

Investigation into Winstone Wallboards Limited

Date: 22 December 2014

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Purpose of this report

1. This report summarises the outcome of the Commerce Commission's (the Commission) investigation into complaints that Winstone Wallboards Limited (Winstone) – part of the Fletcher Building Group – has acted anti-competitively in the manufacture and supply of its plasterboard (GIB).
2. In our view, the evidence does not support a conclusion that Winstone has breached the Commerce Act 1986 (the Act).
3. This summary report has been prepared to provide a public record of our views, the reasons for these views and the decision we took not to pursue enforcement action against Winstone. The report is intended to assist participants in the industry, complainants, witnesses and the general public (including businesses) to understand the investigation and its outcomes.
4. The Commission makes this report publicly available in accordance with its statutory functions and powers, including under section 25 of the Act, which allow the Commission to make information available with respect to the carrying out of its functions and the exercise of its powers.
5. The Commission emphasises that the views we have formed, as contained in this report, have not been tested in court. Where we have made assessments, we have proceeded by asking whether the conduct described could ultimately be proven in court. However, only a court can make findings of fact or law, and this report does not purport to do either. Rather, it records the Commission's view on this investigation and the reasons for its decision not to pursue enforcement action against Winstone.

Executive summary

Our investigation

6. In August 2013, we received a complaint alleging that:
 - 6.1 Winstone has supply agreements with major merchants which preclude them from stocking other plasterboard brands and limit access to advertising and technical information for those brands;
 - 6.2 the rebates Winstone pays to merchants effectively prevent other plasterboard suppliers from accessing merchants and competing; and
 - 6.3 Winstone has or is engaging in predatory pricing, either through its rebates or by targeted price reductions when a competing plasterboard supplier is tendering for a job.
7. In October 2013 we received a second complaint alleging similar behaviour.

8. Broadly, the complaints raised two potential ways in which Winstone may have breached the Act:
 - 8.1 **conduct or agreements that foreclose competitors** in breach of sections 27 or 36 of the Act, either by:
 - 8.1.1 Winstone entering into exclusive agreements with merchants that have the purpose and/or effect of substantially lessening competition; or
 - 8.1.2 Winstone paying rebates to merchants and builders that induce them to purchase or stock plasterboard exclusively or almost exclusively from Winstone, thereby foreclosing competitors;¹ and
 - 8.2 **predatory pricing** by Winstone in breach of sections 27 or 36 of the Act, either by:
 - 8.2.1 paying rebates at such a level that the effective price being offered by Winstone is predatory; or
 - 8.2.2 discounting prices in a predatory way when competing with rivals on a specific job.

Conduct or agreements that may prevent competition

What we looked at

9. We considered whether:
 - 9.1 Winstone's agreements with major merchants – ITM, Mitre 10, Bunnings and Carters² – contain contractual terms requiring them to purchase exclusively from Winstone or exclusively stock GIB; or, short of that,
 - 9.2 the rebates in Winstone's agreements with merchants effectively induce them to stock or purchase exclusively or almost exclusively from Winstone.
10. If such agreements exist, the question is whether those agreements prevent or hinder a rival plasterboard manufacturer/importer from being an effective competitor, by limiting their ability to enter, expand, or to otherwise be a cost-effective competitor.
11. Given a willingness and an ability for merchants to supply an alternative plasterboard brand to GIB, we similarly considered whether demand for a competing brand was constrained by rebates paid by Winstone to builders.

¹ Under s 3(5) of the Act, the aggregate effect of multiple provisions can be assessed under s 27. We therefore considered the combined effect of multiple rebates to multiple merchants, similarly for builders.

² PlaceMakers is interconnected with Winstone so we did not include it in our analysis. For the purposes of this report, references to major merchants exclude PlaceMakers.

12. In carrying out this investigation, we drew a distinction between stocking and supplying. Stocking occurs when a merchant purchases an item and holds a certain amount in its stores or warehouses. In this way, the merchant has an inventory risk associated with the purchase. In contrast, supplying a product refers to ‘indent supply’, which is when a merchant will supply an alternative product on request.

Contractual provisions requiring merchants to purchase exclusively or almost exclusively from Winstone?

13. Only one major merchant has an agreement with Winstone that it will exclusively stock GIB.
14. We do not consider this one agreement sufficient to give rise to a substantial lessening of competition. Setting aside for the time being whether the rebates induce exclusivity or near-exclusivity, given that only one major merchant is required to stock GIB exclusively, a rival plasterboard supplier can still have its product stocked by three other major merchants, collectively comprising about []% to []% of the plasterboard market.
15. Further, all major merchants are able to indent supply other plasterboard brands.

Do Winstone’s rebates substantially lessen competition in the plasterboard market?

16. The evidence does not demonstrate that Winstone’s rebates induce merchants to exclusively or almost exclusively stock or supply GIB, resulting in rival plasterboard suppliers struggling to expand in the market.
17. We considered whether merchants agree to rebates (rather than lower wholesale prices) because merchants are sharing in some of the profits Winstone might make from excluding its competitors.
18. However, we concluded that:
- 18.1 it is not clear that merchants’ profits from selling or supplying GIB are greater than they otherwise would be without Winstone’s rebates; and
- 18.2 there are other factors that appear to have limited rival plasterboard suppliers’ entry and expansion, including:
- 18.2.1 Building Code compliance (for plasterboard products used for bracing);
- 18.2.2 GIB being the preferred product of those involved in the designing, consenting and building of houses, including for obtaining the necessary building approvals from councils;
- 18.2.3 rival plasterboard suppliers not appearing to offer major merchants sufficiently compelling prices to compensate for the risk of dual-stocking; and

18.2.4 the existence (at least until recently) of import duties on plasterboard.³

19. Given that all major merchants can indent supply, we also considered whether merchants had no or little demand for alternative plasterboard on an indent basis because builders were unwilling to purchase alternative plasterboard for fear of losing their own rebates from Winstone. We concluded that these rebates were insufficient to suggest a breach of section 27.
20. We also considered whether Winstone was taking advantage of substantial market power in breach of section 36 through the rebates it pays.⁴ To take advantage of substantial market power a firm is required to act in a way that it would not if it was operating in a competitive market. Given rebates are found in competitive markets, it is difficult on that basis alone to distinguish between rebates that raise competition concerns and those that do not. Therefore, we cannot conclude that there has been a breach of section 36.

Predatory pricing

What we looked at

21. In regard to predatory behaviour, we looked at whether:
- 21.1 Winstone's plasterboard rebates result in its effective wholesale prices being below cost for the contestable portion of demand,⁵ with the aim of foreclosing entry or effective expansion by competitors, and also limiting potential competition for the non-contestable portion of demand; or
- 21.2 when facing competition from a rival plasterboard manufacturer for individual jobs, Winstone drops its prices for those jobs so significantly that its revenue (taking rebates into account) falls below cost with the aim to drive out competition, allowing Winstone to maintain high returns on other, including future, jobs.

No evidence of predatory pricing in breach of sections 27 or 36

22. We concluded that it is unlikely that Winstone's rebates result in below-cost pricing in breach sections 27 or 36.

³ Elephant's anti-dumping duty has been set at zero since 2012 (<http://www.med.govt.nz/business/trade-tariffs/pdf-docs-library/current-duties-and-completed-investigations/nz-customs-instructions-plasterboard-from-thailand.pdf>).

⁴ While not necessary to reach a final view, we considered it likely that Winstone has substantial market power (see paragraphs 62 to 64).

⁵ Contestable demand is the portion of demand that is open to competition. It is in contrast to non-contestable demand, which is demand that is committed (at least in the short-term) to a particular supplier's product. This commitment can arise for a variety of reasons, including, for example contractual commitments. In this particular case, a portion of demand is non-contestable because of limited flexibility in end-users' demand for particular brand, GIB.

23. Similarly, based on the evidence we obtained, it is unlikely that Winstone is breaching section 27 or 36 by pricing individual jobs below cost.

Our conclusion: no further action

24. The evidence does not support a conclusion that Winstone has breached the Act.
25. We acknowledge that Winstone’s market share is very high and has been for many years. This does not, however, appear to be driven by exclusive agreements with merchants, rebates offered to merchants or builders, or an anti-competitive predatory strategy.
26. Rather, as well as entrants not making sufficiently attractive offers to merchants to induce them to stock their product or for builders to request supply, it appears that Building Code compliance, combined with the preferences of those involved in designing, consenting and building houses, contribute to Winstone’s continued high market share.
27. It is outside the Commission’s functions and powers to inquire into these market features.

Our investigation

28. We commenced our investigation in August 2013 after receiving a complaint about Winstone’s rebates and pricing. We received one further complaint alleging similar concerns.
29. We interviewed and gathered information from a number of industry participants, including:
- 29.1 Winstone;
 - 29.2 all major merchants, except PlaceMakers;
 - 29.3 Knauf, Elephant and Element (Winstone’s present and past competitors);
 - 29.4 two commercial construction companies⁶ and nine national and regional residential group home builders;⁷
 - 29.5 a specialist installer;⁸
 - 29.6 BRANZ;⁹ and
 - 29.7 Christchurch City Council.

⁶ []

⁷ []

⁸ []

⁹ BRANZ is a research institute sponsored by the construction industry. BRANZ has a commercial arm which conducts independent product appraisals that form part of the product assurance framework.

Overview of the New Zealand plasterboard industry

30. Before setting out the details and findings of our investigation, we provide a brief overview of the New Zealand plasterboard industry.

Particular features of the New Zealand plasterboard market

31. Almost unique to New Zealand, plasterboard is commonly used as a structural building product in residential or other light timber-framed construction projects, providing part of the bracing equation for the building as a whole.^{10 11} In the rest of the world, plasterboard is used as a wall or ceiling lining product and must only support its own weight and that of any insulation or electrical products resting on it.
32. To use plasterboard as a structural component, a branded system that complies with the Building Code must be specified in the architectural plans before a council will grant building consent. The most recognised and widely used compliance certification is a BRANZ appraisal, which market participants have said can be difficult, lengthy and expensive to obtain.¹² Winstone has BRANZ appraisals for all of its products. Knauf obtained BRANZ appraisals for its bracing and wet area lining plasterboard systems (after twelve months), although it has not yet obtained certification for its fire resistant plasterboard system. Other types of plasterboard systems, such as those used in certain parts of wet areas, eg, in behind showers and bath, can also require Building Code compliance. Some building applications also require a plasterboard sheet to have multiple performance and appraisal specifications, eg, bracing and wet area combined.
33. However, BRANZ appraisals are not the only way to comply with the Building Code. Elephant, for example, does not presently have a BRANZ appraisal for its plasterboard products. Its plasterboard systems have been appraised by an independent consulting engineer and can be specified in architectural plans in compliance with the Building Code.
34. Alternatively, plasterboard that does not have a BRANZ or equivalent appraisal can be used for building projects that do not require consent, such as do-it-yourself (DIY) projects, relining older houses that do not require bracing plasterboard, or other non-structural building work.
35. Regardless of the technical regulatory environment, some builders and consumers may require BRANZ appraisals for their own purposes. For example, [] advised that it 'will only use appraised products where possible. It is too risky otherwise'.¹³

¹⁰ NZ 3604 is the standard for timber-framed buildings.

¹¹ Light steel framed buildings can also use plasterboard bracing systems.

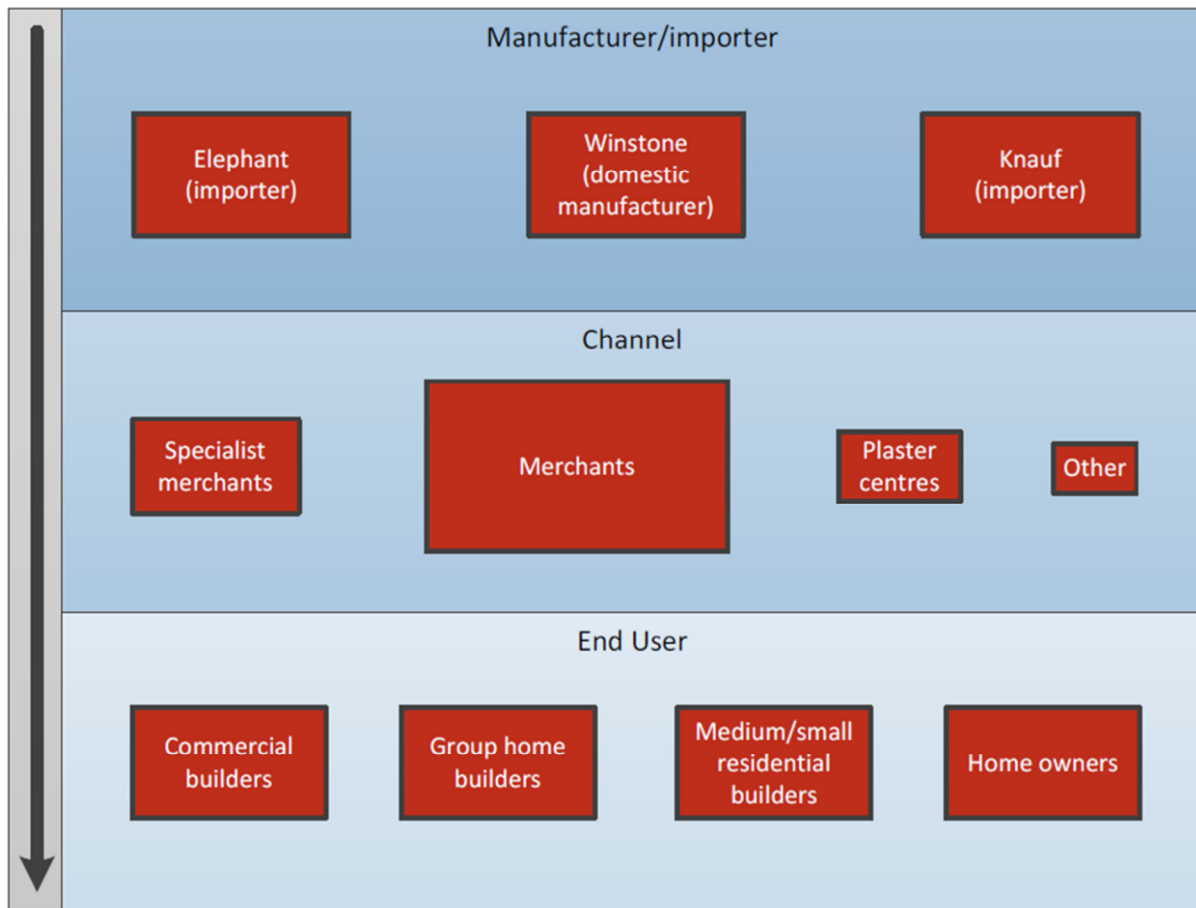
¹² [] and www.mbie.govt.nz/pdf-library/about-us/consultations/residential-construction-sector-options.pdf at page 17.

¹³ []

36. Aside from building regulations, a further but unrelated relevant historical feature of the New Zealand plasterboard market was the long-standing existence of anti-dumping duties on imported plasterboard. These duties were removed with effect from 1 June 2014. In the case of Elephant plasterboard, the anti-dumping duty rate has been at 0% since at least January 2012.¹⁴

Manufacturing/importing and wholesaling

Figure 1: Functional levels of the plasterboard market in New Zealand



37. Winstone is the only New Zealand manufacturer of plasterboard. Importers include Elephant, Knauf, and Bunnings. Since 2009 Bunnings has sold ProRoc plasterboard for its range aimed at DIY customers and those using plasterboard for non-consented building work.^{15 16 17}

¹⁴ See “Plasterboard from the Kingdom of Thailand Non-confidential New Zealand Customs Service Anti-Dumping Duty Instructions”, Ministry of Economic Development, January 1, 2014, at 1. (<http://www.med.govt.nz/business/trade-tariffs/pdf-docs-library/current-duties-and-completed-investigations/nz-customs-instructions-plasterboard-from-thailand.pdf>).

¹⁵ Bunnings has imported ProRoc directly since mid-2013.

¹⁶ ProRoc plasterboard, apart from wet area board, does not meet Building Code requirements. As such, ProRoc likely provides little constraint on plasterboard sales for end uses that require consent.

¹⁷ In addition, we are aware of some very small scale importing from Asia of alternate plasterboard by smaller independent merchants such as []. We also understand that [] is

- 37.1 Elephant is the New Zealand distributor of Elephant Board, which is manufactured in Thailand by the Siam Gypsum Company, a subsidiary of Boral Limited. Elephant has been present in the New Zealand market for over 25 years, but has never had a significant share of the market.
- 37.2 Knauf is part of Knauf Gips KG, the German multinational building products manufacturer. Knauf entered the New Zealand market in 2013, having been selected (along with Winstone) as one of the two preferred suppliers of plasterboard for the Christchurch rebuild.^{18 19} Knauf manufactures its plasterboard in Australia, and established retail centres in Auckland and Christchurch. However, the Auckland facility closed down in July 2014. Knauf can supply plasterboard direct from its distribution warehouses in Auckland and Christchurch.
38. Despite the presence of these importers, Winstone remains the largest wholesale supplier of plasterboard. It has maintained a market share of over 90% of the wholesale supply of plasterboard in New Zealand for many years.^{20 21}
39. The strength of Winstone's brand is demonstrated by the fact that in New Zealand plasterboard is predominantly referred to as 'GIB' and this has been the case for some time. []²²

Distribution

40. Plasterboard is primarily distributed through the five major building merchants with national coverage: PlaceMakers,²³ Carters,²⁴ ITM,²⁵ Bunnings²⁶ and Mitre 10.^{27 28}

currently investigating whether to enter the New Zealand plasterboard market, although we have no indication of timing.

¹⁸ Knauf acquired Element NZ on 1 July 2013. Element NZ imported the plasterboard brand British Plasterboard from Thailand between 2008 and mid-2013.

¹⁹ []

]

²⁰ []

²¹ In January 2014, David Thomas, Winstone's General Manager, was reported as saying that Winstone had a 94% market share. http://www.nzherald.co.nz/business/news/article.cfm?c_id=3&objectid=11189400

²² []

²³ There are 58 PlaceMakers stores throughout New Zealand. PlaceMakers supplies mainly to trade customers and is the number one or two merchant in that segment.

²⁴ Carters is the retail arm of Carter Holt Harvey Limited. Carters supplies mainly to trade customers and is the number one or two merchant in that segment.

²⁵ ITM is a co-operative of building merchants. ITM supplies mainly to trade customers. It has 93 stores throughout New Zealand.

²⁶ Bunnings is owned by Wesfarmers Pty Limited. Bunnings has 51 stores throughout New Zealand. Bunnings supplies mainly the DIY market segment or to smaller builders.

²⁷ Mitre 10 is a co-operative of building merchants. It has 38 Mega stores and also a number of smaller format Mitre 10 and Hammer Hardware stores. Mitre 10 supplies mainly to the DIY market segment or to smaller builders.

41. Together these five merchants account for nearly all plasterboard sales in New Zealand.²⁹ Table 1 sets out Winstone’s sales, broken down by merchant/channel for 2013.

Table 1: Winstone’s sales by merchant/channel

Merchant/channel	Share of Winstone’s total plasterboard sales (2013)
PlaceMakers	[]%
Carters	[]%
ITM	[]%
Mitre 10	[]%
Bunnings	[]%
Others	[]%
Specialist	[]%

Source: Winstone Wallboards Ltd (14 October 2013)

42. There is a distinction between whether a merchant stocks plasterboard, or merely supplies it on request (indent supply). With the exception of Bunnings (which stocks a limited range of ProRoc plasterboard), merchants do not stock plasterboard other than GIB. All major merchants provide indent supply. One merchant must give Winstone an opportunity to provide a quote if it is asked to supply another competitor’s plasterboard.

End-users

43. End-users include commercial builders, group home builders, small-to-medium sized builders and DIY customers.
44. While these end-users usually order GIB through a merchant, rather than directly from Winstone, they do sometimes have rebate agreements with Winstone. For example, Winstone’s contract with [] is characterised as a ‘loyalty agreement’³⁰ and involves Winstone paying:

44.1 [];

44.2 []; and

44.3 []³¹

45. We understand that similar rebate agreements exist with other large builders.

²⁸ The other merchant of reasonable size is Buildlink. It is a co-operative of building merchants based mainly in the North Island but also with a store in Christchurch. BuildLink sells mainly to small to medium sized trade customers.

²⁹ Winstone, for example, distributes around []% of its GIB brand plasterboard through these five building merchants.

³⁰ []

³¹ []

Winstone's supply agreements with merchants

46. Winstone has supply agreements with all major merchants. These written agreements are broadly similar to each other, in that they:
- 46.1 are [] to [] years in duration;
 - 46.2 with one exception, do not contain exclusive stocking clauses; and
 - 46.3 contain a number of different rebates agreed with the merchants, ranging from volume and growth rebates to advertising subsidies and relationship rebates that are paid periodically in lump sums.
47. Table 2 below summarises the plasterboard rebate payments made by Winstone to PlaceMakers and the other four largest independent merchants, for the year ending 30 June 2013. In aggregate, these rebates ranged from []% of total plasterboard sales or \$[] for [], to []% of total plasterboard sales or \$[] for [].

Table 2: Breakdown of rebates for plasterboard from Winstone to merchants for the year to 30 June 2013

For Year Ending June 2013	PlaceMakers	Carters	ITM	Mitre 10	Bunnings
Volume of plasterboard purchases	[
Volume rebate					
Floating Volume Rebate					
Short payment					
Growth rebate					
Advertising Subsidy					
Short Paid Advertising Subsidy					
Fixed Advertising Subsidy					
Floating Performance Rebate					
Fixed Floating Support					
Total Rebates					
Rebates as a proportion of total plasterboard purchases]

Source: Winstone Wallboards Ltd (31 October 2013)

48. Rebates as a percentage of total plasterboard purchases have not materially varied over the last four years.

Table 3: Rebates paid by Winstone for plasterboard as a percentage of merchant plasterboard revenue 2010-2013

	PlaceMakers	Carters	ITM	Mitre 10	Bunnings	BuildLink
2013	[
2012						
2011						
2010]

Source: Winstone Wallboards Ltd (31 October 2013)

Legal framework for Commerce Act issues raised

Section 27 of the Commerce Act

49. We considered whether Winstone is engaging in exclusive dealing in a way that substantially lessens competition in breach of section 27 of the Act.

Substantial lessening of competition test

50. Section 27 prohibits any person from entering into or giving effect to a provision of an arrangement that has the purpose, effect or likely effect of substantially lessening competition in a market.
51. The substantial lessening of competition test is a relative standard. It requires us to compare the likely state of competition with the alleged anti-competitive provisions in place (the factual) with the likely state of competition if those provisions were not in place (the counterfactual).
52. Importantly, the substantial lessening of competition test exists to protect the process by which rival firms compete for custom. It is not focused on protecting individual firms.³² Section 27 is designed to prevent agreements which, for example, raise barriers to entry or expansion, and are therefore likely to harm consumers. In this respect a firm with market power can breach section 27 if, but for the agreement, new competition would likely emerge.³³
53. Whether a provision has the effect of substantially lessening competition is a question of fact. An effect must follow directly from the provision without an intervening cause.³⁴
54. One hallmark of a competitive market is the extent to which participants within it possess 'market power'. Market power is the ability to profitably and sustainably raise prices above competitive levels. The substantial lessening of competition test asks whether a party's market power would increase, or be maintained, relative to what it would be without the arrangement.
55. If competition is lessened, comparing the factual to the counterfactual, we must assess whether that lessening is substantial (in other words, real or of substance).³⁵

³² *ANZCO Foods Waitara Ltd v AFFCO New Zealand Ltd* [2006] 3 NZLR 351 (CA), at [242].

³³ *Transpower v Todd Energy* [2007] NZCA 302 at [113].

³⁴ *Commerce Commission v Bay of Plenty Electricity Ltd* HC Wellington CIV-2001-485-917, 13 December 2007 at [343].

56. A 'likely' effect of substantially lessening competition means a real and substantial risk that competition will be substantially lessened. This is something more than a possibility, but does not need to be more likely than not.³⁶
57. In assessing the overall impact of an arrangement in a market, pro-competitive and anti-competitive effects arising in that same market must be considered.³⁷
58. In this case, we looked at whether one or more of the provisions of Winstone's agreements with merchants have the purpose and/or effect or likely effect of substantially lessening competition in the market for the wholesale supply of plasterboard. Our assessment takes into account the cumulative effect (or likely effect) of Winstone's agreements with all major merchants.³⁸

Exclusive supply agreements under the Commerce Act

59. Exclusive supply agreements – or exclusive dealing, as it is sometimes known – are not unlawful under the Act. Only exclusive supply agreements that have the purpose, effect, or likely effect or substantially lessening competition in a market (or which amount to a taking advantage of market power) are unlawful.³⁹
60. We recognise that any exclusive supply agreement between a supplier and a customer necessarily prevents another supplier from supplying the customer. However, that alone is not sufficient for a finding that competition has been or is likely to be substantially lessened. Whether, in fact, an exclusive supply agreement has the purpose, effect, or likely effect of substantially lessening competition depends on the circumstances of each case. In particular, it depends on whether an exclusive supply agreement prevents or hinders a rival supplier from being an effective competitor by limiting their ability to enter, expand, or to otherwise be a cost-effective competitor in the market.⁴⁰

Section 36 of the Commerce Act

61. We considered the rebate predation and targeted predation scenarios under section 36. Section 36 of the Act prohibits a person that has a substantial degree of market power from taking advantage of that market power for the purposes of:

³⁵ A lessening of competition includes hindering or preventing competition (s 3(2), Commerce Act).

³⁶ *Port Nelson v Commerce Commission* (CA) above n 31 at [562-563].

³⁷ *Fisher & Paykel v Commerce Commission*, [1990] 2 NZLR 731, (HC) at 740. *Commerce Commission v Port Nelson* (HC) above n 25 at 433; *Shell (Petroleum Mining) Company Ltd v Kapuni Gas Contracts Ltd*, (1997) 7 TCLR 463 (HC), at [531].

³⁸ And builders, s 3(5) of the Act.

³⁹ Exclusive supply agreements are a common feature of many markets and are undertaken by firms with and without market power. This makes it very difficult to show that any exclusive supply agreement breaches s 36 of the Act.

⁴⁰ Although decided some time ago, the High Court's decision in *Fisher & Paykel* [1990] 2 NZLR 731 illustrates that exclusive dealing provisions must be assessed on their facts. That case centred on whether Fisher & Paykel's – which at time manufactured about 75% of New Zealand's whitegoods – exclusive dealing clause with retailers substantially lessened competition. The Court found the clauses did not substantially lessen competition on the basis that the clauses did not foreclose significant retail space, particularly given the agreement of which that clause formed part could be terminated on 90 days' notice by the retailer.

- 61.1 restricting the entry of a person into a market;
- 61.2 preventing or deterring a person from engaging in competitive conduct; or
- 61.3 eliminating a person from a market.

Substantial degree of market power

- 62. A firm's size and financial resources do not provide it with substantial market power.⁴¹ Rather, a business has market power when it is not constrained in the way in which it would be constrained in a competitive market.
- 63. In this case, if we do not consider Winstone to be substantially constrained by competitive pressures in the plasterboard market, then it will have a significant degree of market power.⁴²
- 64. While we do not find it necessary to reach a final view, we consider it likely that Winstone has a substantial degree of market power. As such, we focus instead on whether Winstone has taken advantage of any substantial market power it may possess through its pricing practices.

Anti-competitive purpose

- 65. In terms of purpose, it is the purpose of the person with market power (ie, Winstone) that is relevant. Purpose may be indirectly inferred from relevant conduct or circumstances, such as contemporaneous documents,⁴³ or directly inferred from evidence of a business taking advantage of its market power.⁴⁴

Taking advantage of market power and predatory pricing under section 36 of the Commerce Act

- 66. A business takes advantage of its substantial degree of market power when, as a matter of practical business or commercial judgement, it would not have engaged in the conduct if it did not have that market power. This is known as the counterfactual or comparative assessment that has been required by the courts.⁴⁵
- 67. Both the rebate predation and targeted predation scenarios involve complaints that Winstone is pricing 'too low'.
- 68. Competition law is slower to interfere with businesses lowering prices (whether by rebates or otherwise) than with increasing prices. A business offering lower prices is usually indicative of competitive conduct. While low prices can harm competitors, it

⁴¹ *Boral Messer Masonry Limited v Australian Competition and Consumer Commission* [2003] 195 ALR 609.

⁴² *Commerce Commission v Telecom Corporation of New Zealand Limited* [2010] NZSC 111 (0867) at [33].

⁴³ Section 36B, Commerce Act and *Union Shipping NZ Ltd v Port Nelson Ltd* [1990] 2 NZLR 662 (HC) at 709.

⁴⁴ *Telecom Corporation of New Zealand Ltd v Clear Communications Ltd* [1995] 1 NZLR 385 (PC).

⁴⁵ *Commerce Commission v Telecom Corporation of New Zealand Ltd* [2010] NZSC 111, at [34]-[35].

is when those prices render competitors less competitively effective (ie, when they are predatory) that there is likely to be harm to the competitive process.⁴⁶

69. In terms of section 36, predatory pricing is pricing that is below cost – usually taken to be avoidable costs (ie, the costs that Winstone avoids if it does not produce the products in question),⁴⁷ – and that pricing makes sense because of the firm’s substantial market power. For example, in some cases, the firm with market power will subsequently increase prices after driving out a rival to recoup its losses.

Does Winstone have exclusive agreements with merchants that substantially lessen competition?

70. Winstone’s written agreements with three major merchants do not include an express requirement that they only stock GIB. Nor does it appear that Winstone has entered into oral variations of those agreements, or other understandings or arrangements with merchants that require merchants to purchase exclusively from Winstone.
71. The lack of an exclusivity requirement is consistent with some market behaviour. Bunnings stocks imported ProRoc plasterboard in addition to GIB. However, we recognise that ProRoc plasterboard’s uses can be more limited than those of GIB.
72. One merchant has an agreement with Winstone that requires it not to stock or promote alternate brands.
73. However, this agreement by itself is unlikely to breach section 27. This is because it is unlikely to prevent a rival plasterboard supplier from being able to enter or expand in the market. A rival supplier can still have its product stocked by three other major merchants (about []% to []% of the market in total).
74. In addition, all major merchants are able to indent supply other plasterboard brands. The agreement referred to in paragraph 72 above also requires that particular merchant to actively promote GIB if a customer requests an alternative product, and to only supply the competing product after having done so. Further, if the merchant has not been able to convince the customer to switch to GIB, the merchant must tell Winstone so it can follow up with the customer.
75. As a result, this merchant can only supply competing plasterboard to a customer in confined circumstances, which may result in exclusivity. However, this merchant was able to supply about \$[] of Elephant plasterboard in the year to 30 June 2013.⁴⁸

⁴⁶ The Privy Council considered predatory pricing in *Carter Holt Harvey Building Products Group Limited v Commerce Commission* [2004] 11 TCLR PC. This case followed the majority judgment of the High Court of Australia in *Boral Messer Masonry Limited v Australian Competition and Consumer Commission* [2003] 195 ALR 609.

⁴⁷ See Baumol (1996), Predation and the Logic of the Average Variable Cost Test, *Journal of Law and Economics* 49. This cost measure is consistent with the judgment in *Telecom Corp of NZ Ltd v Clear Communications Ltd* [1995] 1 NZLR 138 regarding access pricing.

⁴⁸ []

Do Winstone's rebates have the effect or purpose of substantially lessening competition?

76. The rebate provisions contained in Winstone's agreements with its merchants would breach section 27 if they had the purpose, effect, or likely effect of substantially lessening competition in the plasterboard market (or any other market).
77. As has already been outlined in this report, Winstone has a very large market share and its competitors have struggled to expand in the market. While three major merchants are not required to exclusively stock GIB, the reality is that, with the exception of Bunnings, all these merchants only stock GIB. In addition, merchants largely only supply GIB as well. The share of the market accounted for by indent supply of alternative plasterboard is unlikely to be greater than []%.⁴⁹
78. We therefore considered whether rebates have allowed Winstone to increase or maintain its market power by inducing exclusivity or near exclusivity, and, as a result, hindering or preventing other competitors from expanding in the plasterboard market.
79. For the reasons we explain, we consider the evidence does not demonstrate that Winstone's rebates are preventing rival plasterboard manufacturers from entering and expanding in the market. Rather, we consider there are other features of the market preventing competing plasterboard suppliers from gaining traction.

How can rebates substantially lessen competition?

80. As a starting point, we would not expect merchants to agree to rebates that limit their choice of supplier and increase their costs. However, there may be circumstances where merchants may nonetheless agree to such arrangements.
81. These circumstances could play out in the following way:
- 81.1 Supplier, 'A', is better off if it can prevent effective entry or expansion by a rival, therefore maintaining or increasing its market power and earning higher profits;
- 81.2 merchants, however, would be worse off unless A provides them with a way to benefit from less competition;
- 81.3 A achieves higher profits through exclusion by offering rebates that are conditional on enough merchants⁵⁰ purchasing a certain portion of their requirements in a given period from A.⁵¹ The merchant is willing to agree to

⁴⁹ This is based on Winstone's own recent assessment of total market share of 94% (see footnote 21), combined with an understanding Winstone sells strictly through merchants, while other plasterboard suppliers do not. In October 2013, Winstone estimated sales by competing plasterboard suppliers through the merchant channel to be about []% [].

⁵⁰ Such merchants must collectively have market power in their own markets. Otherwise an entrant could simply by-pass them and gain entry to the market through other merchants.

⁵¹ These rebates may be explicitly contingent on a certain percentage of the merchant's requirements over a set period being from A, eg, a 10% rebate if at least 80% of annual requirements are purchased from

this because the payments are ‘fixed’ (ie, lump sum payments made at regular or semi-regular intervals) and fixed payments are less likely to be passed through to customers than wholesale price decreases;⁵²

- 81.4 this incentivises merchants to remain with A even if a new entrant offers a lower wholesale price (as measured on an equivalent quality/service basis), equivalent (or even better) rebates or a better quality product, because the merchants fear that new entry will result in lower wholesale prices and reduce merchant profits; and
- 81.5 rival plasterboard manufacturers are therefore foreclosed or almost foreclosed from the merchant channel, rendering them less competitively effective.
82. We investigated whether Winstone’s rebates have incentivised merchants not to support new entry in this way.
83. In doing so, we have primarily focussed on the effect of the rebates. This is because, in terms of the purpose element in section 27, in this case, the rebate provisions provide little clue as to whether Winstone’s intention is to substantially lessen competition or not. We have therefore inferred purpose from the way the rebates operate in practice, as well as how market participants viewed them.

Have the rebates had the effect of substantially lessening competition?

84. In summary, we consider that the evidence does not demonstrate that the rebates are preventing rival plasterboard manufacturers from entering and expanding in the market. Rather, there are other features of the market contributing to competing suppliers struggling to expand in the market.

Evidence that the rebates might be anti-competitive

85. There are a number of features that need to be present for a rebate to be anti-competitive. Most particularly, in this case, we would expect to see merchants retaining rebates as a share of the profits from the agreement, rather than competing them away to end users in the form of lower prices.
86. However, there is no clear evidence that merchants are retaining rebates or passing them on to their customers. Some merchants advised us that rebates are not passed

supplier A. Alternatively, they may take the guise of a volume rebate, where the volume thresholds are targeted at a particular merchant’s usual requirements, eg, a 10% rebate if at least 80 units are purchased from supplier A in a year given an understanding that 100 units are normally purchased in a year.

⁵² Firms are generally less inclined to pass through fixed payments for three reasons. First, fixed payments are typically received at the end of a fixed period, say at the end of the year or quarter, ie, after the product has been sold. Second, the size of the payment is often uncertain, depending on a variety of factors, including the volume of product sold, as well as the portion of requirements accounted for by the brand in question. Third, the payment may be earmarked by either the supplier or the retailer for a particular use, such as advertising.

onto customers.⁵³ Those merchants advised that these retained rebates are distributed to individual stores on a pro rata basis, according to sales of GIB, while others advised that they use the rebates for head office funding and marketing (although often in lieu of stores or franchisees having to directly fund these head offices).⁵⁴

87. Other evidence suggests that rebates may, in fact, be passed through to customers more generally.

87.1 Two merchants advised that discounts are offered to some customers based on annual spend.⁵⁵

87.2 Another advised that it has a loyalty programme spread across all products which enables customers to accrue points that they can exchange for rewards.⁵⁶

88. Further, the evidence suggests that merchant margins⁵⁷ on plasterboard are in line with margins merchants earn on other building materials. Although not determinative, this evidence does not support a finding that plasterboard rebates are retained by merchants – bearing in mind that the margins on other building products may or may not be good proxies for the plasterboard market.

89. We therefore do not find the evidence on the question of pass-through sufficiently compelling to conclude that rebates are likely to form (in part or in whole) a payment to merchants to exclusively or nearly exclusively stock and/or supply GIB.

90. We also considered the form of the rebates. As noted at paragraph 46, there are a range of rebates. The evidence relating to what these rebates are contingent on and whether they had a ‘loyalty’ element is not always clear. This is particularly the case for “relationship rebates”, as well as some marketing and promotion payments, in that not all agreements articulate the degree of support required to maintain these rebates.⁵⁸ The volume rebates also [

was inconclusive.]⁵⁹ Again, the evidence on this

⁵³ [], [] and [].

⁵⁴ [] and [].

⁵⁵ []

⁵⁶ []

⁵⁷ Calculated after rebates have been accounted for.

⁵⁸ []

⁵⁹ []

91. Given the evidence of pass-through for rebates is not sufficient to find a breach of section 27, we go on to consider the evidence on the effect rebates may be having on merchants’ stocking decisions.

Are Winstone’s rebates driving, or materially influencing, merchants’ decisions not to stock non-GIB plasterboard?

92. The evidence we obtained suggested that three major merchants are generally willing to dual-stock. The reason these merchants have not done so is that alternative suppliers have not offered a sufficiently compelling price point that would compensate the merchants for the inventory risk they would incur from stocking a bulky product with little and uncertain demand.

93. Being stocked by a merchant is important for a plasterboard manufacturer. There is some evidence that not being stocked by merchants decreases the attractiveness of plasterboard to builders. For example, we were told that some merchant stores will not accept returned plasterboard unless the brand is already stocked in that store.⁶⁰ In addition, not being stocked in store means that Winstone’s competitors cannot advertise at the point of sale and customers may not necessarily know that a competing product is available. Technical manuals, which are important where plasterboard is being used as a bracing system, may also not be available.

94. With the exception of Bunnings, no merchant stocks plasterboard other than GIB. However, in our view, there is insufficient evidence to support a conclusion that rebates are causing merchants not to dual-stock.

95. The evidence suggests that merchants would consider dual-stocking under the right circumstance⁶¹ and that they do not believe their rebates would be at risk.

95.1 No merchants believe that their rebates would be significantly compromised through increased sales of alternative plasterboard brands, other than via the natural decreases in aggregate volume rebates that may arise from lower sales of the rebated product.⁶² In addition, competing plasterboard manufacturers also offer discounts, which may partially mitigate any lost Winstone rebates.⁶³

95.2 Nor do merchants consider that a [] to earn those rebates. While Winstone’s volume rebates [], our evidence is that []. For example, [].

⁶⁰ []

⁶¹ With the exception of [].

⁶² Significant stocking of alternative brands has not occurred. Therefore, irrespective of merchant expectations, it is possible that Winstone's responses could escalate if they perceive more of a competitive threat.

⁶³ For example, [].

- 95.3 No merchants believe that the existence of rebates has impeded their ability to pursue stocking agreements with competing plasterboard brands. Most merchants have explored dual-stocking agreements with alternative plasterboard suppliers. While these negotiations were generally unsuccessful, merchants asserted that failures were based on logistical concerns or perceived deficiencies in service, quality, or price, rather than the risk of lost Winstone's rebates.
96. However, merchants (with the exception of Bunnings) do not in fact dual stock. It appears the main reason for this is because stocking plasterboard carries with it considerable inventory risk and that alternative plasterboard suppliers have not offered a sufficiently compelling price point to compensate them for that risk.
97. In regard to the inventory risk, we consider that:
- 97.1 plasterboard is a bulky, fragile product that is difficult to transport and takes up a significant amount of space. Without sufficient existing demand for alternative products, merchants are not generally willing to put limited shelf space aside to stock them. Doing so leaves less space for other, better-selling products.⁶⁴
- 97.2 demand for alternative plasterboard is generally low and also uncertain because it is largely driven by the specifications of architects and customers, rather than merchant stocking decisions. As such, while merchants have some influence over the type of plasterboard sold (which is consistent with suppliers preferring their product be stocked by merchants), they are limited in the extent to which they can drive the sales of a slow moving plasterboard product.
- 97.3 Knauf's product has features that increase the inventory risk for a merchant stocking it:
- 97.3.1 Knauf's plasterboard has serrated rather than taped board ends. While this is standard in the Australian market, other plasterboard sold in New Zealand has taped board ends which improve presentation and help the product avoid damage in storage, delivery and from onsite movements.
- 97.3.2 Knauf requires longer notice for deliveries, and makes those deliveries less frequently than Winstone, which offers next-day delivery anywhere in New Zealand.

⁶⁴ A lot of plasterboard ordered through merchants is actually delivered directly from the supplier to the construction site. As such, there is even less incentive for merchants to maintain a significant stock of plasterboard in-store.

98. Given this risk, any entrant would have to offer merchants a sufficiently compelling price point to merchants to compensate them for the risk associated with stocking. Such a price point is independent of any rebate since, as noted at paragraph 93, it does not appear that merchants’ rebates from Winstone are at risk if they dual stock. We are of the view that alternative suppliers did not offer such a price point.

98.1 In July 2013 Knauf acquired another plasterboard distributor, Element, which at the time was supplying imported ‘ProRoc’ plasterboard to Bunnings. Bunnings subsequently decided to source ProRoc directly []⁶⁵.

98.2 In and around January 2014, one merchant entered into negotiations to stock Knauf plasterboard. The negotiations also included terms for indent supply. The merchant indicated that [] but this was not sufficient to compensate the merchant for Knauf not having an adequate delivery platform, no technical support in New Zealand, lack of adequate specification and insufficient coverage to fix problems immediately.⁶⁶

98.3 One merchant did not consider there was much price difference between Elephant and Winstone plasterboard.⁶⁷

99. On this basis, we could not conclude that the rebates were a significant reason for merchants not to dual-stock (or, in the case of Bunnings, to dual-stock a particular type of plasterboard).

100. Even though merchants do not dual stock, it is also relevant that major merchants supply competitors’ products on request (although, as outlined at paragraphs 74 to 75 above, one major merchant’s indent supply is on a much more constrained basis). The builders we interviewed all confirmed that they are able to source alternative plasterboard brands as needed. If a builder’s favoured merchant does not carry the appropriate brand, or cannot source it, the builder will go elsewhere. That said, the reality is that there is very little indent supply on the part of any of the merchants.

101. In the next section we explore why this may be the case. Particularly since the question of the right price point is likely to be less relevant in regard to indent supply since at that point the decision to purchase the product would have already been made. In that context, we also consider whether rebates to builders have played a role in the limited demand for alternative plasterboard.

Other reasons why existing competitors have had difficulty winning market share

102. There are reasons, beyond Winstone’s rebates, which explain the difficulties competitors have had in expanding in the plasterboard market. These reasons include the structural impediments in New Zealand we have already identified in the

⁶⁵ []

⁶⁶ []

⁶⁷ []

plasterboard market. We consider these reasons for each of the relevant suppliers, as well as in general.

Elephant

103. We consider there are a number of potential causes of Elephant’s inability to gain traction in the market.

103.1 Elephant has experienced difficulties in getting its products accepted by architects, builders, and (until recently) councils. In particular, Elephant's BRANZ certification, which it received in 2008, was revoked in 2011.⁶⁸ Since 2011, Elephant has used a consulting engineer's appraisal for its performance applications, so that it can meet the Building Code and achieve council consent. While losing its BRANZ appraisal was not critical, Elephant's market share fell from approximately []% to []%.

103.2 It has been suggested that Elephant has not been able to win market share, due to predatory pricing by Winstone. One Elephant sales representative advised that [].⁶⁹ However, as discussed in the next section, we do not consider that the evidence before us supports a finding of predatory pricing by Winstone, as opposed to aggressive (but legal) price competition.

Knauf

104. Although Knauf is a multinational plasterboard supplier successfully operating in 60 countries worldwide, a number of compounding factors appear to have impeded its ability to grow in the New Zealand market.⁷⁰

104.1 It took twelve months for BRANZ to approve Knauf’s plasterboard products.

104.2 For a time Knauf had issues with getting its plasterboard systems approved by some councils;⁷¹ even in cases where it had the appropriate BRANZ appraisals. Knauf said there were sometimes extra consent costs such as engineers’ fees when customers wanted to switch away from a GIB bracing system in particular.⁷²

104.3 Although it already distributed another, complementary, building product in New Zealand (insulation), Knauf established a separate distribution system

⁶⁸ [] []

⁶⁹ []
⁷⁰ []

⁷¹ [] and www.mbie.govt.nz/pdf-library/about-us/consultations/residential-construction-sector-options.pdt page 17.

⁷² []

for plasterboard, involving separate staff, warehousing, deliveries and retail locations.⁷³

104.4 Knauf provides its Australian hard copy technical manual to end users. Although these manuals are widely used by specifiers and builders, a large portion of the content ([]%) in Knauf's manual is apparently inapplicable to New Zealand.⁷⁴ In comparison there is an extensive GIB manual available and in wide use.

104.5 Knauf set up its own dedicated plasterboard sales outlets in Auckland and Christchurch, which may have impeded its ability to negotiate product placement with major merchants as these centres were effectively in competition with the merchant channel.

104.6 []⁷⁵

104.7 As noted at paragraph 97.3, Knauf's plasterboard has different product features to Winstone's and longer delivery notice requirements.

105. We note, however, that while Knauf is currently reviewing its operations in New Zealand, it appears to have made some recent progress.

105.1 If Knauf completes more BRANZ testing and appraisals it would have a complete suite of BRANZ appraised products with which to challenge Winstone.

105.2 Knauf told us that it has begun to see 'spontaneous specification' of its products by architects and builders. This has led to increased profile and the potential for higher sales.⁷⁶

105.3 While Knauf no longer believes that its initial forecasts of a []% to []% market share are likely, it is of the opinion that a []% to []% market share is plausible by the middle of next year.⁷⁷

106. That said, there is speculation that Knauf may be scaling down its New Zealand operations. Given what end users require from a plasterboard supplier, this could be negatively affecting sales and other opportunities. []

⁷³ []
⁷⁴ []
⁷⁵ []
⁷⁶ []
⁷⁷ []

]78

Other structural impediments

107. The difficulties these competitors faced with expansion have also been compounded by the structural features of the New Zealand market. As outlined above, Knauf and Elephant struggled with some councils’ reluctance to give consent to building works that use non-GIB plasterboard, even where that plasterboard had a BRANZ or other compliant form of appraisal.⁷⁹ This was compounded by the fact that Winstone and GIB have a long history in New Zealand, and the product has become very familiar to designers, specifiers and regulatory authorities.⁸⁰

108. For example, [] advised that:

... some councils/individuals treat Winstone’s manual [technical installation manual] as part of the Building Code, rather than what it is: a technical manual. There is widespread inconsistency... In part, this seems to be an issue with the quality of [council] staff, with many staff being inexperienced.⁸¹

109. We were told that GIB is often specifically named on plans for projects. This can create issues if a builder/installer wishes to switch to alternative products.⁸² [] advised that:

... [h]aving to deal with council to change is a hassle and cost; not everyone would think it is worth ‘rocking the boat’. Changing the plans to use something other than GIB could delay whole project and therefore be risky and expensive.⁸³

110. Such conduct is likely to have held back the growth of competing plasterboard manufacturers. However, we have been told that there has been recent activity to inform councils about the compliance requirements under the Building Code.⁸⁴ This appears to have led to improvement in the process for assessing Building Code compliance.⁸⁵

78 []

79 []

80 MBIE’s Residential Construction Sector Market Study examined these types of issues in regulatory framework and related areas.⁸⁰

81 []

82 []

83 []

84 []

85 []

Rebates to builders

111. We also considered whether plasterboard rebates paid by Winstone to builders could, of themselves, have the purpose or effect of inducing exclusivity from builders in breach of section 27 of the Act. Based on the evidence before us, however, we do not consider that these rebates are having an anticompetitive effect, or at least not one of a material kind. Builder rebates for plasterboard are much smaller (on a pro rata basis) than the rebates paid to merchants, suggesting that any loyalty effect may also be smaller.

112. Also, as already noted, builders confirmed that they are able to source alternative plasterboard brands as needed and we obtained examples of this. Such examples exist for both builders who receive rebates from Winstone and those who do not.

112.1 []⁸⁶

112.2 []⁸⁷

113. While most builders only use GIB, it was unclear whether this was causally related to a rebate agreement or the builder’s own preference (or another factor).

Conclusion on whether the rebates substantially lessen competition

114. Our evidence does not suggest that Winstone’s rebates have an exclusionary effect in breach of section 27. We consider that Winstone’s rebate agreements with merchants and builders incentivise merchants to increase sales of Winstone’s plasterboard, and builders to use it. Further, that Knauf and Elephant have been limited in their expansion by high barriers to entry against a strong incumbent.

115. However, without evidence that the rebate agreements have an anticompetitive purpose, have prevented or significantly impeded competition by Elephant and Knauf, or have been retained as supra-competitive profits by merchants, we cannot establish that Winstone's rebate agreements with merchants have resulted in the exclusion of potential competitors.

116. While competitors to Winstone have not been particularly successful, their lack of success can be contributed to a number of factors unrelated to rebates. As such, we do not believe that Winstone's rebate agreements have resulted in a substantial lessening of competition.

⁸⁶ []
⁸⁷ []

Is Winstone taking advantage of its substantial market power for an anti-competitive purpose?

117. It would be difficult to establish that the rebates Winstone pays to merchants breach section 36. As set out above, to be in breach of section 36, a firm with substantial market power must act in a way that it could not if it were in a competitive market.
118. Given that rebates are also found in competitive markets, it is difficult on that basis alone to distinguish between rebates that raise competition concerns and those that do not. We would not therefore be able to establish a breach of section 36 on the basis of the counterfactual test.

Has Winstone engaged in predatory pricing in breach of sections 27 or 36?

119. To assess whether Winstone is engaging in predatory pricing, we have considered whether Winstone has been pricing below avoidable costs in either the rebate predation or the targeted predation scenario.

Winstone's avoidable costs

120. Assessing whether Winstone's prices are below its avoidable costs requires us to estimate the prices merchants actually pay Winstone, taking into account both rebates and Winstone's avoidable costs.
121. We used the same avoidable cost estimate in both the rebate predation scenario and the targeted predation scenario. We did not complete a detailed forensic review of Winstone's costs. Rather, we used what we consider would be an upper bound estimate of Winstone's avoidable costs based on its available accounts.⁸⁸

Rebate predation scenario

122. Winstone pays rebates to merchants to help convince them to buy GIB, rather than other brands. The result of the rebates is that merchants will end up paying lower effective prices; indeed, Winstone's effective price is the price paid by the merchant for plasterboard, taking account of rebates.
123. The question is whether Winstone's effective prices are predatory and, if so, whether they breach sections 36 or 27 of the Act. More specifically, our concern is ensuring that Winstone's rebates do not result in prices that foreclose competition, ie, that have a substantial anti-competitive effect.
124. However, our analysis has to take into account the fact that there is evidence that some end-users will always use GIB, and will not consider alternative brands.
125. This makes applying the counterfactual test required for section 36 difficult. Winstone's market power is likely to be the very reason it has a portion of volumes which are 'non-contestable'. Nevertheless, when applying the counterfactual test, it appears that a firm, acting rationally, would offer loyalty rebates in the way

⁸⁸ We have used Winstone's 2013 Annual Report for this analysis.

Winstone does if it did not have substantial market power (ie, if it did not have the non-contestable share).

126. In fact, as outlined above, loyalty rebates are common in competitive markets. We have therefore not considered the application of section 36 further but focussed on whether Winstone's effective prices breach section 27.

Our approach: working out price by applying the rebates only to the contestable share

127. We have applied rebates only to those additional sales which Winstone wins or retains (or could win or retain) as a result of the rebate – which we call the 'contestable share'. This approach provides a high water mark for predatory anti-competitive conduct.

Size of the contestable share

128. The contestable share is the volume of plasterboard purchases which one plasterboard supplier could realistically capture from another in the short term.
129. Importantly, the contestable share is not the same as the current market share of the participants. In particular, the contestable share includes the amount of plasterboard that a merchant currently purchases from Winstone but could otherwise purchase from Knauf or Elephant (absent any rebates effect).
130. Assessing the likely contestable share is challenging and estimates will necessarily be uncertain. But as a general rule, the larger the contestable share, the less likely it is that the loyalty rebates would lead to below-cost pricing. This is because the rebates would be attributed to a larger volume of sales.
131. Our best estimate is that across the market the contestable share would likely be at least []%, but not more than []%. The evidence we have relied on in reaching this conclusion is:
- 131.1 Winstone's GIB brand appears to be preferred brand of builders and specifiers and its share is about 94% of the market according to Winstone;⁸⁹
- 131.2 Elephant has previously captured up to []% of the market;
- 131.3 Knauf is aiming for a [] to []% market share but would be happy with [] to []%. Knauf's investment in entering the New Zealand market reveals its views that the contestable share of the market must be at least []%, otherwise it is unlikely to have entered; and
- 131.4 about []% of Bunnings' plasterboard purchases are not GIB.⁹⁰
132. Despite our views, given the uncertainties over the size of the contestable share, we have used a range of contestable share amounts in our analysis.

⁸⁹ See footnote 21.

⁹⁰ []

Level of rebates

133. Although merchants advised that they would need to sell a ‘significant’ amount of rival plasterboard products before their rebates would be affected, it is difficult to determine the exact amount of rebate a merchant would lose if it switched away from Winstone. Many of the conditions that attach to rebates are unclear. A change in merchants’ support for Winstone would also likely impact on future rebate negotiations.
134. While there are two available approaches to modelling rebates,⁹¹ we have used the more conservative approach of including all fixed rebates in our modelling.

The results of our effective price versus avoidable cost analysis

135. Based on these assumptions – contestable share approach, contestable share between [] to []%, upper bound estimate of rebates lost and upper bound estimate of avoidable costs used – Winstone’s effective average prices do not fall below costs, including the rebates paid to merchants.
136. The only modelled scenarios where Winstone’s prices fall below costs are where the contestable share is less than []% for three of the four merchants. (**Attachment A** sets out our merchant-by-merchant analysis.)
137. However, even then, that conclusion is very cautious, considering the assumptions around the level of avoidable costs and the extent of rebates that would be lost.
138. We therefore consider that Winstone’s effective prices are likely to exceed its avoidable costs. Winstone’s loyalty rebates and the resulting effective prices are unlikely to foreclose entry or expansion; that is, they are unlikely to have the purpose, effect, or likely effect of substantially lessening competition.

Targeted predation scenario

139. The presence of targeted predation is usually only problematic when it allows a firm to maintain market power. That is, a firm is able to foreclose the market by pricing below cost when facing competition from a rival plasterboard manufacturer for individual jobs. In these instances, Winstone would have to drop its prices for those jobs so significantly that its revenue (taking rebates into account) falls below cost with the aim to drive out competition, allowing Winstone to maintain high returns on other, including future, jobs.
140. We were told that when Winstone faces a quote from a competing plasterboard manufacturer/importer, it reduces its prices by up to []%.

⁹¹ The first is to model volume-related rebates only. These are rebates where merchants lose only the proportion of volume rebates that they would be otherwise entitled to if they purchased the contestable share from the incumbent. The second is to model all additional ‘fixed’ rebates, including relationship and advertising rebates as well as volume-related rebates. This latter approach may include more rebates than it should as it is unclear whether a merchant would lose all of the ‘fixed rebates’ from Winstone if it shifted only a small proportion to another supplier.

141. However, based on our analysis, a []% reduction in Winstone’s plasterboard price would still see Winstone’s prices above its avoidable costs.⁹²
142. We therefore asked both Elephant and Knauf for examples of Winstone responding to competition by dropping its wholesale prices.⁹³
- 142.1 Elephant provided [] specific quotes where Winstone had bettered Elephant’s price. Winstone provided us with wholesale quotes for those jobs. Elephant also provided some information from one of their sales representatives, []].
- 142.2 Knauf provided [] quotes where Winstone was said to have lowered its wholesale price to beat Knauf’s price. We asked Winstone to provide its corresponding wholesale prices for those quotes. Winstone could identify and provide nine matched quotes, and we used these in our analysis.
143. Of the twelve specific quotes provided to us where we had a matching Winstone quote, we identified one job (Customer C) where Winstone’s prices were below our high water mark calculation of Winstone’s avoidable cost.

Table 4: Analysis of individual pricing – [] identified customers

Customer	Winstone quote for (standard GIB 10mm)	Winstone’s average avoidable costs	Price above/below avoidable cost
Customer A ([])	[]	[]	Above
Customer B ([])	[]	[]	Above
Customer C ([])	[]	[]	Below
Customer D ([])	[]	[]	Above
Customer E ([])	[]	[]	Above
Customer F ([])	[]	[]	Above
Customer G ([])	[]	[]	Above
Customer H ([])	[]	[]	Above
Customer I ([])	[]	[]	Above

⁹² Our analysis shows only one instance where Winstone priced at []% or more below competitors. This is (Customer C) in Table 4.

⁹³ []

Table 5: Analysis of individual pricing – [] identified customers

Customer	Winstone quote (standard GIB 10mm)	Winstone's average avoidable costs	Price above/below avoidable cost
Customer J ([])	[]	[]	Above
Customer K ([])	[]	[]	Above
Customer L ([])	[]	[]	Above

144. However, the instance where Winstone's wholesale price was below the high watermark avoidable cost does not, in our view, amount to evidence of a targeted predation strategy. This is particularly so given this customer was a charity and [] bid to supply that customer also appears to have been very low compared to its other quotes.
145. We have also not been provided with evidence to support suggestions that Winstone has dropped its prices by 50% or given away plasterboard on individual jobs.
146. Given the one instance of below cost pricing was in unusual circumstances, we do not consider it likely that Winstone is engaging in targeted predation. Therefore, we have not analysed whether Winstone has been able to foreclose the market by adopting such a strategy.

Our conclusion

147. The evidence does not support a conclusion that Winstone has breached the Act.
148. We acknowledge that Winstone's market share is very high and has been so for many years. This does not, however, appear to be driven by exclusive agreements with merchants, rebates offered to merchants or builders, or an anti-competitive predatory strategy.
149. Rather, as well as entrants not making sufficiently attractive offers to merchants to induce them to stock their product or for builders to request supply, it appears that Building Code compliance (for plasterboard products that are used for bracing), combined with the preferences of those involved in designing, consenting and building houses, contribute to Winstone's continued high market share.
150. It is outside the Commission's functions and powers to inquire into these market features.

Attachment A: Predation quantitative assessment of below cost pricing

1. This attachment sets out the merchant-by-merchant analysis whether Winstone has priced below cost, taking into account its rebates. The main conclusions of this analysis and our methodology are explained in paragraphs 122 to 138 above.
2. For each merchant, we have modelled two scenarios of lost rebates, namely:
 - 2.1 the merchant loses Winstone volume rebates commensurate with any decrease in share of purchase (the low lost rebates scenario); and
 - 2.2 the merchant loses Winstone volume rebates commensurate with any decrease in share of purchase and the merchant loses all marketing and trade rebates (which we assume are lost as soon as its loyalty to Winstone diminishes) (the high lost rebate scenario).

Bunnings

3. Winstone's rebates to Bunnings are [].
4. For Bunnings, we consider the high lost rebate scenario is unlikely as Bunnings already buys about []% of its plasterboard needs from other suppliers, but still receives these marketing rebates.
5. The required prices that an entrant would need to offer Bunnings to compensate it for lost rebates are shown for a range of contestable shares in Figure 2.⁹⁴ From Figure 2, we can see that:
 - 5.1 in the low lost rebate scenario, the entrant's required price does not fall below Winstone's avoidable costs for any share; and
 - 5.2 in the high lost rebate scenario (which we consider unlikely), the entrant's required price is below Winstone's avoidable costs when the contestable share is below []%.

Figure 2: Entrant's required price to Bunnings for a given share of purchases⁹⁵

[]

ITM

6. The required prices that an entrant would need to offer ITM so as to compensate it for lost rebates are shown for a range of contestable shares in Figure 3.
7. ITM receives [] relationship rebate from Winstone, []. However, it is unclear whether ITM would

⁹⁴ This analysis assumes that a merchant would be able to achieve the same retail price for the entrant's product (ie, that additional competition would not lead to lower downstream retail prices).

⁹⁵ []

lose all of its relationship and advertising rebates should it switch some of its purchases to an entrant. [].

8. From Figure 3, we can see that:
 - 8.1 in the low lost rebate scenario, the entrant's required price does not fall below Winstone's avoidable costs for any share; and
 - 8.2 in the high lost rebate scenario, the entrant's required price is below Winstone's avoidable costs when the contestable share is below []%.

Figure 3: Entrant's required price to ITM for a given share of purchases
[]

Mitre 10

9. The required prices that an entrant would need to offer Mitre 10 so as to compensate it for lost rebates are shown for a range of contestable shares in Figure 4.
10. Mitre 10 receives [] relationship rebate from Winstone, which is []. However, as with other merchants, it is unclear whether Mitre 10 would lose all of its relationship and advertising rebates should it switch some of its purchases to an entrant.
11. From Figure 4, we can see that:
 - 11.1 in the low lost rebate scenario, the entrant's required price does not fall below Winstone's avoidable costs for any share; and
 - 11.2 in the high lost rebate scenario, the entrant's required price is below Winstone's avoidable costs when the contestable share is below []%.

Figure 4: Entrant's required price to Mitre 10 for a given share of purchases
[]

Carters

12. The required prices that an entrant would need to offer Carters a merchant so as to compensate it for lost rebates are shown for a range of contestable shares in Figure 5.
13. Carters receives [] relationship rebate from Winstone, which is []. As with other merchants, it is unclear whether Carters would lose all of its relationship and advertising rebates should it switch some of its purchases to an entrant.

14. From Figure 5, we can see that:
- 14.1 in the low lost rebate scenario, the entrant's required price does not fall below Winstone's avoidable costs for any share; and
 - 14.2 in the high lost rebate scenario, the entrant's required price is below Winstone's avoidable costs when the contestable share is below about []%.

Figure 5: Entrant's required price to Carters for a given share of purchases

[]