

DAIKEN / DONGWHA

RESPONSE TO NZCC LETTER OF ISSUES DATED 22 DECEMBER 2017

INTRODUCTION

1. The following sets out Daiken New Zealand Ltd's ("**Daiken**") response to the preliminary views set out in the Commission's 22 December 2017 Letter of Issues ("**LOI**") in relation to Daiken's application for clearance to acquire Dongwha New Zealand Ltd ("**Dongwha**") (the "**Acquisition**").
2. Daiken is grateful for the opportunity to respond to the LOI, and looks forward to meeting with the Commission to discuss this response further.

EXECUTIVE SUMMARY

3. Daiken agrees with the Commission's views in its LOI that:
 - (a) the Acquisition does not give rise to any competitive effects concerns in relation to the acquisition of wood fibre;
 - (b) the Acquisition does not give rise to any unilateral effects concerns in the supply of any MDF product;
 - (c) the Acquisition does not give rise to any competitive effects concerns in the supply of downgrade MDF; and
 - (d) [].
4. This demonstrates that the Commission has satisfied, or is close to satisfying, itself that a number of aspects of the Acquisition, including in relation to a number of different customers, do not give rise to any competition concerns.
5. The one aspect the Commission is still testing is whether the Acquisition could give rise to a substantial lessening of competition due to increased potential for coordinated effects in the supply of raw (non-downgrade) MDF, []. Daiken is confident that no such concerns are likely to arise – including because:
 - (a) there is no evidence that Daiken and Nelson Pine Industries Limited ("**NPIL**") are currently coordinating in respect of either the price offered to domestic customers or the volume of product sold to domestic customers. This strongly suggests that conditions for coordination are not currently present in the market for the supply of raw MDF;
 - (b) there is no evidence that Dongwha represents a material constraint on Daiken. Apart from its long-standing arrangements with Laminex, Dongwha's presence as a supplier of raw MDF in the New Zealand market is insignificant: it imposes no material constraint on Daiken or NPIL and, therefore, the removal of Dongwha will not materially change the existing competitive conditions for the supply of raw MDF to domestic customers;
 - (c) to the extent that Dongwha currently imposes any constraint on the incentive or ability for Daiken and NPIL to coordinate prices or volumes, such constraint will be

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preserved post-Acquisition by Laminex due to the proposed Product Supply Agreement with Daiken, []; and

- (d) in light of the above, the Acquisition will not materially alter the conditions for coordination between Daiken and NPIL. More specifically:
- (i) prices for the supply of raw MDF are not currently transparent, and will be no more transparent post-Acquisition;
 - (ii) Daiken and NPIL will continue to face difficulties in the allocation of customer volumes, and such allocation will be no easier post-Acquisition;
 - (iii) there will be no material change in the ability of Daiken and NPIL to detect deviations from any agreement or understanding to coordinate in respect of price or volumes;
 - (iv) there will be no material change in the ability of Daiken and NPIL to punish deviations from any agreement or understanding to coordinate in respect of price or volumes; and
 - (v) Daiken and NPIL have asymmetric market shares and cost structures, and will continue to do so post-Acquisition.

6. Accordingly, Daiken is confident that:

- (a) there is no likelihood of any materially increased potential for coordinated effects in the supply of raw MDF; and
- (b) therefore, there is no likelihood of a substantial lessening of competition in the factual in comparison to the counterfactual.

NO INCREASED LIKELIHOOD OF COORDINATED EFFECTS CONCERNS

7. The LOI, at paragraph [47], says that the Court of Appeal has said weight can be given to theoretical concerns in "three-to-two" mergers. While such theories can be used as an initial screen, as the LOI recognises, they are of course far too simple for considering the effects of any given transaction.

8. Specifically, for coordinated effects concerns to arise, it is necessary to consider whether any given transaction materially changes market conditions to increase the likelihood of coordinated conduct between competitors – including by considering how that transaction, based on market-specific quantitative and qualitative factors, makes it easier for the remaining firms to:

- (a) reach and sustain agreement on key dimensions of competition;
- (b) detect deviations from the agreement, so as to dissuade firms from cheating for fear of punishment; and
- (c) deter such deviations from coordination by means of more effective punishments (e.g., faster and more costly to the cheating firm).

9. While the Acquisition, on its face, reduces the number of firms manufacturing MDF in New Zealand, Daiken is confident that it does not materially increase the likelihood of coordinated conduct as between the factual and counterfactual, including because:

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- (a) there is no evidence that Daiken and NPIL are currently coordinating in respect of either the price offered to domestic customers or the volume of product sold to domestic customers. There has been a considerable degree of customer switching and []. This strongly suggests that conditions for coordination are not currently present in the market for the supply of raw MDF;
- (b) there is no evidence that Dongwha represents a material constraint that []:
- (i) Dongwha has not won any large domestic customers from Daiken and, with the exception of Laminex, does not supply substantive amounts of premium raw MDF to any of the large domestic customers served by Daiken or NPIL. There is no evidence that Dongwha has competed aggressively to win the business of these large customers. Rather, [];
- (ii) [].
- As a result, the removal of Dongwha will not materially change the existing competitive conditions for the supply of raw MDF to domestic customers;
- (c) to the extent that Dongwha currently imposes any constraint on the incentive or ability for Daiken and NPIL to coordinate prices or volumes for some customers through its supply of raw MDF to Laminex, such constraint will be preserved post-Acquisition under the terms of the proposed Product Supply Agreement with Daiken. Under this agreement:
- (i) []; and
- (ii) []; and
- (d) in light of the above, the Acquisition will not materially alter the conditions for coordination between Daiken and NPIL in the market for the supply of raw MDF to New Zealand customers. More specifically:
- (i) prices for the supply of raw MDF are not currently transparent, and will be no more transparent post-Acquisition;
- (ii) Daiken and NPIL will continue to face difficulties in the allocation of customer volumes, and such allocation will be no easier post-Acquisition;
- (iii) there will be no material change in the ability of Daiken and NPIL to detect deviations from any agreement or understanding to coordinate in respect of price or volumes;
- (iv) there will be no material change in the share of the domestic market on which Daiken and NPIL could each benefit from coordination. Daiken will continue to serve Laminex primarily from Dongwha's plant at Matura at prices agreed under the Product Supply Agreement and, given its location advantage, will continue to serve its other domestic customers with most of their raw MDF requirements from its existing plant at Rangiora; and
- (v) there will be no material change to Daiken's cost structure that would make it substantially less asymmetric with that of NPIL. Daiken will continue to operate the Matura plant as a stand-alone facility and does

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not expect to achieve any substantial cost efficiencies other than those outlined in paragraphs 4.5 to 4.8 of its application for clearance, [] which do not come about from Daiken operating two sites or at a larger scale.

- 10. In light of the above, there is no class of customer that is any more vulnerable to being subject to price rises as a result of coordination between Daiken and NPIL than at present.
- 11. Accordingly, Daiken is confident that:
 - (a) there is no likelihood of any materially increased potential for coordinated effects in the supply of raw MDF; and
 - (b) therefore, there is no likelihood of a substantial lessening of competition in the factual in comparison to the counterfactual.

No evidence that Daiken and NPIL are currently coordinating in respect of prices or volumes

- 12. There is no evidence to suggest that there is currently an explicit or tacit understanding in place between Daiken and NPIL to coordinate prices for domestic customers, allocate these customers or share their volumes.
- 13. [].
- 14. []:
 - (a) [];
 - (b) [];
 - (c) [];
 - (d) []; and
 - (e) [].
- 15. [].
- 16. [].
- 17. []:
 - (a) [] and [].
 - (b) [].

No evidence that Dongwha represents a material constraint on the prices currently offered by Daiken and NPIL to domestic customers

- 18. The LOI correctly identifies that it is important for the Commission to focus on whether Dongwha is playing any substantial role on constraining prices in the market, and/or if it would play any role in constraining or destabilising any coordination in the counterfactual.
- 19. The evidence is that Dongwha is not playing any significant role in the competitive arena. Therefore, its removal as a third party competitor does not materially change the competitive

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conditions in the marketplace, nor remove a constraint on any potential for coordination between Daiken and NPIL. It is well recognised that the removal of a firm that does not behave as a material competitor is unlikely to increase the risk of coordination.

20. In that context, it is relevant that the Commission has previously observed that Dongwha:

- (a) is, at best, a "fringe" competitor that "provides only limited competition to NPIL and [Daiken]";¹
- (b) does not have a material influence on the pricing behaviour of (what is now called) Daiken and NPIL;² and
- (c) to the extent it participates in the New Zealand market, is a "price follower".³

21. The current market dynamics continue to support the Commission's findings that Dongwha is not a material competitor in the New Zealand domestic market, and therefore that its removal could not be regarded as likely to lead to increased potential for coordination in the factual in comparison to the counterfactual. This is demonstrated by the following:

- (a) Dongwha NZ has long been, and continues to be, primarily export focused. [].
- (b) Dongwha accounts for less than [] of sales of MDF to New Zealand customers outside of Laminex and is therefore at most a *de minimis* competitor. Aside from its sales to Laminex, less than [] of Dongwha's MDF output is sold to customers in New Zealand, and that is []. Of its non-Laminex domestic sales:
 - (i) []. Downgrade is a waste product that arises from production overruns and the cutting of MDF to meet customer size requirements for premium MDF products. Because the price that manufacturers can achieve on sales of downgrade are considerably lower than those they can achieve on sales of premium MDF, they each have an incentive to minimise the amount of downgrade they produce. [] [];
 - (ii) approximately []; and
 - (iii) the remainder is sold to [].
- (c) Dongwha's very limited sales of premium MDF to customers other than Laminex reflects the significant disadvantages it faces in competing with Daiken and NPIL in the supply of MDF to domestic customers. In particular, both NPIL and Daiken are located much closer than Dongwha to the small number of large customers for raw MDF that primarily require supply to the major cities of Auckland, Wellington, and Christchurch, as well as Nelson. As a result, NPIL and Daiken incur lower transport costs in supplying these large customers, particularly those located very close to their plant and those with a national footprint. They also have the ability to offer these customers more flexible supply arrangements with shorter lead times for delivery and more frequent delivery, which reduces the customer's need to hold stock on-site; and
- (d) [].⁴ []:

¹ [100] of 2008 Decision.

² [100] of 2008 Decision.

³ [110] of 2008 Decision.

⁴ [].

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- (i) [];
 - (ii) []; and
 - (iii) [].
- (e) [].⁵ [].
- (f) []:
- (i) [].
 - (ii) [].
22. In light of the above, it is not correct to suggest, as the LOI does at paragraph [54.3], that Dongwha's relatively small portfolio of domestic customers means it has a greater incentive to increase sales to New Zealand customers than Daiken or NPIL. That has not been demonstrated by Dongwha's behaviour in market. [].⁶ []:

- (a) [];
- (b) []; and
- (c) [].

Laminex Product Supply Agreement replicates status quo

23. The Product Supply Agreement between Daiken and Laminex further means that the Acquisition does not give rise to any increased potential for coordination as between the factual and counterfactual. The executed copy of this Product Supply Agreement is **enclosed**.
24. Specifically, under the Product Supply Agreement Laminex will not only have sufficient volumes to satisfy its own internal needs for raw MDF [], but it will also have [], with scope to grow volumes over time, to continue to compete domestically with Daiken, NPIL and other distributors in the sale of raw MDF to other customers. This will mean that Laminex will continue to be able to act as a constraint on Daiken and NPIL in the domestic raw MDF market.
25. Specifically:
- (a) [];
 - (b) []; and
 - (c) [].
26. Being able to grow its purchases by ~[] to [], when its current internal demand for raw MDF is just ~[], provides Laminex with significant scope to grow to compete if market opportunities were to arise – in particular in the context of a market where total New Zealand demand for raw MDF is estimated at ~[]. This means that Laminex would have volumes available for resale that represent up to ~[] of total third party (i.e. non-Laminex internal)

⁵ [].

⁶ [].

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demand, and the additional volumes that Laminex would have available under the Product Supply Agreement would allow it to double the size of its existing distribution business. [] [].⁷ There is no reason why Laminex's ability to expand its volume of sales in New Zealand should be considered more limited than Dongwha's currently is, and to the contrary should be greater given (unlike Dongwha) Laminex:

- (a) already has an existing MFB and MDF distribution business with a strong market presence and established logistics networks and warehouses around New Zealand ([]); and
- (b) would be able to expand those volumes without needing to be concerned about damaging relationships with MDF export customers (as it would fall to Daiken to manage the volume expectations of overseas customers).

27. [].

28. Laminex's ability to expand in New Zealand either as a distributor/reseller of raw MDF or as a manufacturer of laminated products is also supplemented further if market opportunities were to arise in New Zealand given:

- (a) Laminex, at Gympie, currently has capacity to manufacture [] of MDF, of which [] is exported (representing [] of total New Zealand demand); and
- (b) Laminex has established freighting arrangements across the Tasman, and warehouses in New Zealand.

29. It is also not the case that the price at which Laminex is able to purchase MDF from Daiken could be prone to coordination. Specifically, the terms of the Product Supply Agreement []:

- (a) [];
- (b) [];
- (c) []; and
- (d) [].

30. Accordingly, it is not the case that those prices could be prone to coordination.

Prices are not transparent, and will not be transparent post-Acquisition

31. The New Zealand MDF market is not a market with "transparent" prices, or in which MDF manufacturers are able to obtain up-to-date or accurate information each other's prices.

32. Daiken currently supplies [] with raw MDF.⁸ These [] customers []⁹ comprise [] of Daiken's total domestic supply of raw MDF, with Daiken's remaining domestic sales directed to [].

33. []. Namely:

- (a) []; and

⁷ [].

⁸ [].

⁹ [].

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- (b) [].
34. Specifically, []. For example:
- (a) [];
- (b) [];
- (c) []; and
- (d) [].
35. Even for those customers that do [].
36. Even to the extent some customers may use pricing information from one MDF supplier when negotiating with another, that only occurs where customers choose to do so and the information disclosed may be inaccurate or out-of-date.
37. Given it is within a customer's control to decide if/when any information is disclosed, they could readily withhold such information if there were concerns about uncompetitive prices in the market. This means that there would be significant difficulty in deterring cheating from any coordinated pricing level, given:
- (a) there would be no guarantee any specific price cutting would in fact be disclosed to the other party, or would be disclosed accurately; and
- (b) even if it was, there could be a significant lag before any such information is passed to the other competitor (if at all) given transmission of that information is in the control of the customers.
38. Pricing is also not the only element of competition for customers, which further undermines the potential for Daiken and NPIL to coordinate on price. []. These more "complex" aspects of the price/service combination further undermine any prospect for Daiken and NPIL come to an agreement or understanding on an optimal pricing level or allocation of domestic volumes post-Acquisition.
39. Accordingly, prices are not currently transparent in the market, and the Acquisition will not make those prices any more transparent.

Volume allocation would remain difficult to achieve and would be made no easier post-Acquisition

40. Given that Dongwha does not currently supply any large domestic customers or represent a constraint on prices for major customers other than Laminex, Daiken and NPIL will be in no better position to reach an agreement over the sharing of volumes post-Acquisition.
41. An understanding over the allocation of customers or volumes will likely be difficult for Daiken and NPIL to arrive at and sustain post-Acquisition for a number of reasons.
- The role of the Product Supply Agreement in frustrating the ability to reach agreement over the allocation of volumes*
42. An agreement or understanding to share volumes would likely be difficult to achieve by virtue of the fact that, post-Acquisition Daiken will be []. As a result, Daiken will not be capable of benefiting from the price rises that might arise from coordination with NPIL on approximately

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[]% of its domestic supply for a period of at least 15 years (i.e., of the [] or so of raw MDF currently supplied by Daiken and Dongwha,¹⁰ Daiken will only have the potential (and, as described elsewhere, no increased ability) to benefit from coordination in respect of around [] post-Acquisition).¹¹ To the extent that Laminex takes advantage of its right to increase the volume of raw MDF that it acquires from Daiken under the Product Supply Agreement, this percentage could fall further again.

43. By contrast, Daiken does not know what agreements NPIL has with any customers, including whether any agreements []. On the assumption that NPIL has no agreements [], NPIL may benefit from an understanding over the allocation of volumes on all of its domestic supply, which Daiken estimates to be in the order of []m³ of MDF ([] more than Daiken). This asymmetry in the potential benefits to be derived from coordination by each of Daiken and NPIL would likely inhibit their ability to reach an understanding over the appropriate allocation of domestic volumes between them.¹²
44. Irrespective, the split of domestic volumes between Daiken and NPIL which may potentially be subject to price rises under any agreement to coordinate will not change markedly from the status quo. This is because:
- (a) the vast bulk of the domestic volumes that Daiken will be acquiring through the acquisition of Dongwha (being those to Laminex) will be subject to the Product Supply Agreement and so []; and
 - (b) Dongwha does not serve many other domestic customers and (as set out in paragraph 21(b) above), those that it does serve [].
45. As a result, the incentive for Daiken and NPIL to coordinate post-Acquisition as a result of any change in their domestic market share will be largely unchanged. Daiken will continue to serve Laminex with the same or greater volumes from Dongwha's plant at Matura and [] in accordance with the terms of the Product Supply Agreement.

The role of the Product Supply Agreement in hindering the ability to achieve any agreed allocation of volumes

46. Second, the Product Supply Agreement with Laminex can be expected to inhibit the ability of Daiken and NPIL to benefit from any attempt at coordination and/or achieve any desired allocation of domestic volumes. This is because Laminex competes with other customers of Daiken and NPIL in the supply of laminated products as well as in the distribution of raw MDF to smaller customers. If Daiken and NPIL raise prices to Laminex's competitors, they will place those competitors at a disadvantage to Laminex and risk the reallocation of sales of MDF from those customers to Laminex. In particular:
- (a) []; and
 - (b) [].
47. Under the Product Supply Agreement, Laminex has the ability to increase the volume of MDF it acquires from Daiken by up to [] in 2019 and potentially by up to [] in 2020.¹³ [], this would reduce the volume of MDF on which Daiken and NPIL could collectively benefit from coordination.

¹⁰ This excludes Dongwha's sales of MDF to itself, which it used to produce MFB for sale to Laminex and others.

¹¹ [].

¹² [].

¹³ [].

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The role of substitute products in hindering the ability to achieve any agreed allocation of volumes

48. Third, the ability of Daiken and NPIL to achieve any desired allocation of volumes will also be inhibited by the ability of customers to switch to alternative products in response to an increase in price. As outlined in **Figure Six** of the submission, almost all large customers can substitute at least a portion of their demand for MDF to substitute products as an alternative to MDF (such as imported board, particle board, and so on). Furthermore, as noted later in this response at 66(d)(ii), [] and []. The prospect of customers considering those alternatives will only increase, with for example:

- (a) the increasing prevalence of imported MFB;
- (b) the prevalence of MDF available from Asia;
- (c) Borg is understood to be increasing its MDF capacity by [], which will create more opportunities for the threat of imports from Australia; and
- (d) the increasing quality of fine particle board.¹⁴

49. Accordingly, there would continue to be uncertainty over whether a fall in customer demand is due to diversion to NPIL/Daiken or whether customers are substituting to other products.

The relevance of export market conditions to the sustainability of any agreement or understanding over the sharing of volumes

50. The ability for Daiken and NPIL to reach and sustain any agreement over the sharing of volumes will also be frustrated by continual fluctuations in export market conditions, which influence the relative costs and benefits of cheating on any agreement or understanding to coordinate.

51. Continual fluctuations in export markets occur due to:

- (a) foreign exchange rates;
- (b) changes in demand for downstream outputs if the MDF is being processed into products that are further exported from that country (e.g. furniture made in Southeast Asia for export to Europe); and
- (c) the economic conditions of that local country.

52. Periods of soft demand or low margins in key export markets are inevitable and during those times the incentive to cheat on any agreement to coordinate may be greatly enhanced, which will likely undermine any incentive of Daiken and NPIL to implicitly agree on any allocation of customers or volumes.

53. That is particularly the case given MDF manufacturing is a high fixed-cost business, with each supplier having a strong incentive to achieve volumes as close to capacity as possible in order to:

- (a) avoid unnecessary shut-downs; and

¹⁴ Particle board is typically lower cost than MDF products and improvements in quality mean that it has certain advantages over MDF as a substrate, e.g. it is easier to cut than MDF, resulting in less wear and tear on cutting equipment.

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- (b) achieve the recovery of fixed costs with the highest margin possible over the average cost of supply.
54. The continual ebb and flow of export market conditions will therefore have implications for the sustainability of any agreement to allocate volumes, and hence the ability of Daiken and NPIL to reach such an agreement in the first place.
55. Furthermore, the ability and costs of punishing any deviation will also be uncertain and potentially significant given that detection could take some time, which means that export market conditions could be materially different again by the time of detection. If so:
- (a) the party attempting to impose the punishment may incur costs from having capacity allocated to lower-margin domestic sales; and
 - (b) the party toward whom the punishment is directed may be able to mitigate the costs of punishment by directing any surplus capacity toward supplying product into export markets.

No change in the ability of Daiken and NPIL to detect deviations

56. As noted above, because Dongwha does not have any substantive domestic customers other than Laminex, NPIL and Daiken will be in no better position post-Acquisition to detect deviations from an agreement to coordinate (as they already know when they lose volumes that these are not going to Dongwha).
57. In any case, the ability of Daiken and NPIL to detect deviations from an agreement to coordinate will continue to be frustrated by other factors that will inhibit their ability to discern whether a fall in demand by one or more customers is due to cheating, or whether it is due to some other external factor such as a fluctuation of downstream demand or substitution to other products or suppliers.
58. In particular, to the extent that they split their supply between Daiken and NPIL, it will likely be difficult to discern whether a fall in the monthly demand of customers is due to the offer of low prices by the other or changes in downstream demand. The monthly volume of product supplied to [], as demonstrated in the **Figures One** and **Two** below.

[]

[]

59. The ability to detect deviations from an agreement to coordinate will also be frustrated by the factors outlined above, including:
- (a) the potential for Laminex to increase its share of downstream markets in response to price rises for its competitors under any coordinated agreement or understanding;
 - (b) customers having the ability to substitute to other products such as imported board, particle board and so on; and
 - (c) variations in customer demand in the ordinary course of business.

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No change in the ability of Daiken and NPIL to punish deviations

60. Daiken and NPIL's ability to punish any deviation from an agreement to coordinate will not materially increase post-Acquisition. Daiken's ability to do so is limited as diversion of large amounts of export volumes comes at a risk that Daiken will lose all the volumes of a major customer, not just that proportion of volume used to punish deviation. This would be very costly to Daiken as:
- (a) a sudden inability to fulfil export customers' requirements would come at the inevitable expense of relationships and reputation with export customers;
 - (b) the hole in volumes could not be filled by an increase in domestic sales – Daiken would need to attract a new export customer which often takes a significant length of time; and
 - (c) for the reasons outlined at 53, loss of volumes (even for a short period of time) can have significant impacts on the recovery of fixed costs, margins, and average cost of supply.
61. Accordingly, any attempt at punishment through the diversion of export volumes would likely be a high cost strategy (with those costs likely to be felt over a lengthy period of time), and Daiken and NPIL's ability to impose such punishments would not be changed by the Acquisition.

Daiken and NPIL have asymmetric market shares and cost structures, and will continue to do so

62. For the reasons outlined in the clearance application, Daiken and NPIL will continue to operate with a very different scale, and asymmetry in market share and cost structure.
63. Although Daiken's capacity and domestic market share will inevitably increase as a result of the acquisition of Dongwha's assets and customer base, [].
64. In terms of cost structure, there are unlikely to be any significant changes from the status quo given that Daiken will operate the Mataura plant (which is over 500km away) as a separate production facility, with no scope for any significant efficiencies in production from co-location of raw materials or plant and equipment. NPIL will continue to run its MDF business with a very different structure to the merged entity, namely one that is:
- (a) vertically integrated with its own forestry assets (in a region with its own fibre conditions);
 - (b) not vertically integrated in the supply of MFB;
 - (c) co-located with its own resin supplier;
 - (d) co-located with its LVL business;
 - (e) located on a single site (whereas the merged Daiken entity will have two MDF plants spread across two regions some 500km apart); and
 - (f) located at a different distance from key customer bases than Daiken.

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65. This means that there will be no material increase in the symmetry of Daiken and NPIL's market shares and cost structure and, therefore, no material increase in their ability to reach a common assessment of the optimal industry price.

NO VULNERABLE CLASS OF CUSTOMERS

66. The above demonstrates that there will not be any class of customer that will be more vulnerable to price increases / quality decreases through coordination in the factual in comparison to the counterfactual. The Acquisition does not make any material difference to the vulnerability of any class of MDF customers to coordinated effects:

(a) **Large customers:** []:

(i) [];

(ii) []; or

(iii) [],

[].

(b) **Laminate manufactures:** Laminate manufacturers []:

(i) []; and

(ii) [].

[].

- (c) **Distributors:** As in the case of merchants, above, distributors, such as Laminex, NZ Panels (Impey's and Anthony Shearer), are typically of a size and scale that provides them with []. In particular, the key distributors in New Zealand (NZ Panels and Laminex) are vertically integrated with broader laminate manufacturing operations, [].

- (d) **Merchants:** Equally, merchants will continue to have material countervailing power:

- (i) Merchants tend to be of large scale, and therefore typically exercise significant buyer power in negotiations, including through leveraging volume-based discounts. This accords with the Commission's previous observation in Decision 431 in relation to building merchants:

The Commission's enquiries have confirmed that the acquirers are in a sufficiently strong position to prevent the merged entity from unilaterally raising the price of MDF without losing significant market share. These acquirers have confirmed that MDF is treated as a commodity product that is particularly price sensitive, and that they are quite prepared to shift their custom to the alternative manufacturers if market conditions change.

- (ii) Merchants have substantial expertise in sourcing various products cost-effectively from around the world, and so would be well-placed to resist

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price increases from coordinated effects by threatening to import raw MDF from overseas. []. Further, [];

- (iii) In any event, [].
- (e) **Cabinet makers, joiners, furniture makers, etc:** There will be no adverse impact on this category of customers:
 - (i) For many applications, these customers are able to switch to other substrates, or imported value-added MDF. []); and
 - (ii) The parties will continue to be constrained by the presence of Laminex in this space. []. Laminex already has a substantial presence as a distributor such that these customers would readily switch to Laminex as an alternative supplier of raw MDF if opportunities were arise. []. These customers can, and do, switch their purchases to distributors, and so could benefit from the negotiating power exercised by those groups (as referred to above) – including being able to benefit from [].
- (f) **Mouldings customers:** The Commission has previously found that "there are a number of substitutes for MDF mouldings" - including for example raw pine wood, which is used widely for mouldings.¹⁵ That position remains the same, and moulding customers will continue to have a number of competitive alternatives, demonstrating that they would not be vulnerable to uncompetitive price increases. [].
- (g) **Downgrade MDF customers:** The Commission has observed that the manufacture and supply of downgrade MDF is likely to be part of a separate, broader packaging materials market, because there are numerous alternative substitutes, and the Commission has not expressed any concerns in respect of customers for downgrade MDF. Again, those customers would not be vulnerable to uncompetitive price increases.

67. Accordingly, the evidence demonstrates that there will not be any class of customer that will be more vulnerable to price increases/quality decreases through coordination in the factual in comparison to the counterfactual.

CONCLUDING COMMENTS

68. For the reasons outlined in this submission, Daiken is confident that:
- (a) there is no likelihood of any materially increased potential for coordinated effects in the supply of raw MDF; and
 - (b) therefore, there is no likelihood of a substantial lessening of competition in the factual in comparison to the counterfactual.

¹⁵ <http://www.sppnz.co.nz/product/spp-pine-mouldings/>