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Determination

Tuakau Proteins Limited and Graeme Lowe Protein Limited [2014] NZCC 26

The Commission:	Dr Mark Berry Sue Begg Anna Rawlings
Summary of application:	An application from Tuakau Proteins Limited to acquire Lowe Corporation Limited's Tuakau rendering and trucking businesses, Lowe's Hawera rendering plant and equipment.
Determination:	Under section 66(3)(a) of the Commerce Act 1986, the Commission gives clearance for Tuakau Proteins Limited to acquire the Tuakau rendering and trucking businesses and Hawera rendering plant and equipment of Graeme Lowe Protein Limited.
Date of determination:	25 November 2014

Confidential material in the document is denoted by [ ].

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The proposal

1. On 14 July 2014, the Commerce Commission (the Commission) received an application for a newly formed company, Tuakau Proteins Limited (Tuakau Proteins or the Applicant), to acquire certain animal rendering business interests from Graeme Lowe Protein Limited (Lowe), and a 50% shareholding in Kakariki Proteins Limited (Kakariki). The application was subsequently varied on 19 August 2014 to exclude the acquisition of the 50% shareholding in Kakariki.[1]

2. Post-acquisition, Lowe will own 50.1% of Tuakau Proteins. The remaining 49.9% will be owned by Glenninburg Holdings Limited (Glenninburg). Glenninburg will be 82% owned by Taranaki By-Products Limited (TBP) and 18% owned by Stephen Dahlenburg (a 50% shareholder of Kakariki). Stephen Dahlenburg will have a management role at Tuakau Proteins.

3. The acquisition would result in ownership and management overlaps between three renderers – Lowe, TBP and Kakariki. TBP and Lowe's parent company, Lowe Corporation Limited, are already linked through their joint ownership of Hawkes Bay Protein Limited (HBP), as set out in paragraph 31. Attachment 1 is a diagram of the links between the companies with and without the acquisition.

4. Although these overlaps will only be partial (ie, this is not a full merger of Lowe, TBP and Kakariki), we have assessed the acquisition as if it were a full merger. We have also assessed it on the basis that the companies were previously independent of each other.[2] We consider this the most conservative basis on which to assess the competitive impact of the acquisition. If the acquisition is unlikely to substantially lessen competition under a full merger, then it is unlikely to substantially lessen competition under lesser ownership links between the parties.

The decision

5. The Commission gives clearance to the proposed acquisition. The Commission is satisfied that the proposed acquisition will not have, or would not be likely to have, the effect of substantially lessening competition in any market.

Our framework

6. Our approach to analysing the competition effects of the proposed acquisition is based on the principles set out in our Mergers and Acquisitions Guidelines.[3]

The substantial lessening of competition test

7. As required by the Commerce Act 1986, we assess mergers using the substantial lessening of competition test.

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[1] Letter from Russell McVeagh (19 August 2014).

[2] The exception is Lowe's and TBP's joint ownership of HBP. Lowe acquired 49.9% of HBP in March 2014. Clearance was not sought for this acquisition and this Determination does not consider the competition effects (if any) that this acquisition has had.

[3] Commerce Commission, *Mergers and Acquisitions Guidelines*, July 2013.

8. We determine whether a merger is likely to substantially lessen competition in a market by comparing the likely state of competition if the merger proceeds (the scenario with the merger, often referred to as the factual), with the likely state of competition if the merger does not proceed (the scenario without the merger, often referred to as the counterfactual).[4]

9. A lessening of competition is generally the same as an increase in market power. Market power is the ability to raise price above the price that would exist in a competitive market (the 'competitive price'),[5] or reduce non-price factors such as quality or service below competitive levels. Similar to a merger between competing suppliers, a merger between competing buyers may lessen competition by increasing the merged firm's ability, unilaterally or in coordination with other firms, to exercise market power when buying products. Buyer market power is the ability to profitably depress prices paid to suppliers to a level below the competitive price for a significant period of time. This can lead to the withdrawal of supply from the market.

10. Determining the scope of the relevant market or markets can be an important tool in determining whether a substantial lessening of competition is likely.

11. We define markets in the way that we consider best isolates the key competition issues that may arise from the merger. In many cases this may not require us to precisely define the boundaries of a market. A relevant market is ultimately determined, in the words of the Act, as a matter of fact and commercial common sense.[6]

When a lessening of competition is substantial

12. Only a lessening of competition that is substantial is prohibited. A lessening of competition will be substantial if it is real, of substance, or more than nominal.[7] Some courts have used the word 'material' to describe a lessening of competition that is substantial.[8]

13. Consequently, there is no bright line that separates a lessening of competition that is substantial from one that is not. What is substantial is a matter of judgement and depends on the facts of each case. Ultimately, we assess whether competition will be substantially lessened by asking whether consumers in the relevant market(s) are likely to be adversely affected in a material way.

When a substantial lessening of competition is likely

14. A substantial lessening of competition is 'likely' if there is a real and substantial risk, or a real chance, that it will occur. This requires that a substantial lessening of

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4 *Commerce Commission v Woolworths Limited* (2008) 12 TCLR 194 (CA) at [63].
5 Or below competitive levels in a merger between buyers.
6 Section 3(1A). See also *Brambles v Commerce Commission* (2003) 10 TCLR 868 at [81].
7 *Woolworths & Ors v Commerce Commission* (2008) 8 NZBLC 102,128 (HC) at [127].
8 *Woolworths & Ors v Commerce Commission* (2008) 8 NZBLC 102,128 (HC) at [129].

competition is more than a possibility, but does not mean that the effect needs to be more likely than not to occur.[9]

The clearance test

15. We must clear a merger if we are satisfied that the merger would not be likely to substantially lessen competition in any market.[10] If we are not satisfied – including if we are left in doubt – we must decline to clear the merger.

Key parties

Lowe Corporation Limited

16. Lowe Corporation Limited is a family-owned company operating in the meat and meat by-products industries. It wholly owns Lowe, which has rendering operations at its plants in Hawera (Taranaki) and Tuakau (North Waikato).

17. Until recently, Lowe's Hawera plant toll rendered bovine material on behalf of Silver Fern Farms Limited (SFF) to produce Halal edible tallow and bovine meat and bone meal.
[
][
].

18. Lowe also has a dissolved air flotation waste plant, which clarifies wastewater by removing contaminants, at this site.

19. Lowe's Tuakau plant processes bovine and poultry material on dedicated lines, and all species on a mixed species line. It can also process blood and feathers.

20. The Tuakau plant currently processes bovine material from SFF's Te Aroha, Dargaville and Paeroa
plants[
].

21. Lowe Tuakau offers a daily shop collection service in the upper North Island. The service collects calves (from mid-June to the end of October) and meat waste from butchers, supermarkets, fish merchants, home kills, pork and poultry producers and various other food processors. This service collects bovine, ovine, equine, porcine, poultry, piscine and caprine material.

22. The outputs of the Tuakau plant are:

    22.1. inedible tallow, poultry oil, bovine, poultry, and mixed species meat and bone meals;

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9 Ibid at [111].

10 Commerce Act 1986, s 66(1).

22.2. feather meal; and

22.3. blood meal.

23. Lowe Corporation Limited's other interests include:

23.1. a 49.9% shareholding in HBP (described below at paragraphs 31-32)[11];

23.2. farming operations in Hawkes Bay; and

23.3. property development and investments (including a 17.46% holding in Blue Sky Meats (N.Z.) Limited in the South Island).

Taranaki By-Products Limited (TBP)

24. TBP is also a family-owned business. It owns a rendering facility at Okaiawa (approximately 10 kilometres from Lowe's Hawera plant in Taranaki), and is co-owner with Lowe of HBP. TBP owns the remaining 50.1% of HBP. TBP does not collect material from shops or dead stock.

25. TBP's Okaiawa rendering facility has a bovine line (operating on a toll basis), a poultry line (on a toll basis), a feather line (on a toll basis), and a blood line.

26. TBP also has a 50:50 joint venture with ANZCO Foods Limited (ANZCO) called Taranaki Bio Extracts Limited, which takes bovine material and turns it into edible tallow, extracts, and gelbone for gelatin manufacturing. This business is also located at the Okaiawa facility.

27. TBP processes bovine material from ANZCO and Alliance Group Limited (Alliance). [[12]]

28. TBP produces bovine meat and bone meal, mixed meat and bone meal, poultry meal, feather meal, blood meal, inedible tallow and poultry oil.

Tuakau Proteins Limited – the Applicant

29. Tuakau Proteins is a newly formed company for the purpose of the proposed acquisition. Should the acquisition proceed, Tuakau Proteins will be 50.1% owned by Lowe. The remaining 49.9% will be owned by Glenninburg Holdings Limited (Glenninburg). Glenninburg will be 82% owned by TBP and 18% owned by Stephen Dahlenburg (a 50% shareholder of Kakariki).

30. The intention is that Tuakau Proteins will process volumes from [ ].

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11 Lowe Corporation Limited acquired this interest in April 2014.

12 [ ]

Hawkes Bay Protein Limited

31. HBP is 50.1% owned by TBP and 49.9% owned by Lowe Corporation Limited and processes ovine material in Napier.

32. HBP processes ovine material, and a small quantity of cervine material. It processes material from
[
].

Kakariki Proteins Limited

33. Kakariki is a renderer situated near Feilding (Manawatu). It is 50% owned by Turk's, its largest poultry material supplier, with the remaining 50% owned by other parties, including Stephen Dahlenburg.

34. Kakariki operates a mixed rendering line with a focus on poultry, porcine, and piscine material. It operates a regular collection service from shops in the lower North Island as well as in Auckland.[13]

35. Kakariki produces mixed meat and bone meal, fish meal, inedible tallow and poultry oil.

Wallace Corporation Limited

36. Wallace Corporation Limited (Wallace) operates the largest independent rendering plant in New Zealand, at Waitoa in Waikato. Its raw material catchment area is the upper North Island.[14]

37. Wallace has a mixed line (which renders bovine, ovine and cervine material), a poultry line and a feather line. It produces poultry meal, mixed species meat and bone meal, feather meal, blood meal, mixed species tallow and poultry tallow. Wallace renders material from
[
].

38. Wallace also collects material from shops in the Auckland, Waikato and Bay of Plenty regions.

39. Wallace produces mixed tallow, poultry tallow, Halal meat and bone meal, feather meal and poultry meal.

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[13] [ ].

[14] www.wallace.co.nz/Rendering.html

PVL Proteins Limited

40. PVL Proteins Limited (PVL) is a mixed species renderer located in Auckland. PVL is owned by the Wilson Hellaby Group and renders on behalf of its parent company and other meat processors.

In-house renderers

41. AFFCO Meat Processors Limited (AFFCO) does all of its own rendering in-house. It operates several sites and processes both bovine and ovine species. [ ]

42. Alliance renders its own ovine material, but does not presently do any bovine rendering[ ].

43. Taylor Preston does all of its own rendering on-site at its Wellington plant on a mixed line. [ ].

Overview

44. Table 1 provides an overview of the current main independent (those that are not vertically integrated with a meat processor) renderers in the North Island, and what species they process.

Table 1: North Island independent rendering capability

Renderer	Ovine line	Mixed line / Bovine line	Blood line	Poultry line	Feather line	Shop collection
Lowe Hawera	✗	✓	✗	✗	✗	✗
Lowe Tuakau	✗	✓	✓	✓	✓	✓
TBP	✗	✓	✓	✓	✓	✗
Wallace	✗	✓	✗	✓	✓	✓
Kakariki	✗	✓	✗	✗[15]	✗	✓
HBP	✓	✗	✗	✗	✗	✗

15 Kakariki processes poultry material on a mixed line.

Industry background

Rendering

45. Livestock is processed by meat processing companies and smaller butchering, home killing and farm operations. This produces by-product material such as blood, offal, feathers and bone.

46. Rendering is the processing of that material into stable, value-added products.

47. The rendering process involves heat treatment, separation, pressing and drying to produce a range of finished products:

    47.1. dry products – such as meat, bone and feather meals which are used for animal feed, pet food, fertiliser; and

    47.2. wet products – such as oils and edible and inedible tallows which are used in animal feed, bio-diesel production, cosmetic and pharmaceutical manufacture, and food production.

48. Rendering can be carried out on lines dedicated to one species, or on a mixed species line. In many cases, bovine material is processed on a mixed line as the output products produced from bovine material do not generally demand a premium price over products produced from mixed material. Rendering plants are highly automated, and are most cost-effective when they are used to process large volumes. Plants are limited in the volumes that they can process by conditions under their resource consents.

49. Some meat processors have on-site rendering facilities, while others need to transport material to another location to be rendered. In some cases, material is taken to another site owned by the processor. For example, Alliance renders all its own North Island ovine material from its Dannevirke and Levin sites at its Levin plant. It then sells and markets the outputs.

50. Rendering can also be carried out on a toll basis where the meat processor pays the rendering firm a processing fee and retains ownership of the material throughout the process. The meat processor then markets and sells the rendered outputs itself.

51. In other cases, the material is sold to a rendering firm who will render the material and sell the rendered outputs. Those without significant volumes of material, or without the expertise to market the outputs, are likely to take this option.

52. The transport of materials purchased by rendering firms differs depending on the scale of the meat processor. For example, a large processor will typically have a dedicated transport arrangement with the rendering company whereas a smaller processor such as a butcher will have its material collected as part of a scheduled collection run that aggregates material from a number of smaller suppliers.

53. The base output products are mixed tallow and meal. Ovine meal and cervine meal command higher prices than bovine or mixed meal. Typically, ovine meal sells at a

premium of 30-40% above bovine or mixed species meal, although market fluctuations do occur.

54. Certain markets have particular requirements. For example, to sell into the EU market, a rendering line cannot have switched species more than once in the previous year. Some markets (eg, Indonesia, Israel) do not accept material containing pork and some markets want products to be Halal (eg, some Middle East countries).

55. The vast majority of outputs are sold as commodity products in export markets. All ovine meal is exported, mostly for use in pet food. The small percentage of meal that is sold domestically is generally used for animal feed. Some of the small percentage of tallow that remains in New Zealand is further processed into edible products, and other grades are used in bio-diesel. Poultry oil is often used in animal feed.

With and without scenarios

With the acquisition

56. With the acquisition, the merged parties would acquire:

    56.1. the assets, including contracts, of Lowe's rendering and trucking businesses operated at Lapwood Road, Tuakau (excluding Lowe's stock, debts and cash), which includes plant and equipment used for rendering bovine materials, poultry materials, and mixed species materials, trucks and collection routes; and

    56.2. Lowe's rendering plant and equipment currently situated at Tawhiti Road, Hawera, being plant and equipment used for rendering bovine material (excluding Lowe's equipment at the site used for processing dissolved air flotation waste and dairy waste).

57. In its application, the Applicant advised that
[
.[16]
]

Without the acquisition

58. The Applicant submitted in its application that, if the acquisition did not proceed, it would be likely that at least one, if not both, of Lowe and TBP would explore alternative transactions with other competitors active in the rendering industry. It also stated that, given that there is no certainty as to what, if any, alternative transactions would take place, the relevant counterfactual is the status quo.[17]

59. However,
[

16 [ ]

17 Application, paras 15.1-15.2.

59.1.

59.2.

59.3.
[18]]

60. In support of the above,
[
].

61. In considering the likely without-the-acquisition scenario,
[ ][
].

62. Absent the acquisition, [ ].

63. [ ].

64. We have compared the acquisition against this scenario on the basis that it is the most conservative. Doing so means our analysis is based on a worst case scenario, in the sense that it is the scenario that would give rise to the greatest competition concerns. If the merger is unlikely to substantially lessen competition compared to this worst case scenario, then it is unlikely to substantially lessen competition when compared to any other likely scenario.

Ways in which the merger could substantially lessen competition

65. We have considered two ways in which a merger between Lowe, TBP and Kakariki could substantially lessen competition, namely:

65.1. whether the merged entity could profitably raise the price[19] of toll rendering services above the level that would prevail without the acquisition; and

18 [
]

19 Price in this document refers to all dimensions of competition, including quality, range, the level of innovation, service or any other element of competition valued by buyers.

65.2. whether the merged entity could profitably reduce prices paid in the collection and purchase of animal by-products below competitive levels.

Toll rendering services

66. If the meat processors who toll process their by-product material have fewer options as a result of the merger, then there is a potential that they would be faced with higher prices for that processing. As a result, we explored how each individual toll rendering customer's options are likely to be affected by the merger.

Purchase of by-product material

67. Lowe, TBP and Kakariki all purchase by-product material from meat processors. The proposed acquisition could result in a substantial lessening of competition if the merged entity reduced the prices it pays for that material below competitive levels and this resulted in a reduction in the quantity of material supplied for rendering.

68. Whether or not the proposed acquisition will be likely to have the effect of substantially lessening competition depends upon a number of factors, including:

68.1. whether meat processors consider more than one of the merging parties as potential purchasers;

68.2. whether there are other competitive alternatives available to meat processors for the sale of material;

68.3. if there are no other competitive alternatives, whether a reduction in the price paid for material would cause meat processors to reduce the quantity of material they produce; and

68.4. if any meat processors decreased the quantity of material they produced, whether the merged entity would likely find a reduction in inputs profitable for them given consideration of such factors as:

68.4.1. how such a reduction would impact the cost efficiency of their plants;

68.4.2. how such a reduction might impact longer-term access to key inputs; and

68.4.3. whether the merged entity would be able to increase the price it charges for the outputs from the rendering process.

Market definition

Our approach to market definition

69. Market definition is a tool that provides a framework to help identify and assess the close competitive constraints the merged firm would likely face.[20] It encompasses

[20] *Commerce Commission v New Zealand Bus Limited* (2006) 11 TCLR 679 (HC) at [123]. *Brambles New Zealand Ltd v Commerce Commission* (2003) TCLR 868 (HC) at [137].

actual and potential transactions between sellers and buyers, and seeks to capture the factors that directly shape and constrain rivalry between sellers.[21]

70. A market is defined in the Commerce Act as a market in New Zealand for goods and services as well as other goods and services that are substitutable for them as a matter of "fact and commercial common sense". In general, the more closely substitutable two products are, the closer the competition and the greater the competitive constraint between the products.

71. We define markets in a way that best isolates the key competition issues that arise from the merger. In many cases this may not require us to precisely define the boundaries of a market.

72. To help us establish whether customers would switch sufficient purchases to alternative products, we use the hypothetical monopolist test as a conceptual tool. This test asks whether a hypothetical sole supplier of a set of products (or locations) would profitably increase prices for at least one of the merging firms' products (or locations) by at least a small, but significant, amount.[22] This small, but significant, amount is often referred to as a SSNIP – a small, but significant, non-transitory increase in price.

73. In general, the smallest set of products (or locations) in which the SSNIP can be profitably sustained is defined as the relevant product (geographic) market.

The Applicant's view of the relevant markets

74. The Applicant submitted that the relevant markets in which to consider the competition effects of the proposed acquisition are:

    74.1. input markets: the collection of animal by-products; and

    74.2. output markets: animal meals and fats used in animal feed; animal meals and fats used in pet food; and tallow and grease.

75. The Applicant considers the input markets to be North Island markets and the output markets to be national.

The Commission's view of the relevant markets

76. The Commission considers that there are separate input and output markets, and that on the input side there are a number of relevant markets that differ by method of acquisition, species, and by customer location. On the output side, there are also several markets that differ largely on the basis of output product. The only overlap in the supply of output products in New Zealand occurs in the markets for the supply of products based on poultry, and bovine or mixed species inputs.

[21] *Commerce Commission v Air New Zealand Ltd et al* (2011) 9 NZBLC 103,318 (HC) at [124].

[22] The test assumes that all other prices are held at current levels.

Input markets

77. We consider that there are distinct input markets based on three factors related to the rendering of raw material: how the material is acquired; the species of the material; and the location of the material.

Method of acquisition

78. We consider that there are three distinct ways that material is acquired for rendering. One is via a supply-side market, and two are via buyer-side markets.

79. On the supply-side, material is acquired via the market for:

    79.1. the supply of toll rendering services.

80. On the buyer-side, material is acquired via the markets for:

    80.1. the direct collection (and purchase) of by-product material; and

    80.2. the collection (and purchase) on a shop collection run of by-product material.

<u>Toll rendering</u>

81. We consider there to be a market(s) for the supply of toll rendering services by renderers to meat processors who produce the by-product material.

82. Under a toll rendering arrangement, the customer that produces the by-product material (eg, meat processor) engages a renderer to process that material into rendered outputs. The transport of the material to the renderer is usually arranged by the renderer. The customer retains ownership of the material throughout the process and markets/sells the end product on its own account. Toll rendering customers pay the renderer a fee, which includes a processing and a transport component.

83. Toll rendering customers are typically large and sophisticated meat processors who produce large quantities of material as a by-product of their primary business of processing and selling meat. These customers have the capability to market the rendered outputs on their own behalf. Examples of such customers include SFF and Tegel.

84. A renderer that renders material on a toll basis could, without significant cost, switch to the direct collection and purchase of by-product material, and vice versa. As a consequence, we do not distinguish market participants in these distinct markets on this basis (that is, if a renderer currently toll manufactures only, it is still considered a near competitor in the direct collection market, and vice versa). This is because all the renderers have the capability to market the end product.

<u>Direct collection</u>

85. We consider the market(s) for the direct collection of raw material to be buyer-side market(s). That is, the sellers in this market(s) are the by-product material producers

and the buyers are the renderers. Renderers in this market are near competitors to those in the toll processing market.

86. Under a direct collection arrangement, the meat processors sell their material to the renderer, who collects it (dedicated transport) and processes it into rendered outputs. The renderer then markets and sells the rendered outputs.

87. The price paid to a meat processor is typically based on what the renderer expects to make from selling the output products it makes from the raw material. The meat processors who sell into the direct collection markets are typically medium-sized meat processors who lack the scale to market rendered outputs themselves, but produce sufficient volumes of the raw material to justify a renderer investing in dedicated transport arrangements for them.

<u>Shop collection</u>

88. The markets for the shop collection of raw material are also buyer-side markets. That is, the sellers in these markets are the shops and the buyers are the renderers.

89. Under the shop collection arrangement, the supplier of the by-product material, such as a butcher or grocer, sells it directly to the renderer, who collects it as part of a scheduled collection run. The material from multiple suppliers, and of multiple species, is collected by the same vehicle. The renderer processes it into rendered output products, and then markets and sells the output products. Suppliers to the shop collection market are smaller, low-volume processors such as butchers and grocery shops.

90. The price paid to suppliers in the shop collection market varies. Some shops are not paid for their materials, and some are paid a nominal fee. The renderers want the added volumes to increase the efficiency of their plants, and the shops want to dispose of the raw material in a timely and efficient matter. In many cases, their alternative is to pay to landfill the material. The revenue earned by the shops from the sale of the by-product material is insignificant in relation to the overall revenue from the sale of their core products.

91. A renderer who does not buy products on a shop collection run may not be willing to start doing so. The processing of shop collected materials requires a mixed line for processing, and a tolerance of mixed species. It also requires transport for the collection of material, which may not be economical without the guarantee of sufficient volumes. As a result, only those renderers that currently have a shop run are included as existing market participants.

Species specification

Toll rendering and direct collection

92. The Applicant submitted that the relevant product market should be a single multi-species market, given the ease of supply-side switching if demand or available returns were to increase in respect of a particular species.[23]

93. We do not consider that all species should fall into a single market. We consider that, for toll rendering services and direct collection, the relevant product markets are distinct for each of poultry, ovine, and bovine/mixed species. This is due to a number of factors, including:

    93.1. ovine material is more valuable than poultry, which is more valuable than bovine and mixed species material in the ultimate downstream markets (ie, for meal, tallow etc);

    93.2. major customers (particularly the Middle East and the EU) demand single species traceability; and

    93.3. while it is technically possible for renderers to switch a rendering line from one species to another, our understanding is that this is seldom done. A key reason for this is that in order to maintain export certification in certain markets, a line cannot be switched more than once a year.

94. This acquisition does not result in overlap in the supply of toll rendering services and direct collection for ovine material and as such we do not consider these markets further.

Shop collection

95. The separation of markets across species does not apply in the shop collection market. That is, we consider that there is a single market for shop collection of raw materials for the following reasons:

    95.1. suppliers of material for shop collection demand that all species are collected at the same time and typically supply various species;

    95.2. suppliers are paid a single price based on the overall weight of material rather than differing amounts for each species supplied; and

    95.3. renderers collect all materials in aggregate and do not consider it cost effective to operate different collection runs for each species.

[23] Appendix one, letter from Russell McVeagh [ ]

Geographic dimension

<u>Toll rendering and direct collection</u>

96. We consider that different toll rendering customers and suppliers of product for direct collection have different alternatives and, as a consequence, renderers can price discriminate.

97. For the purposes of this acquisition, we consider that the relevant customers (or potential customers affected by the acquisition) are those who would have otherwise benefitted from competition between Lowe, TBP, and Kakariki's rendering facilities. These customers are located for the most part in the lower North Island (see Attachment 2).[24] For toll and direct collection, we do not consider that the proposed acquisition will result in any overlap in the upper North Island.

98. The Applicant submitted that the relevant geographical input markets are those for the North Island. We consider, however, that the affected input market is confined to the lower North Island. This is due to a number of factors, including:

    98.1. meat processors have advised that they seek to engage or sell to a renderer that is situated as close as possible to them because raw animal material begins to deteriorate immediately after an animal's death, and as the material deteriorates, the yield and quality of the rendered output decreases;

    98.2. while deterioration can be slowed by chilling or dosing with acid, our understanding is that the maximum distance that material can optimally be transported is 5-6 hours' drive time (where this drive time takes account of possible delays due to traffic congestion); and

    98.3. the raw material is a bulky, low-value product that is costly to transport.

99. These markets are, however, specific to customer location and requirements so the exact boundaries of the relevant market may differ by customer. For ease of discussion, we refer to the markets as though they were upper and lower North Island markets. We do not, however, lose sight of the fact that particular customers may have differing circumstances.

<u>Shop collection</u>

100. In the shop collection market, Kakariki in the lower North Island offers an alternative to Lowe Tuakau in the upper North Island. This is because [ ]. We consider the geographic overlap in the collection of material from shops in the upper North Island by a renderer located in the lower North Island to be atypical. In most cases, a lower North Island renderer would not be willing to drive the required distances for the quantities available in the shop market.

[24] Being defined by a latitudinal line running from New Plymouth in the west to Wairoa in the east.

101. For the shop collection market, there is no overlap between Lowe and TBP. As described above, there is overlap between Lowe Tuakau and Kakariki in the upper North Island (specifically in the Auckland, Bay of Plenty and Waikato areas). We consider the impact of the merger on competition for shop collection in these geographic areas only.

Output markets

102. There are a number of different rendering outputs (single/mixed species meal, bone meal, blood meal, oils, and edible and inedible tallow). We consider that it is appropriate to define these as separate markets based on the type and species of the output, given that they are supplied and purchased by a different set of suppliers and customers.

103. Customers have informed us that they have a number of options for purchasing rendered outputs and that they would consider buying product from the South Island as well as the North Island. We therefore consider that each of the output markets is likely to be national in scope.

104. In this case, the only overlap in the supply of output products in New Zealand occurs in the markets for the supply of products based on poultry, and bovine or mixed species inputs.

Conclusion on market definition

105. We consider that the appropriate markets in which to consider the competition effects of the proposed acquisition are the markets for the:

105.1. supply of toll rendering services to customers producing poultry raw material in the lower North Island;

105.2. supply of toll rendering services to customers producing bovine/mixed raw material in the lower North Island;

105.3. direct collection of poultry raw material from producers in the lower North Island;

105.4. direct collection of bovine/mixed raw material from producers in the lower North Island;

105.5. shop collection of raw materials in the upper North Island; and

105.6. supply of rendered outputs in New Zealand (including distinct markets by species and type of output).

Competition analysis – input markets

Poultry

Current competition

106. As outlined in Table 1, there are currently three North Island parties who provide poultry rendering services to third parties, on either a toll-processing or direct collection basis: TBP at its Okaiawa plant, Lowe at its Tuakau plant, and Wallace at Waitoa. In addition, Kakariki processes poultry material on a mixed line. Of these, only TBP's plant and Kakariki's plant are active in the lower North Island.

107. There are four main poultry producers in the North Island who provide material for rendering to third parties. They are Inghams (with plants in Auckland, Waihi, and Morrinsville), Tegel (with plants in Auckland and Inglewood), Turk's (Foxton), and Brink's (with plants in Tuakau and Karaka). (See Attachment 3.) Of these poultry producers, only Tegel and Turk's are active in the lower North Island.

108. As such, we have considered whether the proposed merger is likely to result in a substantial lessening of competition to Tegel and Turk's as a result of any decreased competition between TBP and Kakariki. This lessening of competition could occur in either the supply of toll rendering or in the purchase of raw material via direct collection.

The supply of toll rendering services to customers producing poultry raw material in the lower North Island

109. Tegel is [ ][ ][ ], [ ].

110. [ ].

111. [ ].

112. We consider Tegel's options in the lower North Island to be unaffected by the proposed acquisition.

The direct collection of poultry raw material from producers in the lower North Island

113. Turk's is the only seller of poultry raw material for direct collection in the lower North Island.

114. Turk's uses Kakariki for direct collection of its offal by-product material. We note that TBP is a potential purchaser for Turk's by-product material. However, as Turk's is a 50% shareholder in Kakariki, it is unlikely to utilise TBP at Kakariki's expense. Therefore, we consider Turk's options for direct collection services are unlikely to be adversely affected by the proposed acquisition.

115. [

].

116. We consider Turk's options in the lower North Island are unlikely to be affected by the proposed acquisition.

Bovine/Mixed species

Current competition

117. As outlined in Table 1, there are currently three parties who provide bovine/mixed rendering services to third parties, on either a toll-processing or direct collection basis, in the lower North Island. These parties are TBP at its Okaiawa plant, Lowe at its Hawera plant, and Kakariki at Levin.

118. In addition, both AFFCO and Taylor Preston operate in-house rendering facilities for processing their own bovine/mixed species material.

The supply of toll processing rendering services in the lower North Island – bovine/mixed

119. In the lower North Island, there are two customers who currently purchase bovine/mixed species toll rendering services: SFF and ANZCO.

120. ANZCO operates beef processing plants at Eltham and Bulls and [ ] metric tons of material per year.

121. ANZCO has stated that [

[25]]

[25] [ ]

122. ANZCO stated that
[
].

123. Our investigation does not suggest that Wallace is a strong competitive alternative to TBP for ANZCO's volumes. Nevertheless, we consider that the ongoing joint venture relationship between ANZCO and TBP is likely to insulate ANZCO from competitive harm.

124. SFF is the second customer whose toll-processing of bovine/mixed species could be adversely affected by the acquisition. In 2013, SFF entered into a[ ] with Lowe for the toll processing of all of its North Island by-product material.[26]

125. SFF received expressions of interest/bids from
[
].

126. We consider that competition for the SFF volumes occurred at the time it sought tenders for its North Island volumes. SFF was able to obtain a long-term agreement
[ ].
[ ]. We also consider that when this contract expires, Wallace, PVL (and potentially AFFCO) will provide competitive alternatives to Lowe.

The purchase of direct collection raw material in the lower North Island – bovine/mixed

127. There are several factors to consider when determining whether or not a substantial lessening of competition is likely in buying markets (see paragraph 68). First and foremost, we consider whether the proposed acquisition would lead to fewer options for the meat processors who sell to renderers who directly collect their material (see paragraph 68.1).

128. In the lower North Island we have identified three customers who could potentially face diminished competitive options for the sale of their by-product material for direct collection. These customers are:
[
].

129. [ ]currently renders on its own behalf and will continue to do so with the acquisition, and so we do not consider it will be affected by the acquisition.

130. [ ]predominantly an ovine and porcine supplier but does supply some bovine material to TBP
[ ].

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26 Excluding some volumes that were contractually committed to Wallace.

Lowe at Hawera has traditionally rendered SFF volumes only and Lowe Tuakau is relatively distant from Masterton.

131. [ ]and the volume of material produced at its North Island locations is small. [ ] sells its North Island bovine by-product material to TBP. [ ].

132. Alliance informed the Commission that [[27]] [

133. Another factor to consider is whether or not there is a competitive alternative for meat processors, if they face a price decrease by selling to the merged entity (see paragraph 68.2). The sale of material into the direct collection market is also a means of disposal of a by-product. So in this case, the likely alternative option to the sale of material is to dispose of it in the landfill, which would be done at a cost to the meat processor.

134. For example, prior to entering into its current arrangements, [ ]was disposing of its by-product material in a landfill, at a cost of approximately [ ]. It now receives [ ] for its approximately [ ]of material, which accounts for [ ]

135. Another option would be to enter into rendering. [ ]

136. The above suggests that the merged entity may be in a position to reduce the price it pays to [ ]as well, for its by-product material. However, the remainder of our analysis indicates that such a reduction would be unlikely to result in a reduction in the amount of material produced. Moreover we consider that the merged entity would have little incentive to decrease the throughput of their plants.

137. For the acquisition to result in a substantial lessening of competition in a buying market such as this, we would expect to see the meat processors who sell into this market decrease the quantity of material they supply to renderers (see paragraph 68.3). This decrease would occur in response to a decrease in the price received from the renderer. The Commission considers it unlikely that any decrease in the price

[27] [ ]

paid for by-product material would lead to such a reduction in the quantity of that material.

138. As the material is a by-product, its quantity has a direct relationship to the quantity of meat processed. Therefore, firms would need to decrease the quantity of their main output to decrease the quantity of the by-product material.

139. The proportion of revenue received from the sale of by-product material is small compared to the overall revenue received from the sale of meat products (see paragraph 134), so meat processors are unlikely to be incentivised to reduce the volume of meat products in order to reduce the volume of by-product material.

140. Even if there was a reduction in the amount of input rendered (see paragraph 68.4), it would not result in the ability of the merged entity to charge higher prices for the resulting output. This is because we do not consider it likely that the merging parties' market power in the output markets would be increased by the acquisition (see paragraphs 148-156). As a result, it is less likely that the merged entity would find a price reduction that is associated with a reduction in the amount of inputs purchased to be profitable.

141. Similarly, we do not consider that the merged entity would be incentivised to depress prices to a level that would reduce quantity because this would adversely impact the efficient running of their facilities. Rendering firms run more efficiently when they can maximise the volumes going through their plant, and volumes purchased in the direct collection market are significant. We consider that [ ] may lose a competitive alternative with the removal of Lowe. However, if this were to result in a decrease in the price paid for bovine by-product material, this would be unlikely to translate to a decrease in the quantity of material supplied.[28]

Shop collection market – Waikato and Auckland

142. As both Lowe and Kakariki operate scheduled shop collection runs in Auckland, overlap occurs in these markets. Evidence obtained indicates that Lowe and Kakariki compete fiercely for volumes in this market, with Kakariki gaining a number of Lowe suppliers in recent times.

143. Similar to the direct collection market, the shop collection market involves a by-product of a manufacturing operation which must be disposed of. In order for the acquisition to result in a substantial lessening of competition in this market, suppliers of shop material must decrease the quantity of material supplied in response to a decrease in the price received from the renderer. This would involve butchers and other users of shop collection services decreasing the amount of meat they process in response to a decrease in the price they are paid for their by-product material.

144. Businesses on the 'shop runs', such as butcher and grocery shops, told us that they would not decrease the volume of animal waste that they produced if the merged

[28] *Re Oji Oceania Management (NZ) Limited and Carter Holt Harvey Limited* [2014] NZCC 18 at [39-41].

entity decreased the price it pays for that material. This is because the revenue obtained from supplying waste material for rendering is a very small proportion of the overall revenue of the carcass. For example, Progressive Enterprises Limited is paid [ ] for its by-product material in the North Island, but sells approximately [ ] worth of meat products per week.

145. Similarly, the Mad Butcher Group, which has 37 franchises across New Zealand in both large and small centres, stated that the revenue received from selling shop waste to rendering companies is very small, in some cases [ ].

146. The alternative to selling, or giving away, waste to renderers on a shop run is to landfill that waste, which would occur at a cost.

Conclusion on competition analysis – input markets

147. We consider that the proposed acquisition would be unlikely to lead a substantial lessening of competition in any of the affected input markets.

Competition analysis – output markets

148. The majority of domestic purchasing of rendered outputs is carried out by intermediaries who aggregate all types of material from a number of suppliers and market it internationally and domestically.

149. Domestic end users of the products are predominantly primary producers who utilise mixed meal in animal feed. For example, Inghams has a specialised animal feed division that processes meals into a range of animal food products.

150. The Applicant has submitted that the degree of aggregation between the parties in the output markets is minimal, due to the high proportion of rendering that is done on a toll processing basis (and therefore marketed by the primary producers), and because the majority of output is sold internationally.

Output markets – poultry products

151. The majority of poultry rendering in the North Island is carried out on a toll processing basis, with Turk's and Brink's being the only poultry suppliers who sell to renderers on a direct collection basis.

152. [ ], who in turn sell the rendered outputs on their own account. Turk's sells its by-product material to [ ]purchase toll rendering services, and maintain ownership of the material throughout, marketing the rendered outputs on their own accounts.

153. As a consequence, if the parties merged, purchasers of rendered poultry products would continue to have a number of options including purchasing from Wallace, Inghams, and Tegel in the North Island, and Tegel in the South Island.

Output markets – bovine/mixed products

154. There are a number of parties who market finished bovine/mixed rendered products, including AFFCO, Wallace, PVL, Farm Brands Limited (50% owned by SFF), Smith Brothers Trading, Taylor Preston and Lowe.

155. With the acquisition, Farm Brands Limited, AFFCO, Wallace and PVL will continue to be large suppliers of the full range of bovine/mixed rendered products in the North Island. Purchasers will also continue to have the ability to purchase from South Island suppliers.

Conclusion on competition analysis – output markets

156. We consider that the proposed acquisition would be unlikely to lead a substantial lessening of competition in any of the affected output markets.

Determination on notice of clearance

157. We are satisfied that the proposed acquisition will not have, or would not be likely to have, the effect of substantially lessening competition in a market in New Zealand.

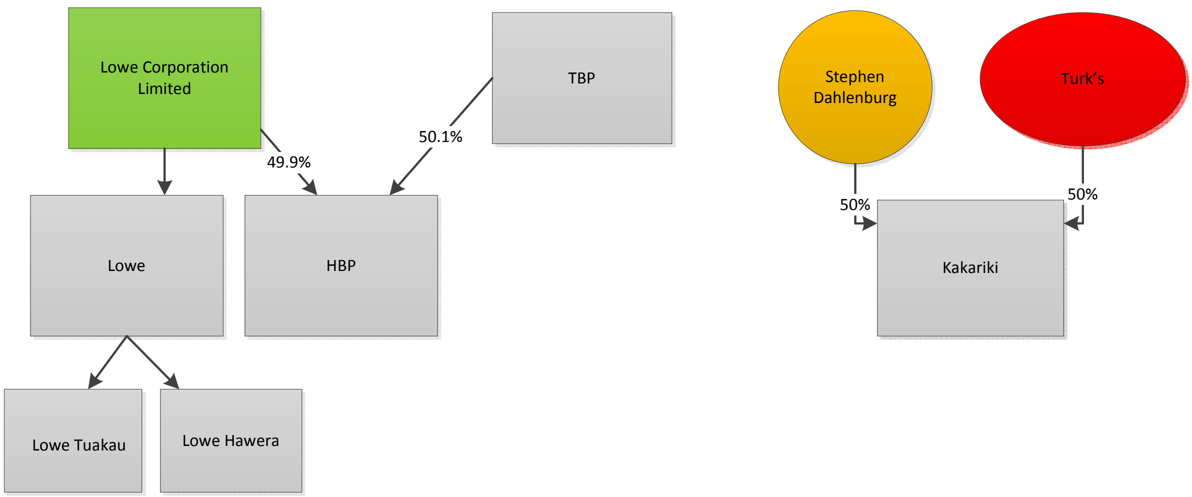
158. Under section 66(3)(a) of the Act, the Commerce Commission determines to give clearance for Tuakau Proteins Limited to acquire the Tuakau rendering and trucking businesses and Hawera rendering plant and equipment of Graeme Lowe Protein Limited.

Dated this 9th day of October 2014

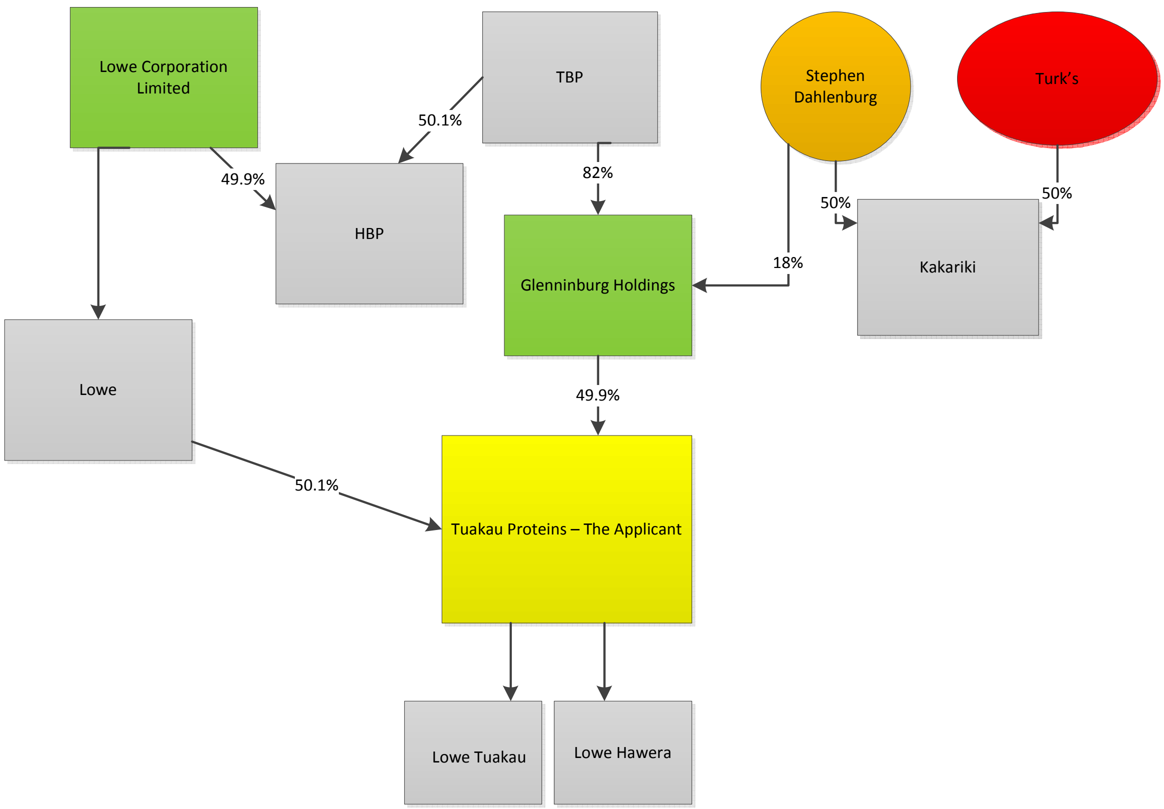
Dr Mark Berry
Chairman

Attachment 1

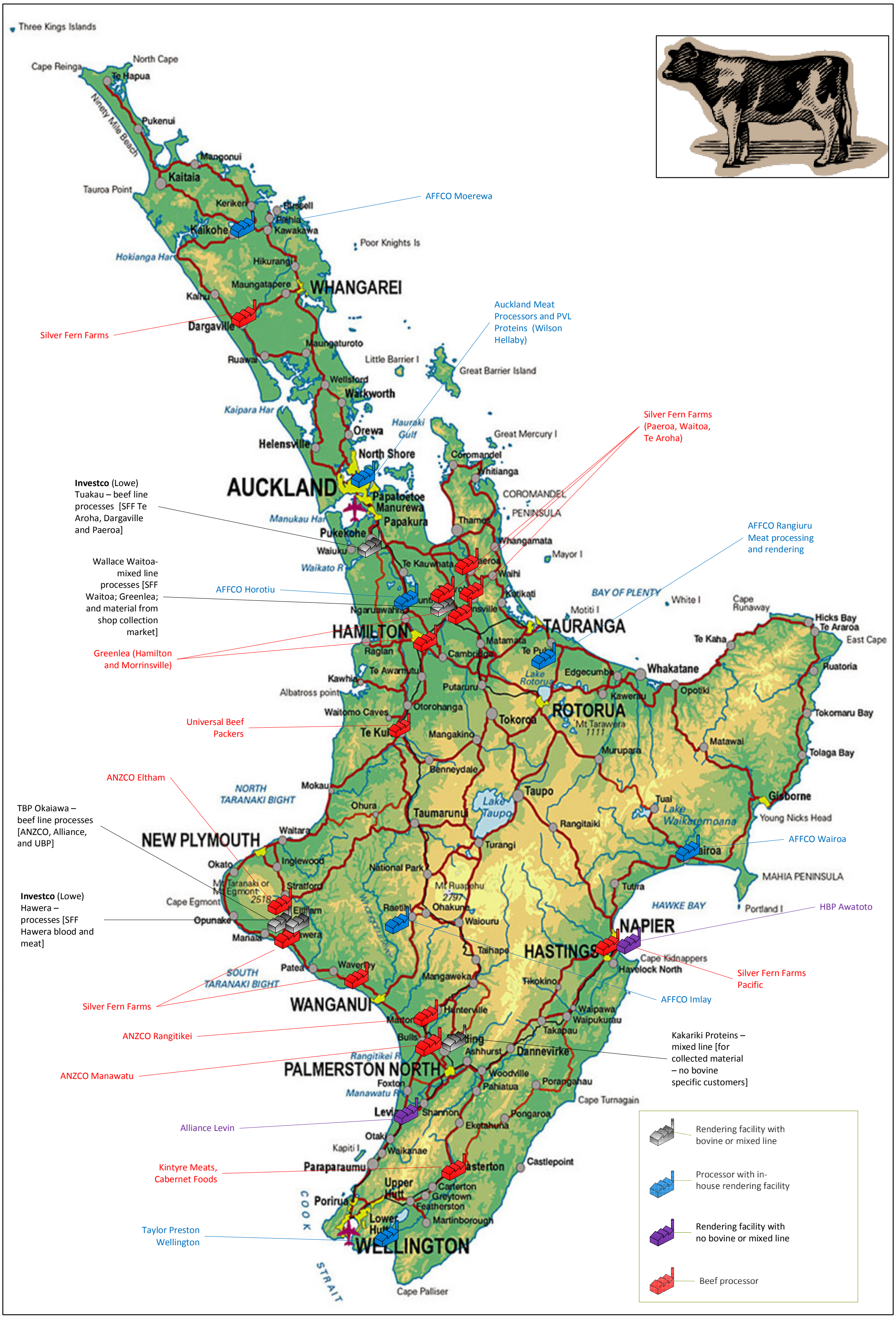
Without the acquisition



With the acquisition



Attachment 2: Bovine map



Attachment 3: Poultry map