



COMMERCE COMMISSION

Decision No. 364

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

Turners & Growers Limited

and

United Flower Auction Limited

The Commission: Dr K M Brown

Summary of Proposed Acquisition: The acquisition by Turners & Growers Limited or any interconnected body corporate of Turners & Growers, of the assets or shares (or any combination of assets or shares) of United Flower Auction Limited, but excluding the export business (including export debtors) of United Flower Auction Limited.

Determination: Pursuant to s 66(3)(a) of the Commerce Act, the Commission determines to give clearance for the proposed acquisition.

Date of Determination: 15 July 1999

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CONTAINED IN SQUARE BRACKETS []**

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THE PROPOSAL

- 1 Pursuant to section 66(1) of the Commerce Act 1986 (the Act), Turners & Growers Limited (T&G) gave notice to the Commission on 5 July 1999 (the application) seeking clearance for it or any interconnected body corporate to acquire the assets or shares (or any combination of assets or shares) of United Flower Auction Limited (UFA), excluding the export business (including the export debtors) of UFA.

THE PROCEDURES

- 2 Section 66(3) of the Act requires the Commission either to clear, or to decline to clear, a notice given under s66(1) within 10 working days, unless the Commission and the person who gave the notice agree to a longer period. No extension was sought by either party. Accordingly, a decision on the application is required by Monday 19 July 1999.
- 3 T&G sought confidentiality for certain information contained in the notice seeking clearance, and a confidentiality order was made in respect of that information for a period of 20 working days from the Commission's determination of the notice. When the confidentiality order expires, the provisions of the Official Information Act 1982 will apply to the information.
- 4 The Commission's determination is based on an investigation conducted by its staff and their subsequent advice to the Commission.
- 5 In the course of their investigation of the proposed acquisition, Commission staff have discussed the application with a number of parties. These parties included growers, wholesalers, florists, flower sellers, and flower auctioneers. Parties both from within Auckland, and throughout New Zealand, provided comment.

THE PARTIES

Turners & Growers Limited

- 6 T&G is a listed company, carrying on business in the property, auctions, and produce industries. This current application only affects T&G's cut flower business. T&G's cut flower business is conducted by Turners & Growers Fresh Limited, a wholly owned subsidiary. The business of Turners & Growers Fresh Limited includes the wholesaling of fruit, produce, and cut flowers.
- 7 T&G operates cut flower auctions in the main centres throughout New Zealand and offers a nationwide cut flower brokerage service.

United Flower Auction Limited

- 8 UFA operates as an auctioneer of cut flowers in the Auckland area. UFA also has a brokerage operation, to buyers throughout New Zealand.
- 9 UFA is also engaged in the export of cut flowers, but the export business is expressly excluded from the proposed acquisition.

BACKGROUND

- 10 The proposed acquisition involves the only two specialist cut flower auctioneers in the Auckland region. As a result of the acquisition the two existing auction floors will be amalgamated into one. T&G submits that they are responding to a widely perceived need for increased efficiency and cost effectiveness in the auction sale process. T&G submits that a single Auckland auction will provide more open competition in the sale of flowers than the current two smaller and more inefficient systems. The proposed acquisition will not result in the amalgamation of cut flower auctions in any other region.
- 11 The proposed acquisition only impacts upon the domestic cut flower industry. There is no overlap between the distribution channels used by export growers and those used by domestic growers. Exporters of cut flowers do not purchase cut flowers from auctions but generally source product direct from export growers.

Overview of Cut Flower Distribution Channels

Auction System

- 12 Industry participants commented that, traditionally, the principal method of distribution has been through the auction system. T&G is the principal operator of cut flower auctions in New Zealand and has cut flower auctions floors in all the main centres. UFA, however, only operates a cut flower auction floor in the Auckland region. There are, and have been, other cut flower auctioneers in various centres throughout New Zealand, operated both by growers and by auctioneers of fruit and produce. Most recently, as T&G has closed down its auction facilities in smaller provincial centres, smaller owner-operated cut flower auctions have been set up.
- 13 In the Auckland region, cut flower auctions are held on four days of the week. T&G conducts its auction on Monday, Wednesday, Thursday and Friday. UFA conducts its auction on Monday, Wednesday and Friday.
- 14 T&G and UFA operate different auction systems. An auctioneer seeking bids from the floor conducts T&G auctions, whereas UFA operates a “Dutch” auction system¹.
- 15 Buyers at the auction range from small independent owner-operated florists and flower sellers to large wholesalers and commission buyers. Industry participants commented that in recent years there has been a trend, particularly from T&G, to try and discourage smaller buyers and growers from using the auction system. T&G advised that the reason for this strategy is to increase efficiencies in the operation of the auction process.

Brokerage

- 16 The two main providers of brokerage services are T&G and UFA. Brokerage involves a company negotiating a fixed price arrangement between a grower and a buyer.

¹ The “Dutch” auction system involves “top-down” bidding. Buyers press a button when a “clock” or “dial” reaches an acceptable price. The person with the first bid is the purchaser. This system does not require an auctioneer to seek bids from the floor, reducing the time per sale and, consequently, the overall length of the auction.

- 17 According to industry participants, this service is one that is currently provided primarily by T&G and UFA as an adjunct to their auction businesses. The day prior to an auction, a price list is sent to growers who then choose whether they want to sell their flowers for a fixed price or submit them for sale at the auction. Similarly, buyers decide whether they want to buy from the brokerage list or the auction.

Wholesalers

- 18 Wholesalers are usually independent businesses which source flowers from the auction system, through brokerage, and directly from growers, and then onsell flowers to florists and flower sellers. For retailers of cut flowers it is usually more expensive to buy flowers through a wholesaler than through the auction system.
- 19 Wholesalers offer retailers the advantages of convenience and guaranteed supply. By using a wholesaler retailers do not have to spend several hours at the auction and retailers can be certain that they get the order of flowers that they require. Industry participants noted that, in particular, buyers will use wholesalers when it is critical that they get a specific order of flowers and they do not want to risk being outbid at the auction. This will usually be the case for big functions such as weddings.

Grower Direct Sale to Retailers

- 20 Retailers may enter into arrangements with growers to supply them with a regular volume of flowers. Generally, it is the grower's responsibility to deliver the flowers to the retailer. The grower will incorporate the freight costs into the overall price. Industry participants commented that growers would generally only enter into such arrangements with large retailers, as it often becomes uneconomical for growers to have many small accounts.
- 21 For many small florists it is not economical to source their product direct from the growers. Growers tend to be specialists in a particular variety of flowers and accordingly a florist would have to deal with many growers to get all the flowers required. It is often more convenient for smaller florists to purchase flowers through the other distribution channels.

THE MARKETS

Introduction

- 22 The purpose of defining a market is to provide a framework within which the competition implications of a business acquisition can be analysed. The relevant markets are those in which competition may be affected by the acquisition being considered. Identification of the relevant markets enables the Commission to examine whether the acquisition would result, or would be likely to result, in the acquisition or strengthening of a dominant position in any market in terms of s 47(1) of the Act.
- 23 Section 3(1A) of the Act provides that:

“the term ‘market’ is a reference to a market in New Zealand for goods and services as well as other goods and services that, as a matter of fact and commercial common sense, are substitutable for them.”

- 24 Relevant principles relating to market definition are set out in *Telecom Corporation of New Zealand Ltd v Commerce Commission*² and in the Commission’s *Business Acquisition Guidelines* (“the Guidelines”)³. A brief discussion of the methodology follows.
- 25 Markets are defined in relation to product type, geographical extent, and functional level. The boundaries of the product and geographical markets are identified by considering the extent to which buyers are able to substitute other products, or across geographical regions, in response to a change in relative prices of the products concerned. A market is the smallest area in which all such substitution possibilities are encompassed. It is in this area that a hypothetical monopoly supplier could exert market power.
- 26 A properly defined market will include products which are regarded by buyers or sellers as being not too different (‘product’ dimension), and not too far away (‘geographical’ dimension). A market defined in these terms is one within which a hypothetical profit-maximising sole supplier of a product could impose at least a small yet significant and *non-transitory* increase in price (the “*ssnip*” test), assuming other terms of sale remain unchanged. It will also include those suppliers currently in production who are likely, in the event of such a *ssnip*, to shift promptly to offer a suitable alternative product, or offer their product to alternative acquirers.
- 27 Markets are also defined in relation to functional level. Typically, the production, distribution, and sale of products proceeds through a series of vertical functional levels, so the functional levels affected by the application have to be determined as part of the market definition. For example, that between manufacturers and wholesalers might be called the “manufacturing market”, while that between wholesalers and retailers is usually known as the “wholesaling market”.

Product/Function Market

- 28 As discussed earlier, the proposed acquisition will effectively mean a reduction from two cut flower auctioneers to one in the Auckland region. T&G submits that the market affected by the acquisition is wider than a narrow cut flower auction services market. T&G submits that at the wholesale level cut flowers are not only sold by auction but also through independent wholesalers, directly from growers to retailers, and through brokerage. T&G submits that, accordingly, the relevant product/function market is the market for the wholesale distribution of cut flowers.
- 29 The Commission considers that the relevant product/function market is the market for the wholesale distribution of cut flowers, as submitted by T&G. The Commission considers that the distribution channels available for buying and selling cut flowers should be considered to be in one product/function market as they are sufficiently close substitutes.

² (1991) 4 TCLR 473.

³ Commerce Commission, *Business Acquisition Guidelines*, 1999, 11-16.

- 30 Growers commented that auctions were currently the main distribution channel as it was the most cost-effective method of distributing cut flowers. However, they felt that the other distribution channels were in direct competition with T&G and UFA's auctions. In particular, growers commented that, were the combined entity to increase commission rates, growers would consider distributing a greater volume of flowers outside the auction system. Similarly, the option was available for buyers to bypass the auction system should the combined entity increase the cost of sourcing flowers from the auction or reduce the level of service.

Geographic Market

- 31 T&G contends that the geographic extent of the relevant market is nationwide. Based on the information available, the Commission considers that the relevant market is a national one, as submitted by T&G.
- 32 From the demand side it appears that buyers predominantly purchase cut flowers within their own region. However, for various reasons, buyers do source flowers from outside their own region. These reasons include availability of supply, the level of service offered by sellers, and the price offered by sellers. Industry participants commented that freight costs were not a deterrent to a buyer sourcing flowers outside their region, particularly as the grower generally paid for the freight.
- 33 From the supply side, it appears that growers readily distribute flowers nationally. Growers appear to be willing to freight flowers to auctions, wholesalers, and retailers throughout New Zealand. Growers, wholesalers and brokerage service providers have a customer base that is generally nationwide.

Conclusion on Market Definition

- 34 The Commission concludes that the relevant market is the market for the wholesale distribution of cut flowers throughout New Zealand.

ASSESSMENT OF DOMINANCE

Competition Analysis Overview

- 35 Section 66(3) of the Act, when read in conjunction with s 47(1) of the Act, requires the Commission to give clearance for a proposed acquisition if it is satisfied that the proposed acquisition would not result, and would not be likely to result, in a person acquiring or strengthening a dominant position in a market. If the Commission is not so satisfied, clearance must be declined.
- 36 Section 3(9) of the Act states that a person is in a "dominant position" if:
- ... a person as a supplier or an acquirer of goods or services either alone or together with an interconnected or associated person is in a position to exercise a dominant influence over the production, acquisition, supply, or price of goods or services in that market ...
- 37 That section also states that a determination of dominance shall have regard to:

- market share, technical knowledge and access to materials or capital;
 - the constraint exercised by competitors or potential competitors; and
 - the constraint exercised by suppliers or acquirers.
- 38 In *Port Nelson Ltd v Commerce Commission* [1996] 3 NZLR 554, the Court of Appeal approved the following dominance standard, adopted by McGechan J in the High Court:
- ...dominance involves more than “high” market power; more than mere ability to behave “largely” independently of competitors; and more than power to effect “appreciable” changes in terms of trading. It involves a high degree of market control.*
- 39 In the Commission’s view, a dominant position in a market is generally unlikely to be created or strengthened where, after the proposed acquisition, either of the following situations exist:
- the merged entity (including any interconnected or associated persons) has less than in the order of a 40% share of the relevant market;
 - the merged entity (including any interconnected or associated persons) has less than in the order of a 60% share of the relevant market and faces competition from at least one other market participant having no less than in the order of a 15% market share.
- 40 However, as Tipping J stated in the High Court decision of *New Zealand Magic Millions Limited & Anor v Wrightson Bloodstock Limited* (1990) 3 NZBLCA 99-175:
- [M]arket share is not the sole determinant of the presence or absence of dominance or market power. The most that can be said is that dominance is frequently attended by substantial market share but all the other relevant factors must be brought to account. For example, a substantial market share without barriers to entry will seldom, if ever, be indicative of dominance.*
- 41 Accordingly, before a conclusion on dominance is reached, it is necessary to consider all factors listed in s 3(9) and any other relevant factors.

The Market for the Wholesale Distribution of Cut Flowers throughout New Zealand

Market Shares

- 42 Estimating the market shares of flower wholesaling has proved difficult, due in part to the lack of a central reporting authority in the flower industry. Further, as the industry is characterised by a large number of small operators, it is difficult to accurately assess both individual market shares, and the overall size of the wholesale flower market.
- 43 T&G submitted estimations based upon the total revenue figure it believed was sold in New Zealand. The Commission has sought to verify those figures through contact with other auction operators, growers, and buyers. Estimates given to the Commission by other market participants are in line with those provided in the application. On the basis of the information provided to the Commission, an estimation of the market share of the combined entity in the wholesale flower market is shown in Table 1.

TABLE 1

**Estimated Market Shares of the Suppliers in the Market
for the Wholesale Distribution of Cut Flowers in New Zealand**

Supplier	Revenue per Annum (\$m)	Market Share (%)
T&G	[]	[]
UFA	[]	[]
Combined entity	[]	[]
MG Marketing	[]	[]
Wholesalers (buying direct from growers)	[]	[]
Retailers (buying direct from growers)	[]	[]
Total	[]	100

44 On the basis of the above figures, the combined entity’s market share does not fall within the Commission’s “safe harbours” (refer para 39), as there is no other single competitor having a market share in the order of 15%. However, the fact that a proposed acquisition may lead to a market share falling outside these “safe harbours” does not necessarily mean that it will be likely to result in the acquisition or strengthening of a dominant position in a market. Additional factors must also be considered before a conclusion on dominance is reached. An analysis of those additional factors follows.

Constraint by Existing Competitors

- 45 As discussed earlier, the proposed acquisition affects only cut flower auction services in the Auckland region. T&G submits that the combined entity would continue to be constrained by the conduct of existing competitors. T&G contends that growers, wholesalers and retailers each have alternatives to the Auckland auction system, to which they could readily shift their custom.
- 46 As outlined in this report (paragraphs 12-21), a number of alternative supply and purchase methods are available to market participants. For the reasons given earlier, the Commission considers that each of these methods is substitutable, and that the availability of these competing methods provides an effective constraint upon the merged entity.
- 47 Given the above factors, the Commission’s view is that it is likely that the combined entity will continue to face effective competition from those alternative supply and purchase methods currently available.

Constraint by Potential Competitors

- 48 T&G submits that there are few barriers to entry into this market and, consequently, that the combined entity will be effectively constrained by the threat of potential entry.
- 49 Industry participants spoken to by Commission staff agree that entry conditions are not onerous. Typically for an auction, an entrant will require access to suitable premises,

and access to suppliers and purchasers. Industry sources commented that these factors are unlikely to be difficult to obtain. Similarly, entry as a wholesaler or broker is also characterised by low entry barriers.

- 50 The most common suggestion made by industry participants was that growers could rapidly, and at low cost, enter the market. In particular, industry participants suggested that if growers were dissatisfied with T&G in Auckland they could set up a competing auction floor. Industry participants commented that it was a similar scenario that had led to UFA being set up 12 years ago. While it is possible for a large grower to enter the market in this manner, industry parties suggested that it is more likely that entry would occur following the formation of a co-operative of growers.
- 51 In addition, industry participants suggested that current auctioneers of fruit and produce are potential entrants into the market. Presently a number of such auctions do sell flowers, but more as a “supplement” to their main auction. A number of parties commented that these operators could either introduce flowers as part of their auction activity, or expand their existing flower auction, in a short period of time and with few impediments to entry or expansion.
- 52 Based on the above factors, the Commission considers that, as T&G submits, entry into the market for the wholesale distribution of cut flowers is not onerous, and can be effected in a timely manner.

Conclusion on Dominance in the Market for the Wholesale Distribution of Cut Flowers throughout New Zealand

- 53 The proposed acquisition will result in an amalgamation of the only two cut flower auctioneers currently operating in the Auckland region. However, the combined entity would be constrained by competition at both a regional and national level, from other auctioneers, wholesalers, brokers, and from growers selling directly to buyers.
- 54 Further, entry conditions are not onerous and are unlikely to represent a major barrier to any prospective entrant wishing to enter the market, or to existing participants seeking to expand their operations.

OVERALL CONCLUSION

- 55 The Commission has considered the impact of the proposal in the New Zealand market for the wholesale distribution of cut flowers.
- 56 Having regard to the factors set out in section 3(9) of the Commerce Act and all other relevant factors, the Commission is satisfied that the proposed acquisition would not result, or would not be likely to result, in any person acquiring or strengthening a dominant position in a market.

DETERMINATION ON NOTICE OF CLEARANCE

- 57 Accordingly, pursuant to section 66(3)(a) of the Commerce Act 1986, the Commission determines to give clearance for the acquisition by Turners & Growers Limited, or any interconnected body corporate of Turners & Growers, of the assets or shares (or any combination of assets or shares) of United Flower Auction Limited, but excluding the export business (including export debtors) of United Flower Auction Limited.

Dated this 15th day of July 1999

Dr K M Brown
Member