

COMMERCE COMMISSION

DECISION NO. 508

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

SOUTH PACIFIC SEEDS PTY LIMITED

and

YATES LIMITED

The Commission: **PR Rebstock (Chair)**
PJM Taylor
DF Curtin

Summary of Application: The acquisition by South Pacific Seeds Pty Limited of the assets and business that comprise the New Zealand vegetable seeds sales division of Yates Limited.

Determination: Pursuant to section 66(3) (a) of the Commerce Act 1986, the Commission determines to give clearance for the proposed acquisition.

Date of Determination: 25 September 2003

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EXECUTIVE SUMMARY

The Proposal

1. A notice pursuant to section 66(1) of the Commerce Act was registered on 25 August 2003. The notice sought Clearance for the acquisition by South Pacific Seeds Pty Limited (“SPS”), of the business of the commercial vegetable seed sales and marketing business owned by Yates Limited (“Yates”).

Market Definition

2. The Commission concludes that, for the purpose of analysing this application, the relevant markets are the:
 - market for the distribution of capsicum seeds to growers of covered crops in New Zealand (“the capsicum seed distribution market”);
 - market for the distribution of tomato seeds to growers of covered crops in New Zealand (“the tomato seed distribution market”); and
 - market for the distribution of cucumber seeds to growers of covered crops in New Zealand (“the cucumber seed distribution market”).

Counterfactual

3. It is likely that if SPS does not acquire Yates, that Yates would continue to trade or be purchased by a third party. Therefore, the Commission considers that the appropriate counterfactual is the status quo.

The Capsicum Seed Distribution Market

4. Post merger, SPS would have 100% of the market share in the capsicum seed distribution market and would be the only participant in the market. This falls outside the Commission’s safe harbour guidelines.
5. The Commission considers that in the factual, the considerable degree of competition that currently exists in the capsicum seed distribution market will be removed, and that there are no other existing competitors operating in this market that could constrain the merged entity.
6. The Commission considers that barriers to entry and expansion for new entrants and existing competitors in the capsicum seed distribution market are low to moderate. The number of distributors is inevitably limited by the limited number of overseas suppliers of these seeds. At present there appear to be perhaps five current and potential suppliers of capsicum seeds to the New Zealand market.
7. The three existing suppliers have [] arrangements with SPS and Yates, but these arrangements appear relatively easy to terminate and consequently the three seed suppliers would each be readily able to change distributors should they be dissatisfied with the performance of SPS post-acquisition. Further, there are a number of seed distributors in New Zealand who possess the required infrastructure and technical expertise to distribute capsicum seeds. As such, the overseas suppliers not only have the option of a new entrant, but the alternative option of a number of non-capsicum seed distributors in the event the supplier is considering switching distributors.

8. The Commission considers that it would be in the commercial interest of each of the suppliers to have their seeds distributed in New Zealand in an efficient manner at competitive prices.
9. The Commission considers that Seminis, and to a lesser extent, Syngenta are credible near suppliers to the distribution market and that, on entry they will distribute their seeds in New Zealand themselves.
10. The Commission is of the view that capsicum growers would place some countervailing power on the merged entity. The Commission considers that the merged entity would be likely to be strongly constrained by the countervailing power of its large upstream suppliers. Post acquisition, it is likely the suppliers would continue to seek market share in New Zealand through the introduction of new varieties, and would ensure that these prices to growers are competitive.
11. Having regard to all the relevant factors, the Commission is satisfied that the proposed acquisition would not have, nor would be likely to have, the effect of substantially lessening competition in the capsicum seed distribution market.

The Tomato Seed Distribution Market

12. The Commission has considered the nature and extent of the contemplated lessening of competition in the tomato seed distribution market. The proposed acquisition would result in the merged entity obtaining a market share of []% and the three firm ratio would be 100%. This falls outside the Commission's safe harbour guidelines.
13. However, the Commission has also considered the nature and extent of the contemplated lessening in the tomato seed distribution market and is satisfied that competitive constraints are likely to exist following the merger from:
 - existing competition;
 - the short and long term entry by potential competitors; and
 - the countervailing power of large suppliers.
14. The Commission is therefore satisfied that the proposed acquisition would not have, nor would be likely to have, the effect of substantially lessening competition in the tomato seed distribution market.

The Cucumber Seed Distribution Market

15. The Commission has considered the nature and extent of the contemplated lessening of competition in the cucumber seed distribution market. The proposed acquisition would result in the merged entity obtaining a market share of []% and the three firm ratio would be []%. This falls outside the Commission's safe harbour guidelines.
16. However, the Commission has also considered the nature and extent of the contemplated lessening in the cucumber seed distribution market and is satisfied that competitive constraints are likely to exist following the merger from:
 - existing competition;
 - the short and long term entry by potential competitors; and
 - the countervailing power of large suppliers.

17. The Commission is therefore satisfied that the proposed acquisition would not have, nor would be likely to have, the effect of substantially lessening competition in the cucumber seed distribution market.

OVERALL CONCLUSION

18. Overall the Commission's view is that the merger is unlikely to substantially lessen competition in the national markets for the distribution of capsicum, tomato and cucumber seeds. Although the merger would give rise to 100% aggregation in the capsicum seed distribution market, the combined entity would be constrained by potential new entry, as well as the countervailing power of suppliers.
19. Accordingly, pursuant to section 66(3) (a) of the Commerce Act 1986, the Commission determines to give clearance for the proposed acquisition by South Pacific Seeds Pty Limited of the assets and business that comprise the New Zealand vegetable seeds sales division of Yates Limited.

THE PROPOSAL

1. A notice pursuant to section 66(1) of the Commerce Act was registered on 25 August 2003. The notice sought Clearance for the acquisition by South Pacific Seeds Pty Limited (“SPS”), of the business of the commercial vegetable seed sales and marketing business owned by Yates Limited (“Yates”).

THE PROCEDURES

2. Section 66(3) of the Act requires the Commission either to clear or to decline to clear a notice given under section 66(1) within 10 working days, unless the Commission and the person who gave notice agree to a longer period. An extension of time was sought by the Commission and agreed to by the Applicant. Accordingly, a decision on the application was required by 26 September 2003.
3. In its application, SPS sought confidentiality for specific aspects of the application. A confidentiality order was made in respect of the information for a period of 20 working days from the Commission’s determination notice. When that order expires, the provisions of the Official Information Act 1982 will apply.
4. The Commission’s approach is based on principles set out in the Commission’s *Practice Note 4*.¹

THE PARTIES

South Pacific Seeds Pty Limited

5. SPS imports and distributes vegetable seeds for sale in New Zealand. SPS was formed in Australia in 1986, and entered New Zealand in 1997. SPS distributes most of its seeds directly to customers, such as commercial vegetable growers, processors and nurseries.
6. SPS also produces vegetable seeds on a contract multiplication basis for Yates and a number of overseas seed companies, however the proposed acquisition will not give rise to any aggregation in this area, as the seed production business that Yates presently owns is to be bought by Enza Zaden BV of Holland (“Enza Zaden”).
7. Of particular relevance to this application is SPS’s distribution of capsicum, tomato and cucumber seeds to growers of covered crops. [] to distribute Enza Zaden’s capsicum and tomato seeds, and an [] to distribute Nickerson Zwaan’s cucumber seeds in New Zealand.

¹ Commerce Commission, *Practice Note 4: The Commission’s Approach to Adjudicating on Business Acquisitions Under the Changed Threshold in section 47 – A Test of Substantially Lessening Competition*, May 2001.

Yates Limited

8. Yates was originally established in New Zealand in 1883. Yates manufactures and distributes garden products in New Zealand and Australia, although it recently announced the sale of its domestic gardening division to Orica Limited.
9. Of relevance to this application is Yates' distribution of commercial vegetable seeds for sale in New Zealand. Yates distributes its seeds through a network of seed merchants and directly to customers, such as commercial vegetable growers, processors, and nurseries.
10. Yates distributes its seeds through its two separate but wholly owned entities, Yates Vegetable Seeds Limited and Webling & Stewart Limited. Of particular relevance to this application is Yates' distribution of capsicum, tomato and cucumber seeds to growers of covered crops. Yates currently has exclusive agencies to distribute the seeds of Rijk Zwaan BV of Holland ("Rijk Zwaan") and De Ruiter BV of Holland ("De Ruiter"), two of the world's biggest seed breeders and suppliers.
11. Yates also engages in product development, breeding its own proprietary varieties in New Zealand and Australia, seed testing, and research and development.
12. Yates's product development division is not included in the sale to which this application relates. Rather, this division is being acquired by Enza Zaden in a contemporaneous transaction.

OTHER RELEVANT PARTIES

Overseas Seed Companies and Breeding Houses

13. Almost all of the world's capsicum, tomatoes and cucumbers seeds are bred and developed in the Netherlands by global seed breeding companies. Of relevance to this application are the major foreign seed companies who specialise in, or are developing, capsicum, tomatoes and/or cucumber seeds which may be suitable for New Zealand growing conditions. These include:
 - Enza Zaden (distributed in New Zealand by SPS);
 - Rijk Zwaan (Yates);
 - De Ruiter (Yates);
 - Bruinsma (a division of Seminis);
 - Syngenta (own distribution);
 - Nunhems (Henderson Seeds);
 - Nickerson Zwaan (SPS); and
 - Hazera (Lefroy).

Other Vegetable Seed Distributors

Seminis Vegetable Seeds New Zealand Limited (“Seminis”)

14. Seminis is a large global seed company based in the United States. Seminis seeds have been distributed in New Zealand by SPS and Yates since 1997. However, in September 2003, Seminis ended this arrangement and now distributes its seeds directly to the New Zealand market.
15. Seminis distributes around 100 seed lines including onions, spinach, carrots, zucchinis, and lettuce. In New Zealand, Seminis seeds are marketed under the brands Asgrow, Petoseed, Royal Sluis and Bruinsma.

Syngenta Seeds Pty Limited (“Syngenta”)

16. Syngenta is part of a multi-national seed company with its head office based in Europe. Syngenta markets its seeds under the S&G brand and specialises in field crops such as sweet corn, cauliflower and carrots and some covered crops. Around [] of its seeds are sold to processors such as Heinz and Talley’s.

Lefroy Valley Seed Co (NZ) Limited (“Lefroy”)

17. Lefroy was established in Western Australia in 1984 and commenced operations in New Zealand in 1990. Lefroy distributes both field crop seeds and covered crop seed, including Hazera tomato seeds and Enza Zaden cucumber seeds.

Henderson Seed Pty Limited (“Henderson”)

18. Henderson was established in Australia in the 1950’s and opened its New Zealand branch in 1999. Henderson specialises in field crop seeds such as onions, lettuce and broccoli. []

Seed Merchants

19. Seed merchants on-sell vegetable seeds obtained from New Zealand seed distributors, to growers, processors and nurseries. Seed merchants mostly sell to small to medium growers who require seed and other agricultural and horticultural products and expertise. Major seed merchants include Williams & Kettle Fruitfed, and Veg-Gro Supplies.

Processors

20. Large New Zealand processors such as Talley’s and Heinz purchase vegetable seeds including peas, beans and sweet corn, on behalf of their contract growers. Seeds used by processors’ contract growers are generally for sowing in fields rather than under glass, are cheaper, and produce vegetables that are often only suitable for processing.
21. Processors source their seeds through importing directly from overseas seed suppliers, or by purchasing from a New Zealand seed distributor or merchant.

New Zealand Covered Crop Growers

22. New Zealand covered crop growers export around 85% of their produce to Australia and Asia. The remaining 15% is sold to domestic customers, with a significant proportion being supplied to supermarkets. The major covered crop growers of capsicums, tomatoes and cucumbers include:

- New Zealand Gourmet Limited (“NZ Gourmet”);
- Southern Paprika Limited (“Southern Paprika”);
- NZ Hothouse Limited (“NZ Hothouse”); and
- Status Produce Limited (“Status”).

THE INVESTIGATION

23. During its investigation, the Commission discussed the application with a number of industry participants including:

- SPS;
- Yates;
- Seminis;
- Syngenta;
- Lefroy;
- Henderson;
- Enza Zaden;
- Rijk Zwaan;
- De Ruiter;
- NZ Hothouse;
- Status Produce;
- NZ Gourmet;
- Southern Paprika;
- Classic Capsicums;
- Leaderbrand;
- Balle Bros ;
- Williams & Kettle Fruitfed;
- Veggro Supplies;
- MAF;
- ERMA;
- New Zealand Grain & Seed Association; and
- New Zealand Vegetable & Potato Growers Federation.

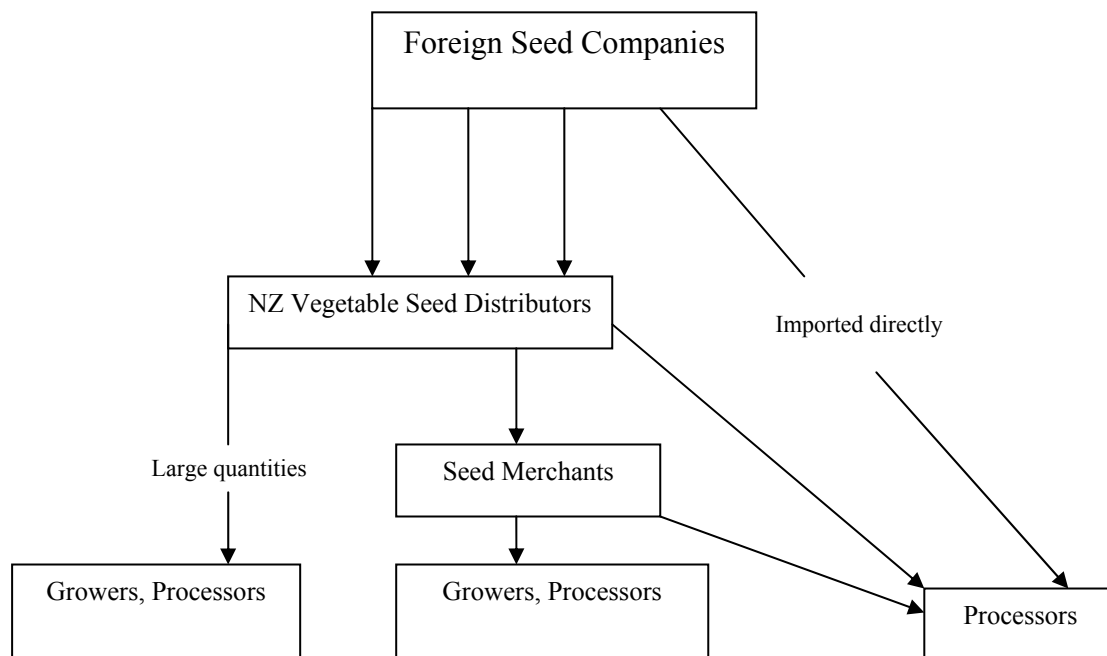
INDUSTRY BACKGROUND

Distribution of Vegetable Seeds in New Zealand

Commercial Growers

24. Large commercial growers in New Zealand generally purchase vegetable seeds directly from a New Zealand vegetable seed distributor. Whereas small to medium growers tend to purchase from seed merchants. The seed supply chain is illustrated in Diagram 1 below.

Diagram 1 - The Supply Chain for Vegetable Seed for Commercial Use in New Zealand



25. Approximately 50% of vegetable seed is distributed through resellers to small to medium growers. The remaining 50% is sold by New Zealand seed distributors directly to large growers. There appears to be a trend within the industry for New Zealand seed distributors to sell directly to the grower. [

]

Distributors




26. New Zealand seed distributors import seed via agency agreements with overseas seed companies. The agency agreements range from being informal verbal arrangements to binding contractual agreements. However, most agencies are exclusive insofar as the overseas company will undertake not to sell its seed through any other New Zealand company.

27. Of relevance to this application are the agencies held by New Zealand seed distributors for capsicums, tomatoes and cucumbers.
28. The world supply of capsicum, tomato and cucumber seed has traditionally been controlled by three Dutch seed companies, Rijk Zwaan, De Ruiter and Enza Zaden. These three Dutch companies currently supply their capsicum, tomato and cucumber seed via Yates and SPS.
29. Other foreign seed companies such as Hazera of Israel, Nickerson Zwaan of the Netherlands and Syngenta have had some presence in New Zealand with tomatoes and/or cucumbers. Seminis, through its Bruinsma brand, is also present in New Zealand but is still developing and trialling capsicum, tomato and cucumber seeds with New Zealand growers.
30. Table 1 outlines the agencies currently held by New Zealand seed distributors. It also outlines the availability of capsicum, tomato and cucumber seed from each agency.

Table 1 – Agencies held by New Zealand Seed Distributors

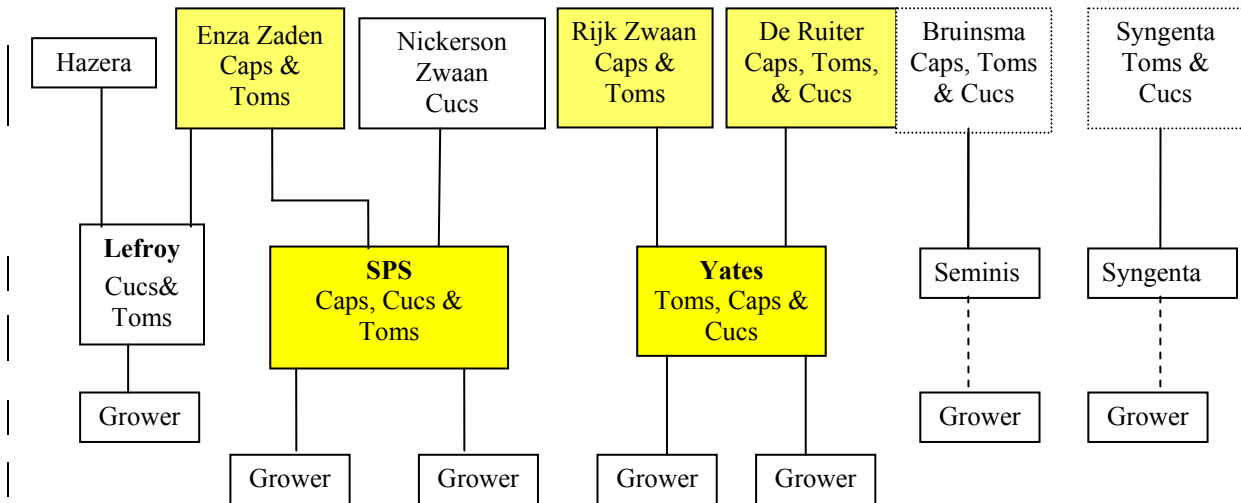
	Capsicum	Tomatoes	Cucumbers
Yates	Rijk Zwaan De Ruiter	Rijk Zwaan De Ruiter	De Ruiter
SPS	Enza Zaden	Enza Zaden	Nickerson Zwaan
Seminis	Bruinsma	Bruinsma	Bruinsma
Lefroy	No variety	Hazera	Enza Zaden
Syngenta	No variety	S&G	S&G
Henderson	No variety	Nunhems	Nunhems

Key

-  Seed has been successfully trialled in New Zealand and is readily available.
-  Seed is currently being trialled in New Zealand and may be available in 1-2 years.
-  No seed is currently available or will not be available for more than 3 years.

31. The supply chain relationships are diagrammatically represented in Diagram 2 below.

Diagram 2: Supply and Distribution of Covered Crop Seeds



Key

Merged Entity

Processors

32. Processors such as Heinz Watties and Talley's purchase vegetable seed on behalf of their contract growers. Processors purchase vegetable seeds in a variety of ways including:

- importing the seed directly from overseas seed companies;
- purchasing from New Zealand seed distributors and seed merchants; and
- purchasing from affiliated companies overseas.

33. Generally, capsicum seeds that are utilised by processor's contract growers are cheaper as they tend to be non-hybridised, and produce lower quality fruit. For example, capsicums grown for processors are grown outdoors from February to June. Outdoor capsicums produce fruit that is suitable for processing and some supermarket sales, but is generally unsuitable for export markets due to its lower quality. In addition, outdoor capsicums have a far shorter growing season due to climatic conditions.

Research, Development and Trials

34. As discussed, many of the world's largest seed breeding companies are located in the Netherlands. Seed breeding companies research and develop new vegetable seed varieties specifically for individual countries. This is because climatic and light conditions vary from country to country. What might grow well in Europe may not perform as well in New Zealand.

35. The development of an original germ plasm that will eventually result in a completely new vegetable seed variety could take up to, or over, ten years. The seed would then

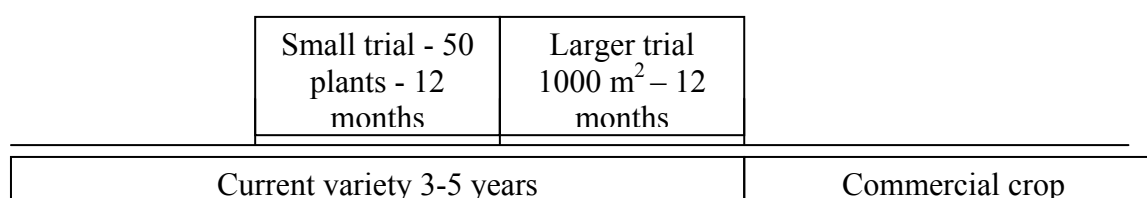
undergo further modification in order to make it suitable for different countries' climatic and light conditions and it is then trialled by individual growers for one to three years.

36. Once the seed is proven to be commercially viable, the grower generally uses that seed for around three to five years. Growers are unlikely to switch to a new seed variety without at least one season of trials as there may be too many risks in relying on an untested new seed, such as uncertainties in fruit size, yield, and overall performance in specific growing conditions.

Capsicums, Tomatoes and Cucumbers

37. Capsicum and tomato seeds begin to produce fruit after three months in the ground. They will then produce fruit for around nine months. Capsicum seeds are purchased once a year around March/April and the crop is planted in May/June.
38. Tomato seeds are also purchased only once per year and most are planted around January. However, many growers stagger their tomato plantings so that tomatoes are produced all year round.
39. Due to this long season, capsicum and tomato growers tend to trial new seed varieties for two to three seasons, being two to three years. A grower may plant thirty to fifty plants in the first season and assess the results. If the results appear promising, the grower will then sow a larger proportion of their crop with the new seed. Again, if the results are still promising, the grower may decide to place the new seed into commercial production. If a grower is not satisfied with a new seed during the initial trials, another seed variety will be trialled. Diagram 3 outlines the general trialling period for capsicums and tomatoes.

Diagram 3 – Implementation Time Frame for Capsicums and Tomatoes



40. Once the grower has planted a large proportion of their crop with the new seed, the grower will tend to “stick” with this seed for three to five years. Capsicum and tomato growers will seldom switch seed varieties in just one season due to the obvious risk in relying on untested seed.
41. New Zealand growers advised the Commission that they are slow to change varieties as they supply export markets that require a certain type of product. For example, with respect to capsicums, the Japanese require a smaller fruit while the United States prefer a larger fruit. New Zealand growers also supply domestic supermarkets that require year round supply. In order to maintain their export and domestic markets, capsicum and tomato growers must be absolutely certain that a new variety will meet the needs of their customers.
42. Cucumber seeds are generally planted three times a year with each planting producing approximately three to four months of cucumbers. Like capsicum and tomato growers,

cucumber growers will trial seeds before committing their entire crop to a new variety. But as there are three plantings per year, cucumber growers are able to trial new seeds more quickly than capsicum and tomato growers. Cucumber growers have specific export and domestic markets and growers might still take around a year to commit their entire crop to a new seed variety.

PREVIOUS INVESTIGATIONS

43. The Commission has previously considered related activities in *Decision 320 Yates New Zealand Limited and Watkins New Zealand Limited and Smiths Horticultural Distributors Limited* 20 March 1998 (“the Yates Decision”).
44. In the Yates Decision, the Commission determined a number of markets, which included a separate market for the wholesale distribution of vegetable seeds to commercial users. The Commission found that the acquisition would not result in any person acquiring or strengthening a dominant position in the market for the wholesale distribution of vegetable seeds to commercial users due to sufficient existing competition and low barriers to entry.

MARKET DEFINITION

45. The Act defines a **market** as:

... 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.

46. For the purpose of competition analysis, a relevant market is the smallest space within which a hypothetical, profit-maximising, sole supplier of a good or service, not constrained by the threat of entry, could impose at least a small yet significant and non-transitory increase in price, assuming all other terms of sale remain constant (the ‘*ssnip* test’). For the purpose of determining relevant markets, the Commission will generally consider a *ssnip* to involve a five percent increase in price for a period of one year.
47. The Commission defines relevant markets in terms of four 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); and
 - the temporal dimension of the market, if relevant (the timeframe).

48. The Commission aims to define the markets in a way that best assists the analysis of the competitive impact of the acquisition under consideration. A relevant market will ultimately be determined, in the words of the Act, as a matter of fact and commercial common sense.

Relevant Markets

Product Dimension

49. The delineation of relevant markets as a basis for assessing the competitive effects of a business acquisition begins with an examination of the goods or services offered by each of the parties to the acquisition. Both demand-side and supply-side factors are generally considered in defining market boundaries. Broadly speaking, a market includes products that are close substitutes in buyers' eyes on the demand-side, and suppliers who produce, or are able easily to substitute to produce, those products on the supply-side.
50. The Commission takes the view that the appropriate time period for assessing substitution possibilities is the longer term, but within the foreseeable future. The Commission considers this to be a period of one year, which is the period customarily used internationally in applying the 'ssnip' test (see below) to determine market boundaries. The Commission will take into account recent, and likely future, changes in products, relative prices and production technology in the process of market definition.

Product definition analysis

51. The Applicant has stated that the market in which there would be an aggregation of business activities as a result of the proposed acquisition is that for the wholesale supply of vegetable seeds to seed merchants and direct sales to end use customers (commercial vegetable growers, processors, and nurseries).
52. The Applicant notes that there are over 40 vegetable groups commercially grown in New Zealand for domestic consumption and export. For each group there are numerous varieties, the seeds of which are (largely) imported from overseas developers and distributors. Growers make their seed purchasing decisions based on the characteristics of the resulting crop, including market demand for certain varieties, consumer and retail attributes, production attributes, and climatic suitability. Seed suppliers promote their portfolio of seeds on the basis of their ability to achieve the desired characteristics.
53. The Commission notes that seeds for growing crops outdoors have different characteristics from those seeds for growing the same crops in a covered environment. For growers with glass houses, who are the principal parties who might be affected by the acquisition, seeds designed for growing outdoors are not a satisfactory substitute. Consequently, the Commission has placed seeds for growing covered crops in separate markets from seeds for growing crops outdoors.
54. When distributing these seeds in New Zealand both South Pacific and Yates import them from the overseas supplier, promote their merits to growers and undertake the retailing function. This may involve assisting growers with trialing the seeds and

providing on-going technical advice. These activities are common to all the seeds they distribute, although new varieties would generally require a different emphasis than for repeat orders of well-established varieties. Distributors could readily add new seeds to their product range, should they be asked to do so by the overseas supplier. In general each seed supplier sells through a single New Zealand distributor, although there are exceptions to this position.

55. As noted above, of major relevance to the issue of product market definition is demand-side substitution. Would growers of one type of vegetable be likely to switch to growing another vegetable in the event of a “small but significant non-transitory increase in price (a “ssnip”) of their seeds? Growers spoken to have indicated that they would usually be unlikely to switch in the event of “a small but significant” increase in seeds prices. To switch can be costly. The growers may have developed expertise in a particular type of vegetable, they may have vegetable-specific supply contracts to meet, and they may have invested in considerable infrastructure designed for a particular vegetable. The growers have noted that seed costs usually represent less than 5% of their total cost of producing the vegetable and, accordingly, a “small but significant” increase in seed prices would constitute a very small increase of the total cost of producing the vegetable in question. In itself, it would not be likely to affect significantly the grower’s choice of crops.
56. Having regard to these matters the Commission has concluded that seeds for each type of vegetable fall within discrete product markets.
57. In this instance the proposed acquisition would result in significant aggregation in respect of the distribution of capsicum, cucumber and tomato seeds. Seeds for each of these vegetables form the product markets the Commission has adopted for the competition analysis below.

Functional Market

58. The production, distribution and sale of a product typically occur through a series of functional levels – for example, the manufacturing/import level, the wholesale/distribution level and the retail level. It is often useful to identify the relevant functional level in describing a market, as a proposed business acquisition may affect one horizontal level, but not others. Alternatively, some acquisitions, such as those involving businesses at different vertical levels, may raise issues related to vertical integration. Generally, the Commission will seek to identify separate relevant markets at each functional level affected by an acquisition and assess the impact of the acquisition on each.
59. In this instance aggregation occurs at the distribution level, and accordingly, this is the functional level adopted for the relevant product markets.

Geographic Market

60. The Commission seeks to define the geographical extent of a market to include all of the relevant, spatially dispersed, sources of supply to which buyers can turn should the

prices of local sources of supply be raised. For each good or service combination, the overlapping geographic areas in which the parties operate are identified. These form initial markets to which a ssnip is applied. Additional geographic regions are added until the smallest area is determined within which the hypothetical monopolist could profitably impose a ssnip.

61. In this instance, the distributors of seeds tend to operate on a national basis and the cost of freight from the distributor to the grower does not represent a significant proportion of total seed costs (due to the small size of the product itself). The Commission considers that it is appropriate to use national markets for its consideration of the application.

Conclusion on Relevant Markets

62. The Commission concludes that, for the purpose of analysing this application, the relevant markets are:
- the market for the distribution of capsicum seeds to growers of covered crops in New Zealand (“the capsicum seed distribution market”);
 - the market for the distribution of tomato seeds to growers of covered crops in New Zealand (“the tomato seed distribution market”); and
 - the market for the distribution of cucumber seeds to growers of covered crops in New Zealand (“the cucumber seed distribution market”).

FACTUAL

63. The Commission uses a forward-looking, counterfactual, type of analysis in its assessment of business acquisitions, in which two future scenarios are postulated: that with the acquisition in question (the factual), and that in the absence of the acquisition (the counterfactual). The impact of the acquisition on competition can then be viewed as the difference between those two scenarios. It should be noted that the status quo cannot necessarily be assumed to continue in the absence of the acquisition, although that may often be the case. For example, in some instances a clearly developing trend may be evident in the market, in which case the appropriate counterfactual may be based on an extrapolation of that trend.
64. In the factual scenario, the merged entity would be the only participant in the capsicum seed distribution market, and one of three players in the tomato and cucumber seed distribution markets. In its application, SPS stated that it has a contract with Yates for the multiplication of seeds and [

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COUNTERFACTUAL

65. The Applicant stated that it was one of a number of businesses invited to submit an offer for Yates. In addition, there is no indication that Yates would cease trading absent the proposed merger. Therefore, it is likely that either a third party would purchase

Yates or that Yates would continue trading. The Commission is therefore of the view that the appropriate counterfactual, in this instance, is the status quo.

COMPETITION ANALYSIS

66. Having defined the counterfactual, the Commission will assess the following for each of the markets:
- the probable nature and extent of competition that would exist in a significant section of the market, but for the acquisition (the counterfactual);
 - the nature and extent of the contemplated lessening by considering market concentration, existing competition and potential competition and other competition factors such as countervailing power; and
 - whether the contemplated lessening is substantial.²
67. The first step in assessing competition is to look at market shares. Market shares can be measured in terms of revenues, volumes of goods sold, production capacities or inputs (such as labour or capital) used. All measures may yield similar results in some cases. Where they do not, the Commission may, for the purposes of its assessment, adopt the measure which yields the highest level of market share for the combined entity. The Commission considers that this will lead to an appropriately conservative assessment of concentration, and that the factors which lead to the other different market share results are more appropriately considered elsewhere during the assessment of the acquisition.³
68. In determining market shares, the Commission will take into account the existing participants (including ‘near entrants’), inter-firm relationships, and the level of imports. This is followed by an application of the Commission’s ‘safe harbours’.
69. A business acquisition is considered unlikely to substantially lessen competition in a market where, after the proposed acquisition, either of the following situations exist:
- where the three-firm concentration ratio (with individual firms’ market shares including any interconnected or associated persons) in the relevant market is below 70%, the combined entity (including any interconnected or associated persons) has less than in the order of a 40% share; or
 - where the three-firm concentration ratio (with individual firms’ market shares including any interconnected or associated persons) in the relevant market is above 70%, the market share of the combined entity is less than in the order of 20%.

The Capsicum Seed Distribution Market

70. At present only two companies distribute capsicum seed to growers of covered crops:

² See *Dandy*, supra n 5, pp 43–887 to 43–888 and adopted in New Zealand: *ARA v Mutual Rental Cars* (1987) 2 NZLR 647; *Tru Tone Ltd v Festival Records Retail Marketing Ltd* (1988) 2 NZLR 352; *Fisher & Paykel Ltd v Commerce Commission* (1990) 2 NZLR 731; *Commerce Commission v Carter Holt Harvey*, unreported, High Court, Auckland, CL 27/95, 18/4/00.

³ See the Commission’s Practice Note 4 for further explanation of the Commission’s approach to market share.

- SPS, which distributes Enza Zaden seeds; and
 - Yates, which distributes De Ruiter and Rijk Zwaan seeds.
71. The Applicant submitted market shares for the wholesale distribution of all vegetable seeds as an aggregate. In light of the Commission’s view that seeds for each vegetable fall within discrete product markets, the Commission, during its investigation, collected market share information based on revenue for each of capsicum, tomato and cucumber seeds for the past two financial years. Table 1 below summarises the market shares of the participants in the capsicum seed distribution market for the 2001-2002 and 2002-2003 years.

Table 1: Market Shares for the Capsicum Seed Distribution market 2001-2002 and 2002-2003

Distributor/Supplier	2001-2002 (\$000s)	Market share (%)	2002-2003 (\$000s)	Market share (%)
Yates				
Rijk Zwaan	[]		[]	
De Ruiter	[]		[]	
	[]	[]%	[]	[]%
SPS				
Enza Zaden	[]	[]%	[]	[]%
TOTAL	[]	100%	[]	100%

72. Presently, there are only two participants in the capsicum seed distribution market, with the ‘three’ firm concentration ratio being 100%. Post merger therefore, SPS would have 100% of the market share in the capsicum seed distribution market. This falls well outside the Commission’s safe harbour guidelines.
73. However, market shares are insufficient in themselves to establish whether competition in a market has been lessened. Additional factors must also be considered before a conclusion is reached. These factors are:
- Existing competition;
 - Potential competition; and
 - Other competition factors such as countervailing power.
74. These factors, along with market concentration, are considered in subsequent sections for each of the relevant markets.
75. After considering the additional factors outlined above, the Commission will assess whether the merger is likely to result in a substantial lessening of competition (“SLC”).
76. Section 2(1)(A) of the Act provides that substantial means real or of substance. Substantial was considered by McGechan J in *Commerce Commission v Port Nelson Ltd* (1995) 6 TCLR 406, 434. He observed:

“substantially lessening competition” is taken as meaning “lessening competition in a way which is more than insubstantial or nominal”. The merely ephemeral and minimal will not suffice. Inevitably, that will involve some attention to relativity; and in the end be a question of judgment on a matter of degree.

77. The Commission considers that it is necessary to identify a real lessening of competition that is not nominal, rather than a quantifiable measure of lessening. The lessening needs to be of such a size, character and importance that it is worthy of consideration.⁴ Overall, the Commission considers that substantially lessening competition concerns a real or substantial impact on a market in a way of a lessening, hindering and preventing the process of workable and effective competition.

Existing Competition

78. In the counterfactual, the status quo, SPS and Yates compete on their respective varietal strengths such as fruit characteristics, colour, and size, as well as on price. As separate entities, SPS and Yates each aim to increase their market share at the expense of the other for two reasons. First it is a profit-maximising strategy in its own-right. Second, it is what their respective overseas seed suppliers expect of them.
79. Tons Zwetloot of NZ Gourmet, the largest producer of capsicums in New Zealand, advised the Commission that [
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80. Other growers also advised the Commission that competition between SPS and Yates is presently strong.
81. As a result of this acquisition there will 100% aggregation in the capsicum seed distribution market. In the factual, the competition between SPS and Yate, as discussed above, will no longer exist. There is no other existing competition in this market that could constrain the merged entity.

Conclusion on Existing Competition

82. The Commission considers that in the factual, the considerable degree of competition that currently exists in the capsicum seed distribution market will be removed, and that there are no other existing competitors operating in this market that could constrain the merged entity.

Potential Competition

Introduction

83. A business acquisition is unlikely to result in a substantial lessening of competition in a market if behaviour in that market continues to be subject to real constraints from the threat of market entry.
84. The Commission will consider the history of past market entry as an indicator of the likelihood of future entry. The Commission is also mindful that entry often occurs on a

⁴ *Dandy Power Equipment Pty Ltd v Mercury Marina Pty Ltd* (1982) ATPR 40-315, 43-888.

relatively small scale, at least initially, and as such may not pose much of a competitive constraint on incumbents within the relevant time frame.

Barriers to Entry

85. The likely effectiveness of the threat of new entry in constraining the conduct of market participants, following a business acquisition that might otherwise lead to a substantial lessening of competition in a market, is determined by the nature and height of barriers to entry into that market.
86. The Commission considers that, for the purpose of considering this issue, a barrier to entry is best defined as an additional or significantly increased cost or other disadvantage that a new entrant must bear as a condition of entry. In evaluating the barriers to entry into a market, the Commission will generally consider the broader 'entry conditions' that apply, and then go on to evaluate which of those constitute entry barriers.
87. It is the overall obstacle to entry posed by the aggregation of the various barriers that is relevant in determining whether entry is relatively easy or not, and therefore whether or not potential entry would prevent a substantial lessening of competition.
88. For entry to act as an antidote to a substantial lessening of competition stemming from a business acquisition, it must constrain the behaviour of the combined entity and others in the market.
89. As noted above, capsicum seeds are supplied to growers in New Zealand through distributors. The distributors hold agencies from overseas suppliers to on sell capsicum seeds to New Zealand growers. In general, a distributor of capsicum seeds in New Zealand would require:
 - an office from which to distribute seed;
 - technical expertise to sell the seed and provide post-sale support; and
 - a supply of acceptable seed from an overseas supplier.
90. Industry participants stated that obtaining suitable warehousing is relatively easy. Seeds are imported in small packets and generally do not present any storage problems. Steve McArthur of SPS stated:⁵

It is very easy to establish a vegetable seed-marketing agency in New Zealand. I have done this for SPS in 1997. I was employed on the 1st of May 1997 and we were fully operational with stock, invoicing and administration office and staff for our opening on the 1st of July 1997.

We leased the office and car. Our only outlay was the computer, fax, office equipment and a seed planter for our trials, the total capital required to start would be [] to start a fully competitive seed business in New Zealand. And if you had an agency such as De Ruiten or Rijk Zwaan, you would be profitable from day one.
91. Industry participants also stated that there were a number of individuals in the industry with relevant technical expertise and who could provide after sales support. These include existing distributors of other vegetable seeds, and seed merchants, such as Williams & Kettle Fruitfed.

⁵ Letter to the Commission dated 18 September 2003.

Acceptable Capsicum Seeds

92. The Commission considers that the key to entering the distribution market is obtaining supplies of acceptable capsicum seeds. There are a number of overseas seed suppliers who produce a wide range of capsicum seeds. However, to be relevant to a new entrant distributor these seeds must:
- be appropriate for New Zealand growing conditions;
 - be acceptable for New Zealand grower's domestic and export markets and therefore commercially acceptable to New Zealand growers; and
 - not be subject to an existing ongoing exclusive distribution agreement.
93. Three Dutch seed suppliers, De Ruiter, Enza Zaden and Rijk Zwaan currently supply 100% of New Zealand's commercially grown capsicums to New Zealand growers. De Ruiter and Rijk Zwaan supply Yates, while Enza Zaden supplies SPS. It is envisaged that immediately following the merger, all of these companies would have their capsicum seeds distributed by the merged entity.
94. As discussed in the background section of this report, a new variety can take up to three years to be fully accepted. Fenton Hazlewood of Seminis noted:⁶
- Typically, it takes more than one season of trialling in order for growers to change the varieties that they plant. One major factor is the needs of the export market, making it a very high priority to make sure the correct product is trialled sufficiently to ensure market fit.
95. This one or two year period between the grower deciding to investigate switching seeds (by running trials, etc) and acquiring the seeds necessary for a full crop can be seen as something of a double-edged sword for distributors. The grower is "captive" to its existing distributor for the period, and this would increase the difficulty of a distributor seeking to enter the market. On the other hand, growers are not all "captive" at the same time and will be operating different trial periods meaning a new distributor could target growers whose commercial crop may be coming to an end. The grower then becomes "captive" to the new distributor for the same period, making new entry by distributors more attractive. On balance, in this case, the Commission has concluded that the switching period constitutes a moderate barrier to new entry into the distribution market.

Existing Exclusive Distribution Arrangements

96. [

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97. [

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98. Rijk Zwaan and De Ruiter [

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⁶ E Mail dated 9th September 2003.

99. Thus the existing distribution agreements [

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100. Further, the Commission considers that seed merchants are likely to be able to expand their services to include distribution of seeds from crops they currently do not handle from overseas seed suppliers. Seed merchants possess the relevant industry knowledge and infrastructure to actively deal with small, medium and large growers in relation to a wide range of horticultural services. As such, the overseas suppliers have the options of a new entrant or an existing non-capsicum seed distributor in the event the supplier is considering switching distributors.
101. The other overseas seed supplier who has capsicum seed available in the short term is Seminis. Seminis is currently trialling a capsicum, Solution, in New Zealand, however, this seed will not be commercially available for another 18 months. Seminis intends to distribute this new seed themselves.
102. The Commission considers that the limited number of potential suppliers of capsicum seeds means that the number of distributors in the market will necessarily be small. However this does not preclude successful new entry or expansion by an efficient non-capsicum seed distributor from occurring.

Conclusion on Barriers to Entry

103. The Commission has considered the various factors relevant to the assessment of the height of entry barriers. These include :
- The distribution function does not require significant investment in sunk cost and capital;
 - Industry knowledge and expertise is important to successful new entry or expansion and can be readily acquired via other existing market participants, such as other distributors and seed merchants.
 - [
-];
- Name recognition and reputation appear to be generally important to successful distribution. However overseas seed companies (such as Seminis) and existing New Zealand distributors of other seeds appear to have the name recognition and reputation necessary to be successful;
 - In total there are only a small number of seed producers who have capsicum seeds suitable for distribution in New Zealand. Until that situation changes, the number of New Zealand distributors will also be small.
104. The Commission has concluded that entry barriers can be categorised as low to moderate.

The “LET” Test

105. The Commission has sought to identify likely new entrants into the market using the “LET” test analysis.
106. In order for the threat of market entry to be such a constraint on the exercise of market power as to alleviate concerns that a business acquisition could lead to a substantial lessening of competition, entry of new participants in response to the exercise of market power must be likely, sufficient in extent and timely (the “LET” test). If they are to act as a constraint on market participants following a business acquisition, which might otherwise lead to a substantial lessening of competition in a market, entry must be relatively easy.

Likelihood of Entry

107. The mere possibility of entry is, in the Commission’s view, an insufficient constraint on the exercise of market power to alleviate concerns about a substantial lessening of competition. 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 its investment, including allowance for any risks involved.

Obtaining an Existing Agency

108. [

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109. The Commission notes that Enza Zaden distributes some of its cucumber seeds through SPS and some through Lefroy. Thus, if Enza Zaden were to become dissatisfied with the merged entity’s performance, it could easily switch all of its seeds to Lefroy.
110. The Commission considers that in the event of the merged entity not performing to the satisfaction of their seed suppliers, it is likely that the suppliers would switch their agency to an existing non-capsicum seed distributor, or a new entrant. The real ability of each of the three existing seed suppliers to switch agencies is likely to represent an on-going constraint on the merged entity. This on-going constraint will be discussed further in the Constraint from Suppliers section of this report.

Syngenta

111. Syngenta is a large multi-national seed supplier with successful commercial capsicum varieties that are available in other countries. Syngenta is currently trialling capsicum seeds with New Zealand growers but [

]. Chris Bone,

General Manager of Syngenta stated:⁷

[

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⁷ E Mail received 29th September 2003.

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112. The Commission considers that while Syngenta's entry to the capsicum seed distribution market may not provide a direct competitive constraint on the merged entity in the immediate future, its programme is sufficiently advanced and promising to make its yet to be chosen distributor a possible competitive threat to SPS in the medium term.

Seminis

113. Seminis is a large multi-national company whose seed breeding house division, Bruinsma, has around 5-10% share of the world's vegetable seed market. Seminis, through Bruinsma, produces red, green, yellow, orange and white capsicum seeds that are distributed worldwide.
114. Seminis does not currently have any capsicum varieties in New Zealand that are commercially available to New Zealand growers. [

that:⁸] However, Fenton Hazlewood, General Manager of Seminis did note

just because a product works in Holland does not automatically mean it will suit our growing conditions. With far greater light levels, vegetative growth can be somewhat of a problem. Remembering that with generally cooler growing conditions in Holland they will breed more vigor within a plant. But essentially a product could more than likely have a market fit.

115. [

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116. The Commission is of the view that Seminis is a likely entrant due to its competition in capsicum varieties throughout the world and is likely to enhance competition in the distribution market on entry post acquisition.

Extent and Timeliness of Entry

117. If entry is to constrain market participants, then the threat of entry must be at a level and spread of sales that is likely to cause market participants to react in a significant manner. The Commission will not consider entry that might occur only at relatively low volumes, or in localised areas, to represent a sufficient constraint to alleviate concerns about market power.
118. Small-scale entry into a market, where the entrant supplies one significant customer, or a particular product or geographic niche, may not be difficult to accomplish. However, further expansion from that "toe-hold" position may be difficult because of the presence of mobility barriers, which may hinder firm's efforts to expand from one part of the

⁸ E Mail dated 9th September 2003.

market to another. Where mobility barriers are present in a market, they may reduce the 'extent' of entry.

119. If entry is effectively to constrain the exercise of market power to the extent necessary to alleviate concerns about a substantial lessening of competition, entry must be likely to occur before customers in the relevant market are detrimentally affected to a significant extent. Entry that constrains must be feasible within a reasonably short timeframe from the point at which market power is first exercised.
120. As discussed above, Seminis appears to be the only current New Zealand seed distributor that is likely to be able to supply New Zealand growers with commercially acceptable capsicum seeds as an alternative to currently available capsicum seed within the Commission's timeframe for analysis.
121. Seminis initially intends to supply one capsicum variety, Solution, and this variety will be available in around 18 months. Seminis advised the Commission that it has a number of other capsicum varieties that it intends to introduce into the capsicum seed distribution market in the near future.
122. New Zealand capsicum growers tend to "stick" with a particular capsicum variety for three to five years. As discussed in the background section, capsicum growers grow specific varieties to meet the needs of their export and domestic customers. A grower will only switch their crop to a new variety, such as the Seminis variety, if they can be certain that the new variety will be as productive as their existing variety, and that their customers will accept it. As such, Seminis' new capsicum variety may not gain an immediate "toehold" with New Zealand capsicum growers.
123. The Commission considers that the extent of Seminis' entry, at least in the short term, is likely to be limited. It offers one coloured variety and in addition, New Zealand capsicum growers are generally reluctant to switch a large percentage of their capsicum crop to a new variety without extensive trialling. However, the merged entity will recognise that testing of Seminis' seeds by a grower may be the first step towards that grower switching away from SPS for a period of at least three to five years (i.e. the period over which growers stick to a particular capsicum variety. Thus while Seminis' distributor may be unlikely to account for a significant proportion of sales over the next year or two, it will nevertheless be likely to exert considerable competitive pressure on SPS well within that time.
124. Notwithstanding their small market share at present, Seminis, and to a lesser extent, Syngenta, are considered likely to provide a competitive constraint on the merged entity in the short-term.
125. In addition, in the event of the merged entity not performing to the satisfaction of their seed suppliers, it is likely that the suppliers would switch their agency to an existing non-capsicum seed distributor or a new entrant. Any such switching is likely to occur in a reasonably short time frame due to the relative ease by which the overseas suppliers could terminate their contract with the merged entity and the ease by which they could utilise the expertise of an existing non-capsicum seed distributor. The Commission therefore considers that the real ability of each of the three existing seed suppliers to switch agencies in a relatively short time frame is likely to represent a significant on-going constraint on the merged entity.

Conclusion on Potential Entry

126. The Commission considers that the policy of each seed supplier to sell its seeds in New Zealand through a single distributor inevitably means that the number of capsicum seed distributors in the market will be small. Currently there are perhaps five capsicum seed suppliers who have seeds which are, or soon will be, suitable for New Zealand conditions. However the ability of new entrant, or an existing non-capsicum seed distributor, to enter the market to provide distribution services for overseas seed suppliers does not appear unduly constrained. Factors affecting entry include:
- the distribution function does not require significant investment in sunk cost and capital;
 - current non-capsicum seed distributors possess the required infrastructure to distribute capsicum seeds;
 - industry knowledge and expertise can be readily acquired via a number of market participants such as existing distributors and seed merchants;
 - brand recognition and reputation appear to be generally important to successful distribution, and this may take time to establish for a new entrant, it would not be an issue for firms already distributing other types of seeds.
127. The Commission also concludes that Seminis and, to a lesser extent Syngenta have the potential to supply seeds to New Zealand distributors, or will have in the near future, and while these distributors' sales may not be significant in the next year or two while growers test the seeds, their competitive influence is likely to be felt well within that time.

Other Competition Factors

Constraint from Buyers

128. The potential for a firm to wield market power may be constrained by countervailing power in the hands of its customers, or alternatively, when considering buyer (oligopsony or monopsony) market power, its suppliers. In some circumstances, it is possible that this constraint may be sufficient to eliminate concerns that a business acquisition may lead to a substantial lessening of competition.
129. Where a combined entity would face a purchaser or supplier with a substantial degree of market power in a market affected by the acquisition, the Commission therefore considers whether that situation is such as to constrain market participants to such an extent that competition is not substantially lessened.
130. Approximately [] of capsicum seed sales in New Zealand are made to the top three growers; NZ Gourmet, Southern Paprika, and NZ Hothouse. However, the proportion of overall production costs that the seed component represents is very small at around 3-5%.
131. Despite this, NZ Gourmet, in particular, considers that it has a strong bargaining position when negotiating price with seed distributors, owing to its relationship with the upstream Dutch seed supply companies. [

132. [

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133. [

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134. De Ruiter and Enza Zaden advised the Commission that while they would detect the loss of sales in New Zealand, it would be difficult for them to detect the corresponding additional sales volume in another part of the world.
135. In contradiction to this view, Mr Abe Adema, Sales and Marketing Director of Rijk Zwaan in Holland, advised the Commission that the close relationships between seed suppliers and growers/nurserymen, and the suppliers and distributors in each country, would facilitate detection by the seed suppliers. Mr Adema said that the seed supplying company deals directly with growers and nurserymen in other countries at least once a year, and in some cases more often, offering technical advice and assisting with trials of new varieties.
136. Through these relationships, Mr Adema opined that a seed supplier would be able to quickly detect any increase in order volumes where there was not an associated increase in growing capacity, thereby detecting any attempt on the part of growers to acquire their seed through alternative sources.
137. Further, Mr Adema said that all seed packets have brands and batch numbers printed on them, which would make the origin of the seed traceable. Mr Adema said that on detection of any such attempt, Rijk Zwaan would prevent the distributor in that particular country from supplying the ‘offending’ grower or nurseryman.
138. Whether suppliers could easily detect attempts to make bypass purchases (and if so whether they would do anything about it), several of the large growers noted that to bypass the local distributor and successfully source seeds overseas would be difficult. Several small growers said they would not contemplate such an exercise as they would take on the risk of faulty seed and a lack of warranty from the overseas seed supplier in respect of germination rates and fruit consistency.
139. The Commission is of the view that while there may be some potential for larger growers to import seeds direct, and this would provide some constraint on the merged entity from attempting to exercise market power, the Commission considers that this countervailing power would not be sufficient in itself to prevent the acquisition from substantial lessening competition in the distribution of capsicum seeds market.

Constraint from Suppliers

140. The Commission has given careful consideration to the relationship suppliers have with their distributors and is of the view that it can be likened in many respects to agency agreements. The relationship can be revoked at short notice, the supplier provides important advice and supervision to the distributor, and the supplier usually has

important direct contact with the seed growers. The supplier has an important incentive to ensure that its New Zealand distributor operates efficiently and competitively to avoid losing market share in New Zealand to other overseas seed suppliers. An inadequate performance by the distributor would be likely to result in it losing the right to distribute the supplier's seeds.

141. Some capsicum growers expressed concern that post acquisition, the three largest suppliers of capsicum seed in the world, and presently the only suppliers to the New Zealand market, would be represented in New Zealand by a single distribution agency. The question was raised whether the suppliers might behave in a collusive manner, either tacitly or explicitly, to raise prices to SPS which would in turn raise prices to growers to recover the price increase from the supplier.
142. The Commission investigated this possibility, particularly in light of the comments of Mr Roland Perenboom, Enza Zaden:

... We, (the suppliers) are always looking at each other's pricing or whatever information we can get from the market. Especially in the capsicum seed distribution market there's a kind of a market leader principle, and that is if it's De Ruiter who is the market leader in yellow, then DR sets the price and the rest follow.
143. The Dutch suppliers argued that they compete vigorously for market share in New Zealand, particularly when a competitor introduces a new variety. All three stated that the situation would be no different post merger.
144. The suppliers advised the Commission that they would rely on the merged entity to separately market their respective seeds, in the same manner that Yates had maintained the Webling and Stewart entity to market De Ruiter seeds and Yates, Rijk Zwaan seeds. In this way, they argued, competition between their respective seeds would continue, and any attempt by the merged entity to depart from such a structure would see one or all of the suppliers seeking an alternative distributor for their seeds. Any ability for them to tacitly collude, they argued, would therefore be unsustainable.
145. As discussed in the section on barriers to entry, while the distributors have exclusive distribution arrangements with the distributors of their seeds, these arrangements can quickly be terminated. Enza Zaden, in particular already has an arrangement with another New Zealand distributor, Lefroy, and could easily switch its distribution if the merged entity made its seed uncompetitive.
146. The suppliers also stated that near entry to the market by Seminis and more distantly, Syngenta, would ensure that they held prices to competitive levels in the New Zealand market. They also advised that they would threaten to revoke a distribution agency if the merged entity unilaterally raised prices.
147. In the event SPS sought to exercise market power post-acquisition by for example, implementing price increases, large growers would also have countervailing power from their ability to switch between the type of capsicum seed they acquire from SPS. The switching would not impact immediately on SPS's total sales, but rather only the proportion of that total which originated from each supplier. However the supplier which was disadvantaged would then have a strong incentive to respond by requiring SPS to reduce the price of the supplier's seeds back to competitive levels, or by finding a new distributor of its product.

Conclusion on Countervailing Power

148. The Commission is of the view that the potential for large growers to buy direct from overseas would provide some constraint (albeit limited) on the merged entity. However, it considers a much stronger constraint on the behaviour of the merged entity would come from the seed suppliers. Each supplier would have a profit-maximising interest in ensuring that its seeds are distributed in an efficient manner at competitive prices. Each currently maintains a close oversight of the New Zealand market and would be aware of any inefficiencies or overpricing by the distributor. Further, large growers would also have countervailing power from their ability to switch between the type of capsicum seed they acquire from SPS. The supplier which was disadvantaged would then have a strong incentive to respond by requiring SPS to reduce the price of the supplier's seeds back to competitive levels, or by finding a new distributor of its product. The supplier's ability to switch distributors, and the availability of a range of alternative non-capsicum seed distributors means that the countervailing power of the supplier over the distributor would be very effective.

Conclusion on Competition in the Capsicum Seed Distribution Market

149. The Commission has considered the nature and extent of the contemplated lessening of competition in the capsicum seed distribution market. The proposed acquisition would result in the merged entity obtaining a market share which falls outside the Commission's safe harbour guidelines.

150. However, market shares are not always an indication in themselves of market power. In this instance the Commission considers that there are a number of factors which together would constrain the behaviour of the applicant post-acquisition so that its market power would not be increased significantly. These factors include:

- seed suppliers would have a strong incentive to ensure that their seeds are distributed efficiently and at competitive prices;
- due to the number of alternative non-capsicum seed distributors each seed supplier would have the ability to switch to a new distributor should it be dissatisfied with the performance of its existing distributor or large growers commenced switching between the seed suppliers;
- as such, the suppliers' ability to switch distributors, and the availability of a range of alternative non-capsicum seed distributors means that the countervailing power of the supplier over the distributor would be very effective.
- should a seed supplier seek a new distributor for its seeds, entry barriers to the distribution of capsicum seeds would be low to moderate;
- there is some potential for larger growers of capsicums to obtain seed supplies direct from overseas;
- Semisis and Syngenta have the potential to supply capsicum seeds to New Zealand in the near future, and to distribute the seeds themselves or to use independent distributors.

Having regard to all the factors the Commission has concluded that the proposed acquisition would not have, nor would be likely to have, the effect of substantially lessening competition in the capsicum seed distribution market.

The Tomato Seed Distribution Market

Existing Competitors

151. There are presently four competitors in the tomato seed distribution market:

- Yates;
- SPS;
- Syngenta; and
- Lefroy.

Market Concentration

152. The market shares for the tomato seed distribution market are as in Table 2 below.

Table 2: Market Shares for the Tomato Seed Distribution Market 2001-2002 and 2002-2003

Distributor /Supplier	2001-2002 (\$000s)	Market share (%)	2002-2003 (\$000s)	Market share (%)
Yates				
Rijk Zwaan	[]		[]	
De Ruiter	[]		[]	
	[]	[]%	[]	[]%
SPS				
Enza Zaden	[]	[]%	[]	[]%
Syngenta	[]	[]%	[]	[]%
Lefroy	[]	[]%	[]	[]%
TOTAL	[]	100%	[]	100%

153. Presently, the three firm concentration ratio is []%. Post merger, the combined entity would have []% of the market share and the three firm ratio would be 100%. This falls outside the Commission's safe harbour guidelines.

Existing Competition

154. The tomato seed distribution market is served by more distributors than the capsicum seed distribution market. Lefroy has managed to secure a reasonable share of the tomato seed distribution market through its distribution of Hazera seeds. In addition, Syngenta []

155. [] advised the Commission that they are presently trialing varieties from several distributors and that competition between the distributors is keen, particularly as the newer 'truss' tomato seeds has been developed.

156. Distributors also noted the keen competition in this market, particularly in respect of the larger growers. They expected that this competition would continue post merger.

Conclusion on Existing Competition

157. The Commission is of the view that competition in the tomato seed distribution market is significant and that this is unlikely to change post acquisition.

158. While the Commission considers that the level of existing competition is likely to constrain the merged entity, in order to assess fully the impact of the acquisition in the relevant markets the Commission has gone on to consider potential competition.

Potential Competition

159. As with capsicums, a new entrant would need to obtain a suitable variety of seed that is either commercially acceptable in New Zealand or at least ready to be trialled with New Zealand growers. However, obtaining an actual supply of suitable tomato seeds appears to be less difficult than for capsicums, as there are more international breeders of these seeds. In addition, there are presently two near entrants, [], to the tomato seed distribution market.

160. [] Both these distributors have credibility in the produce industry and, in the case of Henderson, is supplied by a large global supplier of seed, while Seminis itself is able to supply its own seeds.

Conclusion on Potential Competition

161. The Commission considers that the near entrants Seminis and Henderson would enhance competition in the tomato seed distribution market post acquisition.

Other Competition Factors

Constraint from Buyers

162. Tomato growers presently have a choice of four distributors, post acquisition that would reduce to three. Despite this, growers would still have sufficient choice of distributor. As there are more tomato varieties available than capsicum varieties, tomato growers tend to trial varieties more frequently. As such, the time between switching varieties is likely to be less.
163. Growers such as NZ Hothouse and Status advised that they can and do switch between distributors and that in their opinion that ability would remain if the merger proceeds.

Constraint from Suppliers

164. As was the case for the capsicum seed distribution market, suppliers of tomato seeds are likely to have significant countervailing power post acquisition, particularly as in this market there are distributors independent of the merged entity. Any loss of market share to competitors through raised prices is likely to have the suppliers seeking alternative distributors such as non-tomato seed distributors.

Conclusion on Countervailing Power

165. The Commission is of the view that tomato growers would offer the merged entity a degree of countervailing power. In addition, the Commission considers that the merged entity would be constrained by the countervailing power of its large upstream suppliers.

Conclusion on Competition in the Tomato Seed Distribution Market

166. The Commission has considered the nature and extent of the contemplated lessening of competition in the tomato seed distribution market. The proposed acquisition would result in the merged entity obtaining a market share which falls outside the Commission's safe harbour guidelines.
167. However, the Commission has also considered the nature and extent of the contemplated lessening in the tomato seed distribution market and is satisfied that competitive constraints are likely to exist following the merger from:
- existing competition;
 - the short and long term entry by potential competitors; and
 - the countervailing power of large suppliers and buyers.

The Cucumber Seed Distribution Market

Existing Competitors

168. There are presently five competitors in the cucumber seed distribution market:
- Yates;
 - SPS;
 - Lefroy;
 - Syngenta; and
 - Seminis.

Market Concentration

169. The market shares for the cucumber seed distribution market are as in Table 3 below.

Table 3: Market Shares for the Cucumber Seed Distribution Market 2001-2002 and 2002-2003

Distributor /Supplier	2001-2002 (\$000s)	Market share (%)	2002-2003 (\$000s)	Market share (%)
Yates				
Rijk Zwaan	[]		[]	
De Ruiter	[]		[]	
	[]	[]%	[]	[]%
SPS				
Nickerson Zwaan	[]	[]%	[]	[]%
Syngenta	[]	[]%	[]	[]%
Lefroy	[]	[]%	[]	[]%
Seminis	[]	[]%	[]	[]%
TOTAL	[]	100%	[]	100%

170. Presently, the three firm concentration ratio is []%. Post merger, the combined entity would have []% of the market share and the three firm ratio would be []%. This falls outside the Commission's safe harbour guidelines.

Existing Competition

171. The cucumber seed distribution market is served by five competitors. Lefroy has managed to secure a reasonable share of the cucumber seed distribution market through its distribution of Enza Zaden cucumber seeds. In addition, Syngenta and Seminis, as relative newcomers to the market, have managed to pick up a small amount of market share.
172. NZ Hothouse, a large grower of cucumbers, advised the Commission that it is presently trialing varieties from several distributors and that competition between the distributors is keen.
173. Distributors also noted that competition is healthy in the cucumber seed distribution market particularly in respect of the larger growers. They expected that this competition would be enhanced post merger, as the two new entrants to the market gain market share.

Conclusion on Existing Competition

174. The Commission is of the view that existing competition in the cucumber seed distribution market is significant and that this is unlikely to change post acquisition.
175. While the Commission considers that the level of existing competition is likely to constrain the merged entity, in order to assess fully the impact of the acquisition in the relevant markets the Commission has gone on to consider potential competition.

Potential Competition

176. As with capsicums and tomatoes, a new entrant would need to obtain a suitable variety of seed that is either commercially acceptable in New Zealand or at least ready to be trialled with New Zealand growers. Like tomatoes, obtaining an actual supply of suitable cucumber seeds appears to be less difficult than for capsicums, as there are more international breeders of these seeds. Further, cucumbers are planted three times per season and meaning new varieties may be trialled at a quicker rate than tomatoes or capsicums. Two competitors, Seminis and Syngenta, have recently entered the cucumber seed distribution market.

177. [

] All of these distributors have credibility in the produce industry and are supplied by large global suppliers of seed.

Conclusion on Potential Competition

178. The Commission considers that the near entrant would enhance competition in the cucumber seed distribution market post acquisition.

Other Competition Factors

Constraint from Buyers

179. Cucumber growers presently have a choice of five distributors, post acquisition that would reduce to four. Despite this, growers would still have sufficient choice of distributor, as there are many cucumber varieties available. As the growing cycle of cucumbers is shorter than for capsicums and tomatoes, cucumber growers tend to trial and switch varieties more frequently.

180. NZ Hothouse advised that they can and do switch between distributors and in their opinion that ability would remain if the merger proceeds.

Constraint from Suppliers

181. As was the case for the tomato seed distribution market, suppliers of cucumber seeds are likely to have significant countervailing power post acquisition, particularly as in this market there are distributors independent of the merged entity. Any loss of market share to competitors through raised prices is likely to have the suppliers seeking alternative distributors such as non-cucumber seed distributors.

Conclusion on Countervailing Power

182. The Commission is of the view that cucumber growers would offer the merged entity a degree of countervailing power. In addition, the Commission considers that the merged entity would be constrained by the countervailing power of its large upstream suppliers.

Conclusion on Competition in the Cucumber Seed Distribution Market

183. The Commission has considered the nature and extent of the contemplated lessening of competition in the cucumber seed distribution market. The proposed acquisition would

result in the merged entity obtaining a market share which falls outside the Commission's safe harbour guidelines.

184. However, the Commission has also considered the nature and extent of the contemplated lessening in the cucumber seed distribution market and is satisfied that competitive constraints are likely to exist following the merger from:

- existing competition;
- the short and long term entry by potential competitors; and
- the countervailing power of large suppliers and buyers.

OVERALL CONCLUSION

185. The Commission has considered the probable nature and extent of competition that would exist in the:

- market for the distribution of capsicum seeds to growers of covered crops in New Zealand;
- market for the distribution of tomato seeds to growers of covered crops in New Zealand; and
- market for the distribution of cucumber seeds to growers of covered crops in New Zealand.

186. The Commission considers that the appropriate counterfactual for comparison is the status quo.

187. The Commission has considered the nature and extent of the contemplated lessening of competition. In each of the three markets, the proposed acquisition would result in the merged entity obtaining a market share which falls outside the Commission's safe harbour guidelines.

188. However, the Commission has also considered the nature and extent of the contemplated lessening, in terms of the competitive constraints that would exist following the merger from the:

- countervailing power of large suppliers;
- entry by potential competitors; and
- constraint posed by existing competition.

189. The Commission is satisfied that the proposed acquisition would not have, nor would be likely to have, the effect of substantially lessening competition, in the:

- market for the distribution of capsicum seeds to growers of covered crops in New Zealand;
- market for the distribution of tomato seeds to growers of covered crops in New Zealand; and
- market for the distribution of cucumber seeds to growers of covered crops in New Zealand.

DETERMINATION ON NOTICE OF CLEARANCE

190. Accordingly, pursuant to section 66(3) (a) of the Commerce Act 1986, the Commission determines to give clearance for the proposed acquisition by South Pacific Seeds Pty Limited of the assets and business that comprise the New Zealand vegetable seeds sales division of Yates Limited.

Dated this 25th day of September 2003

Paula Rebstock
Acting Chair