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Public version

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MATTER NO. 02-341-9209
DATE 10 March 2011

Dear Hamish

Preliminary response to Godfrey Hirst submission

We refer to your email of 7 March 2011 enclosing a (purportedly) confidential submission from Chapman Tripp on behalf Godfrey Hirst and an accompanying economic report from Castalia.

As noted in our 8 March email to you, it is difficult to respond to those documents in detail without being able to share a redacted version of those documents with our client.

Having said that, it is apparent to us that both documents (particularly the Chapman Tripp document) contain numerous unfounded and uncorroborated assertions and factual errors. The statement that Whakatu and Kaputone are "rural" areas is one of the more obvious ones, and we expect our client will identify others if given a chance to comment.

The Chapman Tripp document is also heavily emotive and makes allegations that CWH has misled the Commission or provided "wrong" information.

We reject these accusations for the reasons explained in this letter. A close inspection shows that they are without foundation. Often they represent a misreading of what has been said or simply reflect a statement that was been taken out of context.

We also **enclose** a memorandum from NERA which provides a preliminary response to some of the "issues" raised in the Castalia report.

We are providing these preliminary comments now as we think the comments made serve to highlight the (lack of) weight the Commission should give to these documents. In preparing this response we have not been able to get any direct input from our clients and they may have further comments or clarifications they wish to make once a public version is available.

Overall, we believe that these submissions are an attempt by Godfrey Hirst to game the Commission and to use the Commission process to damage CWH's bid for NZWSI to Godfrey Hirst's own commercial advantage. [

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1. Appendix B - Paragraph 5.14:

The submission claims that paragraph 5.14 of the Application is “wrong”. Paragraph 5.14 reads:

The impacts of this steady decline in available demand have been further exacerbated by the emaciation of New Zealand's wool processing industry due, primarily, to the growth of low cost textile and apparel manufacturing in developing countries, most notably China.

The claim that this paragraph is “wrong” is said to be because rationalisation of the scouring industry in New Zealand has been the result of the declining wool clip due to falling sheep numbers and the fact that scours themselves have become bigger and more efficient, with only the largest and most technologically advanced remaining competitive and viable.

CWH stated in the Application that rationalisation has occurred due to the declining wool clip as a result of falling sheep numbers which it said has resulted in less wool available for processing. The Application addresses the claim that wool scouring demand is a function of the size of New Zealand's sheep flock (which is declining) in paragraphs 5.5 – 5.13 of the application. CWH also agrees that, certainly, economies of scale are relevant and CWH has highlighted this in the Application.

Further to the points on the Chinese constraint raised in the Application, CWH has provided the Commission with further detail on this constraint in its letter dated 22 February 2011.

Read in its proper context and having regard to the word “exacerbated” in paragraph 5.14, it is clear that CWH's statement is not, and was not intended as, a definitive statement regarding the causes of a decline in available demand. It is difficult to determine how a blanket statement that this paragraph is “wrong” can be made.

2. Appendix B – Paragraph 5.15

The submission claims that this comment is in respect of paragraph 5.19 of the Application, although it is apparent that this comment in fact relates to paragraph 5.15 of the Application.

The submission claims that CWH's comment in relation to the growth of exports of greasy wool to China is “wrong” and says that exports of greasy wool have not increased in the past decade and have instead remained relatively steady. The submission says that this has resulted only in an increase to the *percentage* of the clip that is exported greasy as a result of the reduced total clip.

This statement is not wrong.

First, the comment in the Application is in relation to exports of greasy wool to *China*, and not to *total* greasy wool exports. Wool export figures published by Meat NZ between the years 2005-2010 show that there has been an increase in the greasy wool exports to China:

- July to June 2009-2010: 36,142 tonnes (26,384 tonnes, clean equivalent);
- July to June 2008-2009: 34,248 tonnes (25,001 tonnes, clean equivalent);
- July to June 2007-2008: 29,435 tonnes (21,488 tonnes, clean equivalent);
- July to June 2006-2007: 28,025 tonnes (20,458 tonnes, clean equivalent); and
- July to June 2005-2006: 34,370 tonnes (25,090 tonnes, clean equivalent).

Second, Meat NZ wool export figures from 2005-2010 show that total exports of greasy wool have increased since 2006/2007, although they declined from 2005/2006 level:

- July to June 2009-2010: 41,405 tonnes (30,226 tonnes, clean equivalent);
- July to June 2008-2009: 41,221 tonnes (30,091 tonnes, clean equivalent);
- July to June 2007-2008: 38,084 tonnes (27,801 tonnes, clean equivalent);
- July to June 2006-2007: 37,316 tonnes (27,241 tonnes, clean equivalent); and
- July to June 2005-2006: 46,966 tonnes (34,285 tonnes, clean equivalent).

3. Appendix B - Paragraph 9.2

The submission states that CWH's statement that "around 85% of New Zealand's wool production is exported" is "wrong".

CWH does not agree.

The "around 85%" number corresponds to the figure cited at paragraph 38 of Decision 666. CWH's understanding was that this number is likely to remain relevant and has used this figure in calculations, and has footnoted where it has done so.

It is consistent with the indicative wool flows diagram provided to the Commission by CWH, and data from IWTO. In respect of the latter, using the last full year recorded in the 2010 edition of IWTO Market Information (which was provided to the Commission by CWH when the Application was filed), New Zealand's wool production in 2008 (clean equivalent) was 155,234 tonnes. New Zealand's exports of Raw Wool (including greasy, scoured and carbonised wool) were 135,587 tonnes. As a percentage, this equates to 87%.

4. Appendix B - Paragraph 9.8

The submission states that CWH's assertion that a merchant has the ability to export greasy wool and to have that wool scoured offshore instead of using a New Zealand scourer is "wrong". The submission adds that greasy wool exported by a merchant is sold to a manufacturer which may blend it with wool from other countries at their discretion, with the merchant having no involvement post delivery.

This appears to overlook the constraint that is imposed on CWH by the potential for the export of greasy wool overseas. The relevant question is to ask whether CWH is constrained by the potential for merchants to export greasy wool overseas, rather than to assess whether merchants in fact currently export greasy wool for scouring on their own account in China.

In addition, in its letter dated 22 February 2011, CWH has provided the Commission with specific examples of merchants who either already export greasy wool overseas, or who have told CWH that they will send wool overseas greasy if it is not satisfied with CWH's offering. In this same letter, CWH notes that it is becoming increasingly viable for customers to export greasy wool to China and then to re-export that wool in a processed/semi-processed form to a customer in another country, for example, Icebreaker has done this and CWH understands that coarse wool has been re-exported as yarn.

5. Appendix B - Paragraph 14.3

CWH's Application notes that Chinese wool scourers have become aggressive in the purchase of wool scouring assets and over recent years, many Australian scours have

closed and the surplus plant has been acquired by Chinese wool scourers and relocated to China.

The submission says that of the scours closed and exported from New Zealand, most have gone to South America, USA and India, not China.

CWH's comment in the Application was in relation to Australian scour closures, not New Zealand closures. [

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6. **Paragraph 15.21**

The submission notes an "obvious error" in relation to the claim that 21% of New Zealand's wool is scoured in China.

CWH acknowledges that the word "exports" has been omitted from this paragraph, i.e. the sentence should read "21% of New Zealand's wool *exports* are being scoured in China". However, the same sentence is included in the Application in a number of other paragraphs and so it is difficult to see why this is raised as an issue.

To clarify how these calculations in paragraph 15.21 of the Application have been arrived at, CWH has used the wool export figures published by Meat NZ for July to June 2009-2010:

- For the year July to June 2009-2010, total wool exports from New Zealand were 122,893 tonnes. Total wool exports to China (in clean tonnes) were 46,282 tonnes. As a percentage this is 38%.
- Converting the 36,142 greasy tonnes into clean tonnes is calculated by multiplying the greasy tonnes figure by 0.73. This results in 26,384 greasy tonnes (clean equivalent). The 57% figure is calculated by dividing 26,384 by 46,282.
- The 21% calculation comes from dividing 26,384 by total wool exports of 122,893.

Please let us know if you have any questions in relation to this letter.

Yours sincerely

[Sgd: Phil Taylor / David Blacktop]

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