

Statement of Preliminary Issues

Perry Metal Protection Limited/ CSP Coating Systems

25 January 2013

Introduction

1. On 24 December 2012, the Commerce Commission (the Commission) received an application from Perry Metal Protection Limited (PMP) seeking clearance to acquire the CSP Coating Systems (CSP) division from Fletcher Steel.
2. The public version of the application can be accessed on the Commission's website at: <http://www.comcom.govt.nz/assets/Uploads/Perry-Metal-CSP-Coating-Systems-clearance-application-21-December-2012-Public.pdf>
3. This Statement of Preliminary Issues outlines the key competition issues that the Commission currently considers will be important in deciding whether or not to give clearance. The issues highlighted in this statement are based on the information available at the time of publication, and may change as the Commission's assessment of the application for clearance progresses. Therefore, the issues highlighted in this Statement of Preliminary Issues are in no way binding on the Commission.
4. The Commission invites interested parties to comment on the likely competitive effects of the proposed merger. The Commission requests that parties who wish to make a submission do so by **8 February 2013**.

The transaction

5. Under the terms of the proposed merger, PMP would acquire the Auckland and Christchurch galvanizing businesses carried on by CSP, a division of Fletcher Steel Limited. The application also includes a statement that if the acquisition proceeds, PMP intends to divest assets in the South Island.

Relevant parties

6. PMP is a wholly owned subsidiary of Perry Group Limited. It carries on hot-dip galvanizing businesses located in Auckland, Hamilton, Tauranga, Wellington, and Christchurch. Hot-dip galvanizing protects steel from corrosion by immersing the steel in molten zinc creating a protective coating layer.
7. CSP is a division of Fletcher Steel Limited, which is in turn a subsidiary within the Fletcher Building Limited group of companies. It operates two galvanizing businesses, one in Auckland and the other in Christchurch.
8. In Auckland, CSP offers sand blasting, hot dip galvanizing and industrial painting services for metal protection. This painting includes zinc metal spray, epoxy and other standard coatings. CSP's Christchurch operation primarily provides hot dip galvanizing.

Analytical framework

9. In the context of an application for clearance, the Commission must consider whether or not an acquisition substantially lessens competition in any market. The Commission's analytical framework for assessing whether an acquisition is likely to result in a substantial lessening of competition is described in the Commission's Mergers and Acquisitions Guidelines. The application of the guidelines depends on the facts in each case. In any assessment, the determination of the relevant market or markets may be an important tool. The Commission determines the relevant market or markets by identifying the areas where the businesses of the acquirer and the target overlap. The Commission then considers the relevant products and geographic regions that may be close substitutes from both a customer's and a supplier's point of view.
10. The Commission uses forward looking analysis to assess the degree of any potential lessening of competition in the relevant market or markets arising from a proposed acquisition. Therefore, the next step is to establish the two hypothetical future scenarios; with the acquisition and without the acquisition.
11. The impact of the acquisition is the difference in competition between those two scenarios.
12. The Commission analyses the extent of competition in each relevant market for both the 'with' and 'without' scenarios in terms of the following.
 - 12.1 Existing competition – the degree to which existing competitors compete and their ability to expand their operations in the event that the merged firm raises prices.
 - 12.2 Potential competition – the ability of businesses to enter the market on sufficient scale in order to provide competitive constraint.
 - 12.3 The countervailing market power of buyers – the potential for a business to be sufficiently constrained by purchasers' ability to exert influence on price, quality and/or terms of supply.
 - 12.4 Coordinated behaviour – whether the acquisition would enhance the ability of market participants to collude either tacitly or explicitly.
13. A comparison of the extent of competition in the relevant markets both with and without the acquisition enables the Commission to assess the degree by which the proposed acquisition might lessen competition. If the lessening is likely to be substantial, the Commission may not give clearance to the proposed acquisition.

Preliminary issues

14. The Commission intends to focus the investigation on the following areas.

Market definition

15. In its application, PMP submitted that there are separate markets in the North and South island for the provision of steel protection coating services:
 - 15.1 North Island market - as stated above, PMP operates four galvanizing plants in the North Island which are located in Auckland, Hamilton, Tauranga and Wellington.
 - 15.2 South Island market- PMP and CSP each own one of the only two galvanizing plants in the South Island. The plants are both situated in Christchurch.
16. The Commission will consider whether North Island and South Island markets for steel protection coating services as identified by the applicant are the appropriate geographic markets, or whether the relevant markets are narrower regional markets.
17. The Commission will also consider possible distinctions between steel protection coating services, such as hot-dip galvanizing, sandblasting and industrial painting to ascertain whether hot-dip galvanizing could be considered a discrete product market.

Existing competition

18. PMP submitted that the proposed merger does not raise any competition concerns in any North Island market because:
 - 18.1 direct competition will continue from the two other Auckland based galvanizers, and a third galvanizer that currently only undertakes internal work, but is capable of resuming the acceptance of work from third parties;
 - 18.2 competition will continue from other galvanizers in other North Island locations that source work directly from Auckland based steel fabricators, or that galvanize items that are fabricated in one region for customers located in other regions;
 - 18.3 competition will also be provided by a large number of applicators that apply protective paint systems to steel items, particularly for larger items;
 - 18.4 the actual or threatened importation of galvanized products will continue to constrain the pricing of galvanizing similar products in New Zealand;
 - 18.5 there are low barriers to expansion and entry; and
 - 18.6 the market conditions post acquisition will not be conducive to coordinated conduct.
19. To remove any competition concerns in the South Island, PMP has offered to divest assets in Christchurch to a third party on terms to be agreed with the Commission.

20. PMP has submitted that pending such a divestment, both businesses would be managed separately. Following reaching agreement of the divestment proposal, PMP submitted that there would be no composition, asset or purchaser risks.
21. The issues the Commission will consider in regard to existing competition include:
 - 21.1 whether the existing competitors in the market have the capacity to increase their throughput;
 - 21.2 whether the existing competitors in the market have the ability to service larger customers and larger bits of steel (exceeding 6m in length); and
 - 21.3 the different abilities of existing competitors in the market to effectively compete, depending on transport costs and any other factors.

Potential competition

22. PMP submitted that barriers to entry and expansion are low, and that the market conditions post the proposed-merger will not be conducive to coordinated conduct.
23. The Commission will consider the conditions of entry and expansion and whether these are likely to inhibit future potential competitors from constraining the merged firm.

Countervailing Power

24. The Commission will consider the extent to which customers have a degree of countervailing power that would constrain the merged firm.

Next steps

25. In line with the Commission's Merger and Acquisitions Clearance Process Guidelines (available on the Commission's website at www.comcom.govt.nz), the Commission has established a draft timeframe for consideration of PMP and CSP's application. An extension of time has been agreed to by PMP and CSP such that the Commission should make its final decision by **25 February 2013**. To keep up to date with changes in relation to timing and to find relevant documents, visit the public Clearance Register on the Commission's website at: <http://www.comcom.govt.nz/clearances-register/>
26. The Commission will be contacting parties it believes will provide the best information to help it assess the preliminary issues identified above.
27. The Commission also invites submissions from any other parties that consider they have information relevant to the Commission's consideration of this matter. If you wish to make a submission, please send it to the Registrar, at registrar@comcom.govt.nz with the reference 'Perry/ CSP' in the subject line of your email, or The Registrar, PO Box 2351, Wellington 6140 by 4pm **8 February 2013**. Please clearly identify any confidential information contained in the submission and provide contact details.

