

SUMMARY OF MAIN ISSUES

1. The application is redacted to the extent that it is not possible for Godfrey Hirst to effectively engage.
2. The confidentiality issues that existed in 2011 do not exist in the cooperative merger proposed in the application meaning there is no need for the level of redaction in the application.
3. The Application is anti-competitive with respect to the proposal to caveat Clive, Whakatu and Kaputone sites preventing their use as wool scourers.
4. No public benefit apart from savings to the applicants themselves is contemplated by the application. In particular: no R&D is contemplated; no extra value will be added to the wool; no innovation or new technologies are proposed.
5. The original 2011 application proposed to retain Clive as an emergency contingency site. This is missing from the present proposal and there is a very real and definite risk of interruption to Godfrey Hirst and Cavalier spinning and carpet manufacturing operations as a consequence. If not retained, Clive site should be divested with resource consents in place.
6. Is this proposal to create a monopoly even necessary – these are not failing businesses. CWH made a profit in excess of \$10M in 2012/13 and \$5M in 2013/14. The NZWSI scourers are reportedly close to capacity with the Whakatu site operating 24/7 for in excess of two years, only stopping for breakdowns, maintenance and public holidays.
7. The decline in the national sheep flock appears to be reducing and the statements that wool production will fall further are speculative.
8. The Application will mean the same capacity remains in the South Island after the merger, but will that capacity all contained in the same building.
9. The Application again suggests that there are many plants available in China that would compete for commission scouring. This is not true and most of the examples provided are set up to process fine merino wool rather than NZ coarse crossbred types. The very new Compass Wool Processors in Malaysia is vertically integrated to a NK Chemicals, a Singapore based wool grease processor and focus on high grease yielding Australian merino but state they would “consider” processing coarse carpet wool. CWP state on their website that they intend for 60-70% of their 45Mkg throughput to be 17-25 micron Australian merino with the balance made up of finer wool plus 26-32 micron crossbred but that coarse NZ types of 34-40 micron would also be “considered.”
10. The ability of overseas wool scourers to restrain CWH from increasing tariffs is grossly overstated. The Application claims that increases of 10-15% would make scouring wool in China or Malaysia viable however our research puts this number at closer to []%.
11. Scouring of NZ wool in Malaysia or China is not a viable alternative to NZ for NZ based carpet manufacturers for reasons of logistics, price and quality. Further, if it was it is likely that all further processing would follow resulting in the complete loss of the carpet industry from NZ including over 1000 existing production jobs nationwide.

12. The merged entity will be able to exercise market power not only by increasing price but also by reducing service levels – eg old scouring tariff included free freight in, free freight out, free storage, free single volume bleach, off season discounts. There will be no incentive to retain these. Overseas wool scourers don't provide this service level.
13. The NZWSI scour at Kaputone is the most environmentally friendly scour in NZ and the only one treating effluent to any degree. The Application proposes to remove and sell this effluent treatment plant which would result negative environmental impact at best, but possible damage to NZ's reputation as an environmentally responsible country.
14. We dispute the "quality benefits" CWH claim as a result of their innovation and plant modifications. We explained at the 2011 conference how the claimed improvement is more likely a result of a change mix in the wool types processed at Awatoto and Whakatu.

AUTHORISATION APPLICATION

4.5/4.6 Restructuring

It is proposed that the Whakatu, Clive and Kaputone site will each be sold with a caveat preventing its use for wool scouring. This is anti-competitive, particularly as it would remove the most likely alternative available sites for any party wishing to establish a wool scour, particularly in the North Island.

5.8 Overseas Industry Rationalisation

It should be recorded that the rationalisation of wool scouring in overseas markets, particularly Australia followed the relocation of downstream processing, mainly to China. This is not the case in NZ because we have two substantial carpet manufacturers who both require scoured NZ wool.

5.13 Adding Value to NZ Wool

The application suggests that this transaction would “enhance value within New Zealand’s wool industry by adding value to greasy wool grown in New Zealand.” This is patently untrue because wool scouring adds no value to wool other than the cost of processing. Rather, wool scouring is a critical and necessary step prior to further processing which does add true value to wool, over and above the cost of processing.

5.21 Chinese Scouring Capacity

The application emphasises how important volume is to wool scouring businesses. The application also suggests that Chinese wool scourers are a viable, efficient and quality alternative to NZ based wool scouring and then states that “the top 18 scour lines in China alone have a combined capacity of nearly twice New Zealand’s scouring capacity.” Given that there are only 7 scours in NZ it would appear that China’s scouring industry has a long way to go before becoming as efficient as NZ.

5.27 Economies of Scale

It is true that the merger would create economies of scale but there would be no incentive for the scourer to offer a more cost competitive service as a result because they will not have any competition. It is more likely that the scourer would retain these incremental cost improvements to increase their own profitability.

5.51/2 Selling the Clive Plant

It was considered important in the 2011 application that the Clive site be retained, partly as an emergency provision in the event that Awatoto or Timaru suffer a catastrophic event. What has changed so that this is no longer necessary?

5.56 Kaputone Rationalisation

The Kaputone scour is the only wool scour in NZ that treats its effluent prior to discharge. Whakatu, Clive, Awatoto and Timaru all send their waste to the municipal wastewater treatment

plant where it is mill screened then discharged to the sea. Given that each wool scour has an environmental loading equivalent to a town of approximately 20000 people it is clear that this transaction will have a detrimental environmental impact however there is not mentioned in the application or accounted in the economic analyses of benefits and detriments.

9.8 International Wool Production

The application states that NZ grows around 8% of the world's greasy wool. Whilst this might be technically true the more important statistic is how much of the world's greasy carpet wool is grown in NZ, understood to be over 50%. This is why we still have a viable carpet industry in NZ.

9.9 Overseas Scouring of NZ Greasy Wool

Overseas scouring will only ever be a viable option for wool that is not further processed in NZ and GH is unaware of any NZ wool ever being exported for scouring then returned to NZ. From a merchants perspective scouring NZ wool overseas would comprise significant additional risks and costs including;

- Lack of control.
- Additional packing (dumping) costs in NZ.
- Additional freight costs.
- Quality concerns.

9.10 Wool Summary

Again the application quotes percentages and suggests that greasy wool exports are increasing when the truth is that greasy wool exports have only slightly increased and the changing percentages are more the result of a decline in the total clip, effectively skewing the percentage numbers.

13.2 Confidentiality

The application records measures to be put into effect to protect confidential information between the merged entities shareholders however there is no such provision to protect the confidentiality of information concerning customers wool such as Godfrey Hirst from Cavalier.

15.16 Constraint from Overseas Wool Scours

The application records that 25% of NZ greasy wool is scoured in China and suggests this indicates the extent of competition that CWH faces from Chinese Scourers. This does not apply to wool that is further processed in NZ and creates the potential for GH to be unfairly constrained by a competitor owned monopoly supplier of an essential service.

15.20 Overseas Wool Scouring

GH has obtained indicative scouring rates from Compass Wool Processors however we are unable to compare these to those submitted by CWH due to this information being redacted in the application.

CWP have provided the following tariffs;

Scouring Tariff

- Batch Fee of US\$1,000.00 per scourment
- Scouring Tariff of US\$0.17/kg charged on the greasy weight.

This would suggest a 20000kg scourment would cost US\$5,250 or approximately NZ\$6,800 or NZ27c/kg which compares to a cost of around NZ32c/kg for processing in NZ.

In addition to the cost of scouring would be the cost of dumping and packing the greasy wool in NZ for export to Malaysia, approximately NZ\$ 2,200 or NZ9c/kg.

Also not disclosed is the fact that CWP can only pack 13.6T of scoured wool into a standard 20' container compared to 20T in NZ, meaning that two 20' or one 40' container will be required for onwards cartage compared to only one 20' container in NZ. The cost of this would be significant.

By our calculations the cost for GH to scour wool at CWP then return it to NZ equate to at least []/kg compared to NZ []/kg for processing in NZ. This provides the opportunity for CWH to increase scouring tariffs for the scouring of GH wool by []% before it would be viable for us to process overseas.

The more likely scenario is that GH would move all its manufacturing off shore and import our carpet back into NZ resulting in the loss at least 500 manufacturing jobs. Additionally, this would likely make it necessary, in order to remain competitive, for Cavalier to follow resulting in the loss of another 500 manufacturing jobs and an entire industry gone.

15.26 Chinese Wool Scouring Industry

Of the 10 Chinese wool scouring companies suggested by CWH at least 7 are specialist merino processors that will not process NZ crossbred wool.

15.30 Australian Scouring Industry

The demise of the scouring industry in Australia followed the relocation of the further processing to China. Essentially all the Australian wool had to go to China or another country anyway so there was no need for an Australian scouring industry. This is different to NZ in that there remains a strong carpet manufacturing industry, largely because NZ produces the best and the most carpet wool of any country.

The constant comparison of NZ wool and processing to Chinese and Australian is misleading because they are largely completely different fibres (merino vs crossbred wool) producing completely different products (apparel vs carpet).

19.1 Potential Competition

Decision 725 concluded that a price increase of 5-10% would likely result in a competitor entering the scouring market. This is unlikely, it would be much higher.

25.39 Sale of Surplus Plant

CWH state that they intend to sell the surplus plant from Clive and Timaru. This has not been the case previously and most plant has been scrapped for minimal value. What is different this time. Would they sell to GH? If not is this anti-competitive behaviour by a monopoly supplier.

25.59-25.63 Quality benefits

Quality benefits were disputed and dismissed by the Commission in 2011. Nothing has changed in the interim.

26.24 Increased Supply Risk

This appears to be a repeat of the 2011 application however the new application proposes to increase the supply risk by closing and selling the Clive site which was previously intended to be retained, in part as a contingency in the event of temporary or permanent interruption to processing at Awatoto or Timaru.

The potential to transport wool inter-island is very expensive and not an option in the event that the other island's plant is operating at capacity.

The ability to store greasy wool until the plant problem is resolved ignores the interruption this would cause to downstream processors manufacturing operations that rely on continuous availability of scouring services.

26.27 Pilot plant as contingency

The pilot plant capacity is so limited it should be disregarded as a contingency.

27 Interested Parties

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