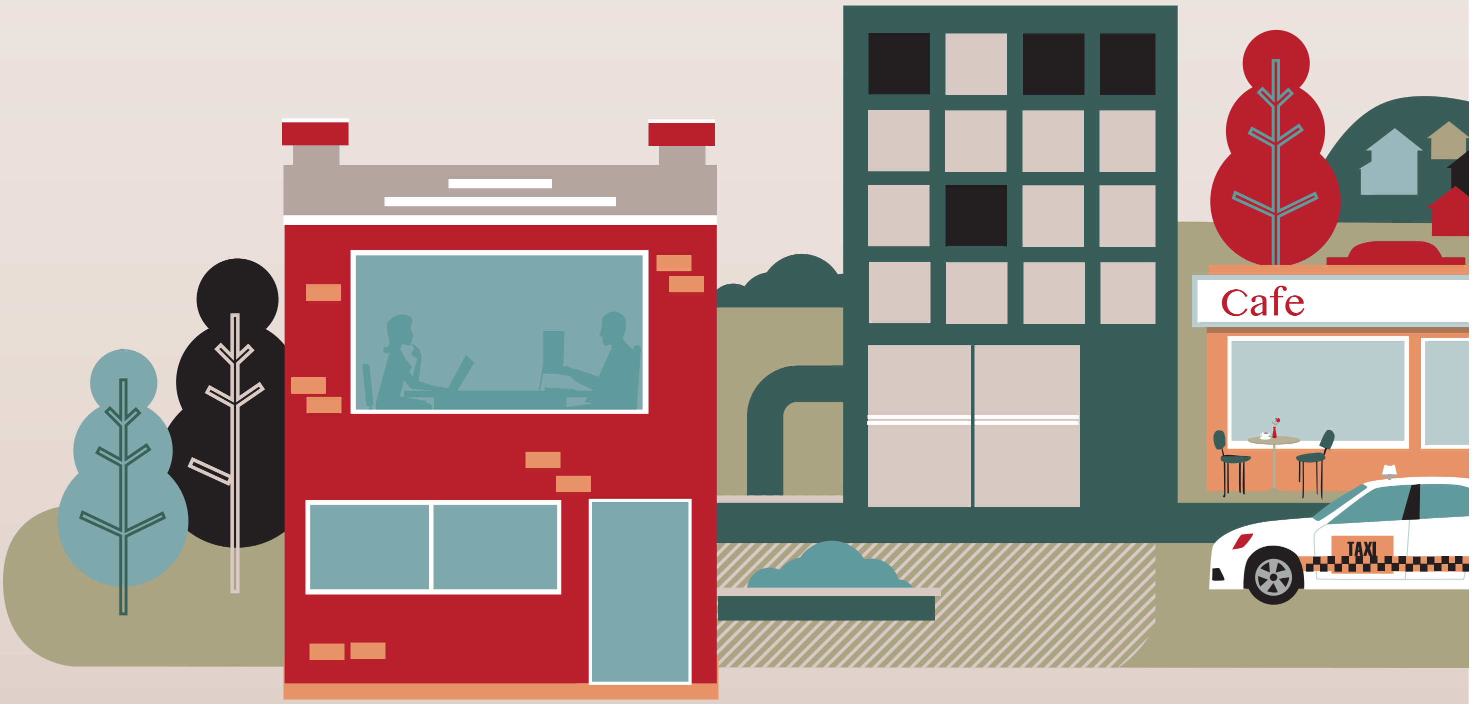
REPORT

COMMERCE COMMISSION
NEW ZEALAND
Te Komihana Tauhokohoko

2023/24

Ex-post merger review report



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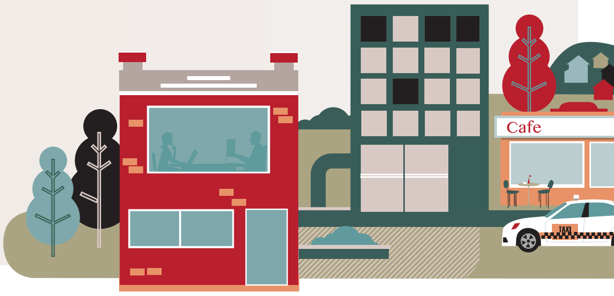

Executive summary

1 Effective merger control contributes towards New Zealanders receiving the benefits of competition, including greater value, innovation, productivity and choice. The Commerce Commission (the Commission) is responsible for preventing anti-competitive mergers which may harm consumers and New Zealand markets. A key indicator in the Commission's Statement of Intent: 2023-2027 is that harmful concentration of market power is prevented through merger control.[1]

2 Going forward we will undertake ex-post reviews of our merger decisions every two years and publish our lessons. The purpose of this is to identify meaningful trends and insights, contributing to the continual improvement of the merger regime.

3 The Commission has reviewed some of its merger decisions several times since 2015.[2] However, this is the first time we have published a report on our findings. Our report sets out three key insights:

3.1 the likelihood and extent of potential entry and expansion is commonly overstated by market participants;

3.2 market participants tend to overestimate the ability and likelihood of third parties to exercise countervailing buyer power; and

3.3 dynamic markets may require alternative analytical frameworks for defining relevant markets and assessing likely competitive effects.

4 These and other useful insights from the reviews are informing our current mergers work. We expect that the insights gained in these reviews will be valuable for the Commission's review of its Mergers and Acquisitions Guidelines, which is underway.

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1 Commerce Commission "Statement of Intent: 2023-27", pg. 36. Available at: https://comcom.govt.nz/__data/assets/pdf_file/0016/321721/Statement-of-Intent-2023-2027.pdf.

2 The Commission first undertook some ex-post reviews of past merger decisions in 2015, focussing on cases between 2011 and 2013. A similar exercise was undertaken in 2016, looking at merger decisions made in 2013 and 2014. The Commission renewed the practice in 2019 with a review of six merger decisions made between 2014 and 2016. This process was replicated in early 2023, looking at merger decisions made between 2017 and 2019.

Introduction to the report

5 Mergers and acquisitions can bring many benefits to the New Zealand economy by making it possible for firms to be more efficient and innovative.[3] However, some mergers also have the potential to lessen competition to the detriment of consumers.[4]

6 The purpose of the Commerce Act 1986 (the Commerce Act) is to promote competition in markets for the long-term benefit of consumers within New Zealand.[5] One of the ways it does this is by prohibiting any person from acquiring a firm's assets or shares if that acquisition would be likely to substantially lessen competition in a New Zealand market.[6] Under the Commerce Act merging firms can apply to the Commission for clearance or authorisation of a proposed merger.

7 When making clearance and authorisation decisions under section 66 or 67 of the Commerce Act, the Commission must make a forward-looking assessment of whether a merger is likely, or may be likely, to result in a substantial lessening of competition. Ex-post merger reviews observe what has happened in a given market following a decision. Understanding whether the predictions made in a decision about how markets will evolve and the strength of constraints on the merged entity have occurred can be a useful source of lessons, allowing us to amend our methods or continue good practice. Looking back at past merger decisions can therefore help the effective functioning of merger control going forward.

8 The reviews focused on specific key predictions made by the Commission, merging parties and/or third parties at the time of a merger assessment that influenced the decision. Therefore, instead of looking at one case in detail, the Commission reviewed several cases in this paper. In instances when the post-merger situation did not eventuate as predicted, we have sought to identify the reasons and to learn lessons on our approach to these issues, with the objective of improving future decision making processes.

9 The purpose of our ex-post merger reviews is not to determine whether the original decision of the Commission was correct or incorrect, compared to alternative decisions available to the Commission at the time. Instead, our reviews evaluate key factors of a decision and assesses whether the Commission's predictions have eventuated as expected.

3 The terms "merger" and "acquisition" are used interchangeably throughout this report.

4 Commerce Commission "Mergers and acquisitions guidelines" (May 2022) at [1].

5 Commerce Act 1986, s 1A.

6 Commerce Act 1986, s 47.

10 The cases that we selected across the two most recent reviews in 2019 and 2023 were:

Table 1: Case selection for 2019 ex-post review

Merger	Year	Industry	Decision
Mylan / Abbott EPD	2014	Pharmaceuticals	Cleared
Atlas Copco / Ash Air	2014	Industrial machinery	Cleared
Tuakau Proteins / Graeme Lowe	2014	Animal rendering	Cleared
Reckitt Benckiser / Johnson & Johnson	2015	Personal lubricants	Declined
Cavalier Wool Holdings / NZ Wool Services[7]	2015	Wool scouring	Authorised
Wallace / Farm Brands / Keep it Clean	2016	Animal rendering	Cleared

Table 2: Case selection for 2023 ex-post review

Merger	Year	Industry	Decision
Tronox / National Titanium Dioxide Company	2017	Titanium dioxide	Cleared
Trade Me / Limelight Software	2018	Motor vehicle advertising and DMS	Declined
Heinz / Cerebos[8]	2018	Table sauces	Cleared
Daiken New Zealand / Dongwha New Zealand	2018	Raw MDF panels	Cleared
Goodman Fielder NZ / Lion – Dairy & Drinks (NZ)	2018	Yoghurt	Cleared
Ingenico Group SA / Paymark	2018	Payment systems	Cleared
Fletcher Building / Waikato Aggregates	2019	Concrete sand	Cleared

7 We note that we were unable to finish our review of the Cavalier Wool Holdings/NZ Wool Services case.

8 We note that we were unable to finish our review of the Heinz/Cerebos case.

11 We consider the three key lessons that we can take from the reviews are:

11.1 **The likelihood and extent of potential entry and expansion is commonly overstated by market participants.** Further testing through written evidence (eg, internal documents) may be required to test whether stated plans to enter or expand are likely to materialise, including the timeframes within which this is likely to happen. Additional evidence may also be required in some mergers to assess the extent to which likely new entry (or exit) and expansion will constrain the merged entity.

11.2 **Market participants tend to overestimate the ability and likelihood of third parties to exercise countervailing buyer power.** This supports the need not only to understand the mechanisms that a customer might use to prevent price increases, but also how likely they are to use those mechanisms in practice to constrain the merged entity from increasing prices. Further testing through written evidence (eg, internal documents, examples of instances when countervailing power was successfully used) may be required to test the ability and likelihood of customers to exercise countervailing power post-merger.

11.3 **Dynamic markets may require alternative analytical frameworks for defining relevant markets and assessing likely competitive effects.** Given challenges created by using static analytical frameworks for purposes of assessing mergers in dynamic markets, in future the Commission may consider adopting alternative frameworks for the purpose of defining relevant markets and assessing the likely competitive effects in rapidly changing markets. There may be future cases where emerging consumer trends create new areas of overlap and/or remove previously competing products from a relevant market. The Commission is currently reviewing its Mergers and Acquisitions Guidelines to determine the importance that will be placed on market definition compared to competitive constraint in dynamic markets.

12 Our reviews have also identified several other insights in addition to these key lessons which are informing our current merger reviews and decision-making processes. We discuss these briefly at paragraphs 41-47 below.

13 While the purpose of this review has not been to assess the Commission's overall merger performance, most predictions made by the Commission in its decisions have borne out as expected.

Summary of approach taken to ex-post merger reviews

14 The Commission's focus when undertaking ex-post reviews is to determine whether specific factors in a decision, such as how markets have developed and the strength of constraints on the merged entity, have eventuated as expected. Our approach has been informed by the experience of overseas competition agencies, as well as best practice guidelines issued by the OECD.[9]

15 The evaluations do not seek to determine whether the Commission's original decision was 'correct'. We acknowledge that it is impossible to perfectly predict what might happen in the factual or counterfactual to the decision. Further, isolating and measuring the impact of a merger against all other factors that may have affected a market is not straightforward.

16 In determining whether a transaction is likely to have the effect of substantially lessening competition in any market, the Commission is required to take a forward-looking approach, asking whether there is a real and substantial risk, or a "real chance" that a substantial lessening of competition will occur as a result of the transaction. To be "likely", a substantial lessening must be more than a mere possibility, but it need not be more likely than not to occur. Should an effect that the Commission considered to be likely to occur, fail to occur (or fail to occur in the manner or within the timeframe predicted by the Commission), this does not necessarily suggest that the Commission was incorrect to have considered, at the point it reached its decision, that that effect had a real chance of occurring.

Case selection

17 In selecting cases to review and identifying the key questions, we selected those that we believed presented the most potential to learn lessons. We considered factors that were key to each decision which may have observable characteristics post-decision, or whether lessons relating to a particular factor (eg, potential new entry and/or expansion) would be particularly useful for future decision making. For example, we considered:

17.1 how easy it would be to test whether the Commission's assessment of the critical factor has borne out with hindsight;

17.2 the level of uncertainty around how the factor would likely evolve at the time of the decision; and

17.3 whether it would be particularly valuable to assess the effectiveness of the Commission's approach to assessing the factor.

18 Most of the selected cases, with the exception of Cavalier Wool Holdings/NZ Wool Services (authorised), Trade Me/Limelight Software (declined) and Reckitt Benckiser/Johnson& Johnson (declined) were cleared by the Commission. However, we consider the selected cases provide a broad spectrum of the merger work the Commission undertakes across a variety of markets. The selected cases also range in complexity and the markets and/or industries relevant to the merger, as well as how far through the clearance or authorisation process they went.

9 OECD "Reference guide on ex-post evaluation of competition agencies' enforcement decisions" (April 2016). Available at: https://www.oecd.org/daf/competition/Ref-guide-expost-evaluation-2016web.pdf.

Approach to conducting ex-post reviews

19 Having selected cases, reviewers then read the confidential version of decisions, looked at the underlying files, and where possible, spoke to relevant members of the case team to get a better understanding of key issues considered at the time of each acquisition and which parties would be best to interview. Based on these, two or three key questions for review were selected for each case.

20 The reviews in this report were conducted internally. While there are potentially benefits to conducting ex-post merger reviews using an external team, using an internal team enabled us to minimise confidentiality constraints and facilitated communication with the original case teams, while also ensuring the team has a strong understanding of the Commission's merger review process.

21 We sought to answer our questions by requesting information and interviews with relevant parties in each market and supplemented this with desk research where possible. Our goal was to answer our specific set of questions, while taking note of unexpected developments in the relevant markets.

Confidentiality

22 Alongside information obtained by the Commission at the time of the relevant mergers, ex-post reviews also rely on information provided by market participants on a voluntary basis. As much of this information is commercially sensitive to the interested parties, it is unable to be included in this report. This report provides a summary of the high-level findings and key lessons from our two most recent reviews conducted in 2019 and 2023.

Limitations of ex-post reviews

23 There are several practical and methodological challenges when undertaking ex-post merger reviews. The key limitations we have identified during our reviews include:

23.1 Markets are influenced by many factors, many of them unrelated to the merger, and it is not possible to accurately account for all of these.

23.2 We have not been able to interview or collect information from every relevant party in each market since participation in these reviews is entirely voluntary. We have also often had to rely on qualitative anecdotal information about changes in price and other parameters of competition such as quality and innovation.

23.3 The COVID-19 pandemic has affected all markets to some extent. This means that the effects of the mergers on competition may be distorted compared to what may have otherwise been expected. We sought to account for this to the extent possible.

Key lessons

24 The Commission's review of past merger decisions has provided useful insights for case teams and decision makers. The key lessons are summarised below.

The likelihood and extent of potential new entry and expansion is commonly overstated by market participants

25 In most merger cases, the conditions for entry and expansion are a focus for investigation as they are a key source of constraint on the merged entity. We must consider the likelihood, sufficiency and timeliness of entry and/or expansion to determine whether it would constrain the merged entity from exercising any market power that may result from the merger. While barriers to entry and expansion may not be conclusive in themselves, they commonly form part of the Commission's decision to clear, authorise or decline a merger.

26 The evidence that informs the Commission's assessment of barriers to entry and expansion often comes from market participants as assertions of strategic intent or opinion based on industry experience. A couple of the cases selected for review highlight the difficulty that may come from relying on what is largely anecdotal evidence on the ability and likelihood of potential new entry and/or expansion. We discuss this further below.

27 An issue the Commission is commonly faced with is market participants or potential entrants expressing interest in entering/expanding (or even re-entering) or, particularly in bidding markets, that they would likely participate in the next tender.

28 While the threat of publicly declared expressions of interest to enter and/or expand may have some effect on the merged entity's behaviour, even if actual entry and/or expansion does not eventuate, our review showed the importance of properly testing the credibility of such threats. Where such declarations are made, we will require additional written evidence (eg, internal documents) from potential new entrants and/or existing competitors that are intending to expand in the relevant market(s) to assess the likelihood, extent and timing of planned new entry and/or expansion.

28.1 For example, our review of the Ingenico/Paymark case showed that, while the merged entity was aware competitors likely had the intent and financial ability to develop rival payment switches, it does not appear to have considered this a credible threat. Market participants told us that the potential threat of rivals building alternative switches has not impeded Paymark's ability to impose significant prices increases on its rivals during recent renegotiations of wholesale and aggregation contracts. This suggests the threat of entry has not impacted Paymark's behaviour in ways the Commission expected at the time of the acquisition.

29 Our reviews also show that if intent to enter and/or expand is not declared publicly by firms and does not proceed past a mere expression of future interest, it is unlikely to have any material effect on the merged entity's behaviour. We therefore consider further verification of the actual ability and likelihood of competing firms to enter and/or expand beyond a mere anecdotal signalling of possible intent is appropriate in most cases, especially if it is being used by merging parties as evidence of potential entry/expansion that will materially constrain the merged entity.

30 When overseas firms consider potential entry and/or expansion into New Zealand, it is difficult for the Commission to verify the extent to which such threats are likely to materially affect the merged entity's behaviour.

31 An assertion of intent to enter and/or expand by an overseas entity may be relevant to a merger assessment, but in most instances the Commission is unable to accurately predict the ability, likelihood, extent and timing of such entry taking place. Political, regulatory and other structural factors can change entry and/or expansion conditions from the extent asserted by an overseas entity (or third party discussing the potential entry by an overseas firm) at the time of the decision.

31.1 For example, in the Tronox/Cristal case, our investigation did not place significant weight on the likelihood of entry and/or expansion of Chinese suppliers in New Zealand. However, the Chinese government's recent ban on construction of new plants producing sulphate titanium dioxide, historically considered inferior to chloride titanium dioxide in New Zealand, has led to Chinese suppliers switching production to the chloride process, thereby increasing volume of titanium dioxide available to New Zealand customers. The result was a greater degree of entry and/or expansion in New Zealand by Chinese manufacturers than was expected at the time of the merger.

32 In this instance the increase in supply of titanium dioxide by Chinese suppliers appears to have had a positive effect on competition in the market following the merger. However, it shows the difficulties involved in assessing the ability and likelihood of potential new entry and/or expansion by overseas firms. In the absence of written evidence on strategic intent from overseas firms to enter (eg, internal documents), we may reduce the weight we place on anecdotal evidence regarding the likelihood and/or ability by overseas firms to enter and/or expand into New Zealand where appropriate.

33 Finally, our review highlighted that in dynamic markets, or in markets where there is uncertainty about potential new entry and/or expansion, those factors and changing dynamics need to be taken into account when we are weighing up the likelihood of new entry.

Market participants tend to overestimate the ability and likelihood of third parties to exercise countervailing power

34 The ability of a merged firm to exercise increased market power may be constrained in situations where customers possess special characteristics that give them the ability to materially influence the price charged by the merged firm. For example, some customers may be in a position to discipline the merged entity by sponsoring entry or self-supply through vertical integration.[10]

35 Our ex-post reviews identified some instances where market participants at the time of the acquisition overestimated the ability and likelihood of customers to exercise countervailing power. For example, our review of Mylan/Abbott showed that the ability of Pharmac to exercise countervailing power to prevent price rises has been less effective than anticipated at the time of the merger assessment due to the discontinuation of tender processes in the relevant markets post-merger.

36 Countervailing power is difficult to assess due to the inherent complexity and intangibility of negotiations and bargaining power. Where appropriate we may seek to obtain additional information from relevant parties to not only understand the mechanisms that a customer might use to prevent price increases, but also how likely they are to use those mechanisms in relation to the relevant products affected by the merger.

10 In this regard we note that many merger applicants do not properly assess countervailing power in their submissions to the Commission but tend to focus their analysis on buyer power instead.

Rapidly changing markets may require alternative analytical frameworks for defining relevant markets and assessing likely competitive effects

37 Emerging consumer trends and technologies may create new areas of overlap and/or remove previously competing products from a relevant market in rapidly changing markets.

38 Our review highlighted the difficulty of assessing competitive effects in rapidly changing markets and the need to gather as much information and evidence as possible during the merger assessment to consider the potential effects of changing preferences. In some instances, emerging consumer preferences and trends may lead to the Commission's assessment of market definition and competitive effects at the time of the acquisition changing rapidly in the period post-merger.

38.1 For example, in Goodman/Fielder the Commission defined separate markets for mainstream yoghurt and Greek yoghurt. There was mixed evidence at the time on whether Greek yoghurt was its own market or part of the mainstream or non-mainstream (premium) yoghurt market. The Commission took a conservative approach and analysed the Greek yoghurt market separately, reasoning that if there was no substantial lessening of competition in the narrower Greek or mainstream markets, there was unlikely to be a substantial lessening of competition in a wider market.

38.2 However, our review shows that consumer preferences have changed materially in the period since the acquisition. The information we have received during our review suggests there are now more Greek yoghurt products overlapping with functional health premium yoghurts such as Greek non-fat/low-fat yoghurt, Greek probiotic yoghurt and Greek high protein yoghurt. This suggests that Greek yoghurt may now be considered as part of a wider premium yoghurt market, instead of a separate narrow market as defined during the Commission's original assessment. In this case the Commission's decision to clear the acquisition was not impacted by the decision to take a conservative approach to defining relevant markets. However, our review highlights the difficulties of assessing the likely competitive effects of an acquisition using a static market definition analytical framework that may not appropriately account for emerging consumer trends in rapidly changing markets.

38.3 In the Ingenico/Paymark case, while emerging alternative payment systems were not considered to be a significant constraint at the time of the decision, the Commission considered they may limit the merged entity's incentive to foreclose rivals post-merger. However, following the acquisition, these alternatives appear to exist as relatively complementary products to traditional payment systems rather than viable substitutes. This shows the appropriateness of exercising caution when placing weight on the potential competitive constraint of technology still in a relative stage of infancy.

39 There may be future cases where emerging consumer trends create new areas of overlap and/or remove previously competing products from a relevant market. Our reviews have identified the need for carefully considering market definitions in dynamic markets to determine how sensitive the competitive effects analysis may be to those definitions. It has also confirmed that, although market definition is a useful analytical tool, it may be appropriate to place more weight on competitive constraints when assessing mergers in dynamic markets. We may therefore seek additional evidence from relevant parties to support claims about future substitutes and/or constraints in dynamic market mergers.

40 The Commission is aware of the challenges involved in applying static analytical frameworks to mergers in dynamic markets. As part of its proposed review of its Mergers and Acquisitions Guidelines, the Commission will be reflecting on the relative weight that will be placed on static market definition compared to competitive constraint in dynamic markets.

Other lessons

41 We have identified further insights from our reviews which are of particular relevance to certain types of mergers and/or industries.

Purchasing and contractual mechanisms in market can be significantly affected by a merger or acquisition

42 Competition is often the driving force behind processes such as tenders, and an increase in the concentration of a market can significantly alter the dynamics of these processes. For example, our review of Mylan/Abbott shows that a market where contracts were tendered with two likely bidders pre-merger may see the tenders discontinued post-merger. This is because the sole remaining bidder (the merged entity) may no longer have an incentive to bid, with sole supply guaranteed. If this becomes an entrenched position in the market, it may prevent new entry by firms which would otherwise have been able to bid in a tender process.

Finite and/or natural resources may have a significant impact on several elements of competition

43 Our ex-post review of Fletcher Building/Waikato Aggregates identified that competitive dynamics in industries where market participants rely on finite and/or natural resources can be materially affected by competitors' differing abilities to access these resources. Given the relative scarcity of such resources, it may be difficult for new entrants to secure a foothold in the market. Furthermore, for existing market participants, they may be constrained by the natural limit of the resource they are able to extract.

Entry or expansion by retail brands into supermarket channels can be heavily dependent on available shelf space, which is often at a premium

44 Potential new entrants that sell retail grocery brands rely on obtaining supermarket shelf space to gain market share and constrain incumbent firms. However, our ex-post review of Reckitt Benckiser/Johnson & Johnson identified the difficulty of obtaining supermarket shelf space when considering whether competing lubricating brands would be able to expand to constrain the market leaders. When assessing the likelihood and extent of supermarket entry and/or expansion it should be considered that smaller retail brands attempting to enter or expand into supermarket channels will often struggle to do so unless there is an exit (or decline in market share) by an established brand or overall growth in the category (which would be expected to increase allocated shelf space).

Non-price theories of harm are becoming increasingly important

45 Non-price theories of harm, such as innovation impediment, are increasingly becoming a greater consideration for the Commission. For example, our review of Ingenico/Paymark showed that the merged entity's dominance in the switch-to-issuer (S2I) switching services market impeded the development of rival technology by other companies. Where appropriate, we may put greater emphasis on how a merger could affect both price and non-price dimensions of competition going forward. We expect that this approach will be flexible, and the appropriate weight given to each dimension will change based on the particular merger under review.

More weight could be placed on written evidence when there are multiple possible competitive counterfactuals

46 When there are multiple possible counterfactuals, more weight could be placed on written evidence (eg, internal documents) as opposed to other forms of evidence provided to the Commission to verify which one is most appropriate to consider. For example, our review of the Daiken/Donghwa case showed that the Commission received potentially conflicting written and narrative submissions on the most competitive counterfactual from the merging parties. We will consider in future cases placing more weight on written evidence when there are multiple possible competitive counterfactuals.

The existing frameworks for assessing vertical mergers may need to be updated in line with recent global developments

47 Our reviews have showed some inconsistencies in the type of evidence collected by the Commission to assess future ability and incentive of the merging parties to foreclose rivals in vertical mergers. While this is unlikely to have materially impacted the Commission's assessment of vertical effects in the mergers included in this review, we will be reviewing the existing framework used for assessing vertical mergers as part of our wider review of the Mergers and Acquisitions Guidelines.

Attachment: Summaries of ex-post merger reviews

1 The results of our reviews of selected cases differed in both detail and utility. On a number of cases, we found it difficult to collect evidence from a broad range of market participants so as to have a fully formed view of the state of competition following the relevant merger. Accordingly, we have set out summaries of five cases selected for review that we consider yielded the most beneficial lessons for the Commission's practice moving forward.

2 We note that our summaries in this section reflect market conditions at the time when each respective review was conducted. However, we acknowledge that this may no longer be accurate in some instances due to rapidly changing market conditions and the time that has elapsed since our reviews and publication of this report.

Tronox and National Titanium Dioxide Company

Commission decision

3 In June 2017, Tronox sought clearance to acquire the global assets of the National Titanium Dioxide Company's (Cristal) titanium dioxide business. Following the acquisition, the merged entity would become the largest supplier of chloride titanium dioxide (C-TiO2) in the country.

4 The acquisition reduced the number of established suppliers of titanium dioxide in New Zealand from three to two, with Chemours the other supplier on a large scale. The Commission concluded that, while the acquisition would result in an increase in market concentration, it was unlikely to substantially lessen competition for the following reasons:

4.1 the merged entity would continue to face considerable constraint from Chemours and other smaller suppliers following the acquisition;

4.2 potential entry and/or expansion of other titanium dioxide producers;

4.3 limited ability and incentive to foreclose competing manufacturers from accessing titanium dioxide inputs; and

4.4 no material enhancement in ability of industry participants to coordinate.

Ex-post findings

5 Our ex-post review of this case involved interviews with competitors and one customer, focusing on two key questions:

5.1 whether Chemours had continued to constrain the merged entity; and

5.2 whether other competitors demonstrated an ability and/or willingness to enter or expand in the titanium dioxide market since the acquisition.

6 While market participants indicated that most suppliers had increased prices in relatively small and steady increments following the acquisition, they noted that this was a consistent trend prior to the acquisition as well and none considered the price rises unreasonable. Furthermore, the significant increases in freight costs, blamed on the COVID-19 pandemic, had required suppliers to increase prices to cover these.

Has Chemours remained an effective competitor to the merged entity in the titanium dioxide market?

7 All parties interviewed indicated that Tronox and Chemours continue to be the main suppliers of titanium dioxide in New Zealand and compete with one another to provide the best quality product for customers. Large customers will tend to spread purchases across multiple suppliers, typically the merged entity, Chemours and one of the smaller suppliers.

Have other competitors demonstrated an ability or willingness to enter or expand in the New Zealand market since the acquisition?

8 When considering potential entry/expansion, the Commission placed greater weight on expansion of large global suppliers with small New Zealand presence rather than greenfields entry. Given the relatively small size of the New Zealand market, it was unlikely to require significant product diversion from other overseas markets to capture the bulk of New Zealand sales.

9 Market participants told us that, following the acquisition, several manufacturers had increased their presence in New Zealand. However, rather than Kronos and Venator (the suppliers the Commission considered most able and likely to expand at the time of the acquisition) expansion had come from Chinese suppliers. We were told that this was the result of several factors, being:

9.1 a decrease in China’s domestic demand due to enforcement of COVID-19 restrictions;

9.2 greater focus on supplying the global market; and

9.3 a general improvement in the quality, performance and consistency together with a ban on construction of new sulphate titanium dioxide plants.

10 While the Commission was aware Chinese production of chloride titanium dioxide had been improving prior to the merger (it historically focused on production of sulphate titanium dioxide, generally considered to be of lesser quality), the change of focus coming with the ban on new sulphate plants, and the effects of COVID-19 on demand in global markets were unexpected market developments that resulted in Chinese suppliers increasing the volume supplied to New Zealand customers.

Mylan/Abbott

Commission decision

11 In October 2014, Mylan sought clearance to acquire Abbott EPD, thereby merging the activities of Mylan and Abbott EPD in the New Zealand pharmaceutical markets. Mylan is a global pharmaceutical company that imports and distributes a range of off-patent (eg, generic) pharmaceutical products in New Zealand through its subsidiary, Mylan NZ Limited. Abbott is a global healthcare company that, prior to the acquisition, imported and distributed a range of patented and off-patent pharmaceutical products through its subsidiary, Abbott Laboratories NZ Limited.

12 In New Zealand, the supply and funding of most prescription medicines is controlled by the Pharmaceutical Management Agency (Pharmac). The verapamil market consists of several different products and regular tenders are held by Pharmac where parties can bid to win three-year contracts to be the sole supplier of the relevant product. To bid at these tenders, parties must have registered (or be in the process of registering) the relevant product with the New Zealand Medicines and Medical Devices Safety Authority (Medsafe).

13 In 2014, Mylan and Abbott EPD were the only registered suppliers of verapamil products in New Zealand, and therefore the two most likely bidders in future tenders. This raised the prima facie concern that the proposed acquisition would lessen competition in the verapamil market.

14 The Commission concluded that, while the acquisition would result in an increase in market concentration, it was unlikely to substantially lessen competition for the following main reasons:

14.1 potential entry in the form of another pharmaceutical firm placing a bid in one of the future tenders, therefore constraining Mylan in the bidding process; and

14.2 countervailing buyer power through Pharmac's potential ability to prevent price increases by Mylan.

Ex-post findings

15 Our ex-post review of this case involved interviews with Pharmac and a competing pharmaceutical firm. We also supplemented our review with desk research and information on pricing and tenders from Pharmac. Our review focussed on three questions:

15.1 whether another supplier has entered the New Zealand verapamil market;

15.2 whether the purchasing and contractual mechanisms have changed in the period post-merger; and

15.3 whether Pharmac's countervailing power has been able to constrain Mylan's prices since the acquisition.

Has another supplier entered the New Zealand verapamil market?

16 Market participants indicated that no competing firms had made any bids since the acquisition and that they had no plans to bid in future due to the declining profitability in the verapamil market. There appears to be no alternative suppliers to Mylan in the event of a price increase. However, in this regard it is worth noting that irrespective of the lack of new entry in the verapamil market, prices appear to have remained constant in nominal terms (and decreased in real terms) post-merger.

Are the purchasing and contractual mechanisms (eg, regular tenders) consistent with the Commission's understanding at the time of the acquisition?

17 During the original investigation the Commission's conclusions on the competitive impact of the proposed acquisition were made on the basis that regular tenders would continue to be held by Pharmac. However, as we now understand, there were no bids of any kind in the period 2014 to 2017. As a result, the tender process appears to have been discontinued and the existing supply contracts between Pharmac and Mylan are still in effect.

18 It therefore appears that Pharmac is in a weaker negotiating position than they would be if there were still regular successful tenders. The tender process itself is a reflection of competition in the market, as the prospect of competition for the market acts as one of the drivers for suppliers to bid for a sole-supply contract. Given this, it could be argued that the discontinuation of tenders in the verapamil market is in itself an indicator that there has been a loss of competition.

Has Pharmac's countervailing power been able to constrain price rises?

19 In the original decision, Pharmac appearing to have a large amount of countervailing buyer power was referenced by the Commission as one of the key factors that would constrain a potential price increase post-acquisition.

20 Information provided to us during our review shows that Pharmac has some countervailing power, but also that this power is not absolute. For example, it seems likely that a more aggressive pricing strategy from Mylan would have resulted in higher prices of verapamil products and that Pharmac would have been largely unable to prevent this.

21 However, it is worthwhile noting that ultimately, Mylan seems generally unwilling to engage in more aggressive pricing strategies in the small verapamil market given their dealings with Pharmac in larger pharmaceutical markets. It is noteworthy that despite limited possibility of entry into the market, the price of most products has not risen. This could in itself be considered a result of countervailing power.

22 However, the current equilibrium is slightly less stable than anticipated due to the discontinuation of the tender process. It is unclear what the outcome would be if Mylan changed their stance and attempted to take advantage of their monopoly position.

23 Additionally, it seems Pharmac might be more susceptible to supply-related price changes post-merger. Previously, these changes might have been partially absorbed by Mylan in an attempt to remain competitive. However, Mylan now has much less incentive to do so, and they may simply pass on price rises to Pharmac.

Reckitt Benckiser/Johnson & Johnson

Commission decision

24 Reckitt Benckiser and Johnson & Johnson are both global consumer goods companies that manufacture and sell a range of products into New Zealand markets. In May 2014, Reckitt Benckiser sought clearance to acquire the K-Y personal lubricant brand from Johnson & Johnson, thereby aggregating the Durex and K-Y brands under RB's ownership. This was part of a worldwide acquisition of the K-Y brand.

25 Both brands included basic lubricants (normally for medical use) and enhanced lubricants (more expensive, associated with fun and adventure). Basic lubricants accounted for most of K-Y's sales, whereas enhanced lubricants accounted for most of Durex's sales. The Commission determined that the two New Zealand markets affected by this would be the wholesale supply of personal lubricant to supermarkets and pharmacy wholesalers.

26 In April 2015, the Commission declined to give clearance to the proposed acquisition. The Commission was of the view that there would not be enough existing competition to constrain the merged entity, and there was also limited chance of entry or expansion. Therefore, it considered the merged entity would be relatively unconstrained in both supermarkets and pharmacies post-acquisition.

27 The Commission also considered there was a real chance of K-Y remaining in the market absent the merger, whether supplied by Johnson & Johnson or a third party. Taking this scenario as the counterfactual, the acquisition would result in a significantly less competitive market in comparison.

Ex-post findings

28 Our ex-post review of this case involved interviews with the merging parties, five retailers and one competitor. We also supplemented our interviews with desk research. Our review focussed on two questions:

28.1 whether K-Y exited the New Zealand personal lubricants market and, if so, whether that exit was inevitable; and

28.2 whether other competitors have demonstrated an ability to expand in the respective markets since the acquisition.

Did K-Y exit the New Zealand personal lubricant market(s) and, if so, was that exit inevitable?

29 K-Y, as supplied by Johnson & Johnson, exited the New Zealand market sometime in 2016. K-Y disappeared from both supermarket and pharmacy shelves around this time. However, we note that K-Y has since reappeared in some pharmacies through parallel-importing from Australia. However, it is mostly available online, and its presence in brick-and-mortar pharmacies appears to be quite small.

Have the other competitors demonstrated an ability to expand in their respective markets?

30 The original investigation determined that the main existing competitors did not provide a significant constraint on Durex and K-Y for supply into the supermarket channel. The Commission determined that brand recognition was a significant hurdle that any expansion candidate would have to overcome. While fringe entry was possible with limited brand recognition, expansion would require a large investment in promotion and advertising to generate consumer awareness. Without a significant level of brand recognition and loyalty, it was considered very difficult for a small supplier to get their product stocked on supermarket shelves.

31 Our review established that Ansell have significantly expanded in the New Zealand market since the exit of the K-Y brand from supermarket channels. Market participants advised us that K-Y's exit created an opportunity for other brands to expand, as supermarkets tend not to stock more than two main brands in the lubricant category due to its small size. Therefore, it appears Ansell would not have been able to access their current amount of shelf space if K-Y were still available. It further highlights the importance of supermarkets as a gateway to suppliers gaining access to a market and expanding their market share.

Goodman Fielder/Lion

Commission decision

32 In June 2018, Goodman Fielder sought clearance to acquire the license and assets related to the manufacture and distribution of Yoplait yoghurt in New Zealand. Goodman Fielder New Zealand Limited (Goodman Fielder) is a manufacturer and distributor of a range of grocery products in New Zealand, Australia, and the Asia-Pacific region. It produces an assortment of yoghurt products under brands such as Meadow Fresh and Puhoi Valley.

33 Lion – Dairy & Drinks NZ Limited (Lion) is a beverage company that manufactures and distributes a range of non-alcoholic and alcoholic beverages in New Zealand, Australia, and the United States. Prior to the acquisition, Lion owned a licence from Sodiaal (formerly known as Sodima) to manufacture and distribute yoghurt under the Yoplait brand in New Zealand.

34 The Commission concluded that while the acquisition would result in an increase in market concentration, it was unlikely to substantially lessen competition for the following main reasons:

34.1 strong existing competition from Fonterra;

34.2 the existence of countervailing buyer power from supermarkets; and

34.3 low barriers to entry and expansion.

Ex-post findings

35 We received written responses from the merged entity and a competitor during our review. We also supplemented our review with desk research and informal reviews of the range of yoghurt products currently available online and in-store at supermarkets. Our review focussed on two key questions:

35.1 whether the Commission's original market definition is still appropriate; and

35.2 whether there has been new entry in the relevant yoghurt market(s).

Is the Commission's market definition still appropriate?

36 During the original investigation the Commission defined separate markets for mainstream yoghurt and Greek yoghurt. Mainstream yoghurt was characterised as plain or flavoured yoghurt that is sold in 1kg tubs and in packs of 6 or 12 "pottles". The main brands competing in this market were those of the merged entity and Fonterra's.

37 There was mixed evidence on whether Greek yoghurt was its own market or part of the mainstream or non-mainstream (premium) yoghurt market. The Commission took a conservative approach and analysed the Greek yoghurt market separately, reasoning that if there was no substantial lessening of competition in the narrower Greek or mainstream markets, there was not likely to be a substantial lessening of competition in a wider market. The main brands competing in this market were the merged entity's, Fonterra's, The Collective (Epicurean Dairy), and other smaller brands such as Cyclops.

38 Our review shows there are now more Greek yoghurt products possessing characteristics overlapping with functional health yoghurts such as Greek non-fat/low-fat yoghurt, Greek probiotic yoghurt, and Greek high protein yoghurt. There is also a limited range of Greek yoghurt products available in multipacks and pouches (considered characteristics of mainstream products), though this is relatively uncommon. This suggests that Greek yoghurt may now be considered as part of a wider premium yoghurt market, instead of a separate market as defined during the Commission's original assessment.

39 We also understand that the market for dairy free alternatives has grown significantly since the acquisition. While non-dairy products have historically been targeted at vegan and vegetarian consumers, more consumers who do not identify as vegan or vegetarian are buying non-dairy products. Reasons for this include:

39.1 consumers perceive non-dairy products to be healthier and better for the environment; and

39.2 consumers have a wider range of dairy alternatives. For example, plant-based milks include soy, almond, coconut, rice, and oat milk.[11]

40 Consequently, food companies are expanding their range of dairy-free products. Fonterra, as one example, has recently branched out into the non-dairy market.[12] In relation to yoghurt specifically, there are five brands of dairy free yoghurt currently available in supermarkets in New Zealand. Three of these brands were launched after the acquisition.

41 Overall, the Commission's original market definition does not appear to reflect the current dynamics of the yoghurt market. However, we consider it unlikely that an alternative market definition would have materially impacted the Commission's assessment of the overall state of competition in this case given that there has been no significant change to Goodman Fielder's estimated market share of the wider yoghurt market since the acquisition.

Has there been new entry in the yoghurt market since the acquisition?

42 The Commission also relied on the threat of new entry to act as a competitive constraint on the merged entity in the Greek yoghurt market. Entry into the Greek yoghurt market was considered to be relatively more straightforward than entry into the mainstream yoghurt market due to higher margins and a quickly growing market.

43 In the mainstream yoghurt market, the Commission found it unlikely that there would be new entry, or that that existing producers of non-mainstream yoghurt would expand into mainstream yoghurt. This is due to the low-margin, high-volume nature of the market which requires significant scale, shelf-space, and brand awareness. Due to the high barriers of entry into the mainstream yoghurt market, the Commission relied on existing competition from Fonterra to constrain the merged entity.

44 Our review identified that there have been several new entrants to the premium yoghurt market and dairy free yoghurt market since the acquisition. Existing competitors such as Fonterra and Epicurean Dairy have also expanded into these markets. In the mainstream yoghurt market, Goodman Fielder and Fonterra continue to produce the majority of mainstream yoghurt products.

11 https://www.newfoodmagazine.com/article/150352/the-rise-of-the-non-dairy-consumer/
12 https://www.stuff.co.nz/business/farming/129691125/fonterra-takes-first-step-into-nondairy-products

Ingenico/Paymark

Commission decision

45 Ingenico Group SA (Ingenico) was, at the time of the acquisition, a member of the Ingenico Group, based in France. It supplied electronic payment services including payment terminals, transaction routing, and digital payment services.

46 In April 2018, Ingenico, which has since been acquired by Worldline, sought clearance to acquire Paymark Ltd (Paymark), a New Zealand company owned by New Zealand's large four banks, whose primary business was to operate a 'switch' that routes electronic payment transactions from terminals to the relevant financial institutions (the Commission refers to this function as providing "switching services"). With the acquisition, Ingenico would remain a direct competitor against suppliers of terminals and digital payment services, while also providing switching services to those rivals.

47 A switch is a key intermediary in the payment system. It sends transaction information to the correct issuer or acquirer (depending on the type of transaction) so that the funds can be taken from the customer's account and delivered to the merchant. To build links, switch operators must first agree to commercial terms with the relevant issuer or acquirer. Importantly, Paymark remains the only switch that has links with all significant acquirers and issuers, and the only one that can process all switch-to-issuer (S2I) transactions in New Zealand.

48 The Commission considered whether the proposed acquisition would be likely to have the effect of substantially lessening competition by focusing on vertical effects, namely whether:

48.1 the merged entity would have the ability to prevent rivals from competing through having market power over switching services and a mechanism to raise rivals' costs; and

48.2 the merged entity would have the incentive to inhibit rivals from competing because it would gain more profits in the terminal market as a result of this conduct compared with the profits it would lose for switching services.

49 The Commission concluded that the acquisition was unlikely to substantially lessen competition for the following reasons:

49.1 the threat rivals impose from building an alternative network to process S2I transactions;

49.2 the threat that emerging technologies and other technologies that do not use S2I would impose on the merged entity; and

49.3 the ability and incentive of banks to protect competition in terminal supply.

Ex-post findings

50 We interviewed a competitor to the merging parties and an industry expert as part of our review. We also supplemented our review with desk research. Our review focussed on three key questions:

50.1 whether Ingenico has raised prices for its switching services since the acquisition;

50.2 whether rivals have subsequently created or augmented a switch that competes directly with Paymark; and

50.3 whether emerging technologies and other technologies that do not use S2I impose a constraint on the merged entity's ability and incentive to foreclose terminal rivals.

Did Ingenico raise prices for its switching services? If so, why?

51 Our review identified that Paymark remained with Worldline following Ingenico's sale to Apollo and was rebranded as 'Worldline' in September 2021. For simplicity, any reference to Paymark is to the Paymark business now operating as Worldline. As Ingenico's business was sold, Paymark is no longer both a provider of switching services and a supplier of rival terminals.

52 The major operators of switches in New Zealand are still Paymark, Verifone, and Windcave. Paymark remains New Zealand's only switch with links to all significant acquirers and issuers. Paymark's position means that Windcave, Verifone and all potential new entrants into the payment systems market (particularly terminal providers), must negotiate a connection with it.

53 We understand a number of acquirers that are not banks have attempted to enter the terminal market since the acquisition, but have been offered unsustainable terms by Paymark, both in relation to price and time taken to certify terminals. Other stakeholders also consider that Paymark's dominance is impeding innovation.[13]

54 Following the acquisition, the number of issuer links has consolidated, particularly for scheme gift cards (which use S2I processing). This means a rival switch do not need as many links to build a viable switch as originally anticipated at the time of the acquisition.

55 At the time of the acquisition the Commission's primary concern was whether the transaction would be likely to give Ingenico the ability and incentive to inhibit rival supply terminal suppliers from competing by raising the cost of switching services (foreclosing rivals). Information provided to us during the review suggests that the price competitors pay to use Paymark's services has increased considerably in the years following the merger. We also understand that following the acquisition, Paymark raised its monthly merchant administration service fees by a significant amount.

56 On balance, it appears that while prices have increased, these may be justified (at least to some degree) by investments in technology. It is also important to note that one of the significant price increases took place before the acquisition was complete.

Did rivals create or augment a switch that competes directly with Paymark?

57 During the investigation the Commission considered that the merged entity would be limited in its ability and incentive to attempt to foreclose rivals if such conduct would be likely to encourage rivals to build an alternative network. The Commission noted that if rivals did so, the merged entity would stand to lose profits significantly and permanently from both terminals and switching services.

58 The information we received during the review suggests the challenges of building a rival switch considered by the Commission at the time of the acquisition have impeded plans by rivals to build an alternative network following the merger. While the banks' willingness to engage with potential rival switches may have improved, the Commission may have underestimated the time and costs of constructing a rival switch.

59 The Commission also considered that if competitors had a credible threat of building an alternative network, this would motivate Paymark to offer reasonable terms on the wholesale and aggregation agreement. However, it appears that Paymark may not have considered the threat of rivals building their own links as credible. Paymark appears confident in its position, and, regardless of plans by rivals to develop alternative switches, was acutely aware of the barriers they would face. Therefore, threat of entry hasn't impacted Paymark's behaviour in ways the Commission considered it might. Furthermore, other rival and developing technologies do not seem to have had a significant impact on Paymark's advantage in S2I transactions.

13 https://www.mbie.govt.nz/dmsdocument/15074-retail-payment-system-summary-of-submissions-and-initial-decisions, at paragraph 41.

Did emerging technologies and other technologies that do not use S2I impose a constraint on the merged entity's ability and incentive to foreclose terminal rivals?

60 Lastly, the Commission considered the extent to which the growth of competing payment technologies that do not use S2I processing, including new technologies and innovation in existing ones, could affect the merged entity's ability and incentive to foreclose terminal providers. It considered that emerging technologies could affect the merged entity's position in two ways:

60.1 developments that lead to a shift to payment solutions that use switch-to-acquirer (S2A) processing (such as Apple Pay and mobile wallets); and

60.2 new technologies that bypass a switch technology altogether (such as Alipay and We Chat Pay, or developments in open banking APIs).

61 The Commission considered that S2I would continue to be important in the immediate future, and that emerging technologies were unlikely to be a significant part of the market in the short term. However, the Commission did note that raising costs of rivals such that merchants face higher prices and/or degraded quality would likely encourage some degree of substitution to alternative payment types. Therefore, the perceived threat of these alternatives was considered likely to impose some degree of constraint from outside the market on the merged entity's ability and incentive to foreclose rivals in the terminals market.

62 Our review shows that the COVID-19 pandemic has accelerated contactless card payments (which use S2A processing). From 2018 to 2020, the use of contactless payments increased by 62%.[14] This was assisted by some acquirers waiving contactless acceptance fees for merchants during initial COVID-19 restrictions.

63 Market participants consider that while the volume of S2I transactions as a proportion of total transactions has fallen since the acquisition, this has not reduced to a point where S2I is unimportant. While there is a slow decline in domestic EFTPOS usage, it remains a necessity, and there may be a "revival" of EFTPOS in a recession period. This is particularly so given EFTPOS transactions do not incur a merchant service fee in New Zealand. Furthermore, even with payment options increasing, none appear to have impacted EFTPOS' importance. This is consistent with the Commission's conclusion at the time of the acquisition that although reliance on S2I is likely to reduce in future, emerging technologies would not fully replace 2SI.

64 As a merchant, what matters most is being able to accept any and all means of payment. Given the cost, time and effort required to establish a switch with wide coverage and links to the major banks, we consider it unlikely that any potential rival switches will constrain the merged entity to a significant extent in the foreseeable future.

14 https://www.paymentsnz.co.nz/resources/articles/new-zealand-payments-stats-2020-in-review/.

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