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Determination

Pact Group Pty Limited and Viscount Plastics (NZ) Limited [2012] NZCC 11

The Commission:	Dr Mark Berry Sue Begg Dr Jill Walker
Summary of application:	The acquisition by Pact Group Pty Limited to acquire the plastic pails business of Viscount Plastics (NZ) Limited.
Determination:	Pursuant to s 66(3)(a) of the Commerce Act 1986, the Commission determines to give clearance to the proposed acquisition subject to the divestment undertaking dated 8 May 2012 provided by Pact Group Pty Limited under section 69A of the Commerce Act 1986.
Date of determination:	10 May 2012

Confidential material in this report has been removed. Its location in the document is denoted by [ ].

Contents

The proposal

1. Pact Group Pty Ltd (Pact) proposes to acquire 100% of the shares in Viscount Plastics Pty Ltd (Viscount Pty) from LINPAC Mouldings Ltd (LINPAC). Viscount Pty manufactures and supplies packaging products in Australia, the Asia Pacific region, and in New Zealand where its wholly owned, New Zealand registered, subsidiaries are Pacific BBA Plastics (NZ) Ltd and Viscount Plastics (NZ) Limited (Viscount NZ). Pacific BBA Plastics (NZ) Ltd is a holding company with a 100% shareholding in the trading entity Viscount NZ, its only asset. Viscount NZ owns plant and equipment, goodwill in customers, and other business assets required to manufacture both plastic packaging and plastic materials handling products. The former category includes pails and the latter, crates and pallets. Pact's acquisition of the shares in Viscount Pty is termed the broader transaction in these reasons.

2. A notice from Pact under s 66(1) of the Commerce Act 1986 (the Act) was registered by the Commerce Commission (the Commission) on 4 October 2011. The Notice sought clearance "in respect of the proposed acquisition by Pact of the plastic pails business of Viscount." The nature of the broader transaction at first raised issues as to the scope of the application. This was clarified by Pact on 30 November 2011[1] and the Commission has proceeded on the basis that the Notice seeks clearance only for a specific portion of the broader transaction. That is, for Pact's acquisition and control of the assets that comprise Viscount NZ's plastic pails business (the proposed acquisition). These assets are summarised in Attachment 1.[2]

Procedure

3. Section 66(3) of the Act requires the Commission to either clear or decline to clear the acquisition referred to in a s 66(1) notice within 10 working days, unless the Commission and the person who gave notice agree to a longer period. An extension of time was agreed between the Commission and Pact. Accordingly, a decision on the application was required by 11 May 2012.

4. On 8 May 2012 the Commission received an undertaking from Pact, under section 69A of the Act, that Pact would divest certain plastic pails manufacturing equipment and some current Viscount NZ customers. The Commission considered the competition effects of the undertaking in the proposed divestment section below.

5. The Commission's approach to analysing the competition effects of the proposed acquisition and the divestment offer is based on the principles respectively set out in

[1] Russell McVeagh letter of 30 November 2011 at paragraph 49.
[2] Provided to the Commission in Russell McVeagh's e-mail of 26 April 2012 and subsequently clarified.

its Mergers and Acquisitions Guidelines[3] and Mergers and Acquisitions Divestment Remedies Guidelines (Divestment Guidelines).[4]

Statutory framework

6. Any person who proposes to acquire assets of a business or shares and considers that the acquisition may breach s 47 can apply for clearance under s 66 of the Act.

7. If the Commission is satisfied under s 66(3)(a) of the Act that the proposed acquisition will not have, or would not be likely to have, the effect of substantially lessening competition in a market, the Commission must give clearance for the proposed acquisition.

8. The Court of Appeal in *Port Nelson v Commerce Commission*[5]noted that for something to be "likely" it must be "above the mere possibility but not so high as more likely than not and is best expressed as a real and substantial risk that the stated consequence will happen."

9. The High Court in *Woolworths & Ors v Commerce Commission* observed that "…a substantial lessening of competition is one that is "real or of substance" as distinct from ephemeral or nominal. Accordingly a substantial lessening of competition occurs if it is likely that there will be a reduction in competition that is real or of substance."[6]

10. If the Commission is not satisfied that the proposed acquisition will not have or would not be likely to have the effect of substantially lessening competition in a market or it is "in doubt" as to whether that is the case, it must decline the application under s 66(3)(b) of the Act.[7]

11. The burden of proof lies with Pact as the applicant, to satisfy the Commission on the balance of probabilities that the acquisition is not likely to substantially lessen competition.[8] The decision to grant or refuse clearance is to be made on the basis of all the evidence.[9] The Commission will sometimes have before it conflicting evidence

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3 Commerce Commission, *Mergers and Acquisitions Guidelines*, January 2004.

4 Commerce Commission, *Mergers and Acquisitions: Divestment Remedies Guidelines,* June 2010.

5 (1996) 5 NZBLC 104, 150; (1996) 3 NZLR 562-563.

6 *Woolworths & Ors v Commerce Commission* (2008) 8 NZBLC 102,128 (HC).

7 *Commerce Commission v Woolworths Ltd* (2008) 8 NZBLC 102,336 (CA). At para 105, the Court stated that the fact that the Commission is not satisfied does not require that the Commission be positively satisfied that a substantial lessening of competition is likely.

8 *Commerce Commission v Southern Cross Medical Care Society* (2001) 10 TCLR 269 (CA) at para 7 and *Commerce Commission v Woolworths Ltd* (CA) above n7 at para 97.

9 *Commerce Commission v Woolworths Ltd* (CA) above n7 at para 101.

from different market participants and must determine what weight to give to the evidence of each party.[10]

Analytical framework

12. The Commission uses an analytical framework for assessing a substantial lessening of competition in the context of a proposed acquisition. An important tool in this assessment is the determination of the relevant market or markets. To do this, the Commission identifies the areas of overlap between the businesses of the acquirer and the target, and then considers what, if any, products and geographic regions, constitute relevant close substitutes from both a customer's and a supplier's point of view.

13. The Commission uses a forward-looking analysis to assess whether a substantial lessening of competition is likely. This exercise "requires a comparison of the likely state of competition if the acquisition proceeds ("the factual") against the likely state of comparison if it does not ("the counterfactual")."[11]

14. In framing a suitable counterfactual, the Commission bases its view on a pragmatic and commercial assessment of what is likely to occur in the absence of the proposed acquisition.[12]

15. The High Court in *Air New Zealand v Commerce Commission (No.6)*[13] accepted that an absence of market power would suggest there had been no substantial lessening of competition in a market but did not see this as a reason to forsake an analysis of the counterfactual as well as the factual. Justice Rodney Hansen stated that "...a comparative judgment is implied by the statutory test which now focuses on a possible change along the spectrum of market power rather than on whether or not a particular position on that spectrum, that is, dominance has been attained."

16. A comparison of the extent of competition in the relevant markets in the factual and counterfactual scenarios enables the Commission to assess the probable extent of the lessening of competition under the proposed acquisition, and whether that contemplated lessening is likely to be substantial. That assessment is dependent on the facts as disclosed during the Commission's investigation.

17. In addition to existing competitors, the assessment includes an analysis of potential competitors. Potential competitors can act as a constraint on a business or businesses that might otherwise be able to exert market power. An acquisition is unlikely to result in a substantial lessening of competition in a market if the

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10. *Brambles New Zealand Ltd v Commerce Commission* (2003) 10 TCLR 868 at para 64.
11. *Commerce Commission v Woolworths Ltd* (CA) above n7 at para 63.
12. *Decision No. 277: New Zealand Electricity Market,* 30 January 1996, p 16.
13. *Air New Zealand v Commerce Commission (No.6)* (2004) 11 TCLR 347.

businesses in that market continue to be subject to real constraints from actual, or threatened, market entry.

18. If entry is to act as an antidote to what otherwise might be a substantial lessening of competition in a market, that entry must be likely, timely and of sufficient extent to constrain market participants. This is more likely to be the case when conditions of entry or expansion are relatively benign.[14] However, the central question is simply whether or not a merged firm would be constrained by likely market entry (or expansion) in the event it increased prices or reduced services.

19. Under section 69A of the Act, the Commission may accept undertakings to dispose of assets or shares.[15] If divestment undertakings are accepted by the Commission, they are deemed to form part of the clearance. A clearance is void if an undertaking is contravened.[16]

20. As set out in the Divestment Guidelines, upon receiving a divestment undertaking the Commission will consider whether the proposed divestment is sufficient to remedy any substantial lessening of competition that would otherwise arise.

21. In assessing a proposed divestment, the Commission examines the risks associated with the proposed divestment, namely:

- composition risks
- asset risks
- purchaser risks.

Industry background

22. Plastic pails and lids are manufactured by the injection moulding process. This technique involves forcing molten plastic resins of various compositions into a pail and lid shaped moulds at very high pressure. The formed plastic is allowed to cool and the mould is opened to release the pail or lid. In most cases moulds are developed and owned by injection moulding manufacturers. Individual injection moulding machines have the ability to accept a range of moulds to manufacture products of different sizes and shapes.

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14 As discussed in *Re Queensland Co-operative Milling Association* (1976) 8 ALR 481, 516 at "...it is the ease with which firms may enter which establishes the possibilities of market concentration over time; and it is the threat of the entry of a new firm or a new plant into a market which operates as the ultimate regulator of competitive conduct."

15 Under section 69A(2) of the Act the Commission is only able to accept structural undertakings. This means the Commission is unable to accept behavioural undertakings.

16 Section 69AB of the Act.

23. Plastic pails and lids can be manufactured to a range of material specifications, shapes and volumes, and with various decoration options, to meet purchasers' requirements. Specifically, food grade pails are manufactured from virgin, rather than recycled plastic, and dangerous goods pails must meet particular strength standards. Pails can be decorated by in-mould labelling (IML),[17] offset screen printing or stick on labels, again depending on purchasers' requirements.

Parties

Pact

24. Pact manufactures and supplies plastic pails (and a range of other plastic products)[18] in New Zealand through three subsidiaries: VIP Plastic Packaging (NZ) Limited; Alto Packaging Limited; and Tecpak Industries Limited. Pact manufactures its range of plastic pails at its VIP Plastic Packaging (NZ) Limited factory in Auckland.

25. Pact supplies plastic pails to a range of different purchasers throughout New Zealand. Pact's largest customer for plastic pails is Resene Paints Limited (Resene), a paint supplier, which accounts for approximately [ ] of Pact's plastic pails production.

26. At present, Pact has a 19.99% shareholding in National Can Industries Limited (NCI). Pact holds this shareholding through Bennamon Pty Limited and Geminder Holdings Pty Limited (together 'Bennamon'). However, Bennamon recently entered into a share purchase agreement with NCI for the sale of Bennamon's shares to NCI. Accordingly, given there will be no cross-shareholdings between Pact and NCI, the Commission has not considered it necessary to assess whether Pact and NCI are associated entities under s 47 of the Commerce Act.

Viscount Pty

27. Viscount Pty is a multinational company with operations in New Zealand, Australia, Malaysia, Thailand and China. It manufactures a wide range of plastic products including pails, crates, bins, pallets and food containers. Viscount Pty's New Zealand subsidiaries are Pacific BBA and Viscount NZ.

28. Viscount NZ recently closed its Christchurch manufacturing plant, relocating the machinery to its Auckland factory. Even with the closure of its Christchurch plant, Viscount NZ is the largest manufacturer of plastic pails in New Zealand, supplying a range of pails to different purchasers throughout New Zealand from its Auckland

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17 In-mould labelling is a method of decorating plastic products whereby the label is attached to the product inside the mould during the pressurisation process.

18 Pact advised the Commission in Russell McVeagh's letter of 30 November 2011 at paragraph 30 that in Pact's view there was no basis for an application for clearance in respect of any business other than the plastic pails business.

factory. Its largest customers are Dulux Group (New Zealand) Pty Limited (Dulux), Wattyl NZ Limited (Wattyl) and Nestlé New Zealand Limited (Nestlé).

29. The ultimate owner of Viscount Pty is LINPAC, a global packaging company based in the United Kingdom which is owned by a consortium of banks.

National Can Industries Ltd

30. NCI is based in Australia and has operations in New Zealand and Asia. In Australia, NCI manufactures plastic pails and competes in that country with both Pact and Viscount Pty.

31. In New Zealand, NCI makes a range of tinplate products, including paint tins. NCI also imports plastic pails from Australia. In 2007, NCI increased its market share in the New Zealand plastic pails market when it began to supply a high quality IML pail.

32. At present, NCI is a public company listed on the Australian Securities Exchange (ASX). However, it is in the process of delisting which will involve NCI acquiring the Bennamon shareholding, as described above.

Other domestic injection moulders

33. Other than Pact and Viscount NZ, there are a number of other domestic injection moulders some of which manufacture pails. Each of these manufacturers supply only limited volumes in comparison with either Pact or Viscount NZ. These small domestic manufacturers include:

- Uniplas NZ Ltd (Uniplas) based in Wellington
- Plastech Industries Ltd (Plastech) based in Christchurch
- Simaplas Ltd (Simaplas) based in Auckland
- Galantai Plastics Group Ltd (Galantai) based in Auckland
- Talbot Technologies Ltd (Talbot) based in Christchurch.

Purchaser categories

34. Industry participants advised that, while there are a large number of purchasers of plastic pails in New Zealand, they can mostly be divided into three main categories of products: paint and other surface coatings, food, and industrial materials. These

three categories collectively account for most of the sales of plastic pails in New Zealand.[19]

35. Figure 1 shows the estimated breakdown of the market based on the main categories of product.

Figure 1: Sales by industry [

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36. The three largest paint manufacturers: Dulux, Resene and Wattyl, represent [ ] of the total annual sales of plastic pails. In addition, there are a number of other paint manufacturers which also purchase plastic pails but in smaller volumes. These include: Coating Technologies Limited; Paintplus Colour Systems Limited (Paintplus); Agrippa Paints Limited (Agrippa); and Jacobsens Colourplus Limited (Jacobsens).

37. The four largest food manufacturers, Nestle, Goodman Fielder New Zealand Limited (Goodman Fielder), Heinz Wattie's Limited (Heinz Wattie's) and Barkers Fruit Processors Limited (Barkers) represent [ ] of total annual sales of plastic pails.

38. Manufacturers of industrial products also purchase plastic pails for packaging. For example: Winstone Wallboards Limited (Winstone Wallboards) for packaging wall board stopping compounds; Bostik New Zealand Limited (Bostik) for packaging of bulk sealants and adhesives; and EDL Fasteners Limited for packaging of nuts, bolts, screws and other fasteners.

[19] The Commission calculated that these three categories account for approximately [ ] of sales. This amount and the data in Figure 1 are based on customer information provided by Pact, Viscount and NCI. Given that together, these three parties account for [ ] of existing sales of plastic pails, the Commission considers that these figures provide a good representation of the industry.

Commission's enquiries

39. The Commission interviewed and received information from a large number of parties involved in the plastic pails market, namely:

- Pact and Viscount NZ
- other domestic manufacturers of plastic pails and other injection moulded products
- Australian manufacturers and suppliers of plastic pails including NCI
- a representative range of domestic purchasers of plastic pails.[20]

40. The views of many purchasers in the paint segment of the plastic pails market were consistent. However, the responses received from some purchasers using plastic pails to package food or industrial products varied. These variances are discussed later in these reasons.

41. The Commission carefully weighed all the information received from the parties listed above. It has taken into account the incentives, and commercial positions, of parties directly interested in the acquisition. It has attempted, where possible, to test competing views with parties independent of the acquisition, especially when varying views were expressed to the Commission.

Previous decisions

42. Pact submitted that in previous cases, such as *Tec Projects Limited and Tecpak Industries Limited*[21] (The Tecpak Decision) and *Visy Industrial Plastics (NZ) Limited and Alto Holdings Limited*[22] (the Alto Decision) the Commission accepted that large plastic packaging purchasers had countervailing power. This was based on large purchasers' ability to (i) switch to other existing competitors; (ii) support expansion by a smaller manufacturer; or (iii) sponsor new entry. Pact submitted that this countervailing power was a type of constraint particularly relevant in the present case.

43. The Commission has considered its previous plastic packaging decisions and considers that this case is distinguishable on its facts. The Commission's previous decisions analysed different product markets with different competitive dynamics,

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[20] Along with the paint, food and industrial product categories described, about [ ]% of plastic pail purchasers are from other industries. These purchasers include the medical industry, which uses pails for medical waste disposal, and the health supplement industry, while a proportion are also sold at retail.

[21] *Tec Projects Limited and Tecpak Industries Limited* (Commerce Commission Decision 702, 18 November 2010).

[22] *Visy Industrial Plastics (NZ) Limited and Alto Holdings Limited* (Commerce Commission Decision 583, 26 June 2006).

so while helpful, those decisions do not reflect the plastic pails market conditions pertinent to this case. As will become apparent, in this case the Commission considers that many large purchasers (particularly paint manufacturers) would not have the ability to switch to existing competitors; unaided expansion by smaller manufacturers is unlikely; and new entry is unlikely to be sponsored by purchasers.

Market definition

44. The Commission considers the relevant market is the New Zealand market for the manufacture or importation, and supply of plastic pails of up to 20 litres capacity.

45. Both Pact and Viscount NZ supply plastic pails up to 20 litres capacity and both agreed that a separate plastic pails market up to 20 litres capacity exists. [23] Other industry participants agreed with this assessment. The following explains the reasons for the Commission's market definition.

46. The Act defines a market as:[24]

> "… a market in New Zealand for goods or services as well as other goods or services that, as a matter of fact and commercial common sense, are substitutable for them."

47. For the purpose of competition analysis, the internationally accepted approach is to delineate a relevant market as the smallest space within which a hypothetical, profit maximising, sole supplier of a good or service, not constrained by the threat of entry would be able to impose at least a small yet significant and non-transitory increase in price, assuming all other terms of sale remain constant (the SSNIP test). The smallest space in which such market power may be exercised is defined in terms of the dimensions of the market discussed below. The Commission generally considers a SSNIP to involve a five to ten percent increase in price that is sustained for a period of one year.

48. The Commission uses this analytical tool to assess the relevant market in terms of the following five characteristics or dimensions:

- the goods or services supplied and purchased (the product dimension)
- the level in the production or distribution chain (the functional level)
- the geographic area from which the goods or services are obtained, or within which the goods or services are supplied (the geographic extent)

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[23] Pact clarified its original submission where it stated that the market includes up to 25 litre sized pails. Neither Pact nor Viscount produce a 25 litre pail, although Viscount has in the past imported a very limited number of 25 litre pails.

[24] Section 3(1A) of the Commerce Act 1986.

- the temporal dimension of the market, if relevant (the timeframe)
- the customer dimension of the market, if relevant

Product dimension

49. Plastic pails are differentiated by their material composition, shape, capacity, quality (for example food and strength grades), labelling, and type of lid.

Demand side substitution

50. There appears to be limited substitutability on the demand side between plastic pails and other packaging materials. Demand side substitution analysis examines the economic viability of purchasers substituting one product for another. Products are demand side substitutes if enough buyers would switch to the substitute products such that a SSNIP would be unprofitable.[25]

51. Pact submitted that there is some evidence of demand substitutability with other packaging materials, including tinplate pails and 'bag in a box' systems. However, other industry parties advised that the extent of demand side substitutability between plastic pails and other packaging materials varies depending on the product that is packaged.

52. As discussed above, industry participants including Pact, Viscount NZ and NCI all agree that plastic pails are used to contain three main categories of products: (i) paint, (ii) food and (iii) industrial materials:

    52.1 Paint tins are still commonly preferred by some paint manufacturers for small paint tin sizes which range from 0.5 litres to 4 litres. While more expensive, tinplate is suitable to resist corrosion from chemical solvents found in some paints. There is also a perception by paint manufacturers that tin gives the product a premium aesthetic in customers' minds. However, paint manufacturers advised that there has been a move away from tinplate to plastic pails because, on the whole, plastic is significantly cheaper.[26] Paint industry participants did not consider tinplate pails to be feasible economic substitutes for the larger sizes of plastic pails.

    52.2 In respect of food packaged in plastic pails, in the Commission's view, Pact's suggested substitutes for plastic pails for food manufacturers (such as 'bag in a box' systems) have limited potential for demand side substitutability. The advantage of plastic pails over these potential alternatives for

[25] As discussed in more detail below, in a market where there is price discrimination, switching by one set of buyers to substitute products will not necessarily discipline the price to the remaining buyers.

[26] For example, Dulux noted that a 10L tinplate can would cost [ ] times more than a standard 10 litre plastic pail. Interview with Dulux, 14 October 2011.

manufacturers and end users is that pail lids are easily re-sealable. Also, plastic pails have a lower level of food product wastage than the 'bag in a box' system; a sticky product, for example, can be more easily removed from a pail by use of a scraper. Plastic pails are also popular with end users because, after cleaning, they are reusable for storage of other products.

52.3 In respect of industrial materials (for example bulk fasteners and wall board stopping compound), parties such as Winstone Wallboards and EDL Fasteners Limited noted that the re-sealable lid and pail handle, together with the robustness of plastic pails, means that pails are particularly suitable for use on building sites.[27] Winstone Wallboards noted that while it does supply its wall board stopping compound in both plastic pails and cardboard cartons, the cardboard cartons are marketed as a pail refill product and are intended to complement the pails. Winstone Wallboards also informed the Commission that its customers have a strong preference for plastic pails which they can reuse.

53. Therefore, the Commission does not consider it likely that a supplier of plastic pails would be disciplined by the potential for paint, food and industrial products manufacturers to switch from plastic pails to tinplate pails or bag in the box or any other packaging system.

Supply side substitution

54. Close supply side substitutes are products which suppliers can easily move to produce when they are given a profit incentive to do so. To be a close supply side substitute, suppliers must be able to produce the substitute product with little change to their production facilities and little or no additional investment. The resulting product must be acceptable to consumers as a substitute.

55. Suppliers such as Pact, Viscount NZ and NCI, manufacture a range of pails. They all utilise a number of injection moulding machines that enable them to produce different types and/or sizes of pails simultaneously. While each size and/or shape of pail requires a separate mould, changing moulds is a standard process that may take only up to a maximum four hours (for a very large mould). Manufacturers can and do easily switch production between different pails using different moulds.

56. Other products suggested by Pact as substitutable for plastic pails (although not, in the Commission's view, demand side substitutes) such as tinplate pails and 'bag in a box' systems, are produced using different equipment and different raw materials. As such, the Commission does not consider these types of products to be supply-side substitutes for plastic pails.

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27 Interview with Winstone Wallboards, 17 October 2011 and interview with EDL Fasteners, 17 October 2011.

57. Pact also suggested that injection moulding machines, currently used to manufacture low strength thin walled (food) containers could also be used to manufacture thick walled plastic pails. However, the moulds required to manufacture plastic pails are: more specialised, have finer manufacturing tolerances, are more costly; and are larger, stronger and more robust than the moulds required to manufacture thin walled plastic containers. The Commission therefore considers that there is very limited potential for supply side substitutability between the manufacture of thin-walled containers and plastic pails.

Product differentiation

58. The Commission recognises that product differentiation may mean that different suppliers face different competitive constraints when selling to different purchasers, here paint, food and industrial. While the Commission has defined a product market for all plastic pails (consistent with the applicant's view), the Commission nonetheless considers product differentiation to be important to the competitive dynamics in this market. The Commission considers such product differentiation as does exist in the competitive effects section of these reasons.

59. Pact submitted in its application that plastic pails are not highly differentiated products and that the majority of pails sold in New Zealand are commodity products manufactured using standard moulds that are readily available to any manufacturer.

60. Pact's submission in this regard was not supported by the Commission's investigation. Many parties interviewed had a contrary view. They consider plastic pails are highly differentiated products since plastic pails are:

- made in a range of shapes and styles
- manufactured to a range of specifications, such as drop strength, food grade, tamper proof lids, and anti-skinning[28]
- plastic pails can be made out of a range of different resins and include virgin resins or recycled plastic
- customised with a range of decoration types.

61. Moreover, when interviewed Pact appeared to agree that product differentiation to various degrees does exist in the plastic pails market and pails differ in design, functionality, weight, and type and level of decoration. Pact commented that while

[28] Anti-skinning technology helps reduce paint from being spoilt by dried flakes.

for some purchasers the plastic pail "is just a bucket", for others it is the "quintessential marketing tool" for their product.[29]

Conclusion on product dimension

62. The Commission considers that the limited demand side and supply side substitutability of other packaging materials supports Pact's submission that plastic pails up to 20 litres capacity are in a discrete product market. The Commission does not consider that paint tins, 'bag in a box' systems or other types of packaging would provide other than a minor competitive constraint from outside the relevant market and then only for the lower end of the plastic pail range of sizes.

Geographic dimension

63. All parties, including Pact and Viscount NZ supply and/or purchase plastic pails on a national basis from manufacturing plants located throughout New Zealand. The Commission, therefore, considers that the geographic dimension of the relevant market is national in scope.

Functional dimension

64. Both Pact and Viscount NZ manufacture and supply plastic pails to their customers from New Zealand-based factories. Several other parties, such as NCI (from its Melbourne plant) import their own manufactured pails to supply customers direct. Other parties, such as Stowers Containment Solutions (Stowers) import pails from overseas manufacturers and then warehouse and distribute the pails to meet customers' requirements. The Commission considers the functional level of the relevant market to be that for the manufacture or importation, and supply.

Customer dimension

65. The Commission examines whether the possible competitive effects of a merger are likely to vary significantly across purchasers who acquire the same or similar products. Such differential impacts are possible when sellers can price discriminate between purchasers within a relevant market.

66. When price discrimination between purchasers can or does occur, the Commission considers whether markets based on the purchaser groups who in the face of a price increase are unable to switch or are less price sensitive, would assist its competition analysis. This approach is appropriate if sellers systematically distinguish between groups of purchasers on the basis of particular identifiable characteristics of each of the groups.

29 Interview with Pact, 24 January 2012.

67. The Commission's investigation revealed that that there is no consistency in the sale prices of plastic pails with similar volume or other properties. Almost every customer interviewed by the Commission was charged different prices depending on their individual technical and purchase quantity requirements. This can be seen in information obtained from Pact, Viscount NZ and NCI that showed their sale price ranges for 10 litre pails and lids were respectively [ ].

68. However, the Commission does not consider that the observed price differences are systematic in this case. The Commission considers that this is a case where the evidence shows sellers negotiate prices with customers on the basis of their individual, rather than group, tangible and intangible characteristics. Therefore, this is not a case where systematic prices discrimination lends itself to market segmentation by customer type.

69. Therefore, the Commission has analysed the range of possible competition effects in the relevant market across all purchasers in its competitive effects analysis. As the Federal Court of Australia noted in *Dandy Power Equipment Pty Ltd & Anor v Mercury Marine Pty Ltd*[30] and as cited by McGechan J in *Commerce Commission v Port Nelson Ltd*[31]:

> Although the words "substantially lessened in a market" refer generally to a market, it is the degree to which competition has been lessened which is critical, not the proportion of that lessening to the whole of the competition which exists in the total market. Thus a lessening in a significant section of the market, if a substantial lessening of otherwise active competition may, according to circumstances, be a substantial lessening of competition in a market.

Conclusion on Market Definition

70. The Commission considers that the market relevant to the analysis of the proposed acquisition is that for the manufacture and importation, and supply of plastic pails up to 20 litres capacity throughout New Zealand. In these reasons this market is termed "the plastic pails market" or "the relevant market."

Factual and counterfactual

71. If the proposed acquisition proceeds, in the factual Pact would acquire, and gain control of, all the plastic pails manufacturing assets of Viscount NZ.

72. Viscount Pty advised the Commission that if the broader transaction does not proceed, it would [

30 *Dandy Power Equipment Pty Ltd & Anor v Mercury Marine Pty Ltd* (1982) 64 FLR 238, 260; 44 ALR 173, 192; ATPR 40-315, 43,888.

31 *Commerce Commission v Port Nelson Ltd* (1995) 6 TCLR 406 at 435.

]. This would imply a status quo counterfactual.

73. While Pact and Viscount NZ are by far the two largest plastic pail suppliers in the relevant market and together would have a large market share, the sale of Viscount NZ would be a relatively minor part of the value of the broader transaction. Therefore, in order to facilitate the broader transaction should Pact fail to gain Commission clearance, Viscount Pty agreed that it would separate out Viscount NZ's plastic pails business as a stand-alone entity owned by LINPAC. Viscount Pty has advised that, absent Commission clearance:

    73.1 Viscount Pty would transfer its shares in Viscount NZ to the direct ownership of LINPAC.

    73.2 All the New Zealand assets of Viscount NZ, except those relating to its production of plastic pails, would be transferred from Viscount NZ to Viscount Pty.[32]

74. The Commission considers that NCI would be a potential purchaser of Viscount NZ if the proposed acquisition does not proceed. [

].[33]

75. Therefore, the Commission considers that because the plastic pails assets and business of Viscount NZ would be separated from the broader transaction if the Viscount NZ acquisition does not proceed, and because of LINPAC's clear desire to sell all its Viscount Pty assets, it is likely that Viscount NZ would be sold as a stand-alone, going concern either to an existing participant in the relevant market, such as NCI, or to an investor presently not operating in the market. The competition impacts of either scenario do not differ materially given the small share of the existing competitors (including NCI), and hence the Commission has proceeded on the basis of a status quo counterfactual.

[32] Russell McVeagh letter to the Commission dated 30 November 2011.
[33] Interview with NCI, 25 October 2011.

Competition analysis

Preliminary comments

76. The following sections of these reasons discuss whether post acquisition the merged firm would have the ability to exercise unilateral market power to a degree that there would likely be a substantial lessening of competition.

77. Unilateral market power analysis focuses on the actions of a single firm in the market. The greater the extent that, pre-merger:

- merging parties are close competitors
- remaining competitors in the market are more distant competitors because of, for example, the type, range, reliability of product they offer
- remaining competitors are constrained in regard to their ability to increase production,

the greater the likelihood that post-acquisition a unilateral reduction in output, or increase in prices, would prove to be profitable for a merged entity, and that it would be able to exercise market power on a sustainable basis.

78. A merged entity's combined market shares may provide an indicator of market power. All else being equal, the larger the merged entity's market share, the greater the likelihood of market power. Moreover, the increase in seller concentration caused by a reduction in the number of competitors in a market due to an acquisition is generally an indicator of the extent to which competition in the market may be lessened.

79. However, market concentration is only one of a number of factors to be considered in the assessment of competition in a market.[34] Having identified the level of concentration in a market, the Commission considers all factors which may constrain the merged entity's behaviour in the market to understand the impact of the acquisition on competition.

80. In particular, unilateral market power is unlikely to be exercised when viable entry and/or expansion are likely in a timely fashion and on sufficient scale so as to discipline any substantial lessening of competition.

[34] As the Court of Appeal noted in *Southern Cross* above n8 at para 68, "Market share is relevant to the level and significance of market power but it is not in itself the determinant of market power. What level of market power a firm has, as a result of its market share, will depend substantially on the level of barriers to entry and expansion which apply to the market."

81. The proposed acquisition involves a substantial aggregation of market share. Further, the evidence before the Commission indicates that the remaining market participants are only distant competitors. Hence the question of entry and expansion are central to the competition analysis.

Market shares

82. Pact and Viscount NZ are the two largest suppliers in the plastic pails market and have been for some time.

83. NCI is the third largest supplier of pails in the plastic pails market. NCI imports all its pails from its Melbourne factory and while it has recently increased its sales, Table 1 below shows its presence remains relatively minor.

84. The sales revenues and market shares shown in Table 1 were obtained during the Commission's investigation of the proposed acquisition and, in particular during interviews with each of the market participants listed in the Table. It can be seen that at present the "other competitors" in the market are mostly smaller domestic manufacturers who supply only a limited volume of pails. As Table 1 shows, the combined market share of these smaller domestic manufacturers has been relatively low for some time.

85. Pact's submission as to the market shares in the industry were not corroborated by the Commission's market inquiries and data received from other market participants. The Commission's analysis shows that Pact underestimated the merged entity's market share by overestimating the market shares of importers, NCI, Stowers, and the smaller domestic manufacturers.

Table 1: Estimated market shares for the plastic pails market 2008-2011[35]

Parties	2008		2009		2010		2011	
	Sales Revenue $	Market share	Sales Revenue $	Market share	Sales Revenue $	Market share	Sales Revenue $	Market share
Pact	[ ]	[ ]	[ ]	[ ]	[ ]	[ ]	[ ]	[ ]
Viscount NZ	[ ]	[ ]	[ ]	[ ]	[ ]	[ ]	[ ]	[ ]
Combined entity	*[ ]*	*[ ]*	*[ ]*	*[ ]*	*[ ]*	*[ ]*	*[ ]*	*[ ]*
NCI	[ ]	[ ]	[ ]	[ ]	[ ]	[ ]	[ ]	[ ][36]
Simaplas	[ ]	[ ]	[ ]	[ ]	[ ]	[ ]	[ ]	[ ]
Galantai	[ ]	[ ]	[ ]	[ ]	[ ]	[ ]	[ ]	[ ]
Uniplas	[ ]	[ ]	[ ]	[ ]	[ ]	[ ]	[ ]	[ ]
Plastech	[ ]	[ ]	[ ]	[ ]	[ ]	[ ]	[ ]	[ ]
Stowers	[ ]	[ ]	[ ]	[ ]	[ ]	[ ]	[ ]	[ ]
Other (direct imports)	[ ]	[ ]	[ ]	[ ]	[ ]	[ ]	[ ]	[ ]
Total	**[ ]**	**100%**	**[ ]**	**100%**	**[ ]**	**100%**	**[ ]**	**100%**

Source: Industry participants, Commission estimates.

86. The current three firm concentration ratio is [ ]. Post acquisition, the merged entity (based on sales data) would have a market share of approximately [ ] and the three firm concentration ratio would be [ ], well outside the Commission's safe harbours.

87. However, as noted above, the Commission recognises that market concentration is only one of a number of factors to be considered in the assessment of competition in a market.

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35 Data was gathered by the Commission directly from suppliers. Suppliers were asked to provide the Commission with plastic pails sales revenue for the last four years (1 July to 30 June). Figures have been rounded.

36 NCI's market share [ ]. This is discussed later in the competition analysis.

The Commission's assessment of existing competition

88. The Commission's analysis compares the likely state of competition if the acquisition proceeds against the likely state of competition if it does not. As discussed, in this case the Commission considers the counterfactual is the status quo.

89. The Commission's competition analysis below discusses:

89.1 the state of existing competition and the loss of competition between Pact and Viscount NZ that would occur.

89.2 the ability of NCI to expand by increasing imports from Australia in a manner that would constrain price rises by the merged entity.

89.3 the ability of the small domestic manufacturers to expand sufficiently to constrain price rises by the merged entity.

89.4 the potential for increased imports by other than NCI, to constrain the merged entity.

Loss of existing competition

90. The Commission considers that the proposed acquisition would be likely to result in a significant loss of existing competition. Pact and Viscount NZ are the two largest participants by a large margin. The Commission considers that Pact and Viscount NZ are the closest competitors and are the two main choices for the majority of purchasers in the plastic pails market. This view is consistent with the fact that the merged entity would supply as much as [ ] of the market post acquisition.

91. Figure 2 shows the present plastic pails revenues of Pact, Viscount NZ and NCI (as the third largest supplier in the market) by purchaser group.

Figure 2: Plastic pails sales revenue by purchaser group [

] Source: Pact, Viscount NZ, NCI

92. Figure 2 shows that, currently:

    92.1 Viscount NZ is the largest supplier to all types of purchasers.

    92.2 Pact is, by some margin, the second largest supplier in all purchaser groups except for food, where it and NCI have similar market shares. Pact has a particularly strong presence in the paint purchaser group with its largest customer, Resene, accounting for [ ] of all Pact's total sales.

    92.3 NCI is a distant third in all categories except for food.

93. Figure 3 shows the revenues by purchaser group that would occur in the factual.

Figure 3: Expected plastic pails sales revenue by purchaser group, post acquisition [

]

Source: Pact, Viscount NZ, NCI

94. Figure 3 illustrates that post-acquisition the merged entity would be the largest supplier across all purchaser groups by a substantial margin.

95. The Commission has assessed the likely loss of competition in the factual in comparison with the present level of competition between Pact and Viscount NZ to supply plastic pails to paint, food and industrial product manufacturers[37] under the following heads:

    95.1 competition to supply the individual requirements of different purchasers.

    95.2 numbers of purchasers switching supplier and the potential for this to occur.

    95.3 split supply[38] to purchasers.

Competition to supply the individual requirements of different purchasers

96. Purchasers of plastic pails have informed the Commission that they have stringent specifications for the type, quality, and decoration of the, in some cases large quantities, pails they buy.

97. In the case of paint pail purchasers, the implication of those requirements is that there are few, if any, competitive alternatives available to them other than the merging parties.

[37] Collectively, these purchaser categories represent [ ] of the plastic pails market by revenue.
[38] Split supply refers to purchasers purchasing from more than one supplier for the same product.

98. On the other hand, food and industrial product manufacturers' product and service requirements are such that some, although not all, are prepared to consider imports and the smaller domestic manufacturers' products.

99. Therefore, the Commission considers that in respect of paint manufacturers, Pact and Viscount NZ are the purchasers' two choices and a merger between the two would represent a significant loss of choice for plastic pail purchasers. This effect would be less pronounced for food and industrial product manufacturers. These matters are discussed below.

100. The three largest paint pail purchasers make up approximately [ ] of the total demand in the plastic pails market:

100.1 Resene purchases [ ] pails, worth [ ], per year from Pact and is the [ ] New Zealand pail purchaser by revenue.

100.2 Dulux purchases [ ] pails, worth [ ], per year from Viscount NZ and is the [ ] New Zealand pail purchaser by revenue].

100.3 Wattyl purchase [ ] pails, worth [ ] per year, from Viscount NZ and is the [ ] New Zealand purchaser by revenue.[39]

101. Paint pail purchasers stated that the proposed acquisition would reduce competition in the plastic pails market. They informed the Commission that Pact and Viscount NZ are their only options for plastic pails supply, as paint manufacturers do not currently consider that the existing small domestic manufacturers or importers provide realistic competitive alternatives. Plastic pails are of crucial commercial importance to sales of paint. For example, [ ] made the comment "no buckets, no business".[40]

102. Paint pail purchasers stated their preference to purchase pails from an established domestic manufacturer that they know can provide a consistent high volume supply of quality plastic paint pails. They stated that before they would consider purchasing from a new supplier, they would need sufficient confidence in the experience, ability and reputation[41] of the new supplier to:

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[39] Nestlé is the [ ] purchaser of pails in New Zealand.

[40] Interview with [ ], 5 November 2011.

[41] For example, Harold Demsetz, *The American Economic Review*, vol. 72, no. 1 (March 1982) at 50-51 notes that "{e}xisting firms have an advantage only insofar as their existence commands loyalty. Existence commands loyalty only if it reflects lower real cost of transacting, industry-specific investments, or reputable history, as, in general it will. Long survival at least indicates that the firm has not been a fly-by-night operator. When the cost to consumers of overcoming uncertainty is taken into account – that is, when total system cost is gauged rather than some narrow definition of production cost – then long-lived firms can be seen to offer consumers risk reduction ... A reputable history is an asset to the firm possessing it and or the buyer who relies on it because information is not free."

- supply paint pails on a "just in time" basis including allowance for unpredictable spikes in customer demand

- supply a family of products from which paint manufacturers could purchase a range of sizes

- have pail decoration and design ability

- supply pails of sufficient quality to avoid leakage or damage to the paint

- develop improvements to pails technology, anti-skinning pails being an example

- have the ability to incorporate recycled plastic paint pails into the manufacture of new plastic paint pails.

103. Further, paint pail purchasers have advised the Commission that they would be unlikely to switch to NCI due to (i) concerns about price competitiveness, and (ii) possible supply risks associated with NCI's import model. NCI's inability to meet "just in time" supply would be of particular concern. NCI as a potential constraint on the merged entity is further discussed below.

104. The smaller domestic plastic pail manufacturers do not presently appear to have the ability to meet these requirements of large paint purchasers. For example, [ ] submitted that:

> Small local manufacturers and importers are not an option, having regard to uncertainty as to their ability to supply volume, meet seasonal peaks in demand, ensure quality enhancements and service, and respond to increasing environmental concerns.

105. [ ], the Commission found no recent examples of a supplier other than Pact, Viscount NZ or NCI, being seriously considered as a potential supplier of an entire range of paint pails for a large paint purchaser. Currently, the options for paint manufacturers appear limited to these three firms. With a merger, the choice would be limited to two in circumstances where purchasers do not consider NCI's import model to be a realistic competitive alternative.

106. Smaller paint manufacturers were equally concerned at the suggestion they could switch to another supplier of paint pails. For example, [ ][42] advised the Commission that it would be concerned to lose the existing competition between Pact and Viscount NZ. While it would consider the potential to

[42] Interview with [ ], 2 December 2011.

import pails if the merged entity raised prices significantly, [ ] had little current knowledge of prices or delivery times. [ ] stated:

> Currently what I do is I peg those two (Viscount NZ and Pact) against each other and if they are close I feel good that we are buying at the right price. If one of them went away, I would then have to peg myself against an international price and all the hassle that importing has and that is not an efficient way of doing it because until the box lands you are not too sure on quality and delivery.
>
> Price is one thing, but it's service, I think that must fall in your realm and that is the bit they will have over us if they say now your lead time for printed stuff is 4 weeks, that's a cost to us, that's like putting up the price … if they get together and change the service quality to us and it saves them money then that is effectively a price rise to us and would be most concerned about this as I cannot pass this on. [43]

107. Similarly, [ ] expressed concerns in respect of the loss of pail supply options post acquisition. [ ][44] advised the Commission that in its view, only Pact and Viscount NZ currently have the ability to supply a quality 10 litre pail.

108. The Commission's view is that currently Viscount NZ, Pact and NCI are the only suppliers presently able to meet paint purchasers' needs. The evidence demonstrates that NCI's [ ], renders it a less attractive option compared to Pact and Viscount NZ. Although [ ] purchase their plastic pails from NCI, the weight of the evidence from paint manufacturers, large and small, was that Pact and Viscount NZ were the main supply alternatives. Furthermore, this would remain the position even with a significant price increase by the merged firm.

109. While the majority of food and industrial product manufacturers advised the Commission that Pact and Viscount NZ are the two main options for the supply of their pails, some members of these two purchaser categories stated that the smaller domestic manufacturers, NCI and other importers are currently pail supply options, or would be in the face of price increases in the factual.

110. The key requirement for food purchasers is the ability of the pail manufacturers to supply "food grade" pails. [ ] advised the Commission that Viscount NZ and Pact are presently the only two domestic suppliers of food grade plastic pails capable of meeting its needs. [ ] advised the Commission that imports would not present a competitive constraint on the merged entity because the freight

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[43] Interview with [ ] 2 December 2011

[44] Interview with [ ], 5 December 2011.

costs are likely to be prohibitive and it would be doubtful whether the proper food grade standard could be supplied by importers.[45]

111. That Pact and Viscount NZ are the two main choices for pails for many food manufacturers is reflected in Figure 3. On the other hand, some food manufacturers interviewed by the Commission such as [ ] were flexible in considering the smaller domestic manufacturers, NCI and other imports, as pail supply options.

112. Whilst [ ] of plastic pails in New Zealand, prefers domestic supply, it stated that in the event of price increases in the factual, it would look to Asian-based suppliers. [ ] would rely on existing plastic container suppliers to its Asian businesses to obtain plastic pails for its New Zealand operations. [ ] also had the ability to exercise some degree of commercial pressure on Pact by threatening to switch away from supply by Pact in other countries.

113. That Pact and Viscount NZ are again the two main choices for pails for industrial products manufacturers in the plastic pails market is also reflected in Figure 3. However, again the Commission received varied responses from industrial purchasers on the level of competition between Pact and Viscount NZ. Some industrial purchasers view Pact and Viscount NZ as their only present options while others include NCI, small domestic manufacturers and imports as current supply options.

114. In the Commission’s view, the conflicting responses from food and industrial materials purchasers of plastic pails arise because of differences in their individual circumstances in respect of their:

114.1 purchase quantities and ability to resist price increases.

114.2 downstream markets with different competitive dynamics, meaning varying abilities to pass on any post acquisition price increases.

114.3 end products having different values relative to the cost of the pails so that their abilities to absorb price increases in their production processes vary.

115. Examples are:

[45] Letter from [ ] to Commerce Commission (21 November 2011).

115.1 [ ] stated that Pact and Viscount NZ are its only options because smaller domestic manufacturers and NCI do not supply a pail that meets its strength requirements.[46]

115.2 [ ] stated that it obtains benefits from the competitive tension between Pact and Viscount but that it has also begun trialling imported pails for a proportion of its plastic pails requirements.[47]

115.3 [ ] are both currently supplied by NCI which they consider to be price competitive vis a vis both Pact and Viscount NZ.[48]

115.4 [ ] currently purchase pails from both Simaplas and Pact.[49]

116. However, in spite of the different views expressed to the Commission, given the data shown diagrammatically in Figure 3, the Commission considers that a relatively small proportion of food and industrial manufacturers consider they have plastic pail supply options from other than the merging parties.

Numbers of purchasers switching supplier and the potential for this

117. The evidence available to the Commission indicates that while there has not been a great deal of switching between Pact, Viscount NZ and others in the plastic pails market, the switching that has occurred has involved small volume purchasers and has mostly been between Pact and Viscount NZ. However, despite the low level of actual switching, all purchaser groups informed the Commission that they value the competitive tension provided by the potential for them to switch between two large domestic manufacturers.

118. Pact submitted that because the plastic pails market "is not characterised by the existence of long term contracts, purchasers are freely available to be competed for,"[50] both now and post acquisition. The Commission accepts that [ ] and other than this, there are no substantive contracts between plastic pail suppliers and purchasers which would restrict purchasers from switching between suppliers.

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46 Interview with [ ] 14 Dec 2011.

47 [ ]

48 Interview with [ ] 29 November 2011, Interview with [ ] 28 November 2011.

49 Interview with [ ] 22 November 2011.

50 Dr James A Farmer QC Opinion, 18 January 2012.

119. Nonetheless, the Commission found very limited evidence of switching, particularly for large purchasers. While large purchasers could switch, there appears to be a reluctance to do so due to the cumulative risks to purchasers, already identified, which do not make it worth their while to switch.

120. Pact and Viscount provided lists of their losses and gains of customers over the previous five years. However, examination of that evidence showed that:

120.1 the majority of switching has been between Pact and Viscount NZ.

120.2 Pact and Viscount NZ have lost [ ] volumes to NCI (for example, less than [ ] of Pact's revenue over the previous four years).

120.3 purchaser business closures were also included in the evidence but are not relevant to the switching argument.

120.4 [ ] example of loss [ ] to a small domestic manufacturer.

121. Pact emphasises that it is the 'threat of switching' which is more relevant than evidence of actual switching. Pact submitted that around [ ] of its plastic pail purchasers have avoided a price increase by threatening to switch to imports. It cites specific examples, including [ ], which avoided a price increase and obtained a discount after informing Pact it intended to obtain quotes from Chinese importers and NCI.

122. Viscount NZ informed the Commission that some of its purchasers had switched to imports, although it was mostly able to recapture that business by offering better terms to the purchasers. In Viscount NZ's view, purchasers would continue to have this ability post-acquisition.

123. The Commission's view is that while NCI and other importers have at times been successfully used as competitive threats, Pact and Viscount NZ continue to be the main competitive alternatives for purchasers. This is evidenced by their market shares and the fact that the majority of switching that has occurred has been between Pact and Viscount NZ.

Split supply

124. Pact considers that the presence of split supply in the plastic pails market illustrates that purchasers are willing to entertain two suppliers in the market. Pact argues that, post acquisition, this trend would continue with purchasers using NCI or others for their split supply arrangements to maintain competitive tension.

125. However, as already noted, the Commission has found that almost all paint purchasers have one primary supplier. For example, each of the large paint suppliers in New Zealand has a long standing relationship with their plastic pails supplier.

126. Some large food purchasers do purchase from more than one supplier to maintain competitive tension. For example, [

]

127. However, the Commission notes that any split supply is mostly between Pact and Viscount NZ. Further, the split supply arrangements appear to be the result of a customer preference for the design parameters of a particular pail supplied by one or other of Pact, Viscount NZ or NCI. For example, [

].

128. In summary, the Commission considers that the level of split supply in the market is small and such split supply as does exist, is largely the result of historic relationships driven by a demand for a special design or size of pail rather an attempt by purchasers to ensure competitive tension.

Conclusion on the loss of existing competition

129. Taking into account the information and views provided to it, the Commission concludes that Viscount NZ is presently a significant competitive constraint on Pact in respect of the supply of plastic pails to purchasers in the three categories that the Commission has analysed and that when the factual is compared to the counterfactual, that constraint will be lost.

Would NCI expand importing to constrain the merged entity?

130. If the proposed acquisition goes ahead, the Commission is not satisfied that NCI would provide sufficient competitive tension in the market to constrain the merged entity, either as an existing (as noted above) or expanded competitor. In the Commission's view, expansion of imports by NCI is unlikely to constrain the merged entity because:

130.1 as an importer NCI has an inherent freight cost and logistical disadvantages compared to domestic manufacturers.

130.2 it is capacity constrained to some extent [ ].

Pact's and Viscount NZ's views on potential impact if NCI expanded importing

131. Pact submitted that:

131.1 NCI already imports a range of pails into New Zealand and produces an even larger range of plastic pails in Australia where it is the largest supplier.

131.2 NCI has in the last three years won supply contracts in New Zealand from Pact and Viscount NZ and presently supplies New Zealand Sugar, Goodman Fielder, Unilever, and Heinz Wattie's.

131.3 If the merged entity were to increase price or reduce quality, it is likely that this would incentivise NCI to increase the scale and scope of its imports into New Zealand.

131.4 NCI has the ability to expand supply in New Zealand of every category of pail currently supplied by either Pact or Viscount NZ.

132. Viscount NZ submitted that it considers NCI, rather than Pact, to be its main competitive threat in the plastic pails market. It cited feedback from Viscount NZ's customers on the competitiveness of NCI. Viscount NZ stated that post acquisition NCI would provide effective competition because NCI:

132.1 can meet the needs of all purchasers of plastic pails on price, range and logistics.

132.2 is already supplying a range of different purchasers, including well known food manufacturers and it could use this track record to supply other food purchasers.

132.3 is well placed to supply large paint purchasers given that it already has an established relationship through the supply of its New Zealand-manufactured tin pails. This relationship could enable NCI to bundle both tin and plastic pails to provide an attractive alternative for large paint purchasers.

133. Both Pact and Viscount NZ emphasised that while NCI's market presence may be small, its competitive constraint is felt by both parties. In their view, the threat of losing purchasers to NCI is presently real and would increase post acquisition in the event that the merged firm increased prices or reduced quality.

The Commission's assessment of NCI as a competitor via its imports

134. To assess NCI's position as a competitor – more particularly its ability to expand and replace the loss of competitive choice with the acquisition – the Commission has examined how NCI entered the plastic pails market, its subsequent expansion and assessed its ability to expand further.

135. First, the Commission considered NCI's current position in the plastic pails market in relation to:

135.1 any cost disadvantages vis a vis New Zealand manufacturers.

135.2 any non-price elements of competition that might exist.

135.3 its customer base.

135.4 its import model.

NCI's entry and subsequent expansion into importing

136. NCI's New Zealand factory has been supplying tin plate cans and other packaging products since 1974. In the 1990s, NCI diversified in Australia into manufacturing plastic pails as the trends in packaging were moving away from metal pails to plastic.

137. NCI began importing plastic pails into New Zealand approximately 10 years ago and began importing IML pails about five years ago. [

]

138. The Commission considers that NCI has the potential to provide some competition in the market post acquisition because NCI:

138.1 is a large participant in the Australian plastic pails markets.

138.2 manufactures the required range of plastic pail sizes.

138.3 has a proven record of reliable supply and established relationships with large paint purchasers with regard to the supply of tin pails in New Zealand and Australia.

138.4 could provide a bundle of tin and plastics pails that would be attractive to large paint purchasers.

139. However, NCI itself admitted that its expansion in New Zealand post acquisition will continue to be hampered by the higher costs of its imported pails compared to the costs of those produced in New Zealand by Pact and Viscount NZ.

NCI's cost disadvantage

140. To consider this issue in more detail, the Commission obtained the average variable cost of producing both a 10 litre plastic pail without decoration (from Pact, Viscount

NZ and NCI), and a 10 litre plastic IML pail (from NCI and Viscount NZ).[51] The results are shown below in Table 2.

Table 2: Ex-factory costs for 10 litre pails (including lids)

Parties	Costs	Per unit	Generic 10L Pail	Per unit	IML 10L Pail
Pact	Materials	[ ]			
Ex Auckland	Labour	[ ]			
	Variable cost		**[ ]**	x	No IML pails
Viscount NZ	Material	[ ]		[ ]	
Ex Auckland	Labour	[ ]		[ ]	
	Variable cost		**[ ]**		**[ ]**
NCI	Material	[ ]		[ ]	
Ex Melbourne	Labour	[ ]		[ ]	
	Variable cost		**[ ]**		**[ ]**
Ex Auckland	**Variable cost + transport**	**[ ]**	**[ ]**		**[ ]**

Source: Pact, Viscount NZ, NCI. Note: NCI's costs are converted at a NZD/AUD rate of 0.8

141. As can be seen, the variable costs ex-factory of Pact, Viscount NZ and NCI are not dissimilar (within [ ]). However, NCI has advised that its transport costs from Australia to New Zealand are [ ] per pail and as a result, NCI's variable costs including transport are between [ ]% higher than Pact and Viscount NZ. This represents a significant cost disadvantage for NCI in comparison to Pact and Viscount NZ and supports NCI's claim that its higher costs are impeding its ability to compete effectively in the plastic pails market.

142. This competitive disadvantage is further evidenced by NCI's failure to win large paint customer tenders. NCI expects this situation to remain for the foreseeable future due to the high cost of freight between Australia and New Zealand.

143. NCI advised the Commission that it has not been successful in gaining any of the three large paint manufacturers as customers. The Commission interviewed Dulux and Wattyl to explore the reasons for this:

143.1 [

[51] The Commission used figures for a 10 litre pail as this is the most common type and, in its view, a good benchmark for comparing variable costs across competitors. The Commission recognises that it can sometimes be difficult to compare cost data across firms, due to variations in allocating costs. However, in this case it seems reasonable that the firms' variable costs would be similar as they predominantly use the same inputs into the manufacturing process. The Commission notes that internal New Zealand transport costs would be additional to these costs. However, these costs would be similar across all firms.

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[

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143.2 [

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144. [

][52] [

] In the Commission's view this example of NCI winning a New Zealand pail supply contract is not generally

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52 NCI response to Commission information request (20 December 2011).

applicable. The situation is unique as it arose only as a result of [

].

Non-price elements of competition

145. All paint purchasers advised the Commission that switching to NCI in the factual, even with a significant price increase by the merged firm, would involve risk. For example:

145.1 [ ] noted that NCI had a slightly different size of pail, compared to Pact and Viscount NZ. This could create problems at retail outlets with the potential existing for purchasers of paint to make unfavourable comparisons between the NCI and the other pail designs. However, in spite of this matter, [ ] would reconsider NCI if the merged entity raised prices post-acquisition.[53]

145.2 [ ] advised the Commission that it had trialled NCI's pails but had found the lid design to cause difficulties with the proper mixing of added colours. It received negative feedback about the pails from users.[54] In spite of this, [ ] advised the Commission that it had been able to use the NCI supply threat to negotiate substantially lower prices from its existing supplier. However, it would always have issues with the extra capital required arising from importers' payment in advance requirements.

146. [

].[55]

147. Food purchasers also had non-price based concerns with switching to NCI. [ ], advised the Commission that, while it considers NCI to be an alternative supplier for it in Australia, the longer lead times and extra costs involved with importing pails from Australia would mean that NCI would not be a viable alternative for it either now or post acquisition.

Customer base

148. Although NCI is at a cost disadvantage (and in certain cases at a disadvantage in regard to non-price elements of competition), NCI advised the Commission that it does currently sell to a limited number of "niche" players primarily in the health and food industries. NCI considers that its partial success is due to:

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53 Interview with [ ], 14 December 2011.

54 Interview with [ ], 5 December 2011.

55 [

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148.1 Niche purchasers requiring pails with a high quality IML covering the entire pail surface. NCI was the first to introduce this type of pail in Australia and this design has allowed it to gain "some limited success" with purchasers in New Zealand.

148.2 [ ].

148.3 [ ].

149. NCI provided information that it has approached [ ] potential purchasers in New Zealand over the last three years and has been successful in gaining orders from [ ]. At present, [ ] of NCI's purchasers (by revenue) are food manufacturers while another [ ] are small paint manufacturers. NCI's figures indicate that while NCI is approaching a range of purchasers and has had some success in gaining supply, it has yet to gain a large customer such as a paint manufacturer or a large food supplier.

150. The Commission notes that NCI's limited market presence appears to be a reflection of purchasers using it as a competitive threat that is ultimately not exercised due to resulting price concessions obtained from the incumbent suppliers. However, the Commission also notes that:

150.1 given the length of time that NCI has been operating in New Zealand, it would expect more evidence of it gaining market share if NCI was to be a realistic constraint post-acquisition.

150.2 NCI's customer list suggests that where switching has occurred, the majority of cases have been in regard to pails with high quality decoration, a relatively small proportion of the total plastic pails market.

151. NCI's inability to gain significant market share via its importing model suggests that it is competitively disadvantaged in relation to domestic manufacturers. The issue for the Commission is whether this would change in the event of a significant price increase or reduction in quality.

Import model

152. NCI considers that there are two conditions that would prevent it from expanding its current level of imports in the factual:

152.1 the high landed cost of its imports would remain non-cost competitive compared with local manufacture.

152.2 the threat of a response by the merged entity due to the merged entity's excess capacity.

153. NCI advised that it has no plans to expand its current level of importing even if prices increased post acquisition. Rather NCI would continue to target purchasers which require the high quality IML plastic pail, [ ].

154. Post acquisition, the removal of the competitive constraint between Pact and Viscount NZ is unlikely to improve NCI's cost structure and product quality. Were prices to increase post acquisition, NCI may gain some additional market share in this higher price environment. But the Commission is not satisfied on the weight of the evidence that NCI would be able to replace the significant loss of competition between Pact and Viscount NZ given NCI's significant cost disadvantages and the Commission's concerns over NCI's ability to import a sufficient numbers of pails.

NCI's ability to expand its imports

155. While NCI has been active in attempting to acquire market share, for the reasons set out above, it has not been successful in gaining any large New Zealand customer other than [ ]. NCI advised the Commission that [ ] volumes would "not provide a springboard from which it could grow its market share". NCI maintains that capacity constraints, import transport costs and incumbent responses would prevent further expansion.

156. NCI advised the Commission that even if it were to gain a large customer's business, it would take [ ] to "ramp up" production in order to supply a customer the size of, for example, [ ].[56] NCI submitted that [

]:

156.1 [

].

[56] As set out in the *Mergers and Acquisition Guidelines* at p 29, the Commission considers that "...if entry is to alleviate concerns about a substantial lessening of competition, entry must be feasible within a reasonably short timeframe, considered to be two years, from the point at which market power is first exercised". However, as noted on p 28, "...if the only viable entry occurs at the fringe of the market, and fails to attack the incumbent's core business, then entry cannot be seen as being an effective constraint."

156.2 [ ].[57]

156.3 [ ].This latter figure may be compared with the annual supply of 10 litre of pails to, for example,[ ] in New Zealand of about [ ]units.

157. NCI stated that its [ ] "ramp up" period would enable the merged entity to use its excess capacity to [ ]. NCI advised the Commission that the merged entity could [ ].

158. The Commission notes that neither Pact nor Viscount NZ is currently capacity constrained to any extent. Pact's current utilisation is approximately [ ] while Viscount NZ's utilisation is approximately [ ].[58] In NCI's view, the merged firm's ability to respond using its excess capacity would increase the risk of it expanding in New Zealand.

159. However, the Commission notes that NCI's spare capacity would currently allow it to immediately supply the entire 10 litre pail demand of [ ] large New Zealand paint manufacturer purchasers (or a greater number of smaller purchasers of 10 litre pails). Given the above position, the Commission considers that NCI would, other factors being equal, have the ability to expand its sales in New Zealand in short order. However that said, it would still be unlikely that NCI would be price competitive vis a vis the merged entity.

Conclusion on the competitive constraint of NCI as an importer

160. At present, NCI has a very small presence in the New Zealand plastic pails market [ ]. NCI has been importing plastic pails into New Zealand for approximately 10 years, but it has not obtained a market presence of any significance in this time. Its IML technology has found favour amongst some New Zealand purchasers. However, in spite of that potential entrée into the relevant market, NCI's market share remains small.

161. Importantly, NCI has, to date, been unable to secure a significant contract with a large customer. This is despite NCI having an established presence in New Zealand

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[57] NCI noted that [ ].

[58] This is based on the standard three shifts per day, operating five days per week. Viscount NZ's figure incorporates the closure of the Christchurch plant and redistribution of machinery to Auckland.

through its tinplate division as well as an established reputation for supplying a range of plastic pails in Australia.

162. The Commission acknowledges that for some purchasers NCI would be a viable alternative in the factual. This conclusion would particularly apply to small volume purchasers who require high end IML decoration or who also purchase tin products from NCI.

163. While NCI may provide some competitive constraint post-acquisition, on the weight of the evidence, the Commission considers that for a substantial proportion of purchasers in the market, NCI would not be a credible alternative in the factual.

164. Therefore, in the Commission's view, NCI would not provide a strong competitive constraint on the merged entity post acquisition. In particular, expansion of its supply of plastic pails in New Zealand would be unlikely due to its cost disadvantages in comparison with the merged entity.

The constraint by other existing domestic manufacturers

165. If the proposed acquisition proceeds, the Commission could not be satisfied that the other domestic manufacturers would provide sufficient competitive tension in the market to constrain the merged entity for the following reasons:

  165.1 smaller domestic manufacturers would need to make a substantial step increase in their production volumes to provide a constraint.

  165.2 purchasers are unlikely to sponsor expansion.

166. Of the competitors listed in the application, only four manufacturers of note appear to be presently producing plastic pails in New Zealand, namely:

- Galantai, in Auckland
- Plastech, in Christchurch
- Simaplas, in Auckland
- Uniplas, in Wellington.

Small manufacturers ability to expand

167. Both Pact and Viscount NZ submitted that, while the existing market share of these parties is presently small, if incentivised by the actions of the merged entity these small domestic manufacturers, who supply the same range of pails, would have the ability to quickly expand.

168. In the Commission's view, these manufacturers would only expand if they were able to secure commitments from a number of purchasers of plastic pails:

168.1 [ ] advised the Commission that it is interested in the potential opportunities the proposed acquisition could provide, and it has the ability to ramp up its production if sufficiently incentivised. But it said that to expand it would need to invest and would need certainty that it would be able to recover the investment by a significant increase in pail sales.[59]

168.2 [ ] advised the Commission that it is focused on certain [ ] products and contract moulding and has no intention of expanding its range of plastic pails.[60]

168.3 [ ] advised the Commission that in order to consider expanding its plastic pail range, and therefore its presence in the market, it would ideally need to secure an order to supply one of the three large paint purchasers. It stated that paint manufacturers are resistant to change and would be reluctant to consider it as a pail supply option, [ ].[61]

168.4 [ ] advised the Commission that if prices increased post acquisition, an opportunity for it to expand its range and volume could arise. However, it considers that to be a serious competitor, it would need to obtain surety that it would gain customers. It advised that it would need to spend an additional $500,000 to $700,000 on tooling and decorating equipment to meet the requirements of large purchasers which, to it, would be a significant expenditure. [ ].[62]

Other domestic manufacturers' ability to constrain the merged entity

169. If the proposed acquisition goes ahead, the Commission could not be satisfied that small domestic manufacturers would provide sufficient competitive tension in the market to constrain the merged entity.

170. The Commission accepts that small domestic manufacturers presently provide a supply option for some plastic pail purchasers and that would continue in the factual. For example, [ ],

[59] Interview with [ ], 17 October 2011.
[60] Interview with [ ], 18 October 2011.
[61] Interview with [ ], 13 October 2011.
[62] Interview with [ ], 29 November 2011.

respectively food and industrial products purchasers,[63] currently obtain their plastic pails from small domestic manufacturers and consider them to be price competitive.

171. However, the Commission also notes that small domestic manufacturers could quickly become capacity constrained. In particular, if large paint and food manufacturer purchasers (who, as previously discussed, are unlikely to switch to a small supplier) are excluded, there remains approximately [ ] of the volume of the market. At present, small manufacturers collectively only account for about [ ] of the market. Even if a relatively small portion of all demand by non-paint and non-large food purchasers were to switch to small manufacturers, it appears to the Commission that the available spare capacities of these small manufacturers would be quickly swamped.

172. This would be especially likely if a smaller manufacturer were to secure a large customer. To secure a large customer, a smaller manufacturer would have to invest in a step increase in production to obtain the relevant injection moulding machines and moulds. The Commission's view is that obtaining sufficient customers to make a proper return on that investment is the main factor which would limit expansion of any of the small manufacturers.

173. The Commission considers that, in the factual, large purchasers would be unwilling to encourage expansion of a domestic manufacturer that has no experience of large-volume supply of pails. [ ] advised the Commission that they would only consider switching to a small domestic supplier in the event that post acquisition prices rose by [ ] and that the switch would likely take [ ] years. [ ] advised the Commission that the smaller local manufacturers would not be an option for it due to its large volumes and it would be unlikely to sponsor expansion post acquisition if prices increased.

174. In terms of large food purchasers, one large food customer, [ ], suggested that it would consider purchasing from a small domestic manufacturer if the merged entity's prices increased or its service declined, post acquisition. Alternatively, it would consider importing pails via its connections in Asia.[64] However, other large food purchasers such as [ ] advised the Commission that they would be unlikely to use small domestic manufacturers post acquisition even in the face of prices increases. This was due to the small manufacturers' inexperience in large scale supply, limited pail product ranges and inability to provide innovative developments of pail technology.

63 Interview with [ ], 23 November 2011. Interview with [ ],28 November 2011. Phone call with [ ], 22 November 2011.

64 Interview with [ ], 7 November 2011.

175. Overall, the Commission considers that, post acquisition, paint purchasers and most large food purchasers would not, even in the face of a significant price increase switch their pail purchasing to small domestic manufacturers. They would be concerned about the capacity of the smaller manufacturers and the likely quality of the pail output.

Expansion of imports by other than NCI

176. The Commission considers that expansion of imports[65] either through distributors or by plastic pail purchasers' self supply, would not provide sufficient competitive constraint post acquisition.

Third party distributors

177. Pact submitted that third party distributors (such as Stowers) could readily expand and increase their pail sales by importing increased volumes.

178. However, Stowers advised the Commission that [ ] its imports of plastic pails are limited (see Table 1) as it cannot be assumed that purchasers will accept an imported product. Stowers said that its previous attempts to import and distribute plastic pails (and other plastic products) have been problematic [ ].

179. [ ].

180. Further, Stowers advised the Commission that, as a distributor, [ ].

181. [ ].

[65] Note that while NCI is an importer, the potential for NCI to provide competitive discipline is separately considered above.

182. Another distributor based in Australia, Swiss Pack Australia Pty Limited (Swiss Pack) imports and distributes plastic pails manufactured in India. Swiss Pack noted that with only one major domestic manufacturer of plastic pails in New Zealand post acquisition, an opportunity for Swiss Pack might arise if the merged entity raised prices. However, Swiss Pack recently imported a container of plastic pails to New Zealand but the international freight costs meant that the pails were not price competitive.[66]

183. Small paint manufacturers were cautious about reliance on Stowers or other distributors. [ ] informed the Commission that Stowers' pricing was expensive compared to their current supplier.[67]

184. The Commission considers that imports via third party distributors would be unlikely to provide sufficient competitive constraint on the merged entity post acquisition. Purchasers in general do not view distributors such as Stowers (which has less than [ ] of the plastic pails market) as credible alternatives to local manufacturers.

Direct importing of plastic pails by users

185. Most large purchasers have not seriously considered the option of direct importing. However, in the face of a price increase post acquisition, direct importing may be a realistic option for some food and industrial purchasers. [ ] advised the Commission that, if faced with pail price increases post acquisition, they have the necessary infrastructure in South East Asia to source plastic pails from that region and they would not require a third party distributor to organise such imports.[68]

186. [ ] advised the Commission that it has imported one container load of plastic pails from China. However, to organise that direct import was "challenging".[69] The process took 18 months and even after that time, there are still issues with the quality of the pail decoration. However, if the merged entity raised prices by 5-10% following the acquisition, it would expand its import programme. While the company values the simplicity, and certainty of quality, of local supply, it does consider imports to be a feasible alternative. Similar views were expressed by [ ].

187. In contrast to these views, paint purchasers, both small and large, indicated that their requirements for regular and consistent supply of high quality plastic paint pails

66 Interview with Swiss Pack, 9 November 2011.

67 Interview with [ ], 5 December 2011.

68 The ability of some large food purchasers to directly import and/or use importing as a credible threat to counter a price rise by the merged entity is discussed in the countervailing power section of the competition analysis.

69 Interview with [ ], 25 January 2012.

means that it would take a significant price increase by their domestic supplier, before they would consider direct importing. For example, [ ] considered that importing has inherent risks stating that:

> Overseas suppliers cannot assure certainty of supply, because some factors affecting delivery are beyond their control. The longer and more occasional the supply chain, the greater the risk of interruption. This is particularly relevant for the paint industry as sales of paint undergo significant seasonal variations.

188. [ ] advised the Commission that it would investigate the feasibility of manufacturing pails itself if faced with a price increase of [ ] and directly importing if faced with a price increase of [ ]. Further, a small paint manufacturer, [ ], commented:

> [
>
>][70]

189. [ ] also advised the Commission that while it prefers to deal with a domestic manufacturer, given a price rise, importing was a possible alternative. However, it would remain concerned about the quality of plastic pails imported from Asia and the longer lead times for supply.[71]

190. [ ] advised the Commission that imports would not present a competitive constraint to the merged entity because the cost of freight is likely to be prohibitive. Industrial purchasers, [ ] and [ ] both indicated that the costs of managing currency exchange rate fluctuations, freight costs, lead times and warehousing costs, were prohibitive to their importing. [ ] indicated that its volumes were not high enough to make the effort of importing worthwhile. [ ] indicated that it would consider importing but only if faced with a price increase of at least 10%.

70 Email from [ ], 7 December 2011.
71 Interview with [ ], 1 December 2011.

Conclusion on the constraint from expansion of imports

191. The Commission considers it unlikely that imports, either via third party distributors or through self supply, will constrain the merged entity. While some food and industrial purchasers would be able to import plastic pails in the event that the merged entity increased prices, this only applies to large purchasers which have established logistics networks overseas and experience in sourcing packaging from overseas suppliers. Many small purchasers do not have existing networks, and their volumes would not justify the time and effort required to arrange imports. Moreover, the evidence shows that it would take a large price increase in the factual before the importing of plastic pails would become a viable option for paint manufacturers, large and small.

Potential competition

192. The Commission considers that the potential for competition from entrants would not provide sufficient competitive constraint on the merged entity in the factual. The Commission considers that greenfield entry into the plastic pails market does not satisfy the LET test described below. The Commission is not satisfied that entry would occur without a price increase of at least 20% post-acquisition. Given the importance Pact placed on entry as a constraint, the Commission discusses its detailed reasons for this conclusion below.

193. The Commission considers whether viable entry is likely in a timely fashion and on sufficient scale so as to prevent any substantial lessening of competition in the factual. The Commission analyses whether any businesses, incentivised by price rises by the merged entity, would enter the relevant market and thereafter expand.

194. In doing so, the Commission examines entry conditions, together with any impediments to entry and expansion entrants would face.[72] The likely effectiveness of entry is determined by the nature and effect of the aggregate barriers to entry into the relevant market. As noted by the Court of Appeal in *Southern Cross*:[73]

> Anything is capable of being a barrier to entry or expansion if it amounts to a sig*nificant cost* or limitation which a person has to face to enter a market or expand in the market and maintain that entry or expansion in the long run, being a cost or limitation that an established incumbent does not face. The height of the barrier is a function of the degree of the differential. A barrier to entry or expansion reflects the extent to which an established firm can, in the long run, raise price above marginal cost (supra-competitive pricing) without inducing potential competitors to enter or expand in the market.

[72] Natural, regulatory and strategic barriers to entry are discussed on p 28 of the Commission's *Mergers and Acquisitions Guidelines*.

[73] *Commerce Commission v Southern Cross Medical Care Society* (CA) above n8 at para 73.

195. This part of these reasons examines the requirements for entry and uses the internationally applied “LET” test to assess whether entry would constrain the merged entity. That is, in order for market entry to be a sufficient constraint, entry of new participants in response to a price increase or other display of market power must be **likely** in commercial terms; sufficient in **extent** to cause market participants to react in a significant manner; and **timely** - feasible within two years from the point at which market power is first exercised.

Pact’s submission

196. Pact submitted that NCI’s entry into the plastic pails market through importing demonstrates that barriers to entry are low. Pact also submitted that entry via a greenfield operation and/or imports would be possible if the merged entity raised prices or reduced the quality of its service or products. This is because:

196.1 technological developments have decreased the cost of machinery needed to manufacture plastic pails.

196.2 the capital cost of entry could be justified with a guaranteed supply contract from a large purchaser.

196.3 entry would be likely if the merged entity were to increase prices by 5% to 10%.

The likelihood of entry

197. In order to be a constraint on market participants, entry must be likely in commercial terms. An economically rational firm will be unlikely to enter a market unless it has a reasonable prospect of achieving a satisfactory return on investment, including an allowance for any risks involved.

198. In this case, the Commission has analysed the likelihood of entry by the following paths:

198.1 NCI (or other) establishing a greenfield manufacturing operation by building and equipping a plastic pails manufacturing unit, or

198.2 a new Australian or Asian plastic pails manufacturer providing imports into New Zealand, or

198.3 an existing New Zealand plastics manufacturing business, experienced in the plastics industry but not presently manufacturing plastic pails, installing machinery to do so.

The likelihood of greenfield entry by NCI

199. Pact submitted that a greenfield "first stage" entry with a single line producing only 10 litre plastic pails would cost approximately [ ] million. A "second stage" entry with the capacity to produce a range of eight pail sizes would cost about [ ] million. These costs would cover the necessary injection moulding machines, the necessary moulds and the decorating plant. The Commission tested these costs with industry participants and found them to be reasonably accurate. Details are shown in Table 3 below which sets outs the costs of entry as submitted by Pact, compared to figures obtained from industry participants.

Table 3: Costs of first stage entry

Equipment	Single pail entry – Pact's submission	Industry estimates	Source of industry estimate
Machinery	Standard [ ] Top of the line European design- [ ] million	$400,000 - $1 million plus handle making equipment costing $360,000	Uniplas, NZ Plastics, Packit Packaging, Simaplas, NCI, Viscount NZ.
Moulds	Low tech from [ ] High tech [ ]	$100,000 - $250,000 for a single size, including lid	Uniplas, Plastech, Simaplas, Packit Packaging, Viscount NZ.
Decoration	In-mould labelling with robotics [ ] High quality offset printing [ ]	$200,000 - $300,000 for basic high volume labelling equipment $700,000 - $800,000 for high end labelling equipment	Dulux, Resene, Uniplas, Plastech, Simaplas, NCI, Viscount NZ.
Total	Entry Costs $815,000 - $2,930,000	Second hand equipment $1 million New Equipment $2 million	

Source: Pact, industry participants.

200. The costs of this machinery have to be balanced against the likelihood of positive profitability after entry and the risks of entry. NERA, on behalf of Pact, provided a

multi-period model of the cash flows involved if NCI, in Pact's view the most likely entrant, established a local manufacturing plant.[74]

201. While the Commission does not consider that NCI would be able to provide a competitive constraint in the plastic pails market post acquisition by importing pails, its ability to impose a competitive constraint would be improved if it established a new plastic pail manufacturing plant in New Zealand.

202. The Commission also considers NCI to be the greenfield entrant with the most potential to enter. NCI already has a large manufacturing site in Auckland manufacturing metal containers and has existing relationships with large consumers of plastic pails. The Commission considers that if entry by NCI is not viable, entry by others would be less so.

203. NERA submitted that under its model "with no post-merger price rise, the present value of cash flows is negative, and so expansion by NCI into local manufacturing would not be a profitable strategy". However, according to NERA, with a price increase of 5%, the net present value of profits, which extends over a 20 year period, would range from [ ].[75]

204. The main assumptions of the NERA model are:

- an investment to produce only 10 litre pails
- a 20-year lifespan for capital assets
- annual fixed costs of [ ] and a one-time capital expenditure of [ ]
- [ ] 10 litre pails currently sold by NCI per year
- NCI gains an order to supply [ ] 10 litre pails per annum in the factual
- a discount rate of [ ]
- avoided transportation costs between Australia and New Zealand in the range [ ] per 10 litre pail.

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74 NERA "Pact Group/Viscount: Domestic Entry Model", 19 January 2012.

75 The range of profits depends on the size of avoided transportation costs assumed between Australia and New Zealand. The assumed, avoided transportation costs range from [ ].

205. Of these, one important assumption is incorrect. NCI informed the Commission that in 2011 it sold [ ].[76] If the correct figure is inserted into the NERA model, the net present value of profits over a 20 year period declines by over [ ] to become between [ ]. The Commission also notes that if the model is sensitivity tested, absent the assumed new [ ]supply contract but including a 5% price increase, NCI would have to increase its 10 litre pail sales from [ ] to between [ ], merely to achieve a zero net present value of its 20 year future profits.[77]

206. In the Commission's view the NERA model suggests relatively low returns over a 20 year period even with a [ ] increase in NCI's sales volumes (if in fact that occurred). As already discussed in relation to the question of NCI's expansion (as an existing competitor), the weight of the evidence including that from NCI itself, is that NCI is unlikely to establish a local manufacturing plant.

207. Moreover, the model aside, the Commission notes that the merged entity's excess capacity together with the relatively low volume requirements for pails in New Zealand would be likely to make profitable greenfield entry by NCI an unlikely proposition, with or without the proposed acquisition.

208. NCI itself emphasised to the Commission that the main issue concerning a new investment in a New Zealand pail manufacturing would be low volumes. It stated that there is no single customer that could be targeted that would give NCI sufficient volumes to incentivise investment.[78] For example, [

].

209. NCI provided details of its most recent analysis of the potential for greenfield entry into plastic pails manufacturing in New Zealand. The analysis set out below in Table 4 demonstrates the potential returns NCI could expect if it were to construct a manufacturing plant in New Zealand to supply 10 and 20 litre plastic pails.

210. In respect of its analysis, NCI noted:

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76 NCI response to Commerce Commission information request, 20 December 2011.

77 The range depends on the size of avoided freight costs assumed.

78 [

]

The summary considers the returns for NCI if it was able to gain [ ] of the available New Zealand demand. All of these market share assumptions are unrealistically high, but illustrate why this type of entry is [

].

Table 4: NCI's cost of entry analysis

High level investment analysis if NCI was to enter into the manufacture of 10 L to 20 L IML plastic pails in New Zealand			
Market share gains (10L, 15L & 20L pails)	[ ]	[ ]	[ ]
Estimate Revenue (excludes NCI current revenue) NZD,000	[ ]	[ ]	[ ]
Gross Contribution	[ ]	[ ]	[ ]
Gross Contribution %	[ ]	[ ]	[ ]
Fixed Costs	[ ]	[ ]	[ ]
EBITDA	[ ]	[ ]	[ ]
Depreciation	[ ]	[ ]	[ ]
EBIT	[ ]	[ ]	[ ]
Interest expense	[ ]	[ ]	[ ]
PBT	[ ]	[ ]	[ ]
Tax	[ ]	[ ]	[ ]
PAT	[ ]	[ ]	[ ]
Capital investment (Machinery and infrastructure)	[ ]	[ ]	[ ]
Return on investment (EBIT / Capital)	[ ]	[ ]	[ ]
Payback (years)	[ ]	[ ]	[ ]

Assumptions
Revenue is based on the NCI average sell prices in NZ discounted by [ ] in order to gain market share.
Gross contribution margin is assumed to be[ ].
Fixed costs are based on a small stand alone leased site.
Capital investment is based on equipment similar to that used by NCI Australia for the manufacture of 10 to 20 litre pails and lids.

Source: NCI response to Commission information request (2 December 2011)

211. In NCI's view, the return on investment shown in its model does not justify NCI setting up a greenfield plant, post acquisition. [

]. In addition, NCI believes that, doubtful economic viability aside, if it were to establish a New Zealand plant, the merged entity would reduce domestic pricing and would have considerable incumbent advantage over NCI in negotiations with all other significant purchasers.

212. As indicated by the NERA model, it would be necessary for NCI (or any new manufacturing entrant) to obtain the support of a large customer in the form of a long term supply contract.[79] In the Commission's view, large purchasers, who represent a significant proportion of the market, would be unwilling to provide this support.[80] This option would become a realistic alternative only if large purchasers were faced with price increases of 20% or more.

213. Therefore, the Commission does not consider that greenfields entry, in the form of a new manufacturing operation by NCI, as the potential entrant best positioned to be viable, would occur. As stated a similar conclusion applies to other potential greenfields entrants. This conclusion is based on the following:

213.1 Even with a price increase of over 5%, NERA's entry model requires either the acquisition of a large volume customer by NCI or at least a [ ] step increase in its existing sales to provide positive profitability from entry over 20 a year period. On the other hand, the qualitative evidence that the Commission has obtained shows that achieving that level of increase would not be likely to occur. Under current market dynamics, no large purchaser in the plastic pails market interviewed by the Commission would consider purchasing the requisite number of pails from a new entrant.

213.2 There are quality, logistical and volume risks to all large purchasers if they were to commit to an unproven new entrant, and in the case of paint manufacturers, special technical risks.

213.3 Modelling provided to the Commission by Pact, together with the NCI's statements to the Commission indicates that NCI would not consider entering New Zealand with a new plastic pails manufacturing operation. In NCI's view, given the available volume, the returns generated would be unsatisfactory.

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79 See evidence from [ ]

80 For example, the [ ] all reject this option. Together, these [ ] purchasers account for over [ ]% of purchases in the market.

213.4 the merged entity would have excess capacity and potential entrants would know that it had the ability to act strategically to oppose their entry.[81]

The likelihood of entry by a new Australian or Asian plastic pails manufacturer providing imports into New Zealand

214. In Australia, Pact, Viscount Pty and NCI are the three main manufacturers of plastic pails along with a number of smaller suppliers. NCI is the only firm that currently supplies pails into New Zealand from Australia. Earlier in these reasons, the Commission found that NCI is constrained in its ability to provide a sufficient competitive constraint on the merged entity by expansion of its importation of pails.

215. The Commission also considers that other Australian-based suppliers of plastic pails would be unlikely to enter the plastic pails market in New Zealand post acquisition. A number of these manufacturers advised the Commission that they prefer to focus on expansion in the much larger Australian market, rather than examine entry into New Zealand. They noted that the relatively high freight costs between Australia and New Zealand, and the difficulty in competing against a merged entity, with a strong established presence and surplus capacity, would be disincentives to their entry.

216. Other than NCI, Pact and Viscount NZ, Australian plastic pails suppliers include Mercedes Plastics, Swiss Pack, Cospak, Avya Packaging, Piber Plastics and Arrow Plastics. The Commission interviewed a number of these suppliers to further test Pact's submission that new entry would be likely in the factual.

217. Mercedes Plastics advised the Commission that in 2009 it investigated the feasibility of supplying plastic pails to [ ] in New Zealand. The idea failed because Mercedes Plastics could not supply the requisite range of pails to [ ] specifications. Mercedes Plastics considers that, post acquisition, it would be very difficult to break into the New Zealand market, even given a price rise, because of the merged entity's size."[82] As previously noted, Swiss Pack's solitary attempt to import pails from Australia was unsuccessful due to uncompetitive landed costs. Cospak [83] Avya Packaging[84] and other Australian manufacturers had similar concerns about the difficulties of entering the New Zealand market. While some considered the proposed acquisition could create potential opportunities for them in New Zealand, none had gone so far as to actually carry out a proper analysis of the matter.

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81 The High Court noted in *Air New Zealand & Others v Commerce Commission & Others* (2004) 11 TCLR 347, at para 140: "Although we do not accept that the response of incumbents is a barrier to entry, we accept that their likely behaviour goes to the likelihood, extent and timeliness of entry and is properly part of the competition analysis. It is also properly part of the analysis of what happens following entry".

82 Interview with Mercedes Plastic, 8 November 2011.

83 Email from Cospak, 15 December 2011.

84 Interview with Avya Packaging, 13 December 2011.

218. More relevantly NCI, which has investigated increasing its import volumes, considers that it would be at a significant disadvantage compared to the merged entity. As noted above, the most significant disadvantage facing it (and potentially other Australian companies) would be the additional trans-Tasman freight costs.

219. The Commission does not consider that entry by an Australian manufacturer is likely. The Commission has placed weight on the evidence from parties who have, in the past, attempted to import plastic pails into New Zealand as well as NCI and Stowers who are currently importing.

220. A number of parties indicated that there are numerous plastic pails manufacturers based in Asia. Pact advised the Commission that any one of these suppliers has the potential to supply into New Zealand. It pointed to trade websites such as www.alibaba.com that link to numerous websites advertising plastic pail manufacturers in Asia and from whom it is relatively easy to obtain pricing estimates.

221. Pact suggested that significant costs savings could be achieved by pails purchasers through Asian imports. However, the Commission considers that if this was so, currently there would be significant amounts of Asian pail imports, which is not the case.

222. As with any new entrant, an Asian manufacturer would need a long term supply contract to enter the New Zealand market. Obtaining such a commitment would appear unlikely. As previously discussed, a number of purchasers, particularly paint purchasers, expressed concern over the quality of pails and the supply risks of purchasing from Asian manufacturers. Pact also conceded that there were quality issues with Asian imports.[85]

223. The Commission does not consider that imports from Asian manufacturers would constrain the merged entity.

The likelihood of entry by an existing New Zealand plastics manufacturing business, experienced in the plastics industry but not presently manufacturing plastic pails

224. The Commission has interviewed plastic industry participants, who produce products other than plastic pails, and who were identified as potential entrants by Pact. As discussed below none of these firms consider that the available returns on plastic pails would be sufficient to justify the investment in the relevant machinery. In addition, they lack experience in that particular market.

225. Talbot Technologies currently manufactures only a small volume of small plastic containers. [ ]. It stated that it was

[85] Interview with NERA 18 November 2011.

very familiar with the injection moulding technology required[86] and was interested in expanding into plastic pails but only if the economics were viable.

226. Huhtamaki, a large manufacturer of a variety of plastic packaging does not manufacture plastic pails. Huhtamaki advised the Commission that, [ ]:

226.1 [ ].

226.2 [ ].[87]

227. Cryovac is a manufacturer and distributor of thermo-formed and injection moulded thin walled plastic tubs. Cryovac advised the Commission that it [ ].[88]

228. Bonson, a large manufacturer and supplier of plastic packaging in New Zealand and Australia, advised the Commission that it does not manufacture plastic pails. Bonson stated that, [ ].[89]

229. Packit Packaging Limited (Packit) manufactures a range of injection moulded food containers. It does not manufacture plastic pails. [ ].

Extent of entry

230. If the threat of entry is to constrain market participants not only must entry be likely but entry must also be at a level and spread of sales that is likely to cause market participants to react in a significant manner. Entry that might occur at only relatively low volumes, or in localised areas, does not represent a sufficient constraint to alleviate concerns about market power.

[86] Talbot Technologies is a [ ] owner of a joint venture which manufactures most of New Zealand's injection moulded domestic wheelibins in Auckland. Its Managing Director was a former CEO of Viscount NZ.

[87] Interview with Huhtamaki, 12 December 2011.

[88] Interview with Cryovac, 13 December 2011.

[89] Email from Bonson, 14 December 2011.

231. If a potential entrant was sufficiently incentivised to establish a greenfield plant in New Zealand, it would likely be on a scale to allow the entrant to readily supply large purchasers in order to obtain a return on its investment. It follows that if this were to occur, it would likely be on a scale sufficient to act as a constraint on the merged entity. However, as discussed below, the weight of the evidence is that the ability of a new entrant to obtain contracts, especially from large paint and food purchasers, that are long enough to justify an entrant's investment, is unlikely.

Timeliness of entry

232. If it is to alleviate concerns about a substantial lessening of competition, likely entry of a sufficient extent must be feasible within a reasonably short timeframe, which the Commission typically considers to be two years from the point at which market power is first exercised.

233. The Commission found that the evidence supports Pact's submission that entry on a sufficient scale could be achieved in less than two years. The machinery is readily available and there would be nothing unusual in respect of the lease of a suitable existing factory building that would increase the length of entry. This timing is within the Commission's timeframe for feasible entry.

Conclusions on potential entry

234. If the proposed acquisition goes ahead, the Commission considers that potential entry by any of the three categories of potential entrants analysed would be unlikely. The Commission does not consider that potential entry would constrain the merged entity post acquisition.

Countervailing power

235. The Commission's investigation has shown that some plastic pail purchasers, particularly large food purchasers, would have some countervailing power. However, in the plastic pails market, which is characterised by price discrimination, the price disciplining effects of countervailing power will likely be limited to the buyers with countervailing power. As a result, in this case the effects of countervailing power are likely to be limited to the large food manufacturer subset of pail purchasers.

Assessment of countervailing power

236. The merged entity would be constrained if purchasers were themselves able to exert a substantial influence on the price, quality, or terms of supply of their plastic pails. For this to be the case pail purchasers would have the ability to bypass, or influence the behaviour of, the merged entity in some manner. This could occur if plastic pail purchasers:

236.1 had the ability either to arrange self-supply or to sponsor entry (or expansion).

236.2 as well as plastic pails, bought other products from the merged entity.

236.3 bought either plastic pails or other products from other subsidiaries of Pact, in locations outside New Zealand.

237. Plastic pails purchasers to whom these options are available would be able to threaten the merged entity with countervailing behaviour and obtain price concessions. The likely success of such a tactic would depend on the merged entity's losses from lost sales relative to its gains from increased prices.

Pact's submission

238. Pact submitted that many of the acquirers of plastic pails are large sophisticated companies that have considerable countervailing power. Pact submitted that purchasers could exert countervailing power both now and post acquisition by:

238.1 the threat of self-supply via importing.

238.2 sponsoring expansion by a small domestic manufacturer or a new entrant.

238.3 the threat of switching to NCI.

Ability of purchasers to self supply through imports

239. The Commission considers that some large food and large industrial material manufacturers would have a degree of countervailing power over the merged entity through their ability to self supply through imports. This is because they:

239.1 are well informed purchasers with experience of self-supply via importing.

239.2 have established logistics networks overseas or experience in self-supplying plastic packaging from a range of overseas suppliers from whom plastic pails could be sourced.

239.3 purchase large volumes of pails that do not need high quality (or any) labelling.

240. Many smaller purchasers have advised the Commission that they do not have existing international logistics networks, and their volumes do not justify establishing such networks. Moreover, the Commission's investigation indicates that self supplying by importing plastic pails would not be a feasible alternative for paint purchasers.

Ability of purchasers to leverage buyer power

241. [ ] [ ] advised that if it was incentivised by the actions of the merged entity in respect of price increases for plastic pails, it would put at risk the wider Pact supply arrangement where [ ] has more packaging alternatives. [ ] also considered itself to be in a similar position.

242. [ ][90] [ ][91]

243. While the Commission acknowledges that these are examples of purchasers who consider they could leverage their wider buying power to constrain the merged entity, [ ] account for approximately only [ ] of the plastic pails market by revenue. The situation of these purchasers is different from other large purchasers in the market.

In-house manufacturing

244. The Commission considers that in-house manufacturing would not be a credible option, even for large purchasers. No party interviewed by the Commission could name any plastic pails purchaser in New Zealand that was manufacturing its own plastic pails. [ ]

245. Pact noted in its application that [ ]

[90] [ ].

[91] Interview with [ ], 23 November 2011.

Conclusions on countervailing power

246. The Commission accepts that a handful of customers may have some degree of countervailing power in the factual. However, the majority of purchasers in the plastic pails market, including all paint purchasers, would not have this ability. The Commission does not consider that, post acquisition, any large customer would look to self supply its plastic pails requirements, sponsor expansion of an existing domestic manufacturer or sponsor new entry into the plastic pails market.

247. Given that the sale of plastic pails is characterised by price discrimination, the Commission does not consider that purchasers without countervailing power would benefit from the application of countervailing power of a limited number of purchasers.

248. Overall the Commission does not consider that countervailing power exists in a large enough proportion of the demand side of the plastic pails market to sufficiently constrain the merged entity post acquisition.

Coordinated effects

249. The Commission considers that the proposed acquisition would be unlikely to materially enhance the scope for coordinated conduct.

250. As well as increasing the ability to exercise unilateral market power, an acquisition may make coordination between the remaining businesses more likely, or increase the effectiveness of coordination that is already taking place. The Commission's view is that where an acquisition materially enhances the prospects for any form of coordination between businesses, the result is likely to be a substantial lessening of competition.

251. Pact submitted that the proposed acquisition would be unlikely to result in any coordinated effects in the market for plastic pails. Further, Pact submitted that pricing forces would be unlikely to change in the market as a result of the proposed acquisition. In particular, according to Pact, existing competitors, low barriers to entry, asymmetry of market share and costs, the countervailing power of purchasers, differing business models and the lack of price transparency would hinder the potential for coordination. Pact also stated that there is no history of anti-competitive behaviour in the industry.

252. In the counterfactual the Commission considers that there would be scope for coordination between Pact and Viscount NZ, the two major market participants where the other players are very small in comparison. Pact and Viscount NZ appear to be long time competitors who would have incentives to coordinate. However, post acquisition there would be one player with a very high market share. This

asymmetry of market shares would likely lessen, rather than enhance the potential for coordination. In the Commission's view, the merged entity would have such market dominance in the factual that it would have little incentive to coordinate with the remaining very small volume, market participants.

Conclusion on substantial lessening of competition

253. The Commission concludes that Viscount NZ currently provides a significant competitive constraint on Pact. This constraint would be lost in the factual where the merged firm would have an [ ] share of the plastic pails market and would supply all the large purchasers in the market.

254. The Commission is not satisfied that existing or potential competitors, either alone or when taken together, would be able to replace the loss of this significant constraint. Accordingly, the Commission is not satisfied that the merged entity would be sufficiently constrained from exerting market power in the plastic pails market because:

254.1 While the existing competition from NCI and small domestic manufacturers would remain, the Commission does not consider existing competition in the market is sufficient to constrain the merged entity from exercising market power in the factual. NCI, in particular, has a significant freight cost disadvantage vis a vis Pact and Viscount NZ. After at least a decade supplying the New Zealand plastic pails market, NCI has only gained a [ ] market share and has not been able to obtain the business of any large purchasers. The other competitors are significantly smaller than either Pact or Viscount NZ.

254.2 Paint purchasers, in particular, and some food purchasers identified a number of risks which made them reluctant to switch to a new untested pail supplier. Paint purchasers require a supplier with a proven ability to provide large volumes of high quality pails and food purchasers have to be certain of the ability of manufacturers to supply food grade quality pails. Much of the switching that has occurred was between the two merging parties (as was split supply to purchasers). This risk avoidance is understandable given the importance of proper pail packaging to, for example, a paint business when measured against the very low proportion of total cost added by the pail.

254.3 Small pail manufacturers would be unwilling to expand without the security of a step increase in customer base to support their investment. Moreover, the evidence shows that large purchasers are unlikely to either sponsor expansion or begin self supplying unless faced with price increases of at least [ ].

254.4 Imports from Australia or Asia are not a viable alternative (to other than the small part of the market supplied by NCI) because of high purchase prices, supply logistics costs and risks, and stock holding cost factors.

254.5 Greenfield manufacturing entry by NCI or another local manufacturer, or by Australian or Asia importers, has been shown to be unlikely to be profitable and would be unlikely to occur.

254.6 Some large purchasers may have countervailing power, but this position applies only to a relatively small proportion of the total volume of the plastic pails market.

255. Accordingly, the Commission considers that absent the proposed divestment, it is not satisfied that the proposed acquisition will not have, or would not be likely to have, the effect of substantially lessening competition in the plastic pails market.

The proposed divestment

Introduction

256. Pact has proposed a divestment to remedy competition concerns arising from the proposed acquisition. As set out in the Divestment Guidelines, where the Commission considers that the proposed acquisition is likely to result in a substantial lessening of competition in the relevant market, the Commission considers whether the Applicant's proposed divestment undertaking would remedy the competition concerns identified. The Commission has assessed the composition, asset and purchaser risks associated with Pact's divestment proposal.

The divestment offer

257. On 8 May 2012 the Commission received an undertaking from Pact (Attachment 2), under section 69A of the Act that Pact would divest certain plastic pail manufacturing equipment (including the necessary moulds required) and some current Viscount NZ and/or Pact customers.

258. Pact will give effect to the divestment by creating a new company, "Divestco." Divestco will own the assets being divested. Within [ ] months of completion of the broader transaction, Pact will divest 100% of the shares in Divestco to a third party purchaser, approved by the Commission (the divestee). The price will be established by commercial negotiations between the divestee and Pact.

259. [

]

260. Details of the divestment offer are:

260.1 Pact will divest all the necessary machinery [ ], to supply the sub-contracted customers. Subject to negotiations with the divestee, the injection moulding equipment to be divested would include at least [ ].

260.2 The totality of the equipment divested would provide the divestee with machines [ ] such that it would have the ability to produce [ ] pails and lids, which is approximately equivalent to Pact's 2011 plastic pails production (which gave Pact about a [ ] market share). Hence, while the divestee would have an initial market share of [ ] it would have the capacity to expand to at least [ ] market share if it is sufficiently competitive.

260.3 Pact would further provide the divestee with a sub-contract to supply existing plastic pail customers of Viscount NZ who in 2011 together represented an annual sales revenue of approximately [ ] million or volumes of approximately [ ] pails per annum. [ ].

260.4 [

]

260.5 [

]

260.6 [

].

261. Pact cannot specifically name the proposed divestment customers in its undertaking to the Commission, as Viscount NZ does not wish to provide its customer base to Pact pre-acquisition. However:

261.1 The divestment customers, in aggregate, currently purchase volumes of approximately [ ] plastic pails per year from Viscount NZ.

261.2 Pact has already provided an Information Memorandum to [

]

261.3 [

] It would, therefore, be incumbent on Pact to ensure a package that would make the divestment as commercially acceptable to one of the [ ] potential divestees as soon as possible.

Composition risks

262. These are risks that a divestment proposal may be too limited in scope, or not appropriately configured, to attract either a suitable purchaser or to allow a successful business to be operated in competition with the merged entity.

263. The Commission considers that given the makeup of the divestment, the divestee would have the ability to supply the market with sufficient volume and sufficient range of quality plastic pails.

264. As to volume, Pact has undertaken that the [ ] injection moulding, handle attaching and decorating machines to be divested (actual machinery depends on the requirements of the divestee who might already have such machines with some spare capacity [ ]) would have the capacity to produce [ ]. According to the Commission's estimate, if the divestee was able to gain sufficient permanent customers to reach this level of production it would have a market share of approximately [ ]%.

265. As to range, the Commission has been informed that the machines [ ] to be divested would enable the divestee to supply all the divested customers and enable it to seek new customers [ ]

266. As to quality, the machinery [ ] to be divested are currently producing pails to the standards required by customers. The qualities of the injection moulding machine [ ] will determine the plastic pail quality of the divestee's operations. It would then be left to the divestee to properly manage customer relations including on time delivery.

267. Paint pail purchasers stated their preference to purchase pails from an established domestic manufacturer which included the ability to supply paint pails on a "just in time" basis. Given the divestee would acquire machinery that Pact has undertaken would have the capacity to produce at least [ ] pails and lids per annum which number compares with the largest customer's annual demand of about [ ] pails and lids, the Commission considers that the divestee would have sufficient capacity to accommodate any potential short term demand increases (for example over the summer painting season). Significant concern was expressed at the ability of overseas pails suppliers to supply on a "just in time" basis but this would not be a concern in this instance as the [ ] potential divestees are located in New Zealand.

268. The ability to supply a family of high quality pails is also an important consideration for pail purchasers. As stated, [

] Accordingly, the divestee would immediately be able to supply a range of pails; a range that is already widely used in the market.

269. Therefore, the Commission considers that the divestment is appropriately configured to attract the interest of a suitable purchaser. [

]

Asset risks

270. Asset risks are risks that the competitive capability of a divestment package will deteriorate prior to completion of the divestment.

271. Under the divestment undertaking:

271.1 Pact and Viscount NZ would continue to operate the machinery and supply the customers until all legal and equitable interests in Divestco are transferred to the divestee.

271.2 Pact has undertaken to divest within [ ] months of buying the shares in Viscount Plastics Pty Ltd.

272. Therefore the Commission considers that there is little risk of asset deterioration prior to the divestment.

Purchaser risks

273. The Commission analyses two main purchaser risks, namely that:

- a purchaser acceptable to the Commission may not be available, and/or
- the Applicant has an incentive to sell to a weak competitor for a low price rather than to a strong competitor.

274. In some cases there may be little or no interest from potential purchasers. This might indicate that the assets are unattractive to potential purchasers which may cast doubt on the effectiveness of the undertaking.

275. A buyer acceptable to the Commission may need to have certain attributes that enable it to be an effective competitor in the relevant market. Examples of attributes that may make a buyer acceptable are:

- it is independent of the merged entity.

- it possesses or has access to the necessary expertise, experience and resources to be an effective long term competitor in the market.

- the acquisition of the divested shares or assets by the proposed buyer does not raise competition concerns.

276. Pact has approached [ ] as [ ] potential purchasers. The Commission has interviewed all [ ] and inspected the production facilities [ ]. All have an established presence in the plastic injection moulding industry and produce injection moulded products for purchasers both in New Zealand and overseas. They have the skills and expertise to operate the divested equipment and supply the divested customers under the Pact sub-contract. [ ]. Individually:[

]

277. The Commission considers that any of these [ ] companies would have the ability to easily incorporate an expanded plastic pail business into their present operations. They are each stable and on-going, injection moulding, forward-looking businesses looking for growth opportunities. The divestment will provide each with a potential

step-change in pail production. None of the parties has any existing relationship with either Pact or Viscount NZ.

278. The Commission considers that with the divestment, each of the [ ] potential divestees would have the ability to expand to the same market position that Pact has at present. The Commission does not have concerns with the ability of the divestees to continue to produce the range of high quality pails that is currently being supplied by Pact or Viscount NZ.

279. The Commission notes that the [ ] pails to be divested are already widely used in the industry and could be used to immediately supply a large proportion of the market, without any additional development by the divestee.

280. Therefore, the Commission considers that there are no significant purchaser risks.

Overall conclusion

281. Having considered the proposed divestment, the Commission considers that the divestment is likely to remedy the competition concerns identified in the plastic pails market by providing sufficient constraint on the merged entity to remove the potential competitive harm. The Commission has found no significant risks associated with the divestment.

282. Accordingly, the Commission is satisfied that the proposed acquisition with the divestment, will not have, or would not be likely to have, the effect of substantially lessening competition.

Determination on notice of clearance

283. Pursuant to s 66(3)(a) of the Commerce Act 1986, the Commission determines to give clearance to Pact Group Pty Limited to acquire the plastic pails business of Viscount Plastics (NZ) Limited subject to the divestment undertaking dated 8 May 2012 provided by Pact Group Pty Limited under section 69A of the Commerce Act 1986.

Dated this 10th day of May 2012

Dr Mark Berry
Chair

Attachment 1: List of Viscount NZ assets comprising its plastic pails business

[

]

Attachment 2: The divestment undertaking

PACT GROUP PTY LIMITED

THE COMMERCE COMMISSION

DIVESTMENT UNDERTAKING DEED

RUSSELL McVEAGH

DEED dated 2012

PARTIES

PACT GROUP PTY LIMITED (“**Pact**”)

THE COMMERCE COMMISSION (“**Commission**”)

INTRODUCTION

A. On 3 October 2011, Pact gave notice to the Commission pursuant to section 66(1) of the Commerce Act 1986 ("**Act**") seeking clearance for the proposed acquisition by Pact of the plastic pails business of Pacific BBA Plastics (NZ) Limited ("**Pacific BBA**") and Viscount Plastics (NZ) Limited ("**Viscount NZ**") (the "**Clearance Application**").

B. Pact offers the Commission, as part of the Clearance Application, the divestment undertakings in the form of this deed, pursuant to section 69A of the Act.

OPERATIVE PROVISIONS

1. **Definitions:** In this deed, unless the context otherwise requires:

(a) "**Affiliate**" means, in relation to a party, any person who would be an interconnected body corporate or an associated person of that party as those terms are defined in the Commerce Act 1986.

(b) "**Approved Purchaser**" means a person approved by the Commission in accordance with clause 3.

(c) **"Business Day**" means a day of the week other than:

(i) Saturday, Sunday, Good Friday, Easter Monday, Anzac Day, the Sovereign's Birthday, Labour Day and Waitangi Day;

(ii) a day in the period commencing with 25 December in any year and ending with 2 January in the following year;

(iii) if the first day of January in any year falls on a Friday, the following Monday; and

(iv) if the first day of January in any year falls on a Saturday or a Sunday, the following Monday and Tuesday.

(d) "**Closing**" means the transfer of all legal and equitable interests in 100% of the shares in DivestCo to the Approved Purchaser.

(e) "**Completion**" means completion of the purchase by Pact of the shares in Viscount Plastics Pty Ltd (being the 100% owner of the shares in Pacific BBA, which in turn is the 100% owner of the shares in Viscount NZ)

(f) "**DivestCo**" means a new company incorporated by Pact.

(g) "**Divestment Customers**" means customers that, in aggregate, currently purchase volumes of approximately [ ] plastic pails per year from Viscount NZ, together with, as the context requires, any Substitute Customers, that DivestCo, or an affiliate of DivestCo, is appointed to manufacture for and supply in accordance with clause 2(c) below.

(h) "**Divestiture Date**" means [ ] after Completion.

(i) "**Divestment Equipment**" means the equipment specified in **Confidential Schedule 1**.

(j) "**End of the Business Day**" means 5 pm in Auckland, New Zealand on a Business Day.

(k) "**Proposed Purchaser**" means a person that is not an Affiliate of Pact, and has experience in the injection moulding industry, that Pact:

(i) negotiates with in relation to the sale and purchase of DivestCo; and

(ii) provides details of, pursuant to clause 3, to the Commission for the purposes of the Commission deciding whether to approve that person as an Approved Purchaser.

(l) "**Sub-contract Period**" has the meaning given at clause 2(b).

(m) "**Substitute Customer**" has the meaning given at clause 2(c).

(n) "**Transitional Services**" means such services necessary to assist DivestCo, or its Affiliates, to service the Divestment Customers and are reasonably required by the Approved Purchaser to be provided by Pact during the Sub-contract Period, including, without limitation:

(i) Assistance during the Sub-contract Period, as reasonably required by the Approved Purchaser, in relation to the transition of Divestment Customers to the Approved Purchaser;

(ii) Assistance during the Sub-contract Period, as reasonably required by the Approved Purchaser, in the installation of equipment reasonably required by the Approved Purchaser to service the Divestment Customers; and

(iii) The offer, in Pact's reasonable discretion, to second to the Approved Purchaser, during the Sub-contract Period, one or more of its employees as reasonably required by the Approved Purchaser, for the purposes of assisting the Approved Purchaser to service the Divestment Customers.

2. **Divestment to DivestCo**: Prior to the Divestiture Date, Pact will enter into a contract with DivestCo that provides that:

(a) Pact undertakes to divest, or procure the divestment of, all of Pact's, and/or any other Affiliate of Pact's, legal and equitable interests in the Divestment Equipment to DivestCo at, or soon after, Completion;

(b) Pact undertakes to appoint DivestCo as the manufacturer and supplier of plastic pails and lids to the Divestment Customers from the date on which DivestCo has been sold to the Approved Purchaser and that Approved Purchaser, or an Affiliate of that Approved Purchaser, is able to reasonably commence production of pails for the Divestment Customers until either:

(i) the Approved Purchaser, or an Affiliate of the Approved Purchaser, has supplied [ ] pails bodies to Divestment Customers; or

(ii) the Approved Purchaser, or an Affiliate of the Approved Purchaser, has received revenue of [ ] from sales relating to the supply of pails bodies and lids to Divestment Customers,

(the "**Sub-contract Period**");

(c) If any Divestment Customer seeks a direct supply relationship with Pact during the Sub-contract Period such that DivestCo, or an Affiliate of DivestCo, cannot reasonably be the manufacturer and supplier of plastic pails and lids to that Divestment Customer, Pact undertakes to appoint DivestCo, or an Affiliate of DivestCo, as the manufacturer and supplier of plastic pails and lids for additional customers of either Viscount NZ or Pact that represent equivalent volumes to that Divestment Customer that seeks a direct supply relationship with Pact ("**Substitute Customer**");

(d) Pact undertakes after Closing, to assist DivestCo, or its Affiliates, by providing Transitional Services;

(e) [ ]; and

(f) DivestCo undertakes to, during the Sub-contract Period, provide to Pact every 20 Business Days, for the purposes of Pact monitoring the likely expiry of the Sub-contract Period, aggregated information on:

(i) the total volume of pails bodies DivestCo, or any Affiliate of DivestCo, has sold to Divestment Customers; and

(ii) the total revenue DivestCo, or any Affiliate of DivestCo, has received from sales relating to the supply of pails bodies and lids to Divestment Customers.

3. **Process for approving Proposed Purchaser**: Pact will seek to have the Proposed Purchaser(s) approved by the Commission by providing the Commission with a written notice containing:

(a) **Contact details of the Proposed Purchaser(s):** the name, address, telephone number and any other available contact details of the Proposed Purchaser(s);

(b) **Sale and purchase agreement**: a copy of the draft sale and purchase agreement that Pact proposes entering into with the Proposed Purchaser(s);

(c) **Proposed Purchaser's business activities**: a description of the business carried on by the Proposed Purchaser(s), including the locations at which the Proposed Purchaser(s) carries on business;

(d) **Proposed Purchaser's experience**: details of the experience in the relevant market of the Proposed Purchaser(s); and

(e) **Owner and directors**: the names of the owner(s) and director(s) of the Proposed Purchaser(s).

The foregoing notice will be provided to the Commission no later than [ ] Business Days prior to the anticipated date of Closing so that the Commission may advise Pact in writing whether that Proposed Purchaser will be considered by the Commission to be an Approved Purchaser if it were to purchase 100% of the shares in DivestCo. [ ]

4. **Undertaking to divest**: Pact will divest, or procure the divestment of, 100% of the shares in DivestCo to the Approved Purchaser by the Divestiture Date.

5. **Form of divestment**: Any divestment under clause 4 will be of all Pact's, and/or any Affiliate of Pact's, legal and equitable interests in DivestCo to the Approved Purchaser.

6. **Covenant in connection with sale of DivestCo**: The contract for the sale of the shares in DivestCo to the Approved Purchaser will contain a provision, for the protection of the Approved Purchaser, that Pact, and/or any Affiliate of Pact, will not for [ ] from the date of Closing take any steps to solicit the business of any Divestment Customer that enters into a direct supply relationship with the Approved Purchaser.

7. **Timing:** Pact will be deemed to have complied with the terms of this deed if, by the Divestiture Date, Pact has entered into, or has procured the entry into, a binding sale and purchase agreement to sell 100% of the shares in DivestCo to the Approved Purchaser so long as all actions which are required to be taken prior to, or in connection with, the Closing of that sale and purchase agreement, including as provided at clauses 2 and 3, occur within a period no later than [ ] after the Divestiture Date.

8. **Communication:** Pact will advise the Commission:

   (a) of completion of the purchase by Pact of the shares in Viscount Plastics Pty Ltd, within 1 Business Day following Completion (exclusive of the date of completion);

   (b) no later than [ ] Business Days prior to the entry of the contract with DivestCo, described at clause 2, that the contract will be effected shortly and Pact will provide the Commission with a draft of the contract;

   (c) no later than [ ] Business Days prior to the anticipated date of Closing, of the Proposed Purchaser, pursuant to clause 3, so that the Commission may advise Pact in writing that the Proposed Purchaser will be considered by the Commission to be an Approved Purchaser if it were to purchase 100% of the shares in DivestCo;

   (d) of entry into a binding sale and purchase agreement to sell DivestCo to the Approved Purchaser by providing the Commission, within 1 Business Day of that agreement being executed (exclusive of the date of execution), a copy of the executed sale and purchase agreement; and

   (e) of closing, within 1 Business Day following Closing (exclusive of the date of Closing).

9. **Method of communication:** Any communication required pursuant to clause 8 will be given by Pact sending it by email to registrar@comcom.govt.nz. If receipt of any communication is disputed, Pact may evidence that a communication has been received by the Commission if Pact produces a printed copy of an email which evidences that the communication was sent to the email address specified above by Pact or its legal counsel, with the time and date specified on the email being evidence of the timing of provision of the communication to the Commission.

10. **Governing law**: This deed shall be governed by, and construed in accordance with, the laws of New Zealand and each party hereby irrevocably submits to the exclusive jurisdiction of the courts of New Zealand.

11. **Binding relations**: This deed is intended to create binding and enforceable legal obligations in relation to and for the benefit of the Commission. Pact may, with the written consent of the Commission, vary this deed at any time.

SIGNED AS A DEED

PACT GROUP PTY LIMITED by:

____
Signature of director

____
Name of director

CONFIDENTIAL SCHEDULE 1:

DIVESTMENT EQUIPMENT

[ ]

CONFIDENTIAL SCHEDULE 2:

[ ]