ISSN NO. 0114 - 2720

COMMERCE COMMISSION

DECISION NO. 306

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

GUINNESS PLC

and

GRAND METROPOLITAN PLC

The Commission: Alan Bollard
Peter Allport
Roger Taylor

Summary of Proposal: The merger of Guinness plc and Grand Metropolitan plc and the creation of a new company, GMG Brands plc.

Determination: Pursuant to s66(3)(a) of the Act, the Commission determines to give a clearance for the proposed acquisition.

Date of Determination: 8 September 1997

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MEMORANDUM

To:	Alan Bollard Peter Allport Roger Taylor
From:	John Preston Jane Chilcott
Date:	8 September 1997
Subject	**Business Acquisition: Guinness plc/Grand Metropolitan plc/GMG Brands plc**

Working Day 10: 8 September 1997

Confidential information in this report is contained in square brackets.

THE PROPOSAL

1 On 25 August 1997, the Commission registered a notice from Guinness plc ("Guinness") and Grand Metropolitan plc ("Grand Metropolitan") for clearance to merge the two companies and create a new company, GMG Brands plc ("GMG Brands"). Clearance is sought in accordance with s 4(3) of the Commerce Act 1986 ("the Act") which extends the application of s 47 of the Act relating to business acquisitions, to acquisitions outside New Zealand which affect a market here. Neither Guinness nor Grand Metropolitan directly carry on business activities within New Zealand, but the merger will affect markets in New Zealand.

2 Implementation of the merger will take place in the United Kingdom where both companies are registered. Guinness shareholders will retain their shares in Guinness, which will be renamed GMG Brands, and will hold approximately 47.3% of the

issued ordinary share capital of GMG Brands. Grand Metropolitan shareholders will receive one GMG Brands ordinary share for each Grand Metropolitan share held, and will hold approximately 52.7% of the issued ordinary share capital of GMG Brands.

3 There are a number of other jurisdictions looking into the proposed merger, including the Commission of the European Communities, the United States, Canada and Australia. It is noted that the Commission of the European Communities issued a formal Statement of Objection in respect of the merger in August 1997. The European Commission concluded **[**

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THE PROCEDURES

4 Section 66(3) of the Act requires the Commission either to clear, or to decline to clear, a notice given under s 66(1) within 10 working days, unless the Commission and the person who gave the notice agree to a longer period. As no extension has been agreed, a determination is required by 8 September 1997.

5 This report concludes that staff are satisfied that implementation of the proposal would not result, or would not be likely to result, in any person acquiring or strengthening a dominant position in a market in New Zealand, and recommends that in terms of s 66(3)(a) of the Act, the Commission give clearance to the proposed acquisition.

THE PARTIES

Guinness plc (“Guinness”)

6 Guinness is involved in the production, marketing and sale of spirits and beers around the world. It is also involved in publishing and hotels. Through its wholly-owned subsidiary United Distillers Ltd (“UD”), Guinness owns a number of leading spirits brands including “Johnnie Walker” whisky, “Dewar’s” Scotch whisky, and “Gordon’s” gin. Through another wholly-owned subsidiary, Guinness Brewing Worldwide Ltd, Guinness brews “Guinness” Stout and a number of other beers including “Kilkenny Irish Beer”, “Harp” lager, and “Smithwick’s” ale. In New Zealand, the distribution of Guinness’ beers and UD’s spirits brands is handled by

Allied Liquor Merchants Ltd ("ALM").

7 Guinness does not currently have any direct business operations in New Zealand. However, UD, through its wholly owned subsidiary United Distillers (New Zealand) Ltd, had a presence in New Zealand until March 1997. **[**

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8 Guinness also has a 34% shareholding in Moet Hennessy SA, which produces champagnes and cognacs. The remaining shareholding is owned by LVMH Moet Hennessy Louis Vuitton SA, in France. Guinness and Moet Hennessy have established a number of joint distribution arrangements, but Guinness' rights and obligations under the various joint venture agreements are unaffected by the proposed merger.

Grand Metropolitan plc ("Grand Metropolitan")

9 Grand Metropolitan is a consumer goods company involved in food manufacturing, fast food restaurants, pubs, and the production and marketing of distilled spirits.

10 Grand Metropolitan, through its wholly-owned subsidiary International Distributors & Vintners Ltd ("IDV"), produces and markets a number of leading spirits brands including "J&B" Scotch whisky, "Smirnoff" vodka, "Bailey's Irish Cream", and "Bombay Sapphire" gin. IDV also markets and distributes "Jose Cuervo" tequila under licence. The distribution of IDV spirits brands within New Zealand is handled by New Zealand Wines and Spirits Ltd ("NZWS").

11 Grand Metropolitan also has a 50% shareholding in Entrepreneur Estates Ltd, a company which owns approximately 2,900 pubs in Great Britain. The remaining shareholding is held by Foster's Brewing of Australia.

12 Grand Metropolitan is involved in the food industry through Pillsbury and Burger King. Pillsbury produces a range of refrigerated dough products, frozen foods and other grocery products. Burger King is the world's second largest hamburger restaurant chain with outlets world-wide.

GMG Brands plc ("GMG Brands")

13 As stated earlier, the proposed acquisition involves the merger of Guinness and Grand Metropolitan and the renaming of the merged entity. Guinness shareholders will retain their shares in the renamed entity, and Grand Metropolitan shareholders will receive GMG Brands shares in exchange for Grand Metropolitan shares.

14 GMG Brands will comprise four businesses: United Distillers & Vintners ("UDV"), which will be the combined spirits and wines business of the two companies, Guinness Brewing Worldwide, Burger King, and Pillsbury. UDV will be "the world's leading branded spirits and wines business"[1] and will hold an estimated 5% share of the total world-wide spirits volumes.

15 The applicants state that there are no present plans to rationalise the brands or the distribution of their respective products.

OTHER RELEVANT PARTIES

LVMH Moet Hennessy Louis Vuitton ("LVMH")

16 LVMH Moet Hennessy Louis Vuitton is based in France and is listed on the Paris Stock Exchange. Guinness owns 34% of Moet Hennessy SA, a subsidiary of LVMH Moet Hennessy Louis Vuitton, which principally produces champagnes and cognacs. The remaining 66% of Moet Hennessy is owned by LVMH. LVMH does not directly carry on business activities in New Zealand.

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Allied Domecq

18 Allied Domecq is also involved in the production, marketing and sale of spirits worldwide. The spirits brands owned by Allied Domecq include "Teachers" and "Ballantines" whisky, and "Beefeater" and "Seagers" gin. Allied Domecq does not directly conduct business in New Zealand, with the distribution of its brands in New Zealand being carried out principally by NZWS.

Seagram (New Zealand) Ltd

19 Seagram (New Zealand) Ltd ("Seagram"), a subsidiary of The Seagram Company Ltd based in Canada, is part of an international group involved in the liquor industry. Seagram produces and distributes a number of brands of spirits including "Chivas Regal" scotch whisky, "Absolut" vodka, and "Seagram's" gin. Seagram owns a distillery in Dunedin, producing "Wilson's" whisky.

20 In New Zealand, distribution of Seagram brands is mainly carried out by NZWS. However, ALM and NZ Spirit Merchants Ltd also distribute Seagram brands.

The New Zealand Distillery Company Ltd

21 The New Zealand Distillery Company Ltd ("NZDC") is a co-operative company involved in the manufacture and supply of ethanol/white spirit to the liquor industry and others. White spirit is the base ingredient in gin and vodka.

22 UD holds a 16.7% share in NZDC while IDV holds a 33.3% share. Other shareholders in NZDC are Lion Nathan with a 20.4% shareholding, DB Breweries with 27.0%, and other local interests with 2.6%. The proposed merger will result in the aggregation of the applicants' respective shareholdings in NZDC, giving the merged entity a 50% interest in NZDC.

23 It is noted that **[**

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Allied Liquor Merchants Ltd ("ALM")

24 ALM is a wholly owned subsidiary of DB Group Ltd, and is part of the DB Liquor Group Division, together with International Bottling Company Ltd packaging a wide range of wines and spirits, and NZ Liquor Ltd operating the Liquorland and Robbie Burns retail chains.

25 ALM is involved in the production, importation, distribution and marketing of spirits, liqueurs, wines and beers. For example, ALM handles the distribution of UD spirits brands within New Zealand under an agency arrangement. **[**

]. ALM is also involved in the distribution of a number of other spirits brands, including some of ALM's own brands; for example, "Glenmorangie" and "Colonial" whisky; "Regents Park", "Ambassador", "Liquorland" and "Towerbridge" gin; "Ambassador", "Imperial" and "Liquorland" vodka.

26 Some of the brands for which ALM has agency arrangements are imported in bulk form and then broken down and bottled by ALM in New Zealand. Other agency brands such as "Gordon's" gin, for example, are manufactured in New Zealand in terms of the agency arrangement. Other agency brands are imported as fully-packaged products.

New Zealand Wines and Spirits Ltd ("NZWS")

27 NZWS is involved in the production, importing, marketing and distribution of spirits, liqueurs, sparkling wines and imported beers in New Zealand. IDV has a 25% shareholding in NZWS. The other shareholders in NZWS are Lion Nathan, with a 50% shareholding and management control, and Allied Domecq with a 25% shareholding.

28 NZWS handles the distribution of IDV brands within New Zealand, and is also involved in the distribution of a number of Seagram, Allied Domecq, William Grants, and NZWS's own spirits brands. Seagram brands include "Chivas Regal" and "Wilson's" whisky. Allied Domecq brands include "Ballantines" and "Teachers" whisky, and "Beefeater" and "Seagers" gin. William Grants brands include "William Grants", "Clan McGregor" and "Glenfiddich" whisky. NZWS's own brands include "Christies" gin and vodka.

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30 The Commission has reviewed the links between DB Group Ltd and Lion Nathan and is satisfied that they are not associated companies in terms of the relevant provisions of the Commerce Act 1986.

THE MARKET

General Information

31 The distribution and sale of liquor in New Zealand is primarily regulated by the Sale of

Liquor Act 1989 which states that the sale of liquor to the public requires a liquor licence; e.g.: on-licence, off-licence, club licence. An on-licence authorises the holder to sell and supply liquor for consumption on the premises. An off-licence authorises the holder to sell or deliver liquor for consumption off the premises.

32 There is a large number of brands of spirits available in New Zealand at the present time. For example, *Shaw's Liquor Annual 1995* lists over 90 brands of whisky, over 40 brands of gin, and 30 brands of vodka. It is relevant, however, that many of the leading spirits brands are owned by UD and IDV, and distributed by ALM and NZWS. Furthermore, both ALM and NZWS estimate that together they would distribute **[ ]** of all spirits in New Zealand.

33 The spirits industry is highly brand-oriented, with brands being a means by which a supplier can differentiate its product from other products in the market and develop brand loyalty. A number of industry participants considered that developing and maintaining a brand was an expensive and time-consuming process.

34 Of significance in the spirits industry is the existence of brand agencies. Brand agencies are granted by overseas suppliers to local distributors. As previously stated, ALM and NZWS have agency arrangements with UD and IDV respectively to distribute their leading spirits brands. The ability to acquire, and retain, brand agencies is related primarily to the distributor's performance, and although brand agencies occasionally change hands, it is considered that brand agency arrangements are fairly stable.

Market Definition

35 The applicants submit that the only aspect of the merger that will involve some degree of aggregation in New Zealand markets, will be the combining of the activities of UD and IDV. While the application describes these businesses as "largely complementary", with UD's strength being in whisky, gin, cognac and champagne, and IDV's strength being in vodka, liqueurs and tequila, it acknowledges that there will be some aggregation of market share in relation to gin and vodka.

36 The applicants also submit that it would be appropriate to adopt a broad product market definition encompassing "all liquor" or "all spirits". The application refers to the Commission's earlier investigation of a business acquisition involving the wines and spirits industry in *Magnum Corporation/Dominion Breweries, Decision No 182, 25*

November 1986. In that decision, the Commission identified the relevant function/ product markets as:

- wholesaling of liquor (i.e.: the sale or delivery of liquor to the licensed trade); and
- retailing of liquor.

37 Each of those product markets was held to extend to all forms of liquor, including packaged beer, wines and distilled spirits. On that basis, the applicants submit that a product market definition encompassing all forms of liquor would be accurate.

38 The applicants state that persuasive evidence exists to support a broad product market definition, and referred to a number of reports including the study carried out for the European Commission by Bossard Consultants, *"Competition between Different Categories of Alcoholic Drinks", 6 June 1994;* a report prepared by Strategy in Focus and The Henley Centre for Forecasting, *"Competition between Alcoholic Drinks: An Analysis", November 1991;* and the "*Liquor Review*" report of the Liquor Review Advisory Committee in New Zealand in March of this year.

39 The applicants argue that a broad product market definition is indicated by the substantial degree of supply-side substitution that exists in relation to the different categories of spirits. At the alcohol production stage, distillers are often able to use the same plant to make the alcohol base for use in the production of a number of different spirits. For example, the production of neutral spirits for vodka and gin is part of the normal production process of scotch whisky, creating an opportunity for mixed production in order to maximise capacity utilisation. It is also submitted that economies of scale and scope can be attained at later stages of the production process - bottling, packaging, distribution and marketing.

40 Despite the above arguments, which the applicants claim support a broad product market definition, the applicants have taken a "pragmatic approach" and have adopted narrow product market definitions in all notifications to competition authorities in all jurisdictions affected by the proposed merger. On that basis, the applicants have defined the relevant markets to be the markets for the supply to licensed distributors within New Zealand of -

- whisky;
- gin;
- vodka; and
- tequila.

41 The Managing Director for Segram Australia Ltd, Mr Graham White, [

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42 The functional market in New Zealand consists of producers, importers/distributors, and retailers. The majority of spirits sold in New Zealand are imported. The main competitors at the importation/distribution level are NZWS, ALM, Seagram, Independent Liquor (NZ) Ltd, and NZ Spirit Merchants Ltd. Distributors import spirits from overseas suppliers under brand agency arrangements or distribution agreements, and also distribute locally-owned brands. They undertake the promotion and sale of the product range which may be imported in bulk and bottled in the country, or imported fully-packaged.

43 Distributors are also involved in the production of spirits under brand agency arrangements for the overseas supplier. The spirits are then distributed via supply contracts to various on-licence and off-licence premises including retail liquor chains, independent liquor outlets, licensing trusts, hotels, pubs, restaurants, and so on. Duty free liquor sales also play an important part at the retail level.

Conclusion on Market Definition

44 For the purposes of this report, we consider that narrow product market definitions should be used, and we propose to adopt the market definitions provided by the applicants. Therefore, the relevant markets are defined to be the markets for the supply to licensed distributors within New Zealand of:

- whisky;
- gin;
- vodka; and
- tequila.

ASSESSMENT OF DOMINANCE IN THE MARKETS FOR THE SUPPLY OF WHISKY, GIN, VODKA AND TEQUILA

45 Section 66(3) of the Act, when read in conjunction with s 47(1) of the Act, requires the Commission to give clearance to a proposed acquisition if it is satisfied that the proposed acquisition would not result, or would not be likely to result, in a person acquiring or strengthening a dominant position in a market. If the Commission is not so satisfied, clearance must be declined.

46 Section 3(8) of the Act states that a person is in a "dominant position" if:

> ... a person as a supplier or an acquirer of goods or services either alone or together with an interconnected body corporate is in a position to exercise a dominant influence over the production, acquisition, supply, or price of goods or services in that market and for the purposes of determining whether a person is in a position to exercise a dominant influence ... regard shall be had to -
>
> (a) The share of the market, the technical knowledge, the access to materials or capital of that person ... :
>
> (b) The extent to which that person is constrained by the conduct of competitors or potential competitors in that market:
>
> (c) The extent to which that person is constrained by the conduct of suppliers or acquirers of goods or services in that market.

Current Competition

47 The 1994 Canadean World Alcohol report in respect of New Zealand states that the leading spirits in New Zealand are whisky and gin, with the leading brand of whisky being "Jim Beam" bourbon, and "Gordon's" gin and Seagram having the largest market shares in the gin market. "Smirnoff" vodka is the leading brand in the vodka market.

48 The applicants state that the leading brands of whisky, gin, vodka, and tequila are as follows:

Spirits Brands	UD Brands	IDV Brands	Other Main
Whisky	Johnnie Walker	J&B[2]	Grant's
	Bell's		Jim Beam
	Usher's		100 Pipers
	VAT 69		Chivas Regal
	White Horse		Black Douglas
	McCallan's		
	The Dimple		
	Cardhu		
	The Classic Malts		
	Rebel Yell		
	Bullock Glade		
Gin	Gordon's	Gilbey's	Seagram
	Tanqueray	Bombay Sapphire	Beefeater
	Booth's		
Vodka	Cossack	Smirnoff	Absolut
	Gordon's		Finlandia
	Stolichnaya		Vladivar
Tequila		Jose Cuervo	

49 A number of industry participants stated that there are different levels within each

spirit category, distinguished in terms of price and quality, into which the above brands (and other brands) fall. There are the premium or "upper level" spirit brands such as "Chivas Regal" whisky and "Glenfiddich" whisky; there are the main stream, standard or "middle level" brands such as "Johnnie Walker Red" whisky; and then there are the secondary, price or "lower level" spirits brands.

50 As earlier stated, there are a number of distributors in New Zealand involved in the importation and distribution of spirits, including ALM, NZWS, Glengarry Hancocks Ltd, Independent Liquor (NZ) Ltd, and NZ Spirit Merchants Ltd. However, the two largest distributors, ALM and NZWS, **[** **]** There will be no aggregation of ownership in respect of existing distributors as a result of the proposed merger.

51 Independent Liquor (NZ) Ltd is involved in the importation, manufacture and distribution of liquor. For example, the company distributes "Ivanov" and "Kristov" vodka, "Partington's" and "Carthew's" gin, and "Glen Nevis" whisky. Independent Liquor imports product in bulk from overseas and bottles it for distribution. The company is also involved in the production of gin and vodka. The spirits are distributed to independent liquor outlets throughout New Zealand.

52 NZ Spirit Merchants Ltd, established by the Porirua and Johnsonville Licensing Trusts, is also involved in the importation and distribution of liquor in New Zealand. The company has **[** **]**. The Chief Executive for NZ Spirit Merchants Ltd, Mr Ian McAteer, considered that NZ Spirit Merchants **[**

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53 NZ Spirit Merchants distributes "Vladivar" vodka, "Ultraa" vodka, "Whyte & Mackay" whisky, "Claymore" whisky, "Greenalls" gin, "Ancient" gin, and "Coyote" tequila.

Market Shares

54 In the Commission's view,[3] 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;

- 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.

55 Except in unusual circumstances, the Commission will not seek to intervene in business acquisitions which, given appropriate delineation of the relevant market(s) and measurement of market shares, fall within these "safe harbours".

56 The Distilled Spirits Association of New Zealand collates statistics on spirit sales on a regular basis. Spirits sales in the whisky, gin, vodka and tequila markets for the June year for 1993-1997 are as follows[4] :

Spirits Sales by 9 litre cases, inclusive of imports

Spirits Category	**1997**	**1996**	**1995**	**1994**	**1993**
Scotch	176,194	188,553	190,795	190,735	187,500
Bourbon	173 646	167,745	151,184	138,573	123,351
Other Whisky	44,245	47,292	55,722	49,101	52,889
Total Whisky (incl bourbon)	394,085	403,590	397,701	378,409	363,740
Gin	299,214	328,803	331,252	334,548	343,649
Vodka	123,324	133,000	127,421	129,485	130,576
Tequila	9,275	9,433	9,887	10,281	12,115

57 The applicants have provided market share estimates for the whisky, gin, vodka, and tequila markets for the years 1991-1995. Commission staff have also obtained market share estimates from NZWS and ALM. From those statistics and discussions with industry participants, it is concluded that the market share estimates in the application are reasonably accurate. Minor discrepancies in the market share figures will be noted under the relevant spirit category heading.

Whisky

58 The applicants estimate that market shares in the whisky market are as follows:

Whisky: Sales Volume Market Share Estimates

Brand Owner	**1995**	**1994**	**1993**	**1992**	**1991**
IDV	**[ ]**	**[ ]**	**[ ]**	**[ ]**	**[ ]**
UD	**[ ]**	**[ ]**	**[ ]**	**[ ]**	**[ ]**
Merged Entity	**[ ]**	**[ ]**	**[ ]**	**[ ]**	**[ ]**
Seagram	**[ ]**	**[ ]**	**[ ]**	**[ ]**	**[ ]**
Allied Domecq	**[ ]**	**[ ]**	**[ ]**	**[ ]**	**[ ]**
William Grants	**[ ]**	**[ ]**	**[ ]**	**[ ]**	**[ ]**
Others	**[ ]**	**[ ]**	**[ ]**	**[ ]**	**[ ]**
TOTAL	100%	100%	100%	100%	100%

59 From the data provided by the Distilled Spirits Association and major distributors, the above estimates are considered to be realistic. It is relevant to note that NZWS estimates that Seagram's whisky brand "Wilson's", would have a market share of approximately **[ ]**, which is considerably higher than the **[ ]** estimate provided in the application.

60 It is also noted that NZWS distribute a very small quantity of IDV whisky, namely "J&B Rare" and "Knockando" brands. NZWS estimates that these whisky brands would account for only **[ ]** of the total whisky market in New Zealand. Consequently, the aggregation of market share in the whisky market as a result of the proposed merger would be minor, and it is not proposed to discuss that market in any further detail.

Gin

61 The application states that UD and IDV gin brands face strong competition from Seagram and Allied Domecq, with "Other" gin brands also having a large market

share. It is estimated that market shares by sales volume in the gin market are:

Gin: Sales Volume Market Share Estimates

Brand Owner	**1995**	**1994**	**1993**	**1992**	**1991**
IDV	**[ ]**	**[ ]**	**[ ]**	**[ ]**	**[ ]**
UD	**[ ]**	**[ ]**	**[ ]**	**[ ]**	**[ ]**
Merged Entity	**[ ]**	**[ ]**	**[ ]**	**[ ]**	**[ ]**
Seagram	**[ ]**	**[ ]**	**[ ]**	**[ ]**	**[ ]**
Allied Domecq	**[ ]**	**[ ]**	**[ ]**	**[ ]**	**[ ]**
Others	**[ ]**	**[ ]**	**[ ]**	**[ ]**	**[ ]**
TOTAL	100%	100%	100%	100%	100%

62 NZWS estimates that Allied Domecq would have a market share of approximately **[ ]**, which is considerably higher than the **[ ]** estimate in the application.

63 ALM estimates that its own gin brands, including “Towerbridge” and “Ambassador” would account for around **[ ]** of the gin market.

64 The estimated market share for the merged entity would appear to fall within one of the Commission’s “safe harbours”, having an estimated **[ ]** of the market and facing competition from Seagram and Allied Domecq. Consequently, it is considered unlikely that the proposed merger would result in the creation or strengthening of a dominant position in the gin market.

Vodka

65 In the vodka market, market shares for the leading brand owners are estimated as follows:

Vodka: Sales Volume Market Share Estimates

Brand Owner	**1995**	**1994**	**1993**	**1992**	**1991**
IDV	**[ ]**	**[ ]**	**[ ]**	**[ ]**	**[ ]**
UD	**[ ]**	**[ ]**	**[ ]**	**[ ]**	**[ ]**
Merged Entity	**[ ]**	**[ ]**	**[ ]**	**[ ]**	**[ ]**
Seagram	**[ ]**	**[ ]**	**[ ]**	**[ ]**	**[ ]**
Allied Domecq	**[ ]**	**[ ]**	**[ ]**	**[ ]**	**[ ]**
Others	**[ ]**	**[ ]**	**[ ]**	**[ ]**	**[ ]**
TOTAL	100%	100%	100%	100%	100%

66 NZWS estimates that its own brands of vodka would account for approximately **[ ]** of the vodka market, and ALM estimates that its vodka brands would account for another **[ ]** of the market.

67 From the above estimates, it would appear that the merged entity's market share in the vodka market would fall outside the Commission's "safe harbours". The merged entity would have a market share of slightly more than 40%, with no other single competitor having "no less than in the order of a 15% market share." However, the aggregation is only marginally over the 40% threshold, and in our view the merger would not give rise to dominance concerns. While "Smirnoff" and "Cossack" are the two leading brands of vodka, there is strong competition from Allied Domecq, ALM and NZWS brands.

Tequila

68 Market share estimates for the leading brand owners in the tequila market are as follows:

Tequila: Sales Volume Market Share Estimates

Brand Owner	**1995**	**1994**	**1993**	**1992**	**1991**
IDV	**[ ]**	**[ ]**	**[ ]**	**[ ]**	**[ ]**
UD	**[ ]**	**[ ]**	**[ ]**	**[ ]**	**[ ]**
Merged Entity	**[ ]**	**[ ]**	**[ ]**	**[ ]**	**[ ]**
Seagram	**[ ]**	**[ ]**	**[ ]**	**[ ]**	**[ ]**
Brown Forman	**[ ]**	**[ ]**	**[ ]**	**[ ]**	**[ ]**
Others	**[ ]**	**[ ]**	**[ ]**	**[ ]**	**[ ]**
TOTAL	100%	100%	100%	100%	100%

69 It is considered that the market share figure for IDV's "Jose Cuervo" tequila may be under-estimated, with NZWS estimating that IDV tequila would have a market share of approximately **[ ]**. However, there will be no aggregation of market share for tequila as a result of the proposed merger.

Conclusion on Market Shares

70 There will be some aggregation of market share in respect of the whisky, gin and vodka markets in New Zealand. However, it is considered unlikely that a dominant position in those markets will be created or strengthened as the aggregation in the whisky market will be minimal, the aggregation in the gin market falls within one of the Commission's "safe harbours", and the aggregation in the vodka market falls just outside the "safe harbours" with strong competition from existing vodka brands.

71 Furthermore, market shares are insufficient in themselves to establish whether a dominant position would exist in a market. The Commission considers a range of additional factors before reaching a conclusion as to the acquisition or strengthening of a dominant position in any market, such as the constraint from the threat of market

entry and barriers to entry. These additional factors are discussed below.

Constraints from Market Entry or Expansion

72 The applicants contend that the merged entity will continue to be significantly constrained by existing competitors, and that this constraint will ensure that the merged entity will not, or will not be likely to, acquire or strengthen a dominant position in any market. We agree, as the presence of strong competitors and the potential substitution of different brands within a spirits category would continue to impose substantial constraints on the merged entity.

Vertical Integration

73 The liquor industry in New Zealand is characterised by some vertical integration at the production, distribution and retail levels, with the two major liquor companies, DB Group Ltd and Lion Nathan, operating at two or more functional levels. Such vertical integration can act as an impediment to competition in the market if the concentration of market power at the different levels is high.

74 Although the applicants have not made any decisions in relation to their post-merger distribution arrangements, there has been some speculation from industry participants that **[**

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75 Despite this lack of certainty in relation to post-merger activities in the New Zealand spirits markets, Commission staff have considered the likely competition effects of the proposed merger at the distribution level, and have analysed the possible strengthening of existing vertical links. Many of the leading brands of spirits in New Zealand are owned by UD or IDV, and are distributed by the two major distributors, ALM and NZWS to their own retail outlets. As a result of the proposed merger, those leading brands will be owned by GMG Brands. In the worst post-merger case scenario, the distribution of all of the brands owned by GMG Brands would be placed with either ALM or NZWS, to the exclusion of all other distributors. That distributor would then only distribute those brands to the retail liquor outlets with which that distributor is associated.

76 In our view, the worst case scenario is improbable. If the relevant markets are

individual spirits categories (rather than individual brands), as we have concluded and as has been confirmed by industry participants, then the absence of a particular brand of whisky, gin, vodka or tequila at a retail outlet would result in many consumers purchasing another brand. Given that neither Lion Nathan or DB are dominant at the retail level, a policy of exclusivity in relation to the distribution of brands would be highly likely to result in loss of market share for the exclusive brands.

77 The proposed merger will also have an impact at the distillation level, as GMG Brands will have a 50% shareholding in NZDC. However, NZDC **[**

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78 It is noted that **[**

]. Ethanol is a colourless liquid which results from the alcoholic fermentation of sugar, and may be produced from a variety of materials including lactose (milk sugar), molasses, and starch extracted from grain. Ethanol has a wide range of uses which include the production of gin and vodka, aerosols, cosmetics, food flavourings, pharmaceuticals, surgical spirit, printing inks, car cleaning products and some detergents.

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80 Further, the applicants submit that NZDC will continue to supply white spirit to the whole spirits industry after the merger. While the Commission does not have the legal power to accept such a declaration if it was offered as an undertaking, it nevertheless appears probable that it would be in NZDC's commercial interests to follow such a policy as alternative sources of white spirit are available, and barriers to entry to the market for the distillation of white spirit are low.

Concerns Expressed by Market Participants

81 The Managing Director for Segram Australia Ltd, Mr Graham White, stated that[

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83 Seagram argues that **[**

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84 Seagram states that:[5]

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> **]**.

85 However, it is noted that **[**

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86 Should the merged entity choose to set up its own distribution activities in New Zealand, a large gap would be created in both NZWS and ALM's business activities. Thus, NZWS and ALM would be available to offer their distribution services to existing and new suppliers.

87 Seagram also considers that **[**

]:[6]

> **[**
>
> **]**.

88 Seagram states that **[**

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89 As described earlier, industry participants identified three segments within each spirit category - premium/upper level brands, standard/middle level brands, and budget/ lower level brands. These levels are distinguishable in terms of price and quality/ image. **[**

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90 The European Commission, in its Statement of Objection, [

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91 **[** **]**:

[

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92 **[**

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93 Other industry participants expressed concern that any reduction in competition between the two large distributors in New Zealand would have a detrimental impact on the spirits markets. It was considered that competition between NZWS and ALM has meant prices have been kept under control. Any lessening of competition between the two major players could result in price increases and supply constraints.

94 The Chief Executive for NZ Spirit Merchants Ltd, Mr Ian McAteer stated that [ ]

Barriers to Entry

95 The applicants submit that there are no onerous entry barriers at the production level in the relevant spirits markets, particularly in relation to gin and vodka. Neither vodka nor gin are aged products, and they are produced from neutral/white spirit, supplies of which are readily available to new entrants. The requisite distillation technology is readily available and there do not appear to be any significant barriers to entry in terms of the labelling or bottling requirements.

96 However, industry participants identified a number of entry barriers which they considered to be significant. Brand loyalty was seen as playing a major role in the spirits markets, and developing brand loyalty/brand recognition was considered to be

a lengthy and costly process involving substantial expenditure on advertising and marketing.

97 The importance of distribution in the spirits markets was also highlighted by industry participants. Any new entrant would need to establish a distribution network or develop links with an existing distributor. **[**

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98 Other barriers to entry included the difficulty in a new entrant obtaining prime shelf space in retail outlets, and the need to have a brand portfolio broad enough to be able to compete with existing competitors. Consequently, Seagram argues **[**

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99 The applicants contend that exclusive distribution or brand agency arrangements do not represent a significant barrier because of the "existence of a significant number of independent distribution companies".[7] However, as stated earlier, there are only two major distributors in New Zealand, ALM and NZWS, who distribute a large percentage of all spirits. Nevertheless, lesser know brand agencies are available to other distributors operating in the industry, and to new entrants.

100 Finally, it is noted that the European Commission considers
[

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CONCLUSION

101 While the proposal would involve some horizontal aggregation of market share in the markets for whisky, gin and vodka, it is considered that the proposed merger would not lead to the acquisition or strengthening of a dominant position in those markets. There are strong competitors in each of the product markets, particularly Seagram and Allied Domecq, who will continue to act as a constraint on the merged entity.

102 It is recognised that the merged entity will have an enhanced portfolio of spirits, covering more spirits categories and an increased number of leading brands. However, given that many consumers appear willing to substitute brands, that

competitors such as Seagram and Allied Domecq have leading brands in these categories, and that entry of new brands is feasible, dominance seems an unlikely outcome. It is also considered that should the merged entity place all of its brands with a single distributor, competitors will continue to have access to at least one other distributor with a comprehensive distribution network.

103 It is therefore concluded that the proposed acquisition would not result, and would not be likely to result, in any person acquiring or strengthening a dominant position in the markets for the supply to licensed distributors within New Zealand of:

- whisky;
- gin;
- vodka; and
- tequila.

RECOMMENDATION

104 It is recommended that you give clearance to the proposal under s 66(3)(a) of the Act.

Jane Chilcott Investigator	John Preston Chief Investigator

Jo Bransgrove
Manager

DETERMINATION ON NOTICE SEEKING CLEARANCE: GUINNESS PLC/ GRAND METROPOLITAN PLC

We agree/disagree with the recommendation.

We are satisfied/not satisfied that implementation of the proposal would not result, and would not be likely to result, in any person acquiring or strengthening a dominant position in a market.

Accordingly, pursuant to s66(3)(a) of the Commerce Act 1986 (the Act), we hereby give clearance for the merger of Guinness plc and Grand Metropolitan plc and the creation of a new company, GMG Brands plc.

In terms of s66(5) of the Act, this clearance shall expire twelve months after the date of this determination. Brief particulars of this clearance will appear in the Commission's public register.

This clearance is given only to the proposed acquisition described in the notice seeking clearance dated 25 August 1997.

Dated this day of 1997

A E Bollard	P C Allport	R N Taylor
Chairman	Deputy Chairman	Member

[1] Refer Press Release announcing the proposed merger of Guinness plc and Grand Metropolitan plc, 12 May 1997, Appendix A to the Clearance Application.

[2] The applicants submit that there is no aggregation in the whisky market as "J&B" whisky is not distributed in New Zealand. It is noted, however, that NZWS distributes some IDV brands of whisky (J&B Rare and Knockando), albeit a very small quantity.

[3] Refer Commerce Commission's Business Acquisition Guidelines, 1996, p17.

[4] Statistics provided by the Distilled Spirits Association of New Zealand.

[5] **[ ]**.

[6] **[ ]**.

[7] Refer page 18, para 16.3 of the application.