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COMMERCE COMMISSION

Decision No. 409

Determination pursuant to the Commerce Act 1986 in the matter of an application for clearance of a business acquisition involving:

PORTACOM NEW ZEALAND LTD

and

PORTABLE BUILDINGS LIMITED

The Commission: M N Berry
P R Rebstock
E C A Harrison

Summary of Application: The acquisition by Portacom New Zealand Limited of the business assets of Portable Buildings Limited.

Determination: Pursuant to section 66(3)(a) of the Commerce Act 1986, the Commission determines to give clearance for the proposed acquisition.

Date of Determination: 2 November 2000

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THE PROPOSAL

1. On 18 October 2000, the Commission registered a notice pursuant to section 66(1) of the Commerce Act 1986 (“the Act”), in which clearance was sought by Portacom New Zealand Ltd (“Portacom”) to acquire the business assets of Portable Buildings Limited (“PBL”). The business assets include fixed assets, hire contracts, fleet of portable buildings, intellectual property, and other items of plant and stock.

THE PROCEDURES

2. The notice was received and registered on 18 October 2000. Section 66(3) of the Act requires the Commission either to clear or to decline to clear a notice given under section 66(1) within 10 working days, unless the Commission and the person who gave the notice agree to a longer period. Accordingly, a decision is required by 2 November 2000.
3. The Commission’s decision is based on an investigation conducted by staff. In the course of the investigation Commission staff obtained information from a number of industry parties. These included:
 - Other suppliers of portable buildings for hire and sale:
 - Portable Buildings Limited
 - Rhino Portable Buildings
 - Hirecom
 - Modcom
 - Kiwi-Hire
 - Portabuild
 - Contract Coolstores
 - Hi-Tech Building Systems
 - Potential suppliers of portable buildings for hire and sale:
 - Panel-Tech
 - Insulated Commercial Environments
 - Long Insulation
 - Keith Hay
 - []
 - Micanta Construction
 - Purchasers and hirers of portable buildings:
 - Ministry of Education
 - Fletchers Construction
 - Hawkins Construction
 - Broadcast Communications
4. Commission staff also sought further information from the applicant.
5. The applicant did not request a confidentiality order.

THE PARTIES

Portacom New Zealand Ltd

6. Portacom is a wholly owned subsidiary of Waco International Ltd (“Waco”). Waco is a South African company listed on the Johannesburg Stock Exchange. It has a number of subsidiaries operating throughout the world although Portacom is the only one relevant to this application.
7. Portacom has been in the market since the late 1970’s. At that time the “Think Big” projects were creating demand for temporary on-site offices in remote areas. Portacom entered the market offering modular transportable buildings for hire or sale.¹ Its buildings are used for a variety of applications, but mainly as temporary offices. Portacom has offices located in Auckland, Hamilton, New Plymouth, and Christchurch.
8. The basic Portacom portable building measures 6x3 m. It has a steel box-like frame and “sandwich panel” walls.² The base will be made of wood or steel. The building is manufactured within a warehouse, then transported by truck, rail, helicopter, or barge to where it is required.

Portable Buildings Ltd

9. PBL entered the market in 1993. It is a privately owned company registered with the Christchurch branch of the Companies Office. PBL trades as Quickspace Portable Buildings.
10. Like Portacom, PBL manufactures portable buildings for hire and sale. It has no storage facilities north of Christchurch so mainly operates in the South Island. It does, however, have two North Island customers.

MARKET DEFINITION

Introduction

11. The purpose of defining a market is to provide a framework within which the competition implications of a business acquisition can be analysed. The relevant markets are those in which competition may be affected by the acquisition being considered, and in which the application of section 47(1) of the Act can be examined.

12. Section 3(1A) of the Act provides that:

“...the term ‘market’ is a reference to a market in New Zealand for goods and services as well as other goods and services, that, as a matter of fact and commercial common sense, are substitutable for them.”

13. Principles of market definition are contained in *Telecom Corporation of New Zealand Ltd v Commerce Commission*³, and in the Commission’s *Business Acquisition Guidelines*⁴ (“the Guidelines”). These principles are outlined below.

¹ On its website it proclaims itself to be the originator of relocatable buildings in New Zealand. See <www.portacom.co.nz>.

² Sandwich panels consist of polystyrene encased in Colour-Steel sheets. Sandwich panels are also used in making industrial coolstores and chillers.

³ (1991) 4 TCLR 473.

⁴ Commerce Commission, *Business Acquisition Guidelines*, 1999, pp 11-16.

14. Markets have three dimensions: product type, geographical extent and functional level. (In some situations it is also necessary to allow for time, and to consider a temporal dimension.) A market includes products that are close substitutes in the eyes of buyers, and excludes all other products. The boundaries of the product and geographical markets are identified by considering the extent to which buyers are able to substitute other products, or geographical regions, when there is an incentive to do so because of a change in relative prices. A market is the smallest area of product and geographic space in which all such substitution possibilities are encompassed. Within this space, a hypothetical, profit-maximising, monopoly supplier could exert market power, because buyers, facing a rise in price, would have no close substitutes to turn to.
15. A properly defined market includes products which are regarded by buyers or sellers as being not too different ('product' dimension, and not too far away ('geographical' dimension), and are therefore products over which the hypothetical monopolist would need to exercise control in order for it to be able to exert market power. A market defined in these terms is one within which a hypothetical monopolist would be in a position to impose, at the least, a "small yet significant and non-transitory increase in price" (the "*ssnip*" test), assuming that other terms of sale remain unchanged.
16. Markets are also defined by functional level. Typically, production, distribution and sale occurs through a series of stages, with markets intervening between suppliers at one vertical stage and buyers at the next.

Relevant Market

Product Market

17. The applicant has submitted that the area of activity that Portacom and PBL have in common is the sale and hire of modular portable buildings.
18. The standard portable building produced by the two firms measures 6x3 m. It has a steel or wooden base, a steel frame, and "sandwich panel doors". A unit of this type would sell for around \$9500. Although there are small design differences between the firms' respective products, in terms of functionality they are essentially the same.
19. The main demand for portable buildings would appear to be as temporary offices. For example, construction firms, such as Fletchers and Hawkins, use portable buildings on-site and will shift them to other locations as required. Firms might also use portable buildings while their main offices are being renovated.
20. A secondary demand is for portable buildings of a more permanent nature. Schools, for example, purchase portable buildings because they are quite cheap compared to more permanent materials, can be quickly constructed, and can be added to or shifted as required. Portable buildings are often placed next to warehouses to create more office space. Portable buildings are also purchased for use as a sleep-out or bach.
21. The Commission has considered whether other products could be considered close enough substitutes to be included in the market. For example:
- Firms such as Keith Hay Builders Ltd are known to make (what it describes as being) transportable buildings out of more conventional materials and using more traditional designs. These buildings include a toilet, office, and lunch area. These buildings,

however, cost around \$25,000 and are likely to be far in excess of what is required by a typical user of the Portacom portable buildings.

- It is understood that firms are offering converted shipping containers as temporary construction site buildings. These containers are understood to offer better security than portable buildings. Fletcher Construction has advised, however, containers are used for housing equipment rather than being used as offices, and are substitutable in few instances.
22. The Commission concludes that the above products are only likely to compete at the fringes of the market.
 23. Consideration was given to defining separate markets for “hire” and “sale” of portable buildings. From a demand-side perspective, the decision to hire or buy will depend on how long the firm requires it for.
 24. Industry sources have advised that the period in which firms start switching from hiring to buying is about 1-2 years. These firms could be considered the “marginal customers” for hiring and buying. Switching would occur among marginal customers if the relative hire/sale prices were out of sync. This would provide a constraint in a significant part of the market. The ability of a supplier to switch to and from hiring or selling a unit is also likely to ensure relative hire/sale prices remain constant. In any case, for reasons discussed below, the outcome of the competition analysis will be the same whether or not hire and sale are included in the same market. Accordingly, the Commission will consider hiring and buying within the same market.
 25. The Commission is aware that PBL currently supplies specialised equipment casing for the telecommunications industry. It is understood that presently Portacom has little or no presence in this market so no significant aggregation will occur.⁵ The Commission will not consider this market further.

Functional Market

26. The relevant functional market is that for the manufacture and delivery of portable buildings for sale or hire.

Geographic Market

27. The applicant has put forward arguments that the market is national in extent. It claims that the cost of transportation does not prohibit manufacturers of portable buildings from economically competing for contracts in different islands. Comments made from industry sources, however, tend to contradict this view. In general, the view is that transport costs of portable buildings are high relative to the value of the product, which significantly limits distances they can economically be transported.
28. Industry sources have advised that the transport cost for a standard 6x3 m unit would be around \$1500 to transport from Wellington to Christchurch, and around \$800 from Dunedin to Christchurch (each way). If the unit was priced at around \$9500, this would imply a hypothetical monopoly supplier in Christchurch could potentially raise their prices up to 8.4% while still having a cost advantage over Dunedin suppliers, and, similarly, up to 15.7% for North Island suppliers. This pricing discretion suggests the

⁵ In its application, Portacom has stated that one of its reasons of purchasing PBL is to raise its profile in this area of the market.

geographic extent of the market for sales, is either for each of the South and North Islands, or possibly even limited to regional markets.

29. The Commission has found little evidence of portable buildings crossing the Cook Strait. It is noted that PBL has had contracts for work in the North Island, which might suggest national markets. However, these contracts were for the (aforementioned) telecommunication industries. The products are relatively small and high value, and are not typical of a portable building in general use.
30. It is likely that the geographic market for the hire of portable buildings is narrower than for sales for two reasons. First, revenue gained for a hire contract will be less than for a sale, but the same transport cost applies. Second, in most circumstances, transport costs will have to be paid twice; that is, transporting the unit to the customer and transporting it back at the end of the contract.
31. The Commission has taken the conservative option and considered regional markets. This is on the basis that if no dominance is found in the narrower market, it is unlikely dominance exists in the wider market.
32. The only region where any substantial aggregation occurs is in Canterbury. In Dunedin, PBL has [] unit on hire and made [] sales in the last financial year. The Canterbury market, therefore, will be the only market considered.

Conclusion on the Relevant Markets

33. The Commission concludes that, for the purpose of analysing this application, the relevant markets are as follows:
 - The market for the manufacture and delivery of portable buildings for sale or hire in the Canterbury region (“the market”).

COMPETITION ANALYSIS

Introduction

34. Section 47(1) of the Act provides that:

“no person shall acquire assets of a business or shares, if, as a result of the acquisition, -

(a) That person or another person would be, or would be likely to be, in a dominant position in a market: or

(b) That person’s or another person’s dominant position in a market would be, or would be likely to be, strengthened.”

35. Section 3(9) of the Act states that:

“For the purposes of sections 47 and 48 of this Act, a person has, or 2 or more persons that are interconnected or associated together have, as the case may be, a dominant position in a market if that person as a supplier or acquirer, or those persons as suppliers or acquirers, of goods or services, is or are in a position to exercise a dominant influence over the production, acquisition, supply or price of goods or services in that market...”.

36. Section 3(9) also states that a determination of dominance shall have regard to:

(a) The share of the market, the technical knowledge, the access to materials or capital of that person or those persons:

(b) The extent to which that person is, or those persons are, constrained by the conduct of competitors or potential competitors in that market:

(c) The extent to which that person is, or those persons are, constrained by the conduct of suppliers or acquirers of goods or services in that market.”

37. In the Commission’s view, as expressed in its *Business Acquisitions Guidelines 1999* (page 17), a dominant position in a market is generally unlikely to be created or strengthened, where, after the proposed acquisition, either of the following situations exist:

- The merged entity (including any interconnected or associated persons) has less than in the order of a 40% share of the relevant market; or
- The merged entity (including any interconnected or associated persons) has less than in the order of a 60% share of the relevant market, and faces competition from at least one other market participant having no less than in the order of a 15% market share.

38. The test for dominance has been considered by the High Court. McGechan J stated⁶:

“Dominance includes a qualitative assessment of market power. It involves more than ‘high’ market power: more than mere ability to behave ‘largely’ independently of competitors: and more than power to effect ‘appreciable’ changes in terms of trading. It involves a *high degree of market control*.”

This test was approved by the Court of Appeal⁷.

39. The Commission acknowledged this test in its *Business Acquisition Guidelines 1999*, where it stated that:

“A person is in a dominant position in a market when it is in a position to exercise a high degree of market control. A person in a dominant position will be able to set prices or conditions without significant constraint by competitor or customer reaction⁸”.

40. The Commission’s role in respect of an application for clearance of a business acquisition is prescribed by the Commerce Act. Where the Commission is satisfied that a proposed acquisition would not result, or would not be likely to result, in an acquisition or strengthening of a dominant position in a market, the Commission must give a clearance. Where the Commission is not satisfied, clearance is declined. This test is applied in the following analysis.

⁶ *Commerce Commission v Port Nelson Ltd* (1995) 5 NZBLC 103, 762 103, 787 (HC).

⁷ *Commerce Commission v Port Nelson Ltd* (1996) 5 NZBLC 104, 142 104, 161 (CA).

⁸ *Business Acquisition Guidelines 1999*, p 21.

The Market for Manufacture and Delivery of Portable Buildings for Sale or Hire in the Canterbury Region

Market Concentration

41. An examination of market concentration may give a useful indication of whether a merged firm may be constrained by other participants, and thus on the extent to which it may be able to exercise market power.
42. The applicant has submitted that it would have around 51% of the national hire market while PBL would have around 2%. This would give the merged entity a market share of 53%. This was based on the applicant's estimates of each competitor's hire fleet. Commission staff enquiries have revealed these estimates to be reasonable. However, the Commission has defined narrower geographic markets. In particular, the Commission notes that Rhino Portable Buildings ("Rhino"), which is Portacom's largest national competitor, has little or no presence in the South Island.
43. For ease of analysis, market shares for hire and sales have been estimated separately. The combined entity's market shares in the Canterbury region are estimated below.

Table 1:

Estimated Market Share for the Hire of Portable Buildings in the Canterbury Region

Firm	Units on Hire	Market Share (%)
Portacom	[]	[]
PBL	[]	[]
Sub-total	[]	[]
Portabuild	[]	[]
Kiwi-Hire	[]	[]
Total	[]	100

44. As shown above, the combined entity's market share is very high. It is noted however, that this represents a "worse case scenario" for the combined entity. First, there is no figure estimated for "others" although it is likely that other small suppliers exist. For example, Fletchers has advised the Commission that during quiet periods it will hire out its spare units. Second, the market share figures are based on a conservative geographic market. Portacom and PBL hire out all their units only from Christchurch so extending the geographic market to include all of the South Island would lower their combined market share considerably.
45. For sales it is not meaningful to assess market share in terms of number of units as the size and shape of units can vary considerably. The best estimate for market share in sales is, therefore, likely to be based on revenue from sale.
46. Portacom and PBL had annual sales in the South Island of around [] and [], respectively. In the Canterbury region Portacom and PBL are the only makers of portable

buildings of substantive size. However, the Commission found it difficult to estimate the combined entity's market share as no industry sources were able to give an estimate of the size of the market. In particular, it is unclear how many small firms are making unbranded portable buildings as a non-core business activity. For example, it is known that Panel-Tech makes [] units per year and Insulated Commercial Environments ("ICE") makes around []. It is likely that other firms similar to these make portable buildings as a sideline business.

47. Notwithstanding the likely existence of other manufacturers of portable buildings, based on comments made by industry parties, it is possible the combined entity will have market share of up to []% in the Canterbury region for sales. The combined entity's overall market share, therefore, of both the hire and sale market is likely to be []%. Market share, however, is only one indicator of dominance and other factors must be considered before any conclusions are reached.

Constraint from Existing Competition

48. Kiwi-Hire is based in Rolleston, just outside Christchurch. Its main business is equipment hire and it regards hiring out portable buildings as a "sideline business". However, it has advised Commission staff that it could easily build up its hire fleet if demand was there. There are no impediments to obtaining materials, and labour could be sub-contracted. Kiwi-Hire believes it could build units at the rate of []. Kiwi-Hire has noted the design of its units are "very similar to Quickspace's (PBL's)".
49. Portabuild operates out of Sockburn, Christchurch. It entered the market in 1993 and currently has around [] portable buildings for hire, of its own construction. It has advised the Commission that it could []. In addition, although it does not make portable buildings for sale, this is only because it does not believe sufficient returns are currently available.
50. As mentioned above, some constraint is also likely to come from firms producing portable buildings as part of their non-core business activities.

Constraint from Potential Entry

51. The Commission considers that potential competition to the market, from new entry or expansion by existing market participants, can act as a constraint on behaviour in that market.
52. Industry sources have advised the Commission that barriers to entry are low. This is evidenced by the amount of entry shown around New Zealand in the last ten years. This includes PBL (1993, Canterbury), Portabuild (1993, Canterbury), Kiwi-Hire (1999, Canterbury), Rhino (1994, Auckland), Modcom (1998, Tauranga), and Hirecom (1999, Auckland).
53. In addition to recent entry, the Commission has identified a number of firms that are likely to be potential competitors to the market. These firms are outlined below.

Portable Buildings for Sale

54. Keith Hay Homes Ltd ("Keith Hay") is a nationwide supplier of prefabricated buildings. Currently, Keith Hay supplies "transportable buildings", although it has advised Commission staff that its buildings are designed more for medium to long term

requirements. It notes that a comparable sized building to a standard 6 x 3 Portacom unit costs \$26,600. This building has a toilet, office, and lunch area, and is made with timber frames and Hardie plank walls. This unit is considerably more expensive than the Portacom standard unit. Keith Hay, however, has advised Commission staff that [

].

55. Panel-Tech is based in Islington, just outside Christchurch. Its core business is making insulated industrial fixtures such as freezers and coldstores. It has advised the Commission that each year it makes [] portable buildings, similar in style to those of Portacom. It has further advised [

].

56. ICE operates in Belfast, Christchurch. It specialises in insulated industrial fixtures such as freezers and coldstores. It makes around [] portable building units per year. Most of its contracts come from firms that it has dealt with before that wish to remain “loyal” to ICE. [

]

57. Contract Coldstore operates out of Dunedin. It has [] units on hire in Dunedin and sold around [] units in the last financial year. It has noted that it is similar to PBL although does not specialise in portable buildings. At present it does not compete in Christchurch as it considers that, in general, transport costs prohibit it from being cost competitive. It has advised Commission staff, however, that [

].

58. Rhino Portable Buildings (“Rhino”) is another possible entrant. It is based in Auckland and has turnover of [] comprising of revenue from sale and hire. Currently, it competes only in the North Island although []. Rhino had an office in Christchurch up until 1997. If prices were to rise it is possible that Rhino could re-enter the market offering sales and hire.

59. A further threat to the combined entity is likely to come from firms outside the region “cherry-picking” contracts. The Commission understands that for a reasonable sized contract in (say) Christchurch, firms outside the region will tender for them with the intention of employing subcontractors in Christchurch to build them. A representative of firm might be sent down to supervise the operation and to ensure quality control.

Portable Buildings for Hire

60. In terms of hire, the most likely new entrant is []. []. It has expressed strong interest in entering the market for hire of portable buildings, as it believes portable buildings will complement its other range of goods. [

]

Conditions of Entry

Establishing a Plant

61. A small outlay is required to establish a manufacturing plant. This would include renting a small warehouse, purchasing suitable tools, and hiring of labour. These requirements

are generic to many building/manufacturing firms so it is likely there would be a very small sunk cost component, if any, should a new entrant fail.

62. Industry sources have advised that up to 95% of the cost of a unit is variable. This includes labour and material. Given this high variable cost component, there are few economies of scale. This implies that there is no need to start on a large scale to be able to compete efficiently.
63. Some sunk costs may be incurred in establishing a hire fleet. Once the units have been built there is little that can be done with them if not on hire. To mitigate the risk a new entrant can operate a hire fleet as part of its non-core business activity.
64. As noted earlier, firms can cherry-pick contracts by employing sub-contractors to carry out the work for them. In this way, a firm can gain a presence in a region before entering the market with its own plant.

Brand Recognition

65. Both the brand names “Quickspace” and “Portacom” are well known throughout New Zealand. Portacom is a particularly strong brand, having been in the market since the 1970’s. Industry sources note that many customers refer to a portable building as “a portacom”.
66. The Commission, however, does not believe this would significantly inhibit a current or potential competitor’s ability to compete. Evidence from industry sources suggests that the market is price driven. In addition, the range of similar brand names to emerge over the last ten years (Portabuild, Portacabin, Hirecom, Modcom, Leisurecom) in New Zealand would also serve to mitigate the strength of Portacom’s brand name.

Countervailing Power of Purchasers

67. The ability to shift to alternative suppliers is likely to constrain the merged entity. For example, Hawkins and Fletchers are two users of Portacom portable buildings. Both firms have advised that they would be comfortable switching to new entrants or subcontracting a firm to build a unit, should the price rise unreasonably. Neither firm was concerned over the acquisition.
68. The Ministry of Education, did not express any concerns over the acquisition. It has advised the Commission that it has plenty of options in terms of classroom supply.

OVERALL CONCLUSION

69. The Commission has considered the likely impact of the proposal in the market for the manufacture and delivery of portable buildings for sale or hire in the Canterbury region. Although the merged entity is likely to have high market share it will face the following constraints:
 - Ease of expansion by current competitors;
 - Ease of entry by potential competitors; and
 - Countervailing power by purchasers.
70. The Commission considers these factors to be sufficient to allay any dominance concerns.
71. Having regard to the various elements of section 3(9) of the Act, and all other relevant factors, the Commission concludes that it is satisfied that the proposal would not result, or would not be likely to result, in any person acquiring or strengthening a dominant

position in the market for the manufacture and delivery of portable buildings for sale or hire in the Canterbury region.

DETERMINATION ON NOTICE OF CLEARANCE

72. Accordingly, pursuant to section 66(3)(a) of the Commerce Act 1986, the Commission determines to give clearance for the proposed acquisition by Portacom New Zealand Limited of the business assets of Portable Buildings Limited.

Dated this 2nd day of November 2000

M N Berry
Deputy Chair