

Determination

The Wallace Group Limited Partnership / Wallace Corporation Limited / Farm Brands Limited and Keep It Clean Limited [2016] NZCC 21

The Commission: Dr Mark Berry
Sue Begg
Anna Rawlings

Summary of application: The Wallace Group Limited Partnership seeks clearance to acquire up to 100% of the assets and business of:

- Wallace Corporation Limited;
- Farm Brands Limited, Farm Brands Asset Management Limited and South Canterbury By-Products (2009) Limited; and
- Keep It Clean Limited.

Determination: Under s 66(3) (a) of the Commerce Act 1986, the Commerce Commission gives clearance to the proposed acquisition.

Date of determination: 19 October 2016



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Information

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The proposed acquisition

1. On 26 July 2016, the Commerce Commission (the Commission) received an application from The Wallace Group Limited Partnership (WGLP) under s 66(1) of the Commerce Act 1986 (the Act) seeking clearance to acquire up to 100% of the assets and business of:
 - 1.1 Wallace Corporation Limited (Wallace);
 - 1.2 Farm Brands Limited, Farm Brands Asset Management Limited and South Canterbury By-Products (2009) Limited (collectively Farm Brands); and
 - 1.3 Keep It Clean Limited (KIC).

The decision – clearance granted

2. The Commission gives clearance to the proposed acquisition as it is satisfied that the proposed acquisition will not have, or would not be likely to have, the effect of substantially lessening of competition in a market in New Zealand.

Our framework

3. Our approach to analysing the competition effects of the proposed acquisition is based on the principles set out in our Mergers and Acquisitions Guidelines.¹

The substantial lessening of competition test

4. We determine whether a merger is likely to substantially lessen competition (cause an SLC) 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).²
5. We make a pragmatic and commercial assessment of what is likely to occur in the future, with and without the acquisition based on the information we obtain through our investigation and taking into account factors such as market growth and technological changes.
6. 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'),³ or reduce non-price factors such as quality or service below competitive levels.
7. 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.

¹ Commerce Commission *Merger and Acquisition Guidelines* (July 2013) <http://www.comcom.govt.nz/business-competition/guidelines-2/mergers-and-acquisitions-guidelines/>

² *Commerce Commission v Woolworths Limited* (2008) 12 TCLR 194 (CA) at [63].

³ Or below competitive levels in a merger between buyers.

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.

8. Determining the scope of the relevant market or markets can be an important tool in determining whether an SLC is likely.
9. We define markets in the way that we consider 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. A relevant market is ultimately determined, in the words of the Act, as a matter of fact and commercial common sense.⁴

When a lessening of competition is substantial

10. 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.⁵ Some courts have used the word 'material' to describe a lessening of competition that is substantial.⁶
11. 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

12. An SLC is 'likely' if there is a real and substantial risk, or a real chance, that it will occur. This requires that an SLC is more than a possibility, but does not mean that the effect needs to be more likely than not to occur.⁷

The clearance test

13. We must clear a merger if we are satisfied that the merger would not be likely to substantially lessen competition in any market.⁸ If we are not satisfied – including if we are left in doubt – we must decline to clear the merger.⁹
14. The burden of proof lies with WGLP to satisfy us on the balance of probabilities that the acquisition is not likely to have the effect of substantially lessening

⁴ Section 3(1A). See also *Brambles v Commerce Commission* (2003) 10 TCLR 868 at [81].

⁵ *Woolworths & Ors v Commerce Commission* (2008) 8 NZBLC 102,128 (HC) at [127].

⁶ *Ibid* at [129].

⁷ *Woolworths & Ors v Commerce Commission* (HC) above n 5 at [111].

⁸ Section 66(3)(a).

⁹ In *Commerce Commission v Woolworths Limited* (CA), above n 2 at [98], the Court held that "the existence of a 'doubt' corresponds to a failure to exclude a real chance of a substantial lessening of competition".

competition.¹⁰ The decision to grant or refuse a clearance is necessarily to be made on the basis of all the evidence.¹¹

Industry background

15. The proposed acquisition involves parties that render animal waste material. Livestock processing by meat processing companies, local abattoirs, small butchers, home kill and farm/skinning operations produces by-product material such as blood, offal, feathers and bone (hereafter referred to as animal material). Rendering is the processing of that material into finished products such as meat and bone meal (MBM) and tallow.
16. Rendering can be carried out on processing lines dedicated to one species, or on a mixed species line. In many cases, bovine (beef) material is processed on a mixed line as the finished rendered products produced from beef material do not generally attract a premium price over products produced from mixed material. However, as the final products of other species such as cervine (deer) and ovine (sheep) command a significant premium over the price of mixed/beef products, this animal material is usually processed on species specific separate lines. Lines can be swapped between species if sanitised, depending on export licence requirements.
17. Rendering plants are highly automated, and are most cost-effective when they are used to process large volumes of material. Plants can only process volumes in accordance with their resource consents (relating to, for example, air discharge; ie, odour).
18. Some of the larger meat processors have their own in-house rendering facilities, while others transport material to another location to be rendered. For example, ANZCO Foods Limited has an in-house rendering plant near Ashburton where it renders all of its own South Island beef and sheep material. Alliance, another large meat processor, operates in-house rendering plants at most of its South Island sites; however, its Nelson plant sends its sheep material to Value Protein Limited's West Coast plant for rendering.
19. The vast majority of finished rendered products are exported as commodities. Certain export markets have particular requirements for finished rendered products. These requirements dictate the value of these products and hence the types of animal material processed by the renderer.
20. For example, to sell into the EU market, a rendering line cannot have switched species more than once in the previous year. The EU market also does not accept finished rendered products produced with casualty material because of disease risk. Some markets (e.g., Indonesia and China) do not accept material containing pork. The presence of pork in the material used to produce the finished products

¹⁰ *Commerce Commission v Southern Cross Medical Care Society* (2001) 10 TCLR 269 (CA) at [7]. *Commerce Commission v Woolworths Ltd* (CA) above n 2 at [97].

¹¹ *Commerce Commission v Woolworths Ltd* (CA) above n 2 at [101].

significantly reduces the value of the product. This, in turn, affects the price that the renderer is prepared to pay for the animal material.

21. The rendering industry in New Zealand is beginning to face increasing pressure to manage the risks of cross species contamination of rendered products. International purchasers of the finished products are increasingly relying on DNA testing to ensure, for example, that halal certified material does not contain pork. The financial implications of cross contamination are significant as purchasers will reject large volumes of material if a DNA test is failed and it has implications for the export certification of a rendering plant.
22. The price that is offered for the animal material is usually based on a matrix that includes an index to the international commodity price of the final product. All sheep and deer meal is exported. The small percentage of mixed beef MBM that is sold domestically is generally used for animal feed. Some of the small percentage of blood meal that remains in New Zealand is sold as animal feed also.

Key parties

WGLP

23. WGLP was established in anticipation of this transaction. It is a limited partnership entity that consists of two limited partners which are also vendors in this transaction: Modena Investments (New Zealand) Limited (the parent company of Farm Brands); and Wallace.
24. WGLP also consists of a third general partner, Wallace Group GP Limited, which was also established for the purposes of this transaction, and is responsible for management and control of the WGLP business.

Wallace

25. The business of Wallace includes rendering, tanning, casualty stock and shop collection,¹² dairy farming, composting and other farming businesses. It owns two rendering plants:
 - 25.1 Waitoa (north Waikato), at which it renders beef, poultry and casualty materials; and
 - 25.2 Hororata (near Christchurch), at which it primarily renders pork material, general casualty material and the waste collected from home kill operators and small meat processors.¹³
26. Wallace also produces finished rendered products, including MBM, blood meal and inedible tallow, which it sells to end users and traders, including Farm Brands.

¹² See paragraphs 37 and 39 for a description of shop collection and casualty.

¹³ These include firms which acquire the raw material from meat processing plants and then carry out further processing. Hellers Limited, which produces bacon, sausages and other small goods, is an example of a firm in this category.

Farm Brands

27. Farm Brands is involved in the collection and rendering of animal materials. It owns two rendering plants:
- 27.1 Washdyke (near Timaru), which processes beef and sheep material, as well as casualty stock; and
 - 27.2 Silverstream (Mosgiel), which only processes beef material.
28. Farm Brands also sells finished rendered products, including MBM, blood meal, and inedible tallow produced at its own processing facilities and at third-party facilities (including Wallace).

Keep It Clean

29. KIC is involved in the collection and rendering of animal materials. It operates a rendering plant in Dunedin, at which it processes mainly deer material, casualty stock and shop waste collected from butcheries, supermarkets, home kill operators and small meat processors. It also operates a specialist bone rendering plant and supplies finished rendered products, including MBM, deer meal and inedible tallow.

Other rendering parties

Value Proteins Limited

30. Value Proteins operates a rendering plant at Lake Haupiri on the West Coast. It processes deer and sheep material (including sheep material from Alliance Group Limited's Nelson plant) and some beef and casualty material []. It also supplies finished rendered products: MBM, deer and sheep meal.

ANZCO Foods Limited

31. ANZCO operates a rendering plant at Seafield (near Ashburton). This plant has two lines that are currently used for processing in-house beef and sheep material, as well as animal material from other ANZCO plants in the South Island. ANZCO produces sheep and beef/mixed meal as well as tallow. In the past, ANZCO has also used its processing capacity for third-party material. Previously ANZCO also rendered casualty material but no longer does so.

Alliance Group Limited

32. Alliance operates rendering plants at Lorneville (Southland), Smithfield (near Timaru) and Pukeuri (near Oamaru). These plants are used for processing in-house beef and sheep material into finished products, including MBM and tallow. In addition, the Lorneville plant is used to process casualty material for a single customer (Slinkskins Limited).

Tegel Foods Limited

33. Tegel has a rendering plant in Christchurch, at which it processes in-house poultry material as well as animal material from Van den Brink Poultry Limited's plant near Christchurch. This material is made into poultry meal.
[]].

Other renderers

34. The other firms currently operating rendering plants in the South Island are Blue Sky Meats (N.Z.) Limited (Blue Sky Meats), which renders in-house sheep material at Morton Mains (Southland) into finished rendered products and Prime Range Meats Limited, which renders in-house beef, sheep and deer material into finished rendered products at its plant in Invercargill.

Customers*Toll processing*

35. Toll processing involves the meat processor paying a renderer a processing fee but retaining ownership of the material throughout the process. There is only one toll processing customer affected by this acquisition (Silver Fern Farms Limited-SFF). Farm Brands is in a [] year contract to process SFF's material in the South Island.

Direct collection

36. Direct collection customers include meat processors which supply their animal waste material to a renderer outright. These suppliers differ from shop collection in that they produce greater volumes of material which is typically streamed by species. The streaming means that the renderer is able to turn higher value raw material into higher value final products. Once the renderer has processed the material into finished products, it sells these products to domestic end users or export traders.

Shop collection

37. Shop collection involves the collection and rendering of animal material from small producers of waste. 'Shops' include:¹⁴
- 37.1 butchers and supermarkets that produce animal material from deboning carcasses, or trimming and preparing cuts of meat;
 - 37.2 home kill operators who kill animals on farms and then carry out the butchery of the animal at their own premises; and
 - 37.3 small meat processors.

¹⁴ Application at [7.116]

38. As the volumes of animal material produced by each individual customer are typically low, the material is picked up on a regular collection run. This material is not typically separated by species (although in some instances it is) and is generally processed on a mixed species line (which includes pork material). Not all shops rely on a renderer; in some instances the animal material produced is converted into pet food or 'small goods' which are sold in-store.

Casualty collection

39. Casualty material is produced seasonally and includes the bodies of calves, lambs and cows that die on a farm. The farmer typically has a choice to either bury the body (meaning it is not rendered) or organise a skinner to collect it. Once the skinner has removed the skins, it will then sell the carcass to renderers who render the material into finished product.

Overview of industry parties

40. Table 1 provides an overview of the current independent renderers in the South Island (ie, with the exception of Alliance, those that are not vertically integrated with a meat processor).

Table 1: Parties currently providing independent rendering services in the South Island

Party	Plant location	Rendering					Shop Collection	Casualty collection
		Beef / Mixed	Sheep	Pork/ mixed	Deer	Poultry /Mixed	Mixed species	Mixed species
Wallace	Hororata	-	-	✓	-	✓	✓	✓
Farm Brands	Washdyke, Timaru	✓	✓	-	-	-	✓	✓
	Silverstream, Mosgiel	✓	-	-	-	-	-	-
KIC	Dunedin	✓	-	-	✓	✓	✓	✓
Value Proteins	Lake Haupiri (West Coast)	✓	✓	-	✓	-	-	✓
Alliance	Lorneville (near Invercargill)	-	-	-	-	-	-	✓

Source: Industry participants.

How this merger could substantially lessen competition

41. We have considered two ways in which a merger between Wallace, Farm Brands and KIC could cause an SLC, namely:

- 41.1 selling markets – whether the merged entity could profitably raise the price¹⁵ of toll rendering services or finished products such as MBM or tallow above the level that would prevail without the acquisition; and
- 41.2 buying markets – whether the merged entity could profitably reduce prices paid in the collection and purchase of animal material below competitive levels.

Selling markets

42. Customers that currently have the option to purchase toll rendering services from two or more of the merging parties will have fewer options post-acquisition. Therefore, there is a potential that they would be faced with higher prices for these services. As a result, we have assessed how a toll rendering customer's options would likely be affected by the acquisition.
43. We have also considered whether the merged entity would be able to charge any domestic customers more for finished rendered products, such as mixed beef MBM and tallow.

Buying markets

44. A merger between buyers can result in an SLC if the merged entity has the ability and incentive to impose a quantity-reducing price decrease on its suppliers.
45. A reduction in animal material could result from reduced volumes processed, as shops or large processors divert animal waste to other markets (such as, for example pet food) or otherwise dispose of the material.
46. If a price reduction does not result in less material being supplied to the renderers no deadweight loss arises in the buying market. As such, we would not consider this price reduction to be indicative of an SLC.
47. We have assessed the options available to different groups of suppliers if they were charged for animal materials, their ability to reduce animal waste, and whether the merged entity would have the ability and incentive to charge for animal material waste collection.

With and without scenarios

48. To assess whether competition is likely to be substantially lessened in any market, we compare the likely state of competition with the acquisition to the likely state of competition without the acquisition.¹⁶

¹⁵ 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.

¹⁶ *Mergers and Acquisitions Guidelines* above n 1 at [2.29]; *Commerce Commission v Woolworths Limited* (2008) 12 TCLR 194 (CA) at [63].

With the acquisition

- 49. With the proposed acquisition, WGLP will acquire up to 100% of the assets and business of Wallace, Farm Brands, and KIC. This will include:¹⁷
 - 49.1 Wallace’s rendering plant and equipment at Waitoa and Hororata, the land and buildings or leasehold interest at those sites, and the rendering business, including the benefit of business contracts;
 - 49.2 Farm Brands’ rendering plant and equipment (that Farm Brands operates) located at Washdyke and Silverstream, the land and buildings or leasehold interest at those sites, and the rendering business, including the benefit of business contracts; and
 - 49.3 KIC’s rendering plant, equipment, the land and buildings at Abbotsford, Dunedin and the rendering business, including the benefit of business contracts.
- 50. In its application, WGLP advised that it plans to continue to operate each plant, although it will seek to concentrate the processing of certain species at single sites.¹⁸ WGLP proposes to continue to operate the Hororata plant as dedicated to rendering any animal material which contains pork. WGLP intends to operate the KIC plant as dedicated to rendering deer material.

[]

Without the acquisition

- 51. Without the acquisition, we consider that all three parties would continue to operate independently of one another. We have therefore compared the acquisition against this scenario.

[]

- 52. []¹⁹

- 53. [].

- 54. [].

¹⁷ Application at [3.2-3.5].

¹⁸ Application at [3.7 (b)].

¹⁹ [].

55. []:²⁰

55.1 []

]

55.2 []

]

55.3 []²¹

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[]

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56. []

].²²

57. []

].²³

58. []:

58.1 []²⁴

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58.2 []

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20 []
21 []
22 []
23 []
24 []

[]

]

58.3 []

59. [].

Market definition

Our approach to market definition

60. Market definition is a tool that helps identify and assess the close competitive constraints the merged entity would face. Determining the relevant market requires us to judge whether, for example, two products are sufficiently close substitutes as a matter of fact and commercial common sense to fall within the same market.
61. We define markets in the 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. What matters is that we consider all relevant competitive constraints, and the extent of those constraints. For that reason, we also consider products which fall outside the market but which still impose some degree of competitive constraint on the merged entity.
62. In general, the more closely substitutable two products are, the closer the competition and the greater the competitive constraint between the products.

The applicant's view on the relevant markets

63. WGLP has argued that the following markets are relevant for the present case:²⁵
- 63.1 direct collection of each of beef/mixed, sheep, pork/mixed and deer materials from producers in the South Island;
 - 63.2 the supply of toll rendering services to customers producing each of beef/mixed, sheep and deer materials in the South Island;
 - 63.3 shop collection of animal material in the Canterbury region;
 - 63.4 the purchase for rendering of casualty material from the Canterbury and Southland regions; and
 - 63.5 the sale of rendered finished products in New Zealand for MBM, blood meal, deer meal and inedible tallow.

Our view of the relevant markets

64. In line with our approach in the *Tuakau* decision,²⁶ we consider that the rendering industry is characterised by a series of buying and selling markets.

²⁵ Application at [6.47].

65. Toll rendering markets are selling markets which are defined according to the type of animal material, species, and customer location. The markets for finished rendered products are also selling markets.
66. Animal material which is collected by a renderer from shops, direct processors and casualty suppliers is purchased in a buying market and the relevant markets can be similarly defined according to the type of animal material, species and geographic location.
67. For the purposes of this application, on the buying side, we consider there to be:
- 67.1 separate beef, sheep, poultry and pork markets for the purchase of each animal's waste material from direct processors located in Canterbury (separately, the pork, beef, sheep and poultry direct collection markets);
 - 67.2 a market for the purchase of mixed animal material from shops located in Canterbury (the shop collection market); and
 - 67.3 separate markets for the purchase of mixed casualty material from skimmers located in Canterbury, Otago and Southland (the casualty collection markets in Canterbury, Otago and Southland, respectively).

Buying markets – direct, shop and casualty collection markets

68. For the purposes of this application, we consider the relevant collection markets to be the markets for:
- 68.1 the purchase of mixed animal material from shops located in Canterbury;
 - 68.2 the purchase of animal material from meat processors located in Canterbury, separately for each species, namely beef, sheep, deer, pork and poultry; and
 - 68.3 the purchase of mixed casualty material from skimmers located in Canterbury.
69. The geographic market boundaries of each of these markets depend on where the supplier of the animal material is located. In general, parties have confirmed that animal material is unlikely to be transported more than four hours as the material would start to degrade. Casualty material lasts longer than four hours as a whole carcass degrades more slowly than casualty material that has been broken down,²⁷ and direct collection only requires a single stop so on some occasions may be transported further than shop material. The parties overlap in the collection of shop, casualty and direct material in Canterbury.
70. We consider separate markets for each casualty supplier in Canterbury. This is because each casualty supplier has different alternatives for casualty material supply.

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

²⁷ Interview with [].

71. We do not consider that it is necessary to define narrower customer markets for direct collection or for shop collection despite customers have different alternatives to the merging parties and to rendering supply. This is because:

71.1 in direct collection, defining narrower customer markets does not alter the competitive analysis; and

71.2 Wallace submits it is not feasible to price discriminate between shops [].²⁸

Selling markets – toll processing

72. Apart from toll processing agreements reached between the merging parties, SFF is the only toll processing customer affected by the acquisition. Beef, sheep and deer material is toll rendered for this customer.²⁹

73. Farm Brands and SFF have a [] year agreement which is due to end in []. SFF expressed no concerns regarding the proposed transaction. It identified that it would have several options at the end of the term of this contract:³⁰
[

]. We have not considered these markets any further.

Selling markets – finished products

74. The merging parties overlap in the supply of various finished rendered products in New Zealand, namely MBM, deer meal, blood meal and inedible tallow. The relevant geographic markets are national, although somewhat differentiated as renderers which are closer to a domestic customer have a transport cost advantage.

75. The merging parties use animal material to produce finished goods which are then on-sold to traders and domestic end users. The majority of domestic purchasing of finished rendered products is carried out by intermediaries who aggregate all types of material from a number of suppliers and market it internationally and domestically. Domestic end users of finished rendered products are predominantly primary producers who utilise MBM in animal feed.

76. No concerns have been raised in relation to any finished rendered product market for MBM; blood meal; deer meal; and inedible tallow. The proposed acquisition would only result in limited overlap of some finished goods. For these products, the merging party would continue to face competition from other suppliers of finished

²⁸ Interview with Wallace (3 October 2016).

²⁹ SFF has all of its South Island beef and sheep material toll processed by Farm Brands. Farm Brands subcontracts to Value Proteins the deer and beef material from SFF's Hokitika plant. Farm Brands' contract with SFF also includes the deer material from SFF's Southland plants which is processed by KIC.

³⁰ Interview with SFF (19 August 2016).

rendered products, including AFFCO New Zealand Limited, SBT Marketing (2009) Limited, Wilson Hellaby Limited, Taylor Preston Limited, Alliance and Blue Sky Meats. The intermediaries and final customers we interviewed indicated that there were alternatives to the merging parties' products.³¹ We have not considered these markets any further.

Competition assessment

77. The proposed acquisition would result in aggregation of the merging parties' rendering operations in Canterbury. Each of the merging parties has a presence in a number of different buying markets in this region.
78. However, in all of the relevant markets, we consider the proposed acquisition is unlikely to have the effect, or likely effect, of an SLC. This is because:
- 78.1 in the majority of the affected direct collection markets, the merged entity would continue to be constrained by alternative suppliers. For the direct collection of pork, whereas in the past Farm Brands and Wallace competed against each other, Farm Brands has decided to stop rendering pork. As such, in both the with and without scenarios there would be only one plant in Canterbury which renders material containing pork;
- 78.2 in the shop collection market, the merged entity would likely be constrained from charging customers for collecting services as some of those customers would be able switch to an alternative outlet for their animal materials. This would risk impacting the renderer's processing volumes (where economies of scale are a key facet of the rendering business) such that any input cost savings achieved would likely be outweighed by a consequent loss in production efficiency; and
- 78.3 in the casualty collection markets, given the location of the skimmers, there is limited existing competition between the merging parties and the relevant suppliers of casualty material would also have alternative rendering options.

Competition assessment – the direct collection markets

The direct collection of pork market

79. Direct pork collection involves the collection of pork material, or material that includes pork, from large meat processors or local abattoirs. There are only three meat processors who require direct pork collection services in the South Island:
- 79.1 Freshpork Bay City Limited (Freshpork), which operates a pork only processing facility in Timaru;
- 79.2 Harris Meats (Cheviot) Limited (Harris), which processes pork, beef and sheep at a facility in Cheviot (North Canterbury); and

³¹ Interviews with [].

- 79.3 Ashburton Meat Processors (AMP), which processes mainly pork but also beef and sheep at a facility in Ashburton.
80. Farm Brands holds the contracts to collect the material from all three of these meat processors. Since Wallace took over the Hororata plant in 2014, it has offered its services to all three of these customers. Although none of the offers were taken up by the processors, [] there was a degree of competitive constraint between Wallace and Farm Brands in this market). []³²
81. Despite holding the contracts for all three of the relevant processors, in 2015 Farm Brands made the decision to stop rendering pork material. It instead reached an agreement with Wallace to toll process all material containing pork at the Hororata plant. Farm Brands advised that this decision was due to a change in regulations that it was no longer possible to render pork material on the same line as MBM intended for Indonesia.³³
82. Farm Brands has advised that it would not be prepared to render pork at its plant in future, []³⁴ This is because the volume of pork is small and any additional revenues arising from the increased volume would not sufficiently compensate for the lower value of pork containing MBM or the increased risks of cross species contamination.³⁵ This is consistent with comments from other renderers. ANZCO, Alliance and Value Proteins all stated they would not render pork due to the devaluing of their finished rendered products and the risks of contamination.³⁶ We are therefore satisfied that, in the absence of the acquisition, Farm Brands would not impose a material constraint on Wallace for rendering pork.
83. Farm Brands told us that it would continue to bid for pork collection contracts when they became available, if Wallace's Hororata plant remained open.³⁷ However, given Farm Brands would rely on Wallace to render the pork material and so be exposed to a monopoly price for this rendering. Farm Brands is also unlikely to be able to collect this material significantly more efficiently than Wallace. As a result, the loss of the competitive constraint imposed by Farm Brands in the direct pork collection market

³² For example, the interview with []

³³ Letter from Farm Brands to the Commission (28 September 2016, "Farm Brands response to Commission") at [4] and [5].

³⁴ Letter from Farm Brands to the Commission (28 September 2016, "Farm Brands response to Commission") at [15].

³⁵ []

³⁶ Interviews with ANZCO (24 August 2016), Alliance (24 August 2016) and Value Proteins (29 August 2016).

³⁷ Interview with Farm Brands (3 October 2016).

is unlikely to be substantial.³⁸ That is, the price for direct pork collection is unlikely to be substantially different with or without the merger.

84. We also considered whether KIC might be a potential competitor for pork rendering. []. However, KIC has advised that it no longer processes pork, as it adversely affects the price of its finished goods.³⁹ [].⁴⁰ WGLP notes that KIC refused to accept material from Wallace during a downtime in March 2016.⁴¹ We are therefore satisfied that KIC does not impose a constraint on Wallace in the market for the direct collection of pork.

Direct collection of beef, sheep and poultry markets

85. The merging parties compete to a limited degree for the purchase of beef and sheep material from direct suppliers. Although these suppliers could not reduce their animal waste without incurring disposal costs, as a result of the large volumes of pork free animal material that each produces, they have identified a range of competitive alternatives. These alternatives include other renderers (eg, ANZCO and Alliance), rendering in-house, or sponsoring the entry of a new renderer.

86. The merging parties also compete to a limited extent for the collection of poultry material. Tegel is the only in-house renderer of poultry material in the South Island, rendering such material at its plant in Christchurch.

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87. Tegel expressed no concerns about the proposed acquisition []

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88. We conclude that the proposed acquisition would not be likely to cause an SLC in these markets.

³⁸ Wallace would have the ability and incentive to price up to the monopoly level to Farm Brands. Farm Brands does not have a competitive advantage in transport that would allow it to compete against Wallace while being charged monopoly toll-rendering prices.

³⁹ Interview with KIC (10 September 2016).

⁴⁰ Letter from KIC to the Commission (23 September 2016).

⁴¹ [] and Application at [7.109].

⁴² Interview with Tegel (6 September 2016).

Competition assessment – the shop collection market

89. Shop collection involves the collection and rendering of animal materials from small producers of material, including butchers, supermarkets, home kill operators and small meat processors. All three of the merging parties are involved to some degree in this market.
- 89.1 Farm Brands provides a collection service for butcheries, home kill operators, and small processors in the Canterbury region.⁴³ Farm Brands does not, however, process any of the animal material collected from shops due to the risk of pork contamination. All of the animal material collected by Farm Brands is toll processed at Wallace's Hororata plant.
- 89.2 KIC provides a collection service to butcheries, supermarkets, home kill operators and small processors in Canterbury, Otago and Southland. It does a run each Thursday collecting pork material from customers between Invercargill and Christchurch. KIC does not, however, render any pork material itself; the material is sold to Wallace for processing. KIC also does separate runs twice a week for non-pork shop material, which it processes itself.
- 89.3 Wallace has one truck for shop collection, which it mainly uses for home kill processors. Wallace also has an arrangement to pick up material from [] that are contracted with KIC. Wallace toll processes the material that Farm Brands collects and purchases the pork material that KIC collects.
90. Currently, Wallace is the only renderer of pork material. Farm Brands and KIC rely on Wallace to render all materials containing pork that either party collects. Like the situation in direct pork collection, Wallace would have the ability and incentive to raise prices for pork processing. As such, this acquisition is unlikely to substantially reduce the competitive constraint, compared to the scenario without the acquisition, for the collection of pork material from shops.
91. There is currently no significant overlap between the merging parties for the shop collection of non-pork material. Wallace has only a minimal involvement in shop collection and processing of non-pork material and this activity is confined to small processors and home kill operators. KIC is currently the only renderer of any significance of non-pork shop material. Farm Brands does not currently process material from shops, and has no intention of doing so given the high risk of pork contamination.⁴⁴
92. We have, however, considered whether the merging parties impose a constraint on one another for non-pork collection. We consider that Wallace would be able to offer a non-pork collection service to shops as Wallace currently provides some shop collection services for non-pork material in Canterbury and has previously undertaken shop collection in the North Island.

⁴³ Interview with Farm Brands (11 August 2016).

⁴⁴ [].

93. Farm Brands may also impose some constraint on KIC's non-pork collection service. If KIC raised the price of non-pork collection, a customer could instead choose to have it all collected by Farm Brands, which would also allow it to avoid the effort of separating out the material. Similarly, a customer of Farm Brands that faced a price increase could instead choose to separate out their pork and non-pork products and have that material collected by KIC.
94. However, to the extent that the merging parties may provide some competitive constraint on each other for shop collection of non-pork material, we consider that the merged entity would in any event be unlikely to significantly reduce price or impose a charge for the shop collection of non-pork material.
95. This is because rendering is a high fixed cost operation and so renderers have the incentive to maintain high volumes of material processed at their plants. Some shops have the option to divert animal material waste to pet food or other small goods items instead of incurring a collection cost, [].⁴⁵ If the merged entity sought to test the introduction of a price drop for its Canterbury customers it would risk permanent loss of volumes and therefore adversely affect the economics of its rendering operations.⁴⁶ We consider that any savings the merged entity would achieve by having lowered its input costs would be outweighed by the consequent efficiency loss in its production of finished product.
96. We take comfort that the merged entity would be unlikely to significantly change its terms through the observation that there are no collection charges even where there are monopoly collectors.
- 96.1 Tuakau Proteins has advised us that it does not charge for shop collection in the Auckland region where it is the only existing operator.⁴⁷
- 96.2 In the upper South Island, Mighty Mix, a pet food manufacturer, does a collection run for certain types of animal material and does not charge for collection, despite not facing any other rivals for the product.⁴⁸

⁴⁵ We conducted a survey of butcheries, home-kill operators and supermarkets in the South Island. That survey identified a number of shops which did not rely on a renderer at all. In such cases, the shop disposed of the majority of its animal waste by selling small goods and pet food instore. Of the shops that did rely on a renderer, some shops indicated that they would absorb any drop in price for the animal material (in some cases meaning the introduction of a charge), while others considered that they would reduce their reliance on the renderer by establishing alternatives to dispose of the material (either instore or via third party pet food manufacturers).

⁴⁶ There is some evidence to the contrary. KIC generally offers a free collection service []. Further, six shops claim that they switched to KIC when Farm Brands started charging them for waste removal. Farm Brands however advised that they have not charged for shop collection since 2009, which was when Farm Brands acquired South Canterbury By-Products. (Farm Brands' letter to the Commission (5 October 2016).

⁴⁷ Interview with Tuakau Proteins (10 October 2016).

⁴⁸ Interview with Mighty Mix (31 August 2016).

- 96.3 In Southland and Otago, KIC does a shop collection run but does not charge customers despite facing no other rivals in these regions.
97. Therefore, on balance and after taking into account the relevant factors, we do not consider that the proposed acquisition would be likely to cause an SLC in the shop collection market.

Competition assessment – the casualty collection markets

Casualty collection in Canterbury

98. There are three skinners with operations in Canterbury: Nichols (NZ) Limited (Hororata); Aztan NZ Limited (Hororata); and Slinkskins Limited (Waimate). The evidence suggests that Farm Brands and KIC may impose a degree of constraint on each other in this market.

99. Despite being located on the same site as Nichols and Aztan, Wallace does not appear to be a strong competitor in the market for casualty material.

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- 99.1 Nichols is the largest collector of casualty stock in Canterbury. Nichols supplies most of its animal material to Farm Brands as

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- 99.2 Aztan contracts with KIC to process the material it produces at Hororata.⁵¹

[
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- 99.3 Slinkskins contracts with KIC to process its Waimate material.

[
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100. WGLP has argued that the Canterbury casualty market is competitive and that each of the skinners identified above could switch to ANZCO, Alliance or Value Proteins.⁵³

101. Alliance appears to offer a competitive option for the material Slinkskins produces at its Waimate plant. Slinkskins has an existing arrangement with the Alliance plant in

⁴⁹ Application at [7.157].

⁵⁰ Interview with Nichols (19 August 2016).

⁵¹ Interview with Aztan (26 August 2016).

⁵² Interview with Slinkskins (30 August 2016).

⁵³ [].

Invercargill to toll process Slinkskins' casualty material from its Southland plants and has indicated that it views []⁵⁴
[]⁵⁵

102. ANZCO has processed casualty material in the recent past but has advised us that it has decided to stop rendering casualty material.⁵⁶ The main reason for this decision is due to the risks posed to the value of its exports of finished rendered products. []⁵⁷ We therefore do not consider that ANZCO is a close current or potential competitor.

103. Value Proteins operates a rendering plant on the West Coast. It currently renders casualty material for Slinkskins' West Coast skinning plant.⁵⁸
[]⁵⁹

104. Value Proteins has advised us that it has excess capacity and would be willing to accept more material from the Canterbury region, at a suitably priced rate. []⁶⁰
[]⁶¹].⁶² Based on the volumes of each skinner in recent years, we consider that Value Proteins has some excess capacity so skinners could credibly threaten to switch a portion of their material away from the merging parties. We consider that the potential loss of these volumes would likely be sufficient to deter the merged entity from substantially reducing the price currently paid to Nichols and Aztan for casualty animal material.

105. To conclude, we consider that the Canterbury skinners have alternatives that would impose a sufficient competitive constraint on the merged entity: Slinkskins has Alliance as an alternative, and Nichols and Aztan could threaten to switch a portion of their volumes to Value Proteins. As such, we do not consider the proposed acquisition is likely to cause an SLC in this market.

⁵⁴ Interview with Slinkskins (30 August 2016).

⁵⁵ Interviews with Aztan (26 August 2016) and Nichols (19 August 2016).

⁵⁶ Interviews with ANZCO (22 August 2016 and 15 September 2016).

⁵⁷ Interview with ANZCO (15 September 2016).

⁵⁸ Interview with Value Proteins (29 August 2016).

⁵⁹ []

⁶⁰ Email from Value Proteins (12 September 2016).

⁶¹ []

⁶² Interview with Aztan (26 August 2016).

Casualty collection in Southland and Otago

106. There are three casualty material suppliers located in Southland and Otago: Slinkskins (Southland); Aztan (South Otago); and Newton Slink Skins Limited (Southland). Although these suppliers could not reduce their animal waste material without incurring disposal costs, they did not identify the merging parties as close competitors and instead viewed Alliance (with its plant in Invercargill) as the next best alternative. As such it is unlikely that the merged entity would have the ability to charge for the collection of their animal material in these regions.

Determination

107. 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.
108. Under s 66(3)(a) of the Act, the Commerce Commission determines to give clearance to The Wallace Group Limited Partnership to acquire up to 100% of the assets and business of:
- 108.1 Wallace Corporation Limited;
 - 108.2 Farm Brands Limited, Farm Brands Asset Management Limited and South Canterbury By-Products (2009) Limited; and
 - 108.3 Keep It Clean Limited.

Dated this 19th day of October 2016

Dr Mark Berry
Chairman

