

## Statement of Preliminary Issues

### Concrete Group / Drymix

14 May 2021

#### Introduction

1. On 3 May 2021, we registered a clearance application from Dunlop Drymix Limited (the Applicant), a subsidiary of Concrete Group Limited, seeking clearance to acquire the assets and business of Drymix N.Z. Limited, Drymix Cement Limited, Drymix Bitumen Limited, Drymix Imports Limited, XNP Limited and Romex N.Z. Limited (together, Drymix) (the Proposed Acquisition).<sup>1</sup>
2. The Commission will give clearance if it is satisfied that the Proposed Acquisition will not have, or would not be likely to have, the effect of substantially lessening competition in a market in New Zealand.
3. This statement of preliminary issues sets out the issues we currently consider to be important in deciding whether or not to grant clearance.<sup>2</sup>
4. We invite interested parties to provide comments on the likely competitive effects of the Proposed Acquisition. We request that parties who wish to make a submission do so by close of business on **28 May 2021**.

#### The parties

##### *The Applicant*

5. The Applicant is Dunlop Drymix Limited, a subsidiary of Concrete Group Limited. It is a special purpose company formed to facilitate the Proposed Acquisition.
6. Concrete Group Limited trades in New Zealand through its subsidiary Cemix Products Limited (Cemix). Cemix is a manufacturer and distributor of bagged products used in the construction industry such as bagged concrete, mortar, cement, sand, builders mix and asphalt. Cemix supplies these bagged products throughout New Zealand from its factory in Auckland.

##### *The Target*

7. Like Cemix, Drymix is a manufacturer and distributor of bagged concrete and bagged mortar. Drymix supplies its products throughout New Zealand and it has two

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<sup>1</sup> A public version of the application is available on our website at:  
<http://www.comcom.govt.nz/businesscompetition/mergers-and-acquisitions/clearances/clearances-register/>

<sup>2</sup> The issues set out in this statement are based on the information available when it was published and may change as our investigation progresses. The issues in this statement are not binding on us.

manufacturing plants: one in Feilding in the North Island; and another in Orari (between Ashburton and Timaru) in the South Island.

## The Proposed Acquisition

8. The Proposed Acquisition involves the acquisition of the assets and business of six entities, although most of the relevant assets relate to Drymix N.Z. Limited.<sup>3</sup> All six Drymix entities were placed in receivership between April 2020 and July 2020. Drymix has continued to trade while in receivership and the Receiver for Drymix has run a sales process to sell the assets and business of Drymix as a going concern.<sup>4</sup>

## Our framework

9. Our approach to analysing the competition effects of the proposed acquisition is based on the principles set out in our Mergers and Acquisitions Guidelines.<sup>5</sup> As required by the Commerce Act 1986 (the Act), we assess mergers and acquisitions using the substantial lessening of competition test.
10. We determine whether an acquisition is likely to substantially lessen competition in a market by comparing the likely state of competition if the acquisition proceeds (the scenario with the acquisition, often referred to as the factual), with the likely state of competition if the acquisition does not proceed (the scenario without the acquisition, often referred to as the counterfactual).<sup>6</sup> This allows us to assess the degree by which the proposed acquisition might lessen competition.
11. If the lessening of competition resulting from the proposed acquisition is likely to be substantial, we will not give clearance. When making that assessment, we consider, among other matters:
- 11.1 constraint from existing competitors – the extent to which current competitors compete and the degree to which they would expand their sales if prices increased;<sup>7</sup>
  - 11.2 constraint from potential new entry – the extent to which new competitors would enter the market and compete if prices increased; and

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<sup>3</sup> Clearance application (3 May 2021) at [3.3]: Drymix Cement Limited’s activities related to cement importing that has now ceased; Drymix Bitumen Limited did not undertake any business in New Zealand; Drymix Imports Limited is a non trading shell company; XNP Limited owns land that its rented to Drymix N.Z. Limited; and Romex N.Z. Limited ceased trading in 2018.

<sup>4</sup> Clearance application (3 May 2021) at [3.2].

<sup>5</sup> Commerce Commission, *Mergers and Acquisitions Guidelines*, July 2019. Available on our website at [www.comcom.govt.nz](http://www.comcom.govt.nz).

<sup>6</sup> *Commerce Commission v Woolworths Limited* (2008) 12 TCLR 194 (CA) at [63].

<sup>7</sup> References to price increases in this document should be taken to include a reduction in quality, service or innovation.

- 11.3 the countervailing market power of buyers – the potential constraint on a business from the purchaser’s ability to exert substantial influence on negotiations.

## Market definition

12. We define markets in the way that we consider best isolates the key competition issues that arise from the Proposed Acquisition. In many cases this may not require us to precisely define the boundaries of a market. A relevant market is ultimately determined, in the words of the Act, as a matter of fact and commercial common sense.<sup>8</sup>
13. Cemix and Drymix both manufacture and supply a range of bagged concrete and mortar products. These products are designed for use in small and/or ‘do-it-yourself’ (DIY) projects where small amounts of concrete or mortar are needed. These products are typically supplied in 20 kg bags and sold in hardware merchant stores such as Mitre 10 and Bunnings Warehouse.
14. Concrete and mortar are used for different purposes and so most end users are unlikely to switch between the two products, whether it is in a bag or not.
15. However, the Applicant considers that the relevant market is the national market for the manufacture and supply of bagged concrete and mortar.<sup>9</sup> The Applicant has included bagged concrete and bagged mortar in the same product market because its considers the same machinery can be, and is, used to produce both bagged concrete and mortar products. For example, the Applicant submitted that:
- 15.1 Cemix and Drymix both supply a full range of bagged concrete and mortar products using similar equipment; and
- 15.2 an existing manufacturer of bagged mortar could easily upgrade their existing mixing and bagging equipment to start supplying bagged concrete (and vice versa).
16. In addition, the Applicant considers the relevant product market can be wider than bagged concrete and mortar because end users have other alternatives. For example, the Applicant considers that, if faced with a small price increase for bagged concrete, the end user can simply purchase the necessary ingredients individually (namely sand, aggregate and cement) and mix them using a wheelbarrow and shovel to produce concrete that is very similar to what comes premixed as bagged concrete. The same scenario also applies to bagged mortar (which would involve purchasing sand and cement individually).<sup>10</sup>
17. We will consider:

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<sup>8</sup> Section 3(1A); See also *Brambles v Commerce Commission* (2003) 10 TCLR 868 at [81].

<sup>9</sup> Clearance application (3 May 2021) at [5.22].

<sup>10</sup> Clearance application (3 May 2021) at [5.26].

- 17.1 whether the bagging equipment used to bag concrete varies between that used to bag mortar and/or other construction products and the extent to which bagging manufacturers can and do switch their bagging equipment between producing concrete and mortar;
- 17.2 the degree to which end users of (premixed) bagged concrete would, in the face of a small increase in price, switch to purchasing, individually, the three key components of concrete (being sand, aggregate and cement). We will consider the same question in terms of bagged mortar;
- 17.3 the geographic scope for any bagged concrete and/or mortar product markets and the extent to which existing suppliers compete with one another in different regions of New Zealand; and
- 17.4 whether there are any relevant customer markets including whether customers, such as hardware merchants or other wholesale customers, have particular requirements that may impact on their supply alternatives for bagged concrete and/or mortar.

### **Without the acquisition**

- 18. A key focus of our investigation will be determining the likely ‘without the merger’ scenario(s).
- 19. The clearance application states that, absent the Proposed Acquisition, a likely counterfactual is that the Receiver would break up the relevant assets for sale, and they would leave the relevant market.<sup>11</sup>
- 20. While the Applicant has not submitted that Drymix is a ‘failing firm’, the Commission’s guidance on assessing ‘failing firm’ counterfactuals is relevant. As our guidelines note, if a firm is failing and its assets will leave the relevant market without a merger, there would likely be no material difference between the scenarios with and without the acquisition. As a result, a merger will not substantially lessen competition.<sup>12</sup>
- 21. We will assess the possible scenarios that might arise without the Proposed Acquisition. In this case, we will consider whether the counterfactual submitted by the Applicant is the only likely counterfactual, or whether there are other likely counterfactuals where Drymix’s assets remain in any relevant market(s) and are used to supply concrete and mortar products. This will include us considering and assessing:
  - 21.1 the likelihood of the Receiver selling the Drymix assets and business as a going concern to an alternative purchaser absent the Proposed Acquisition and, if so, the identity of the likely purchaser; and

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<sup>11</sup> Clearance application (3 May 2021) at [3.13].

<sup>12</sup> Commerce Commission, Mergers and Acquisitions Guidelines, July 2019, Attachment E.

- 21.2 the likelihood (in a scenario where Drymix's assets are sold individually absent the Proposed Acquisition) of any of Drymix's assets being acquired by an alternative purchaser that uses those assets to supply concrete and mortar products.

### **Effect of the Proposed Acquisition**

22. In considering the effect of the Proposed Acquisition, we will consider whether it would be likely to substantially lessen competition in the relevant market(s) by assessing whether:

22.1 horizontal unilateral effects might result from the Proposed Acquisition; and

22.2 any coordinated effects might result from the Proposed Acquisition.

### **Unilateral effects: would the merged entity be able to profitably raise prices by itself?**

23. Unilateral effects arise when a firm merges with a competitor that would otherwise provide a significant competitive constraint (particularly relative to remaining competitors) such that the merged firm can profitably increase price above the level that would prevail without the merger without the profitability of that increase being thwarted by rival firms' competitive responses. A merger could also reduce competition if one of the merging firms was a potential or emerging competitor.
24. The question that we will be focusing on is would any loss of competition enable the Applicant to profitably raise prices or reduce quality or innovation of any relevant market by itself?
25. The Applicant considers that the Proposed Acquisition is unlikely to have the effect of substantially lessening competition in any bagged concrete and mortar market (or any other relevant market) in New Zealand because, as noted above, a likely counterfactual is Drymix's assets exiting the market. However, even if Drymix was sold as a going concern, the Applicant considers that:
- 25.1 there would continue to be significant competitive constraint on the merged entity from existing competitors;
- 25.2 substitute concrete and mortar products would provide a substantial constraint on the merged entity's supply of bagged concrete and mortar products;
- 25.3 barriers to entry and expansion are low; and
- 25.4 large retailers would wield a considerable degree of countervailing power and impose a significant competitive constraint on the merged entity.<sup>13</sup>
26. In any relevant market(s), we will consider:

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<sup>13</sup> Clearance application (3 May 2021) at [6.1].

- 26.1 the degree of competitive constraint that Cemix and Drymix impose upon one another now and could potentially impose on one another in the future. To the extent that any competitive constraint between Cemix and Drymix is material, we will assess whether the competition lost between the merging parties could be replaced by rival competitors;
- 26.2 how easily rivals could enter and/or expand in response to an increase in price or a decrease in the quality of the products provided by the merged entity and whether that entry is likely to occur in a timely manner; and
- 26.3 countervailing power and whether hardware merchants (or any other customers) have special characteristics that would enable them to resist a wholesale price increase by the merged entity.

**Coordinated effects: does the Proposed Acquisition make coordination more likely?**

- 27. A merger can substantially lessen competition if it increases the potential for the merged entity and all or some of its remaining rivals to coordinate their behaviour and collectively exercise market power such that output reduces and/or prices increase across the market. Unlike a substantial lessening of competition, which can arise from the merged entity acting on its own, coordinated effects require some or all of the firms in the market to be acting in a coordinated way.
- 28. The Applicant considers that the Proposed Acquisition will not enhance the ability of the merged entity and other competitors to coordinate their behaviour because:<sup>14</sup>
  - 28.1 retail customers have significant countervailing power. Hardware merchants, as the main retail customers, are price sensitive and due to their strong bargaining position and ability to switch to alternative suppliers, including their ability to sponsor entry, they could quickly disrupt any attempt to coordinate behaviour;
  - 28.2 the Proposed Acquisition would not result in the removal of a particularly vigorous or effective competitor;
  - 28.3 barriers to entry are low, and existing suppliers could readily expand and others could enter, which reduces the likelihood of any coordination; and
  - 28.4 there is no history of anti-competitive coordination in the relevant market.
- 29. We will assess whether the Proposed Acquisition would make coordination more likely, more complete or more sustainable. As part of our assessment we will consider whether any of the relevant markets are vulnerable to coordination, and whether the Proposed Acquisition would change the conditions in the relevant markets. In particular, this will involve testing:

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<sup>14</sup> Clearance application (3 May 2021) at [6.22].

- 29.1 the impact of the removal of Drymix as a competitor in any relevant market, including whether it is a particularly vigorous competitor;
- 29.2 post acquisition, the ability and incentive of the remaining firms in the relevant market(s) to coordinate their behaviour to profitability increase their wholesale price to retailers; and
- 29.3 post acquisition, the ability and incentive of the remaining firms in the relevant market(s) to coordinate to allocate the customers that they would supply to.

### **Next steps in our investigation**

30. The Commission is currently scheduled to make a decision on whether or not to give clearance to the Proposed Acquisition by **29 June 2021**. However, this date may change as our investigation progresses.<sup>15</sup> In particular, if we need to test and consider the issues identified above further, the decision date is likely to extend.
31. As part of our investigation, we will be identifying and contacting parties that we consider will be able to help us assess the preliminary issues identified above.

### **Making a submission**

32. If you wish to make a submission, please send it to us at [registrar@comcom.govt.nz](mailto:registrar@comcom.govt.nz) with the reference 'Concrete Group/Drymix' in the subject line of your email, or by mail to The Registrar, PO Box 2351, Wellington 6140. Please do so by close of business on **28 May 2021**.
33. Please clearly identify any confidential information contained in your submission and provide both a confidential and a public version. We will be publishing the public versions of all submissions on the Commission's website.
34. All information we receive is subject to the Official Information Act 1982 (OIA), under which there is a principle of availability. We recognise, however, that there may be good reason to withhold certain information contained in a submission under the OIA, for example, in circumstances where disclosure would unreasonably prejudice the supplier or subject of the information.

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<sup>15</sup> The Commission maintains a clearance register on our website at <http://www.comcom.govt.nz/clearances-register/> where we update any changes to our deadlines and provide relevant documents.