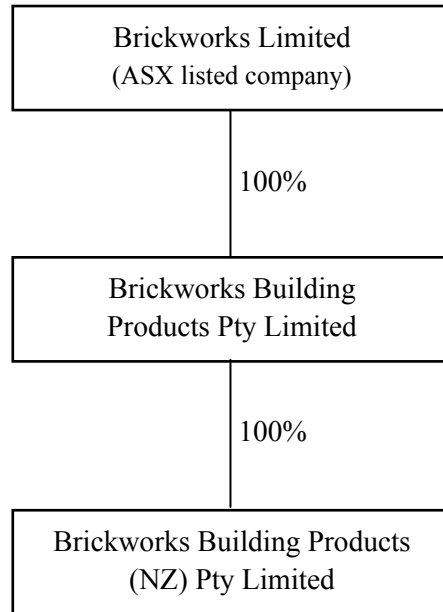
Appendix 1

Shareholder structure diagram of CSR Building Products (NZ) Limited



Appendix 2

Shareholder structure diagram of Brickworks Building Products (NZ) Pty Limited



Confidential Appendices 3-5
