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COMMERCE COMMISSION

Decision No. 512

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

MITEK NEW ZEALAND LIMITED

and

PRYDA NEW ZEALAND AND REID NEW ZEALAND

The Commission: Peter JM Taylor
Denese Bates QC
Donal Curtin

Summary of Application: The acquisition by MiTeK New Zealand ("MiTek") or its related company, MiTek Australia Limited, of the assets and liabilities of Pryda New Zealand ('Pryda") and Reid New Zealand ("Reid"), which are operating divisions of Nylex (New Zealand) Limited.

Determination: Pursuant to section 66(3) (b) of the Commerce Act 1986, the Commission determines to decline the proposed acquisition.

Date of Determination: 13 November 2003

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EXECUTIVE SUMMARY[1]

The Proposal

1. A notice pursuant to section 66(1) of the Commerce Act was received on 6th October 2003. The notice sought clearance for the acquisition by MiTek New Zealand ("MiTek") or its related company, MiTek Australia Limited, of the assets and liabilities of Pryda New Zealand ('Pryda") and Reid New Zealand ("Reid"), which are operating divisions of Nylex (New Zealand) Limited.

Market Definition

2. The Commission has concluded that the relevant markets for this acquisition are as follows:
   - the national supply of general fasteners;
   - the national supply of software-supported connector plates;
   - the national supply of non-software-supported brackets used in prefabricated construction;
   - the national supply of non-software-supported braces used in prefabricated construction;
   - the national supply of truss making machinery; and
   - the national supply of software-supported products for flat roofs and flooring.

Counterfactual

3. [

   ]. The Commission therefore considers that the appropriate counterfactual is the Pryda and Reid businesses being acquired by a party that would not raise competition concerns.

Competition Analysis

General Fasteners

4. In the supply of general fasteners, there is a minor aggregation. Further, there are several existing suppliers of general fasteners, including imports. Consequently, the Commission considers that there is unlikely to be a substantial lessening of competition in the supply of general fasteners.

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[1] This Executive Summary is provided for the assistance of readers of the Commission's determinations. It does not purport to completely encompass all details of the Application,, the Commission's investigation of the facts, the Commission's analysis of those facts, the reasons for the Commission's determinations or the determinations themselves. Readers are referred to the body of the reasons for the Commission's determinations for a complete picture.

Software-supported Connector Plates

5. In the supply of software-supported connector plates, the Commission concludes that compared with the counterfactual where Pryda remains as an effective competitor, the merger would result in a loss of existing competition as it would reduce the number of suppliers from two to one. As the sole supplier, the merged entity would have a 100% market share and could potentially limit the number of software licences available to fabricators, in order to raise prices.

6. The Commission considers that potential entry into the supply of software-supported connector plates is insufficient to provide competition to the merged entity. Barriers to entry are high and it appears that entry from [ ] may be likely and timely but it would be insufficient in extent to prevent the merged entity from raising prices or reducing the quality of product or service. This is because the extent of entry would be affected by the [ ], also there are difficulties in persuading fabricators to switch, as well as a need to gain economies of scale and to provide the same level of guarantee and on-going technical and engineering support as the combined entity.

7. Further, given the limited extent of any likely entry, the large fabricators would have limited countervailing power to prevent the merged entity from raising prices or reducing the quality of product and service supplied.

8. The Commission concludes that the merger is likely to lead to a substantial lessening of competition in the supply of software-supported connector plates. In addition, to the substantial lessening of competition in the supply of software-supporting connector plates, the Commission is concerned that the merged entity would be able to leverage its market power in this market and tie-in sales of other related products, namely braces, brackets and truss making machinery, with sales of software-supported connector plates.

Non-software-supported Brackets and Braces

9. In the supply of non-software-supported brackets, and non-software-supported braces, used in prefabricated construction, the Commission concludes that there would be a loss of existing competition, as the merged entity would become the only supplier. However, the Commission considers that post-acquisition, given that barriers to entry are moderate, there would be scope for potential entry from [ ] which could provide the required "one stop shop" of products, and the large customers of the merged entity are likely to have countervailing power. Consequently, the Commission concludes that the merger is unlikely to lead to a substantial lessening of competition in the supply of non-software-supported brackets and braces used in prefabricated construction.

Truss Making Machinery

10. In the supply of truss making machinery, the Commission considers that there would be sufficient existing competition to prevent a substantial lessening of competition. There are alternative suppliers of jigs, presses, and automated saws that would continue to be purchased from Spida or MangoTech. Further, there is a second-hand market for manual truss-making machinery. In some cases, machinery could be imported, although it may be more expensive and specialised. The Commission considers that there is sufficient existing competition in the supply of truss making machinery, and has therefore not considered the scope for potential competition.

Software-supported Products for Flat Roofs and Flooring

11. The Commission considers that there is unlikely to be a substantial lessening of competition in the supply of software-supported products for flat roofs and flooring, as there would be sufficient competition provided by competing products.

OVERALL CONCLUSION

12. The Commission's view is that the merger is likely to lead to a substantial lessening of competition in the supply of software-supported connector plates due to the lack of existing and potential competition and the lack of countervailing power.
13. Due to sufficient existing competition or potential competition, the merger is unlikely to lead to a substantial lessening of competition in the following markets:
    - the supply of non-software supported brackets used in prefabricated construction;
    - the supply of non-software supported braces used in prefabricated construction;
    - the supply of truss making machinery; and
    - the supply of software-supported products for flat roofs and flooring.
14. The overall conclusion is that pursuant to section 66(3) (b) of the Commerce Act 1986, the Commission determines to decline the proposed acquisition of MiTek or its related company, MiTek Australia Limited, of the assets and liabilities of Pryda and Reid, which are operating divisions of Nylex (New Zealand) Limited.

THE PROPOSAL

15. A notice pursuant to section 66(1) of the Commerce Act was received on 6th October 2003. The notice sought clearance for the acquisition by MiTeK New Zealand ("MiTek") or its related company, MiTek Australia Limited, of the assets and liabilities of Pryda New Zealand ('Pryda") and Reid New Zealand ("Reid"), which are operating divisions of Nylex (New Zealand) Limited.

THE PROCEDURES

16. 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 agreed between the Commission and the Applicant. Accordingly, a decision on the Application was required by 13th November 2003.
17. The Applicant sought confidentiality for specific aspects of the Application. A confidentiality order was made in respect of the information for up to 20 working days from the Commission's determination notice. When that order expires, the provisions of the Official Information Act 1982 will apply.
18. The Commission's approach is based on the principles set out in the Commission's *Practice Note 4*.[2]

THE PARTIES

MiTek

19. MiTek is a US company whose New Zealand offices are located in Auckland and Christchurch
20. In 1963, Automated Building Components New Zealand Ltd (A.B.C.) was formed as a joint venture between Gang-Nail USA and a New Zealand businessman. At this time, the business provided Gang-Nail timber connectors and engineering design services to roof truss fabricators under licence.
21. Over the next 15 years the company was subject to various takeovers, and in 1979, after another such acquisition of its parent company, A.B.C. changed its name to Gang-Nail New Zealand Ltd. In December 2000, Gang-Nail New Zealand Ltd changed its name to MiTek New Zealand Ltd.
22. On 31 July 2001, Berkshire Hathaway Inc. acquired 90% of the shares in MiTek Inc, MiTek's effective parent, with management of MiTek Inc. retaining the remaining 10%. Berkshire Hathaway Inc. is the holding company of various subsidiaries engaged in a number of diverse business activities.

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[2] 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.

23. MiTek manufactures and supplies timber connecting systems. It manufactures and distributes products like connector plates under the Gang Nail brand, and other products like braces and brackets, which are used to join timber to fabricate roofs, floors and walls, under the Lumberlock and Bowmac brands.

Nylex

24. Nylex New Zealand is wholly-owned by an Australian company called Eilloc Pty Limited. Nylex is ultimately owned by Austrim Nylex Limited, which is listed on the Australian Stock Exchange.
25. Ajax Fasteners, Pryda, and Reid are all currently operating as one business and have shared resources under Nylex New Zealand Limited. Ajax sells a range of nuts, bolts, and nails (but not the specialised brackets and braces that are supplied by Pryda or MiTek) to building retail stores such as PlaceMakers and ITM. Ajax Fasteners is not included in this acquisition and will remain a division of Nylex New Zealand Ltd.
26. Nylex is selling the business assets of Pryda and Reid. The Pryda and Reid businesses are operated as one division under common management.

Pryda

27. Pryda manufactures and supplies timber connecting systems to the Australian, New Zealand, Indonesian, Thai, Malaysian and Singaporean building industries. In particular, Pryda supplies integrated systems for the fabrication of roofs, floors and walls, primarily used in domestic house and light timber-framed buildings. Its principal customers are roof, floor and wall frame fabricators. Other customers include retail hardware merchants, timber merchants and timber millers, pallet manufacturers and other users of timber.
28. Pryda also supplies the software that fabricators require to design and construct roofs, floors and walls. Fabricators are licensed to use the Pryda intellectual property. The software provides fabricators with detailing and marking information for cutting timber sections, which can be downloaded to saws and assembly equipment.

Reid

29. Reid manufactures and supplies concrete fastener and concrete lifting systems to the Australian and New Zealand building industries. Concrete lifting systems represent less than [ ] of the combined Pryda and Reid business in New Zealand. Reid also markets and sells construction systems, masonry fastening and handling products for the building and construction industry.
30. Reid specialises in concrete connecting and reinforcement, anchoring, fastening and fixing technologies, in addition to the design of precast concrete and tilt-up lifting systems, primarily used in commercial build construction (predominantly factory and warehouse construction, but also in flats and apartments). Of these products, the sale of concrete fastener systems is the most significant for the business.
31. Reid sells products directly to "precasters" and commercial building companies, such as Firth Industries, Humes Industries, and the Fletcher Group.

OTHER RELEVANT PARTIES

Multinail Australia Pty Limited ("Multinail")

32. Multinail is based in Australia and manufactures and supplies timber connecting systems to the Australian building industry. It is the third largest supplier in Australia (behind MiTek and Pryda). Like MiTek and Pryda it supplies integrated systems for the fabrication of roofs, floors and walls, primarily used in domestic house and light timber framed buildings. Its principal customers are roof, floor and wall frame fabricators in Australia. Multinail also supplies the software that fabricators require to design and construct roof trusses, floor trusses and wall frames.

33. Multinail is also a [ ].

ITW New Zealand Limited ("ITWNZ")

34. ITWNZ trades as Ramset New Zealand ("Ramset"). For the purposes of this Report Ramset means the legal entity ITWNZ. Ramset is ultimately owned by Illinois Tools Works Inc, a company listed on the New York Stock Exchange, and is part of the ITW Group.

35. Ramset provides products and services in the New Zealand concrete industry, and in particular provides concrete fastener systems and concrete lifting systems. Ramset also provides general construction products, such as plaster board and cavity fasteners, power tools and accessories, diamond drilling and cutting products, construction chemicals, and metal and timber fastening products.

36. Ramset is the largest supplier of fasteners for securing steel and timber components to concrete. Ramset operates a national network of 17 branches and sells stock in over 1,000 retail hardware outlets.

37. Ramset is also [ ].

Carter Holt Harvey Limited ("CHH")

38. CHH is Australasia's leading forest products company, and one of the largest forest products companies in the Southern hemisphere. Its forest holdings throughout New Zealand exceed 330,000 hectares. CHH's wood products include sawn timber, medium density fibreboard, Laminated Veneer Lumber ("LVL"), and plywood. It is also New Zealand's largest manufacturer and recycler of pulp and paper. CHH comprises 25 businesses spread over 150 sites.

39. Of relevance to this acquisition is:

- CHH's manufacture of LVL Beams, which are used in the building industry as one way of constructing prefabricated floors and flat and sloping roofs; and
- A CHH division, Carters, has 37 builders' retail outlets throughout New Zealand. Of these, 17 provide prefabricated roof trusses and floors from fabricator plants attached to the store.

Truswal Systems Corporation Inc ("Truswal")

40. Truswal is based in the United States and manufactures and supplies timber connecting systems to the North American building industry and have been in business for around 35 years. In particular, Truswal supplies integrated systems for the fabrication of roof trusses, floor trusses and wall frames, primarily used in domestic house and light timber-framed buildings. Truswal's brands include SpaceJoist, SpaceJoist TE and BRACE-IT. Truswal also supplies the North American building industry with a full line of manufacturing and production equipment.

Robbins Engineering Inc ("Robbins")

41. Robbins is based in the United States and is a family owned company, which began in 1938. Robbins started as a lumber products supplier in the south-eastern United States. In 1975, Robbins expanded into the metal connector plate business, and commenced supplying wood truss manufacturers with connector plates, software and engineering support.

42. Robbins offers a full range of services and products for truss fabrication, as follows:

- truss plate manufacturing;
- complete line of truss manufacturing and material handling equipment;
- Windows® Truss Design Software (OnLine PlusTM);
- Windows® Plant Management Software (InfoStarTM); and
- licensed professional engineering services.

Dunnings Engineering Services Pty Limited ("Dunnings")

43. Dunnings is an Australian company founded in the early 1950's that operates its own fully equipped sheetmetal, cutting, folding and pressing facility supported by a complete range of metal finishing processes. Dunnings also manufactures a range of builders and plumbers hardware products which it distributes to builders retail stores such as Bunnings in South Australia.

Abey Australia Pty Limited ("Abey")

44. Abey was also founded in Australia in the early 1950's and manufactures around 1,200 products including plumbing, masonry, as well as a vast range of general builders' hardware products. Abey markets and distributes these products to large builders' retail stores throughout Australia including Bunnings and Mitre 10.

Frame & Truss Manufacturers Association of New Zealand ("FTMA")

45. The FTMA is an independent industry association that represents wall and roof truss manufacturers. Its members consist of industry participants like suppliers, professionals, group builders, specifiers and certifiers. In total, the FTMA's members consist of 35 fabricators. The FTMA was formed to raise the quality and standards in the frame and

truss industry, and to ensure prefabricated timber roofs and walls remain the preferred building material choice.

INDUSTRY BACKGROUND

Concrete-Lifting Systems

46. In this acquisition, MiTek proposes to acquire both Pryda and Reid. MiTek does not operate a concrete-lifting systems business, thus, the proposed acquisition will only result in aggregation in timber connecting systems, in which, MiTek and Pryda operate. As there will be no aggregation between the operations of MiTek and Reid the concrete-lifting systems market will not be considered further.

Timber Connecting Systems

47. In New Zealand there are two primary methods of constructing residential or small commercial buildings. They are conventional construction which involves the builder constructing roofs, walls and floors "on site", and prefabricated construction, which involves making the roof, walls and floors "off-site".

48. Approximately 90% of new houses, in New Zealand, are built each year using prefabricated roofs, walls and floors. The remaining 10% of new houses are built using conventional construction.

49. Prefabricated roofs, floors and walls can be made from timber or steel. In New Zealand timber prefabrication tends to be used for building residential houses. Steel prefabrication tends to be used in commercial and industrial buildings in order to achieve large spans, and to comply with fire resistance requirements.

50. Of the 90% of prefabrication construction carried out in New Zealand, approximately 3% uses light weight gauge steel, and the remaining 87% uses timber.

51. Prefabricated timber roofs, floors and walls are triangular or rectangular in shape. Trusses comprise wooden chords, which are joined to form the basic shape and webs, which are shorter lengths of timber interior to the frame that join and support the chords.

52. In this acquisition, there is an aggregation in the manufacture and distribution of building components that are used in the construction of timber prefabricated roofs, floors and walls. These building components are:

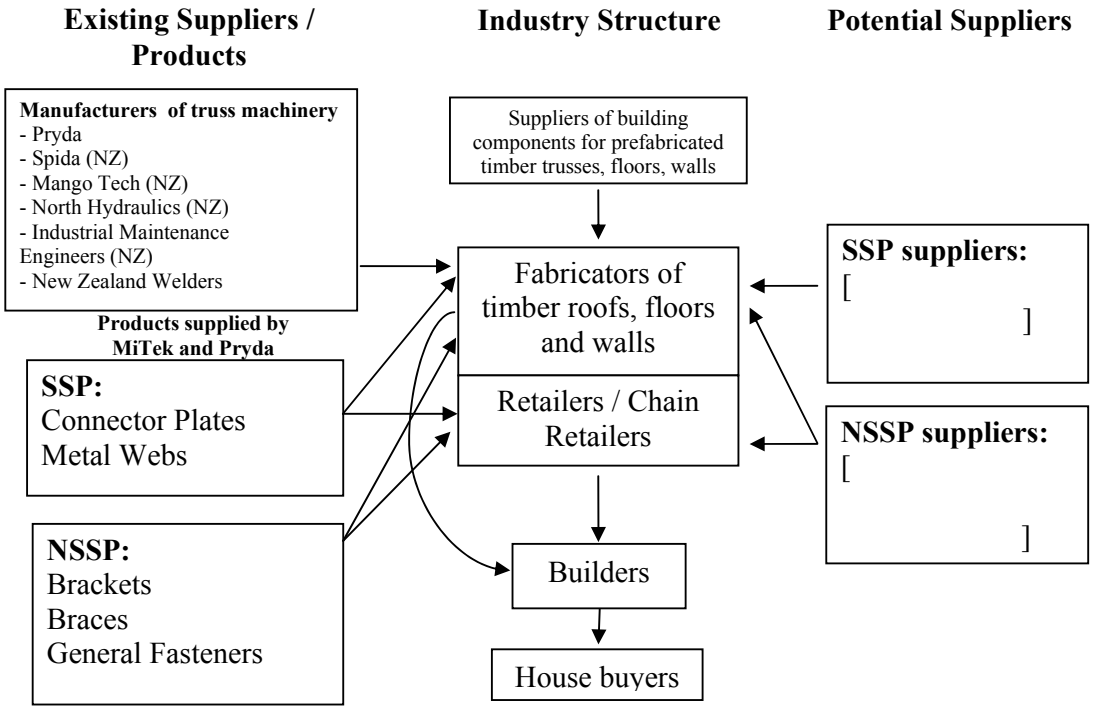
    - truss making machinery;
    - software-supported builders' hardware products; and
    - non-software-supported builders' hardware products.

53. Further details about the products, suppliers and customers are set out below.

54. The suppliers and customers of the building components used in the prefabrication of timber roofs, floors and walls are shown in the diagram below. The main suppliers of building components used in the prefabrication of timber roofs, floors and walls are MiTek and Pryda. Their customers are fabricators who purchase the building components to make timber roofs, floors and walls. The main fabricators in New Zealand are Carters

and PlaceMakers. The prefabricated timber roofs, floors and walls are then sold to builders, whose ultimate customers are the house buyers.

Diagram 1: Prefabricated Timber Construction Industry



Key: SSP: Software-supported products
NSSP: Non-software-supported products

Truss Making Machinery

55. In order to build prefabricated timber roofs, floors, and walls, various types of machinery are used, namely presses, jigs, saws, material-handling equipment, laser projection equipment, lathes, milling machines, automated tables, mitres and mitre pins, nailing and stapling equipment, fans, and blowers.

56. In this acquisition, there would be an aggregation in the supply of presses and jigs that are used for making roof trusses. Saws are used to cut the timber into shape. The timber pieces are then held together by jigs, while connector plates on both sides of the timber are firmly pressed at the joints using presses.

57. Saw, jigs and presses can be automated through computer-aided software. Manually operated machinery can also be used. In New Zealand most fabricators use automated saws, and manually-operated jigs and presses.

58. The main manufacturers of manually operated jigs are Pryda, and New Zealand Welders in Auckland, who supply MiTek, who then on sells the jigs to its customers.

59. The main manufacturers of manually operated presses are Pryda, North Hydraulics and Industrial Maintenance Engineers. These companies supply presses to MiTek, who then on sells them to its fabricators.

60. There are two major suppliers of automated saws in New Zealand, namely Spida, and Mango Tech. Spida and Mango Tech are global players who supply large, medium, and small size fabricators in New Zealand. Both companies also supply MiTek and Pryda, who then resell the machinery on to their customers. [

    ].

61. In this acquisition there is a vertical aggregation in the supply of truss-making machinery as Pryda manufactures and distributes jigs and presses, while MiTek acts a distributor of the machinery to end customers.

Builders' Hardware Products

62. Builders' hardware products used in the construction of prefabricated timber roofs, floors and walls, consists of products that are generally manufactured from pressed steel. These include a wide range of fasteners, brackets and braces, lintels, spacers, springs, hooks and hinges.

63. In this acquisition both MiTek and Pryda supply:

    - general fasteners;
    - connector plates fasteners;
    - braces;
    - brackets; and
    - metal webs.

64. In this acquisition, general fasteners are considered to be nails, bolts and screws that can be used in various ways.

65. Connector plates are punched metal fasteners used to fasten joints in prefabricated timber roof trusses. They are made from strips of mild steel that have been protected against corrosion by hot-dip galvanised zinc coating. The small plates have integral teeth on one side. The product was developed in the 1960s, when it was known as the Gang-Nail connector plate. The connector plates were originally patented in the US, and introduced into New Zealand by Gang-Nail New Zealand Ltd (a predecessor of MiTek).

66. Brackets are metal products that connect or support structural members in buildings. There are a wide variety of brackets that can be used. The main types of brackets affected in this merger are hangers (I-beam hangers and joist hangers), which are U-shaped brackets used to connect joists to the adjoining headers or support beams. They are used when joists have to be butted up to support beams or headers rather than resting on top. Other types of brackets are angle brackets that are used to connect timber to form corners and brackets used to connect timber to concrete, namely post brackets.

67. Braces are pressed metal components that are used to prevent distortion or buckling of a frame or truss. The main types of braces that are affected in this acquisition are angle braces that are used in walls, and strip braces that are used in roofs.

68. Metal webs are used in prefabricated floors and sometimes in roof rafter applications. They are V-shaped components with punched teeth as an integral part of the web.

Software-supported Builders' Hardware Products

69. A number of builders' hardware products are software-supported, where software provides a system for the use of the products and other materials necessary for the construction of various building components. These software systems enable fabricators to design and detail building components, such as timber roofs, floor, walls, beams, columns and lintels that incorporate these builders' hardware products.

70. Software-supported builders' hardware products are:

- connector plates;
- metal webs;
- laminated veneer lumber ("LVL"); and
- I-Beams.

71. LVL is an engineered wood product created by layering dried and graded wood veneers with waterproof adhesive into blocks of material known as billets, and cured in a heated press. LVL is typically available in various thicknesses and widths, and is easily worked in the field using conventional construction tools. LVL is a solid, highly predictable and uniform engineered wood product that is sawn to consistent sizes and is virtually free from warping and splitting. LVLs are used in prefabricated floors and to a lesser extent in prefabricated roofs.

72. I-beams joists are engineered timber sections. They are made of two flanges that are joined by a web and look like an "I" in their cross section. The structure of an I-beam makes it very resistant to heavy loads and buckling. The web is generally made of plywood. The flanges can be made of different types of wood, including LVL (in which case the beams are called "LVL I-beams"). Like LVLs, I-beams are used in prefabricated floors and to a limited extent in prefabricated roofs.

73. In New Zealand the supporting software tends to be bundled with the related builders' hardware products. For instance, fabricators use MiTek and Pryda software with the associated connector plates. The software uses certain engineering properties for a particular type of connector. The software is also linked to automated saws which are used to make trusses. See paragraph 60.

74. Currently, most customers are required to pay MiTek or Pryda albeit a moderate licence fee in order to use their software. The annual licence fee is $350 for the first module, $250 for the second and $100 thereafter. [

].

75. Software-supported products account for [

].

76. MiTek supplies the following software products:

- MiTek 20/20 software -which is used to design roofs, floors and walls. It contains three modules;
  - a layout module- data on the roofs, floors or walls is inputted;

- an engineering module - software calculates the optimal design of the roofs, floors and walls; and
- a detailing module - software specifies the details of every truss in a building, including the number of trusses required, their individual sizes and specifications (including the angle of every cut made by an automated saw), and the number, size and positioning of connector plates.

- MiTek's Matrix Webs - which replace traditional wooden webs in the centre of a truss with tabular steel;
- Posi-STRUTS – used for metal web flooring; and
- GN Lintels - lintels constructed with large connector plates and timber to form beams to carry loads over openings such as doors and windows.

77. Pryda supplies software-supported products under the name "Pryda Solutions" which include the following software components:
    - Pryda Roof - used for roof truss design, estimating, detailing, costing, production and management;
    - Pryda Quote - used in conjunction with Pryda Roof and allows the production of quotes;
    - Pryda Wall - provides detailing and marking information for wall frames; and
    - Pryda Floor - designs floor trusses.
78. Both MiTek and Pryda provide on-going technical and engineering support to their customers. There is no charge for this support.

Customers

79. As shown in Diagram 1 above, software-supported products like connector plates and metal webs, and non-software supported products such as brackets and braces are, supplied to fabricators and builders merchants.
80. Fabricators design and construct prefabricated roofs, floors and walls using the building components sold by the manufacturer, and the software supplied in conjunction with the products. Fabricators sell assembled building components (roofs, floors and walls) to builders. Fabrication factories are not commonly operated as a stand-alone business; instead, they tend to be an "add-on" to a business selling a full range of builders' hardware products. There are approximately 150 fabricator factories in New Zealand. The two largest fabricators are Carters and PlaceMakers.
81. Builders' merchant stores (such as Bunnings, Mitre 10, PlaceMakers and Carters) are supplied with various builders' hardware product lines such as brackets, braces and general fasteners, to service builders as well as "Do-it-Yourself" consumers. No software is supplied to builders' merchant stores for re-supply (although certain builders' hardware stores themselves operate fabricator factories, and thus acquire software in such capacity). Builders' merchant stores on-sell other products to builders, building owners and end-users.
82. The builder almost invariably makes the final decision as to whether prefabricated or conventional construction will be used.

83. MiTek currently supplies [ ] fabricators in New Zealand, while Pryda supplies [ ]. [ ].

84. There are typically no formal supply agreements between a fabricator and its supplier. [ ]. MiTek advised the Commission that this was [ ].

Conduct

85. The cost of connector plates for prefabricated roof trusses represents a small part of the overall cost of constructing a house. MiTek estimated that $230 worth of connector plates are used to build a $120,000 new house of 150m^2.

86. The average cost of manufacturing a timber roof truss of 7-8 metre span, ranges from $120-$180. The production costs of a roof truss may be broken down as follows:

- 10% connector plates;
- 40% timber;
- 40% labour; and
- 10% margin.

87. Both MiTek and Pryda provide [ ]:

[ ]

88. In addition, Pryda offer [ ].

89. Past price increases in MiTek's products have been [ ].

90. In the supply of software-supported hardware products, the Commission found that in the event of failures, fabricators valued the guarantee, and back-up support provided by MiTek and Pryda. [ ].

91. [ ].

92. Further MiTek and Pryda both state that they would [ ].

Regulatory Environment

93. New Zealand does not have "building regulations" that list exact measurements that must be adhered to by builders. Rather, New Zealand has performance based regulations. This

means that MiTek, Pryda or any new entrant must convince a local authority that its roof truss design and connector plates meet the authorities desired requirements.

94. The Commission understands that approval can be achieved from local authorities in the following ways:

- utilise compliance documents from the Building Industry Association such as "Code 3604" which is used by most local authorities as the standard for connector plates and roof trusses;
- obtain an independent engineer's advice and report; or
- obtain certification from BRANZ.

95. The Commission understands that most local authorities accept connector plates and roof trusses that adhere to what is termed in the industry "Code 3604".

PREVIOUS DECISIONS

Australian Competition and Consumers Commission ("ACCC")

96. The ACCC also investigated the acquisition of Pryda and Reid by MiTek[3]. In Australia there are currently three providers of building components for prefabricated roof trusses, walls and frames: MiTek, Pryda and Multinail, so, in Australia this merger would reduce the number of suppliers from three to two. In Australia, the combined entity would have a market share of around 85-90%.

97. [ ].

New Zealand Commerce Commission ("Commission")

98. The Commission has very recently considered related activities in the clearance decision involving ITWNZ's proposed acquisition of Pryda and Reid [4]("the ITW/Pryda Reid Decision").

99. In the ITW/ Pryda Reid Decision, the Commission defined three separate markets:

- the national market for the supply of general fasteners;
- the national market for the supply of concrete fastener systems; and
- the national market for the supply of concrete-lifting systems.

100. The products provided by Pryda were not considered in detail in this decision as the aggregation with ITW occurred primarily with the business activities of Reid. Of relevance to this Application is the market for the provision of general fasteners. In this market, the Commission was satisfied that the proposed acquisition would not have, nor would be likely to have, the effect of substantially lessening competition, as there is sufficient competition provided by existing and potential competitors.

[3] On 14th November, the ACCC opposed the acquisition.
[4] Commerce Commission, Decision No. 510 *ITW New Zealand Limited and Pryda and Reid, divisions of Nylex (New Zealand) Limited*

Other Cases

101. In 1988, the UK Monopolies and Mergers Commission ("MMC" now known as the Competition Commission) investigated the merger between MiTek Industries Inc and Gang-Nail Systems Inc. In this merger, MiTek would have acquired Gang Nail systems and Hydro-Air. However, the MMC concluded that the merger may be expected to operate against the public interest, and recommended that MiTek should divest itself of Gang Nail Systems Ltd.

102. The MMC considered the market for the supply of punched metal connector plates and related machinery. The merged entity would have had a combined market share of 76%. Existing competition was considered to be strong pre-merger, and potential competition post-merger was found to be unlikely to compensate for the loss of competition between Hydro-Air and Gang Nail. The MMC concluded that the choice of available fabrication systems, the incentive to maintain the development of products and services, price, and standards of service, all depended on healthy and active competition, and this was not expected to survive post-merger.

103. In Australia, the Supreme Court of Queensland dealt with a contractual dispute between Multinail and Pryda in 2002. In court, Multinail successfully claimed that Pryda unlawfully induced a significant Multinail customer to switch their building hardware products and associated software to Pryda.

104. In the Multinail case, there is some discussion on the nature of the contracts between building hardware manufacturers and their customers. However, the nature of the contracts discussed, are somewhat unclear as the customer in question was in receivership. The contract for the supply of building hardware and software was, hence, with the receiver, and it is therefore unlikely that the contract is representative of those in the industry.

MARKET DEFINITION

105. 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*.

106. 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.

107. 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).

108. 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 Market

109. 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.

110. The Commission takes the view that the appropriate time period for assessing substitution possibilities is the longer term, but within the foreseeable future.[5] 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.

111. The Applicant submitted the following product markets:

- the software-supported builders' hardware products market;
- the builders' hardware products market; and
- the building components machinery market ("Truss Making Machinery").

112. The Applicant contends that this is a conservative approach, and such markets are defined due to both demand-side and supply-side substitutability.

113. The Commission has considered the demand-side and supply-side factors in each of the markets described above. These factors are explored in further detail below.

Demand-side Substitutability

114. Close substitute products on the demand-side are those between which at least a significant proportion of buyers would switch when given an incentive to do so by a small change in their relative prices.

General Fasteners

115. In the ITW/Pryda and Reid Decision[6], the Commission defined a market for the supply of general fasteners. In this acquisition the same market is considered appropriate.

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[5] In *Tru Tone Ltd v Festival Records Retail Marketing Ltd* [ ] 2 NZLR 351 Smellie J and the Court of Appeal on appeal approvingly quoted an earlier decision of the Commerce Commission in *Edmonds Food Ind Ltd v W F Tucker & Co Ltd* (Decision 21, June 1984) where the Commission had ruled: "A market has been defined as a field of actual or potential transactions between buyers and sellers amongst whom there can be strong substitution, at least in the long run, if given a sufficient price incentive".

[6] Decision No. 510

Connector Plates

116. In New Zealand, connector plates and software are supplied to fabricators on a bundled basis. Fabricators are generally charged a set amount per unit for connector plates, and are charged a nominal licence fee for use and on-going technical and engineering support of the supporting software. Due to the complementary nature of the products, the Commission considers that connector plates and the supporting software should be considered to be elements of the same market.

117. The Commission considers that there is very limited demand-side substitutability between connector plates and other fasteners. Other types of general fasteners, such as nails and screws, can be used in place of connector plates, but they are more time consuming and expensive to use as more labour is involved (nails and screws are rarely used in the making of roof trusses). Therefore due to the engineering involved and specialisation in the connector plate market other fasteners are not an economic alternative.

Non-software-supported Builders' Hardware Products

118. The Commission has spoken to a number of fabricators representing approximately 50%-60% of the industry with regard to the extent of demand substitutability among the different groups of builders' hardware products (e.g. brackets and braces), and within each group of builders' hardware products (e.g. different types of braces). It appears that brackets and braces are not demand-side substitutes as they perform a different function. Also, within the groups of brackets and braces, there are a wide range of products.

119. While it may be possible to define separate product markets for the different types of brackets, the Commission considers that the competition effects of the proposed acquisition are sufficiently captured by an assessment based on aggregating products within the market for brackets.

120. Similarly, the Commission considers that the competition effects of the proposed acquisition are sufficiently captured by an assessment based on aggregating the different types of braces within one product market.

121. Therefore, the Commission considers there to be separate product markets for the supply of brackets and braces.

Truss Making Machinery

122. In New Zealand, truss making machinery is generally not bundled with software and connector plates as it is in other countries. Most New Zealand fabricators own their own truss making machinery, and it appears that, in general, both MiTek and Pryda have been willing to adapt their software to the fabricator's machinery. Thus, truss making machinery can be considered to fall into a separate market to software and connector plates.

123. Traditional ways of fabricating trusses (e.g. placing connector plates manually with a hammer) can be used instead of using truss-making machinery. Also, nails and screws can be used instead of connector plates and they don't require any specialised machinery. While being substitute methods to using machinery, these alternatives are not considered economic and do not provide the level of safety and engineering design that machinery provides.

124. The Commission found that builders almost never make trusses themselves and do not have the experience to make them, the reason being that it is too time-consuming and expensive, even for houses that are relatively simple to build. If a fabricator uses manually-driven machinery, the main substitute is upgrading to an automated system. Most plants above a certain size in New Zealand are likely to be automated in the future.

Metal Webs

125. MiTek and Pryda software can support both metal web design as well as roof truss design. However, in the case of MiTek, users generally only lease the software licence they need for the type of work they specialise in.

126. Metal webs are different products to connector plates. The differ in shape and use, as connector plates tend to be rectangular and are used in prefabricated roofs while metal webs are V-shaped and tend to be in used in flooring and to some extent in roofs.

127. There are two substitutes for metal webs:

- I-Beams; and
- timber webs.

128. With regards to prefabricated floors, timber webs are considered to be a close substitute for metal webs and fabricators use them occasionally. I-Beams are also used as a substitute for metal webs in prefabricated floors, although I-Beams do not allow the passage of air and cables as easily. [

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129. With regards to roofing, there are mainly three types of roofs:

- trussed roofs;
- conventional pitched roofs (which also encompasses cathedral-type roofs); and
- flat roofs.

130. Prefabricated timber trusses (using connector-plates) are used in trussed roofs. Timber rafters, LVL and I-beams are used in conventional and flat roofs. Timber and metal webs can be used in flat roofs. Conventional pitched roofs and flat roofs represent less than 10% of the residential housing market.

131. The Commission found timber webs and I-beams to be substitutes for metal webs, as these products have already gained a large part of the flooring market. However, LVL and I-beams are not considered as substitutes for timber trusses, as roofs that use prefabricated timber trusses represent more than 90% of residential housing and are not substitutes for conventional or flat roofs.

Supply-Side Substitutability

132. Close substitute products on the supply-side are those between which suppliers can easily shift production, using largely unchanged production facilities and little or no additional investment in sunk costs, when they are given a profit incentive to do so by a small change in their relative prices

Software-supported Connector Plates

133. The software-supported systems provided by MiTek and Pryda are primarily dedicated to the production of roof truss design using connector plates, as well as metal webs and wall frames designs. This means that only dedicated software could be used in replacement.

134. It is possible to use multi-purpose software, such as ArchiCAD to support the production of roof trusses, metal webs and frames. However, it would require an important adaptation of the software and thus could not be done in a short time and at low cost. Thus, the Commission considers there is limited supply-side substitutability for software.

135. Connector plates are reasonably easy to produce at low capital cost. However, connector plates purchased from MiTek and Pryda are not compatible with other software for engineering and safety reasons[7]. Thus, the bundling of software and connector plates currently limits the supply-side substitutability that could exist in the supply of connector plates.

Metal Webs

136. Metal webs are more complex to engineer and make than connector plates. This means that the price of a die that makes metal webs is more expensive than that of a die for connector plates. Both MiTek and Pryda import metal webs from Australia.

137. The Commission, therefore, considers that in the supply of metal webs there is limited supply-side substitutability with other products (such as connector plates) because the dies used to produce them are more expensive and complex to engineer.

Non-software-supported Builders' Hardware Products

138. Supply-side substitutability exists among and within the different non-software-supported hardware product groups (e.g. brackets and braces). For instance, the same press can be used to make various types of brackets and braces. It is only a matter of changing the die. The more complex the final product, the more expensive the die will be. The cost of a die will generally vary between $15,000 and $60,000 depending on the complexity of the final product. For example, connector plates are more complex than a post bracket and thus it will cost more to make a die to produce connector plates.

139. Industry participants submitted to the Commission that because of competition in the builders' hardware market a supplier needs to provide a whole range of products in its offer of non-software-supported hardware products, and the cost of producing a whole range is high (for example, there can be up to 40 different types of brackets and braces). As the cost of this is high, the Commission considers that it would not be easy for suppliers of one type of product to switch to offering the whole product range.

140. The Commission considers there to be some degree of supply-side substitutability in the supply of non-software-supported brackets and braces.

Conclusion on Product Market

141. While some supply-side substitutability exists in some of the product markets submitted by the Applicant, due to limited demand-side substitutability, the Commission has

[7] See paragraph 221-224 for further analysis on this point.

decided to adopt narrow product markets for the purposes of analysing this proposed acquisition. These product markets are:

- the supply of general fasteners;
- the supply of software-supported connector plates;
- the supply of non-software-supported brackets used in the prefabricated construction;
- the supply of non-software-supported braces used in prefabrication construction;
- the supply of truss making machinery; and
- the supply of software supported products for flat roofs and flooring.

Functional Market

142. 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.[8] 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.

143. Diagram 1 provides an indication of the functional levels involved in the manufacture and distribution of prefabricated roof trusses, floors and walls.

144. MiTek and Pryda directly sell software-supported products to fabricators. They also sell non-software supported products to retailers. Some fabricators are part of retail chain businesses (e.g. PlaceMakers) and thus sell timber roofs, floors and walls, as well as builders' hardware products.

145. In the supply of software-supported connector plates and in the supply of non-software-supported brackets and braces, MiTek's activity stems across manufacture and distribution and therefore cannot be limited to one specific functional level. The Commission considers the appropriate approach is to consider manufacture and distribution as the "supply" of software-supported connector plates.

146. In the supply of truss making machinery, Pryda manufactures and distributes jigs and presses, while MiTek only distributes the machinery. Therefore separate functional levels could be defined for the manufacture and distribution of truss making machinery.

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[8] *Telecom Corporation of New Zealand Ltd v Commerce Commission* (1991) 4 TCLR 473, 502 The High Court (Greig J, Shaw WJ, Prof M Brunt) noted: "If we ask what functional divisions are appropriate in any market definition exercise, the answer, …, must be whatever will best expose the play of market forces, actual and potential, upon buyers and sellers. Wherever successive stages of production and distribution can be co-ordinated by market transactions, there is no difficulty: there will be a series of markets linking actual and potential buyers and sellers at each stage. And again, where pronounced efficiencies of vertical integration dictate that successive stages of production and distribution must be co-ordinated by internal managerial processes, there can be no market."

Geographic Market

147. 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.

148. The Applicant submitted arguments that the relevant geographical dimension is the whole of New Zealand.

149. The Commission notes that the two major groups of fabricators supplied by MiTek, [ ] have national distribution networks and MiTek supplies to all other fabricators and retailers on a national basis. Pryda also supplies it products on a national basis.

150. Accordingly the Commission considers the appropriate geographic market to be national.

Conclusion on Relevant Market

151. The Commission is of the view that the market definition submitted by the Applicant is too broad. After considering supply-side and demand-side substitutability for all the products supplied by the merging parties, the Commission has identified the following markets products as being relevant to the competition analysis for this proposed acquisition.

- the national supply of general fasteners;
- the national supply of software-supported connector plates;
- the national supply of non-software-supported brackets used in prefabricated construction;
- the national supply of non-software-supported braces used in prefabricated construction;
- the national distribution of truss making machinery; and
- the national supply of software-supported products for flat roofs and flooring.

FACTUAL

152. 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.

153. In the factual scenario, there would continue to be several suppliers of general fasteners. In the distribution of truss making machinery, there would be two suppliers of jigs and

presses including the combined entity, and two suppliers of automated saws Spida and Mango Tech, as well as overseas suppliers and a second hand market.

154. However, the combined entity would be the only supplier of software-supported connector plates, non-software-supported brackets used in prefabricated construction, and non-software-supported braces used in prefabricated construction in New Zealand.

155. MiTek informed the Commission that the merger would provide MiTek with the opportunity to expand into the concrete fastening business (by way of the Reid business). This is an area in which MiTek has no presence currently. [

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COUNTERFACTUAL

156. [

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157. [

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158. However, there is no indication that Pryda and Reid could not continue to operate as divisions of Nylex if the acquisition did not go ahead.

159. The Commission therefore considers that the appropriate counterfactual is that the Pryda and Reid businesses will be acquired by a party that does not raise competition concerns.

COMPETITION ANALYSIS

160. Having defined the counterfactual, the Commission will assess the following for each of the relevant markets[9]:

- 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.

161. 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

[9] 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.

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.[10]

162. In this merger, market shares are measured by sales and/or by volume.

163. 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'.

164. 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%.

165. 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.

166. These factors, along with market concentration, are considered in subsequent sections for each of the relevant markets.

167. 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"), in any market by comparing the expected competition in the factual and counterfactual.

168. Section 2(1A) 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 that:

> "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."

169. 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.[11] Overall, the Commission considers that substantially lessening competition concerns a

[10] See the Commission's Practice Note 4 for further explanation of the Commission's approach to analysing market shares.

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

real or substantial impact on a market in a way of a lessening, hindering and preventing the process of workable and effective competition.

General Fasteners

170. The Commission notes that there is likely to be only a small aggregation in the supply of general fasteners. Further, the Commission has spoken to industry participants who have stated that, post-acquisition, they would have little or no concerns with such aggregation due to the large number of existing suppliers currently supplying the domestic market and the ease by which general fasteners could be imported.

171. Alternative domestic suppliers of general fasteners, include ITW Buildex, NZ Nail, MSL Fasteners, EDL Fasteners, Mico Fasteners, Fastening Supplies, Arrow and Hurricane

172. Consequently, the Commission considers that there is unlikely to be a substantial lessening of competition in the supply of general fasteners. Therefore, this aggregation is not considered further.

Software-supported Connector Plates

Existing Competition

173. At present, MiTek and Pryda are the only suppliers of software-supported connector plates in NZ and post-acquisition the combined entity would have a market share of 100%. Tables 2 and 3 show that regardless of whether market shares are measured by volume or by value, MiTek currently has a market share of [ ] whilst Pryda has a market share of [ ]. Table 3 also shows that MiTek has been [
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Table 2: Market Shares in Supply of Software-supported Connector Plates by Tonnage in 2002

Company	Tonnes Per Annum	Market Share %
MiTek	[ ]	[ ]
Pryda	[ ]	[ ]
Total	[ ]	[ ]
Merged Entity	**[ ]**	**[ ]**

Source: MiTek estimates

Table 3: Market Shares for the Supply of Software-supported Connector Plates by Value During 2001-2003

	Forecast 2003		2002		2001	
	Total Sales $	**%**	**Total Sales $**	**%**	**Total Sales $**	**%**
MiTek	[ ]	[ ]	[ ]	[ ]	[ ]	[ ]
Pryda	[ ]	[ ]	[ ]	[ ]	[ ]	[ ]
Total	**[ ]**	**[ ]**	**[ ]**	**[ ]**	**[ ]**	**[ ]**

Note: Total sales of connector plates includes revenue from software leases and design fees.
Source: Commerce Commission estimates.

174. In the supply of software-supported connector plates, MiTek is currently [ ] and most fabricators considered MiTek to be the market leader that particularly focused on quality of service, while Pryda focussed on price.

175. However, the Commission found that MiTek and Pryda actively compete for customers. Both companies compete on price, quality of service, product innovation and product range.

176. The Commission found that most fabricators were either customers of MiTek or customers of Pryda. Very few fabricators sourced from both suppliers. Examples of fabricators that sourced from both are [ ].

177. [ ] has twenty-one fabricators, [ ] of which are MiTek customers and [ ] are Pryda customers. [ ] stated that its members were free to choose a supplier, and that choice of suppliers was often driven by ownership changes.

178. [

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Switching

179. The Commission found that the level of fabricators switching between MiTek and Pryda was around 3-4% per annum over the last ten years. Further, [

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180. This suggests that there is a low level of switching. The level of switching will be influenced by the costs of switching and the benefits fabricators receive from switching. The reasons for the existence of switching costs that may limit the number of fabricators changing suppliers are considered in further detail below.

181. In the supply of software-supported connector plates, the Commission found that there are costs associated with switching from one supplier to another. The main switching costs for fabricators are the following:

- re-training staff to use the new software;
- loss of production;
- inconvenience of switching; and
- risk of the transition phase not going smoothly.

182. Other countries have also experienced low levels of switching in this market. In the United States, [ ] said that there was a low level of fabricators switching between suppliers because customers who utilise a supplier's software become "captive' for a period of time, and that "it is not easy, and there is not a lot of flipping".

183. In the merger between MiTek Industries Inc and Gang-Nail Systems Inc, the UK Monopolies & Mergers Commission stated [12]:

> Most fabricators use only one of the available fabrication systems, and it is not easy in practice to change from one system to another. Relations between the

[12] MiTek Industries Inc and Gang Nail Systems Inc, Monopolies and Mergers Commission report, July 1988 p36 para 6.11

> truss fabricators and the plate manufacturers are close and our questionnaire survey indicated a high degree of satisfaction with the products supplied and loyalty to their existing suppliers.

184. Similarly, in a recent Australian case, Chesterman J commented on the reluctance of customers to switch suppliers of building hardware products that were bundled with software. Chesterman J stated[13]:

> For practical purposes a fabricator who bought nail plates from one manufacturer must utilise that manufacturer's computer design software. Principally for this reason fabricators tend to remain customers of one manufacturer for substantial periods of time. The effort, cost, and disruption in converting a truss fabrication plant from the design and utilisation of one manufacturer's nail plate to another's is so considerable as to present a substantial disincentive. Conversions do occur but they are rare.

185. The Commission found that switching costs were higher for larger fabricators than for smaller fabricators, because larger fabricators would need to retrain more staff, would face a larger loss of production, and would have more machinery to convert.

186. [ ] stated that some of its members had switched. It stated that the most common reason for changing supplier was due to the change/recruitment of senior staff, who had strong software preferences. It also stated that staff that used the software tended to be loyal to one type of software. The [ ] also confirmed this view.

187. MiTek submitted that over the last 10 years [ ]. Details of companies that have switched over the past 10 years are shown in Appendix 1.

- [

  ].

188. A number of the fabricators contacted by the Commission said that they were reluctant to switch for the following reasons:

- general satisfaction with product and service of their current supplier;
- fabricators employ "detailers" who are almost always trained either in MiTek or Pryda software, and rarely in both. The detailers tend to be extremely committed to one software programme. Switching suppliers would require re-training these detailers. [

  ];
- during staff training, the fabricator experiences a loss of production;
- the actual conversion of the plant to accommodate the new software supplier's equipment. [ ];
- the fabricator runs the risk of mistakes occurring in the production process, as the detailer is not fully trained for 4-6 months; and
- the fabricator is competing with other fabricators for builder's custom on very small margins. If it converts its plant and mistakes are made, or orders are not met on time, due to time taken by their staff to adapt to the new software, the fabricators reputation may be harmed, and important builder's custom may therefore be lost.

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[13] *Multinail Australia Pty Ltd v Pryda (Aust) Pty Ltd & Anor* [ ] QSC 105, para 9.

189. Some of [ ] customers stated that they had frequently been approached by [ ] with proposals to encourage them to switch, though they chose not to do so. Even though these customers didn't switch, it suggests that [ ] was actively competing with [ ], and that [ ] customers chose not to switch because they were content and satisfied with the product and service supplied by their existing provider.

190. Further, both MiTek and Pryda have tried to encourage fabricators to switch by offering better deals. In particular, they have both tried to reduce the switching costs to fabricators by making the transition phase smoother. For instance, the cost of retraining staff to use the new software may be borne by MiTek or Pryda. [

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191. The Commission concludes that there is a reluctance to switch, for reasons of cost, but the low level of switching also appears to be because fabricators are content with their current supplier. However, customers do value the current choice of two suppliers. Therefore, the Commission considers that there is, at present, existing competition and that post-acquisition, due to the removal of this competition, there would be likely to be, a reduction in choice and quality of product and service and an increase in price.

Awarding of Licences

192. Post acquisition, the merged entity would be the only supplier of software-supported connector plates, hence any new fabricator would need to obtain a software licence from the merged entity in order to manufacture roof trusses. Consequently, some [ ] fabricators expressed concern that the merged entity might revoke their software licences, as it might wish to support only [ ] fabricators. It is understood that some fabricators were aware of other fabricators who were unable to purchase a software licence from MiTek or Pryda, because both MiTek and Pryda only grant a limited number of licences to fabricators in geographic areas.

193. [

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[

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194. The Commission considers that there may be some efficiency gains by limiting the number of software licensed fabricators as [ ]. On the other hand, such behaviour could have been undertaken to reduce competition. The Commission therefore considers that there is some scope for MiTek to limit the number of licences it gives out post-acquisition, in order to reduce production, which could in turn result in increased prices of software-supported connector plates.

Tying-in Other Products

195. In the supply of the software-supported connector plates, the merged entity, with 100% market share would have the potential to reinforce the bundling of products by leveraging its market power into related markets by tying in sales of other products to the monopoly product. The fact that a customer would have no alternative supplier for software-supported connector plates suggests that post-acquisition, the customer could be forced to purchase a whole product range rather than just the software-supported connector plates.

196. The Commission also notes that a 100% market share would potentially enable the merged entity to tie-in sales of non-software supported braces and brackets, and also truss making machinery, with sales of software-supported connector plates and thus also raise prices on these products.

197. The Commission understands that in Australia and the United States truss making machinery is bundled with software-supported connector plates and is often provided free of charge to larger customers as an incentive to switch. In most cases, fabricators can only keep the truss making machinery as long as they utilise the incumbent's software and connector plates.

198. Unlike Australia and other parts of the world, truss-making machinery has generally not been bundled in New Zealand. New Zealand fabricators' capital equipment tends to be old but is generally reliable. Most of the time, it is replaced when fabricators decide to upgrade their software system to use automated machinery. As a result, [

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199. The Commission considers there is some scope for the merged entity to adopt the policy of both its parent company and other overseas companies insofar as it may begin to provide New Zealand fabricators with MiTek branded truss making machinery. As fabricators upgrade and update their truss machinery, MiTek will be well placed to offer free equipment on the condition that only MiTek software and connector plates are used. While such a changeover is unlikely to occur in the short term, the Commission nevertheless considers that it may have the effect of locking in existing customers in the medium to long term.

Conclusion on Existing Competition in the Supply of Connector Plates

200. In the supply of software-supported connector plates, the merged entity would have 100% market share. The proposed acquisition reduces the number of suppliers from two to one and the merged entity could potentially limit the number of software licences available to fabricators, in order to raise prices. The loss of competition between MiTek and Pryda is considered to be significant, particularly, as fabricators highlighted that there was currently competitive tension between MiTek and Pryda.

201. Post-acquisition, there would be no existing competition to prevent the merged entity from increasing prices, or reducing the quality of the product and service provided.

202. The Commission also considers, on the balance of probabilities, that the post-acquisition, the merged entity would be able to tie-in sales of braces, brackets or truss making machinery to the monopoly product, and thus hinder competition in other markets.

203. The Commission concludes that the proposed acquisition is likely to lead to a significant reduction in existing competition.

Potential Competition in the Supply of Connector Plates

204. 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.

205. 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.

206. 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.

207. The potential barriers to entry in the supply of software supported connector plates can be considered to be:

- regulatory barriers;
- intellectual property rights;
- bundling of products;
- capital investment;
- switching barriers; and
- strategic barriers.

208. Each of these potential barriers to entry is discussed in further detail below.

Regulatory Barriers

209. In New Zealand, a new entrant in the supply of software supported connector plates, must ensure its connector plates and software meet the various territorial authorities building standards. New Zealand does not have "Building Regulations" that list exact measurements that must be adhered to by builders. Rather, New Zealand has performance based regulations. This means that a new entrant must convince a local authority that its roof truss design and connector plates meet their desired requirements.

210. The Commission has been advised by industry participants as well as the [ ] and the [ ] that New Zealand's performance based building requirements do not represent a major barrier to entry for a new entrant.

Intellectual Property

211. In some cases intellectual property rights can amount to a barrier to entry for a new entrant in a market. Intellectual property rights could include patents, trademarks and copyright.

212. With regards to connector plates, MiTek's product was originally patented. However, this patent expired approximately 30 years ago and subsequently MiTek states that Multinail and Pryda connector plates are a generic version of the MiTek product.

213. MiTek submitted that its software is protected only by copyright. Copyright serves only to protect the expression of an idea and not the idea itself. MiTek considers that such protection does not prevent other persons from developing programmes with the same functionality (provided that, in doing so, there is no substantial reproduction of the code forming the basis of the software).

214. [

].

215. On the balance of probabilities, the Commission considers that the fact that a number of other software systems similar to MiTek's have been developed by Pryda and Multinail demonstrates that copyright is unlikely to amount to a significant barrier to entry for a new entrant.

Bundling

216. In some cases the bundling of products can constitute a barrier to entry. A bundled product means that a new entrant may need to enter the market with a number of related products in order to compete with the incumbent. This could mean the new entrant would face increased sunk costs of providing a range of products and services. Further, the incumbent is likely to provide across-the-board rebates and discounts for the bundled goods and services, which could have the effect of tying in its customers, and therefore of increasing a new entrant's cost of entry.

217. On the other hand, bundling may have associated benefits for consumers and producers. Bundling can allow producers to exploit economies of scope between bundled products, and economies of scale if bundling has an impact on consumer demand. These benefits may be passed on in the form of lower prices to clients or quality improvements. Consumers may also benefit from bundling by receiving only one bill for different services, and thus reducing some of the transaction costs associated with business trades.

218. In this merger, prime facie, the Commission considers that any new entrant would need to provide a fabricator with:

- connector plates (physical product); and
- supporting software.

219. The Applicant states that while in New Zealand connector plates and supporting software are supplied to fabricators as a bundled package, overseas these products are being unbundled. Consequently the Applicant considered barriers to entry in the supply of connector plates and in the supply of supporting software separately.

220. MiTek stated that both MiTek and Pryda software use certain engineering load values for their connector plates, [

]. This is shown in Table 4.

Table 4: Sources of Revenue in this Market in 2002

	Connector Plates	Software Leases	Design Fees
MiTek	[ ]	[ ]	[ ]
Pryda	[ ]	[ ]	[ ]

Source: Commission estimates

221. [

].

222. However, the Commission discounts these arguments on the basis of evidence provided by the majority of key industry players. The Commission is of the view that a new entrant in the supply of software-supported connector plates would need to enter with a bundled product, namely both with the physical product and the software. For instance, a number of fabricators have stated that while it is possible to use a connector plate with non-associated software, they are extremely unlikely to utilise a brand of connector plate that is not compatible with their current software. This is because the software is designed to fit with the connector plate so that all engineering and safety requirements are met.

223. Some commentators said that if a different brand of connector plate were used by the fabricator, these engineering and safety requirements could not be guaranteed. For example, [ ] stated:

[

].

224. This was also confirmed by [

].

225. [

].

226. In addition, industry participants in Australia and the US generally considered that bundling remained the norm for supplying connector plates to fabricators. [

]:

[

].

227. Similarly, [ ] states:

[

].

228. On the other hand, [

]:

[

].

229. However, while it may be technically possible to unbundle software from the physical product, fabricators in New Zealand may not perceive such an option to be cost effective or safe. The Commission considers that there is a risk that due to the need to comply with safety and engineering standards, New Zealand fabricators would not take the risk of purchasing unbundled product and [ ]. Hence, the Commission considers that a new entrant would need to provide a bundled product in order to compete with the incumbent, which would result in increased cost of entry to that new entrant.

Capital Investment

230. A new entrant in the supply of software-supported connector plates would need to invest a large amount of capital in producing the connector plate, and developing and maintaining the supporting software. The capital investment required would be a sunk cost.

231. Sunk costs are generally understood as capital outlay that cannot be recovered (or can only be partially recovered) upon exit. Costs of exit thus will limit the potential entry of third parties in the market, as the risk of non-recovery of the invested capital is high. The Commission considers that the judgement as to whether sunk costs are "high" must be made in relation to the size of the market that a new entrant could serve.

232. From that perspective, the following analysis considers the level of sunk costs and on-going capital commitment required by a new entrant into the supply of software-supported connector plates.

233. The cost of producing connector plates, the supporting software and the on-going technical and engineering support are considered separately in the sections below.

Connector Plates

234. MiTek submitted that the capital investment required by a new entrant to manufacture connector plates and its software is low.

235. A new entrant wishing to supply connector plates could manufacture the product locally or import the product from overseas. These options are discussed in further detail below.

236. With regards to local manufacture, MiTek stated that a basic press may be purchased second-hand for around $40,000-$60,000, and that a tool die (required to bring about the appropriate shape from the press) could also cost around $40,000-$60,000.

237. Most industry participants agreed with MiTek's estimate of the cost of a press. The Commission has also sought independent advice from a tool die-maker, who confirmed that a tool die for a connector plate would cost around $40,000.

238. [ ] estimated that it would cost around $1 million to set up a basic manufacturing facility capable of producing 180 tonnes per annum of a basic range of connector plates. [ ].

239. [ ] has recently investigated the possibility of manufacturing its own connector plates. [ ] estimated that it would require at least four different types of tool dyes to produce four types of connector plates that it would use in manufacturing roof trusses.

240. If a new entrant wanted to import connector plates, [ ] said that it would cost around $45,000 in freight costs to import 180 tonnes of connector plates into New Zealand.

241. [ ] both said if they were to enter, connector plates, along with other hardware products, were likely to be imported from existing production facilities in the [

].

242. The Commission considers that the capital investment required by a new entrant to produce connector plates alone is likely to be low, due to the relative ease and low cost of local manufacture and of importing.

243. However, the Commission considers that as a new entrant would be required to enter the New Zealand market with a bundled package including both supporting software and connector plates, due to the incumbent bundling these products, the cost of manufacturing or importing these products will be significantly raised and will require a higher level of capital investment, especially in terms of setting up manufacturing facilities in New Zealand.

Supporting Software

244. Along with the capital investment required to manufacture connector plates, a new entrant must also provide the supporting software. A new entrant would have the following options:

- developing new software in-house;
- outsourcing software development; and
- adapting existing software.

245. The difference between the second and third option is mainly the cost. In most cases, it is less expensive to adapt existing software than to develop a programme from scratch. These options are discussed in the following paragraphs.

246. MiTek has estimated that developing and implementing a basic package of software that would be able to be used by a fabricator would involve the following:

> It is estimated that it would cost $100,000-$150,000 to commission the design of basic custom-built software, and would take up to twelve months. Such a system would not be as sophisticated as those currently offered by the likes of MiTek and Pryda and Multinail, but would be able to manage to manage the basic design and costing of roof trusses.

247. MiTek estimated that to develop a software programme that would be equivalent to its own, would take four programmers approximately 12 months to develop software and that total development costs would range between $1-2 million.

248. An independent engineering software house [ ] stated that software that is equivalent to that of MiTek's, which includes the ability to design wall frames, would take a minimum investment of $2 million.

249. [

].

250. [ ] disagreed with MiTek's estimation of $1-2 million. In particular it stated:

[

].

251. In relation to developing custom built software, the Commission has spoken with a number of fabricators who have indicated that they are extremely unlikely to develop custom built software as described by MiTek, primarily because software development is not their core business. Fabricators have also stated that if they were to seek alternative software, such software would have to be at the very least equivalent to that of MiTek and Pryda. This is because fabricators value the reliability, ease of use, and engineering, safety, and technical back up, from their existing software packages.

252. [

].

253. The Commission considers, as does MiTek, that custom built software of the nature that MiTek describes, is unlikely to be equivalent to its own. MiTek states that:

> Such a system would not be as sophisticated as those currently offered by the likes of MiTek, Pryda and Multinail, but would be able to manage the basic design and costing of roof trusses.

254. Further, fabricators appear to value the credibility and reliability of their current system and would be unlikely to switch to a custom built software package that not only does not have the equivalent features, but is unlikely to have the same level of on-going technical and engineering back-up. Consequently, the Commission considers that any new entrant would have to provide software that was at the very least equivalent to that of MiTek or Pryda.

255. In considering entry in the form of adapting existing software, the Commission considered the ability for an overseas company to adapt its existing software, as well as the ability for a software provider for steel prefabrication to adapt their software for timber prefabrication.

256. The Commission notes that there are a number of overseas companies that have already developed software for the manufacture of roof trusses. If such an overseas company were to enter New Zealand it would need to modify its software to be compatible with New Zealand's local conditions. Such modifications could include conversion to the metric system and/or New Zealand's different engineering requirements such as different load bearing, and different seismic and wind conditions.

257. MiTek has submitted that such conversion would not present a significant barrier to an existing overseas company entering New Zealand. MiTek states:

> an overseas provider would need to modify its software for New Zealand conditions but this is a straight forward process (we note that Australian software would not need any modification). Consequently, a fabricator would be able to access such software on short notice.

258. [

].

259. However, [

]:

[

].

260. [

]. The Commission understands that these estimates will necessarily be higher than that of [

].

261. An independent engineering software house [ ] highlighted that it would be difficult to estimate the cost of converting overseas software to the New Zealand market but it would be in the region of "hundreds and thousands of dollars" because of the different loading codes and different design specifications for timber.

262. A software company [ ] explained to the Commission that no more than A$400,000 would be necessary to convert their software from steel to timber and to provide a very comprehensive system similar to that of Pryda.

263. The Commission has found it difficult to assess the evidence which to some extent is conflicting. On a conservative basis, it would appear to the Commission that it would cost $1-2 million to develop new software programme.

264. The Commission considers that the production of the supporting-software for connector plates would require significant capital investment in the development of new software or the conversion of existing software from overseas companies. Out of a market of [ ] (see Table 3), a new entrant could reasonably hope to obtain only a fraction of it over a few years. As such, the Commission considers that it is likely that the development and the conversion of software are likely to represent a significant sunk cost to a new entrant. This is also because such specialised software is unlikely to have any

other purpose should entry into the New Zealand market be unsuccessful. Accordingly, the Commission considers that the high levels of sunk cost required represent a high barrier to entering the New Zealand market.

On-going Software Development and Support

265. As well as the initial investment required to develop and implement a software package, industry participants have advised the Commission that on-going capital expenditure is required for software development, as well as for "on the ground" technical and engineering support. As noted earlier in paragraph 91, while there are [ ], the fabricators nevertheless place high importance on the ability of their supplier to provide "on the ground" technical and engineering support in the event of mistakes or faults.

266. Both fabricators and overseas suppliers considered there was little scope for on-going technical and engineering services to be provided remotely by telephone or via e mail. For example, [ ] stated:

[

].

267. [

].

268. MiTek estimated that it spent around [ ] per year on on-going software and engineering support. It also stated that site visits were a particular feature of MiTek's business model.

269. [

].

270. [ ] provided the following estimates for the on-going capital costs for software development and support:

- software development - includes hiring programmers, cutting code, bug fixes and system enhancements – [ ];
- software service - includes helpdesk and all types of software support and assistance – [ ]; and
- customer service - includes training and assistance on-site (mostly in the use of software) – [ ].

271. Accordingly, the Commission considers that on-going software development, and "on the ground" technical and engineering support, is required if a new entrant is to be successful and this is likely to amount to a significant amount per year, and considering the size of the market a new entrant could hope to obtain, it is likely to deter a new entrant from entering the market for software-supported connector plates.

Conclusion on Capital Investment

272. In summary, the Commission considers that given the required investment in software development, support and dyes, the sunk costs are large in relation to the total size of the market a new entrant could hope to obtain (i.e. only a fraction of the [ ] market for 2003). This means that a new entrant would need to get significant market share to enable it to spread its fixed costs. Hence the sunk costs of software development or conversion are likely to represent significant barriers to entry. Further, the on-going commitment of software development and technical support is likely to be a contributing factor in deterring a new entrant.

Switching Barriers

273. A new entrant in the supply of software-supported connector plates would face switching barriers in persuading a critical mass of fabricators to adopt its product. MiTek and overseas companies cited the reluctance of fabricators to switch to a new supplier as a key barrier to entry. The issue of switching costs was discussed in paragraphs 174- 187.

274. Fabricators also commented that post-acquisition, any new entrant would need to not only overcome their reluctance to switch due to loss of production and their detailer's preferences, but be able to demonstrate that their product is :

- credible and reliable with a proven track record in another similar country with features similar to New Zealand's market;
- able to be adapted to their truss making machinery;
- able to provide sufficient "on the ground" technical and engineering back up in the event of faults; and
- backed up with free training.

275. The Commission considers that overseas companies, such as [ ] with their experience in their respective markets, would be likely to demonstrate to New Zealand fabricators that their systems are both reliable and credible. While they might incur some initial capital cost in providing free training, the Commission understands that such expenditure is unlikely to be significant, and would most likely be included in a new entrant's on-going technical support programme.

276. However, the Commission is of the view that new entrants from overseas would find it more difficult to convert a New Zealand fabricator than an existing supplier such as Pryda and MiTek. This is because the overseas companies would not have experience in New Zealand, and hence would find it more difficult than the incumbent in convincing a fabricator to switch.

277. The Commission considers that fabricators are reluctant to switch for a number of reasons as discussed above. Further, a new entrant would face higher barriers from switching costs than the incumbent due to its lack of knowledge and experience in the New Zealand market. However, the Commission notes that the low level of switching also reflects general satisfaction with current suppliers.

278. The Commission considers that the ability of a new entrant to encourage fabricators to switch suppliers would be limited and switching costs, therefore represents a high barrier to entry in this market.

Strategic Barriers

279. In assessing the ease of entry for a new entrant, the Commission considers the merged entity's ability to engage in strategic behaviour that could, potentially, result in barriers to entry for a new entrant. In assessing such strategic barriers, the Commission takes into account previous behaviour of the merging parties.

280. A potential entrant in the supply of software-supported connector plate market is likely to consider how the incumbent would react when it enters. For example, the potential entrant might believe that the incumbent would reduce prices substantially if it were to enter and so reduce the prospective revenue available from entering the market. Therefore, aggressive competition post-entry could deter entry.

281. In this acquisition, the merged entity, as the incumbent, is likely to have first mover advantages allowing it to shape the way the market develops by, for example, reducing or completely deterring the potential for new entrants to enter the supply of software-supported connector plates.

282. The following two sections discuss examples of the merging parties potentially deterring entry.

Deterring Entry

283. [

].

284. The first example, referenced in paragraph 103, involved Pryda engaging in strategic behaviour to win customers from Multinail. Multinail[14] sued Pryda to court over the incident, and demonstrated successfully that Pryda had unlawfully induced a large Australian fabricator contracted to Multinail to switch to Pryda.

285. The second example was of [

].

286. A further example involved [

].

287. The Commission understands that [

].

288. [

[14] Multinail Australia Pty Ltd v Pryda (Aust) Pty Ltd & Anor 14

].

289. [

].

[

]

[

].

290. [

].

291. [

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292. [

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293. [

].

294. [

].

Conclusion on Strategic Barriers

295. In summary, the Commission considers that, post acquisition, strategic barriers to entry in the supply of software-supported connector plates are likely to be increased, as previous behaviour by both MiTek and Pryda, indicate that the merged entity with 100% of the relevant market, is likely to react strongly to any new entry through, for example, [ ].

Conclusion on Barriers to Entry in Connector Plates

296. The Commission has considered the various factors relevant to the assessment of the entry barriers in the supply of software supported connector plates. The Commission concludes that the aggregation of all the barriers to entry in the supply of software-supported connector plates, results in overall high barriers to entry in this market.

The "LET" Test

297. Where barriers to entry or expansion in a market are clearly low, it may be unnecessary for the Commission to identify specific businesses that might enter. In other markets, where barriers are higher, as in this case, the Commission has sought to identify possible new entrants as a way of testing the assessed entry barriers.

298. 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).

Likelihood of Entry

299. 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.

300. Post-acquisition, the combined entity would be the sole supplier of software supported connector plates. The Commission considers that potential entry is likely to occur via an existing overseas supplier of software-supported connector plates or via a new entrant with the capability to develop and implement credible software and manufacture connector plates.

301. Most fabricators stated that they are unlikely to either develop software themselves or contract an independent software house to develop software. This is primarily because the development of software is not their core business. They would also not consider importing connector plates without accompanying software support.

302. The Commission contacted overseas suppliers of software-supported connector plates. [ ] stated that they are unlikely to enter the market for the following reasons:

- the large capital investment in converting their current software to New Zealand conditions;
- the large capital commitment required to guarantee New Zealand fabricators both on-going and "on the ground" technical and engineering support; and
- inherent risks and strategic barriers that they would face in entering a market where the incumbent has 100% market share, and where it is difficult to convince fabricators to switch to a new supplier.

303. The Commission also found that [

].

304. However, the attempt to enter the market was not viable. This was due to:

- [

].

305. [

].

306. [

]. As explained above in the section on capital investment, the existence of economies of scale in software development and the size of the sunk costs in relation to the total market give rise to market conditions that may not allow entry to occur.

307. This said however, the Commission has found [ ] could be a likely entrant into New Zealand. [

].

308. In summary, with regards to this [ ]:

[

].

309. [

]. However, the extent of such entry is discussed in paragraphs 332-336.

310. As noted earlier, [

]

311. [ ].

312. [

].

313. [

].

314. [

].

315. [

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316. The Commission therefore considers that [ ] are likely entrants into the market for software-supported connector plates.

Extent of Entry

317. 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.

318. 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 a firm's efforts to expand from one part of the market to another. Where mobility barriers are present in a market, they may reduce the 'extent' of entry.

319. In the supply of software-supported connector plates, the Commission has considered the extent of [ ] potential entry.

[ ]

320. [

].

321. The Commission notes that [

].

322. [

].

323. [

]:

[

].

324. [

], there is a concern as to whether fabricators would take the risk of purchasing unbundled products. As stated in paragraphs 211-224, fabricators are used to purchasing connector plates and the supporting software from the same supplier in order to comply with safety and engineering standards.

325. Finally, even if [

].

326. [

].

[

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327. [

].

328. Given the switching costs fabricators face when switching suppliers, as discussed in paragraph 174-187 and paragraphs 263-268, post acquisition, the Commission is concerned that if [

].

329. [

].

330. [

].

331. Having considered the evidence, the Commission considers that [

].

332. Further, post acquisition, Pryda fabricators could be disgruntled with having to deal with MiTek. It is also possible that MiTek may wish to operate only one software platform and that Pryda fabricators may [

].

333. On balance, the Commission considers that [ ] entry is unlikely to be sufficient in its extent to constrain the merged entity due to:

- [

].

[ ]

334. [

].

335. Further, given that the merged entity as an incumbent benefits from economies of scale and would be the only supplier of software-supported connector plates, [ ] is unlikely to gain scale economies in New Zealand within two years.

336. In addition, [ ] would need to, at least, provide the same level of guarantee for its products as well as the same level of service as MiTek in order to gain a sufficient number of customers.

337. Accordingly, the Commission considers that [ ] possible entry into the market [ ]. This is because [ ] would not be able to gain a sufficient number of customers to be able to compete with scale economies that would be enjoyed by the combined entity and it would not be able to provide the same level of guarantee and on going technical and engineering support as the merged entity.

Conclusion on Extent of Entry

338. The Commission considers, on the balance of probabilities, that [ ] entry into the market for the supply of software-supported connector plates is likely to be limited and not of a sufficient extent to prevent the combined entity from raising prices or reducing the quality of product and service.

Timeliness of Entry

339. 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.

340. MiTek claim that, depending on the number of programmers employed and their experience, it may take 12 months to develop a software system with similar functionality to MiTek's existing programmes to support builders' hardware products.

341. [

].

342. [

].

343. [

].

Conclusion on Potential Competition in Connector Plates

344. Overall, the Commission considers that [ ] are likely and timely entrants but that either entry is unlikely to be sufficient in extent to prevent the merged entity from raising its prices or reducing the quality of product and service it currently provides.

Countervailing Power in the Supply of Connector Plates

345. 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.

346. 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.

347. In the supply of software-supported connector plates, the large fabricators currently have countervailing power. Table 5 shows that in 2002, approximately [ ] of MiTek's total revenue was from [ ].

Table 5: MiTek Customers

[

]

348. Further, some large fabricators, namely [ ], stated that they had benefited from negotiating lower prices. [ ] said that they required notice and justification for any price increases.

349. [ ] highlighted that they were currently able to exert considerable pressure on MiTek in terms of pricing and service due to the presence of Pryda and that post acquisition such a threat would be lost. Thus, they believed their countervailing power would be reduced as a result of the proposed acquisition.

350. Most of the large fabricators stated that they would be unlikely to order or custom design their own software as it was not their core business. Rather, in the event of an increase in price or a reduction in the quality of service or product by the merged entity, they were more likely to seek an alternative supplier who could provide a bundled product.

351. The Commission, however, notes that these large fabricators stated that they were generally willing to incur 5-10% increases in price before they considered seeking an alternative supplier off-shore. This was mainly due to the difficulties in converting their plants, and the fact that connector plates themselves only represent a small portion of the total cost of a roof truss.

352. [ ] stated that their fabricators would have to be "significantly disadvantaged" in terms of an increase in price by the merged entity before they would consider switching to a new entrant.

353. [ ] stated that they would be "stuck with" MiTek post acquisition and if prices were to rise or service levels decreased they would look to [ ].

354. [ ].

355. The Commission considers that the large fabricators' countervailing power is likely to be reduced post-acquisition because:

- The level of price increase that fabricators would tolerate before considering switching is already above the acceptable limit of 5%-10% in two years. This in itself shows that the countervailing power of fabricator is limited;
- The competitive tension between MiTek and Pryda which enabled large customers to exert countervailing power would be lost;
- The fabricators have limited experience in actually seeking alternative supply overseas; and
- The fact that the extent of any likely entry is limited.

356. The [ ] customer base comprises small and medium sized customers, while around [ ] of [ ] customer base consists of small to medium sized businesses. The Commission considers that this sector of the market is fragmented and is unlikely to exert countervailing power on the merged entity. For instance, the [ ] said that its members would pay a 5% price increase. In addition, some small to medium fabricators advised the Commission that they would have very limited countervailing power and in the event of a price increase of 5-10%, and sometimes higher, they would simply pass the increase in costs onto their customers. For example, [ ] stated:

].

357. While [ ] stated:

[

].

Conclusion on Countervailing Power in Connector Plates

358. The Commission considers that the countervailing power of large customers would be reduced and would be insufficient to prevent the merged entity from raising prices or reducing the quality of product and service. The Commission also considers that small to medium customers of the merged entity would have little or no countervailing power.

Conclusion on SLC in Connector Plates

359. In the supply of software-supported connector plates, the Commission concludes that compared with the counterfactual where Pryda remains as an effective competitor, the merger would result in a loss of existing competition, the merger would reduce the number of suppliers from two to one. As the sole supplier, the merged entity would have a 100% market share and could potentially limit the number of software licences available to fabricators, in order to raise prices.

360. The Commission considers that potential entry into the supply of software-supported connector plates is insufficient to provide competition to the merged entity. It appears that entry from [ ] may be likely and timely but it would be insufficient in extent to prevent the merged entity from raising prices or reducing the quality of product or service. This is because the extent of entry would be affected by the [ ], also there are difficulties in persuading fabricators to switch, as well as a need to gain economies of scale and to provide the same level of guarantee and on-going technical and engineering support as the combined entity.

361. Further, given the limited extent of any likely entry, the large fabricators would have limited countervailing power to prevent the merged entity from raising prices or reducing the quality of product and service supplied.

362. The Commission concludes that the merger is likely to lead to a substantial lessening of competition in the supply of software-supported connector plates. In addition, to the substantial lessening of competition in the supply of software-supporting connector plates, the Commission is concerned that the merged entity would be able to leverage its market power in this market and tie-in sales of other related products, namely braces, brackets and truss making machinery, with sales of software-supported connector plates.

Non-software-supported Brackets and Braces

363. The Commission considers that the competition analysis in terms of non-software supported brackets will be equally applicable to the competition analysis for the market

for non-software supported braces. Accordingly, the following competition analysis and conclusions on existing and potential competition applies to both markets.

Existing Competition

364. In the supply of non-software-supported brackets used in prefabricated construction and in the supply of non-software-supported braces used in prefabricated construction, MiTek and Pryda are the only suppliers in New Zealand. Table 6 shows MiTek and Pryda's sales of braces and brackets in New Zealand in 2002.

Table 6: MiTek and Pryda Sales of Brackets and Braces in 2002

Company	Braces		Brackets		Other	
	Sales $	%	Sales $	%	Sales $	%
MiTek	[ ]	[ ]	[ ]	[ ]	[ ]	[ ]
Pryda	[ ]	[ ]	[ ]	[ ]	[ ]	[ ]
Total	[ ]	[ ]	[ ]	[ ]	[ ]	[ ]

Source: Commission estimates
Notes: Sales are likely to be underestimated as some of sales of braces are included in other product categories. Brackets consists mainly of joist hangers
Data for Pryda is for the period July 2002-June 2003.

365. The Applicant did not provide market share information for its competitors but said that there were a large number of competitors supplying a broad range of builders' hardware products. The list provided is shown in the table.

Table 7: Suppliers of Brackets and Braces

Bracing	Brackets
Goodwood	Rovel International
Multinail	Steelmasters
Carlray	Avon
Dunnings	Multinail
McIntyre	Wilmaplex
	Dunnings
	McIntyre

Source: MiTek

366. The Applicant claims that these companies manufacture and distribute a range of relevant products in Australia that are direct alternatives to MiTek products.

367. During the Commission's investigations, none of the above companies were found to be currently active in New Zealand. However, their potential entry is discussed later on in this report.

368. [ ] some small localised engineering shops produce specialised brackets and braces for particular subdivisions and developments. However, [ ] noted that this represented a very small part of the market].

369. The Commission found that the fabricators who are also builders' hardware retailers currently sourced brackets and braces from MiTek and Pryda. Most customers commented that they valued the choice of purchasing braces from MiTek or Pryda, and that a significant amount of competitive tension currently exists between the two companies.

370. The Commission also found that Pryda and MiTek were able to manufacture customised brackets and braces for customers, and have a large product range in New Zealand. For example, Pryda has 46 different products which include connector plates and different types of braces and brackets, of which there are 94 sub-types that come in 313 sizes.

371. Although there may be some small engineering companies that could provide brackets and braces post-acquisition, they are unlikely to provide sufficient existing competition to the merged entity, as they would have a limited product range and limited gains from economies of scale. The merged entity would be the major supplier of non-software-supported brackets and braces.

Conclusion on Existing Competition in Brackets and Braces

372. The Commission considers that in the factual, the considerable degree of competition that currently exists in the non-software-supported brackets and braces market would be removed, and that there are no other existing competitors operating in this market that could prevent there being a substantial lessening of competition.

Potential Competition in Supply of Brackets and Braces

Barriers to Entry

373. In the supply of non-software brackets and braces used in prefabricated construction, some of the barriers to entry are similar to those of software-supported connector plates. The regulatory barriers are the same, as any new entrant would need to be able to guarantee that certain engineered braces and brackets adhered to various local authorities building standards.

374. On the other hand, no software is required in the supply of braces, although the manufacturing of braces is similar to the manufacturing of the actual connector plates.

375. Some builders' hardware retail outlets stated that a new entrant into the supply of braces would need to provide a product range, comprising not just non-software supported braces, but also other products like non-software supported brackets and software supported connector plates. Such customers valued the "one-stop shop" provided by Pryda and MiTek because it is efficient to purchase all products from one supplier. For example, they were able to benefit from lower costs through consistent invoicing and stock renewal, as well as across the board discounts and rebates granted by the supplier in recognition of the customer purchasing more products from them.

376. Alternatively, [ ] said that while it purchased software-supported connector plates from MiTek, it purchased the majority of its non-software-supported brackets, braces, and other fasteners from Pryda. Consequently, it might be possible for a new entrant to

supply only the range of brackets and braces, as some large buyers in New Zealand are accustomed to purchasing these products from alternative suppliers.

377. In order for the new entrant to provide this "one stop shop", it would be necessary to set up a manufacturing plant that is able to produce the wide range of braces and brackets required by the customer. As discussed earlier, such a manufacturing plant would basically be made up of a number of presses and tool dyes to produce the various products. It would also need to include some welding facilities to produce some brackets and braces that require particular engineered quality.

378. A new entrant in the supply of non-software-supported brackets and braces would need to purchase tool dyes that could range in cost from $15,000 to $60,000, for more complicated dyes. A number of presses, welding equipment and other machinery would be needed and could be obtained on the second hand market for around $40,000. [ ] estimated that it would cost around $1 million to set up basic manufacturing facilities in New Zealand that could produce brackets and braces, as well as connector plates.

379. The Commission considers that the actual capital investment required by a new entrant to produce only brackets or braces is likely to be low due to the apparent ease and relative inexpensive by which the product could be manufactured in New Zealand. However the Commission notes that if a new entrant were forced to enter the New Zealand market with a bundled package consisting of a range of brackets and braces, due to the incumbent bundling these aforementioned products and the range of products it supplies, the cost of manufacturing or importing these products would be significantly raised and may require a higher level of capital investment, especially in terms of setting up manufacturing facilities in New Zealand.

Conclusion on Barriers to Entry in Supply of Brackets and Braces

380. The Commission considers that barriers to entry in the supply of non-software-supported brackets and braces are moderate. This is because there is a significant level of capital investment required by a new entrant to provide a "one stop shop" that is able to manufacture the volume and wide range of products builders' hardware retailers and fabricators require. This capital cost could be increased by the incumbent bundling braces and brackets with the monopoly products where there is no alternative, namely, software supported connector plates.

The "LET" Test

Likelihood of Entry

381. MiTek provided a list of potential competitors in the supply of non-software-supported brackets and braces.

382. [

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383. Some [ ] also stated that they were unlikely to enter the New Zealand market due to:

- shipping costs being high because of the weight of the product;

- their concentrating on manufacturing specialised products for niche markets in Australia; and
- their having little experience or contacts in the New Zealand market.

384. On the other hand, [ ] said that it would consider entering New Zealand in the supply of brackets and braces. [

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385. In addition, [ ], stated that it might enter the New Zealand market in 2004. It explained that it would enter irrespective of whether MiTek acquires Pryda, and that it would [

].

386. The Commission notes that the cost of importing hardware products encompasses not only freight but also stocking. The latter can be substantial and thus potentially precludes small importers from importing.

387. The Commission therefore considers that entry in the supply of non-software-supported brackets and braces is likely via [

] if it were to win the custom of a large New Zealand builders' hardware retailer, or via [ ].

Extent of Entry

388. In the supply of non-software supported brackets and braces used in prefabricated construction, the extent of any likely entry from [ ] would likely to be sufficient in extent to prevent the merged entity from increasing its prices.

389. All [ ] companies would be able to provide both the volume and range of products required by some of the large fabricators in New Zealand, and their likely entry is therefore considered to be sufficient in extent .

Timeliness of Entry

390. In the supply of non-software supported brackets and braces used in prefabricated construction, the Commission considers that entry is likely to be timely to prevent the merged entity from raising prices. The likely entrants in this market already, have manufacturing facilities and experience in producing these products in [ ]. Therefore, expansion into New Zealand is unlikely to take longer than two years. In particular, [ ] said that it is considering entering New Zealand next year which is well within the Commission's two year time frame.

Conclusion on Potential Competition in the Supply of Brackets and Braces

391. The Commission considers that barriers to entry in the supply of non-software supported brackets and braces are moderate because of the need to provide a range of braces and brackets. However, entry in the supply of non-software supported braces and bracket

used in prefabricated construction is likely and timely, and sufficient in extent to prevent the merged entity from raising prices.

Countervailing Power of Buyers in the Supply of Brackets and Braces

392. In the supply of non-software-supported brackets and braces used in prefabricated construction, the large fabricators said that they considered their ability to import, especially from Australia, to be a "credible threat", and that this would be likely to prevent any price gouging by the merged entity. For example, [

].

393. As noted above, there are [ ] companies such as [ ] that are willing to enter the New Zealand market which adds weight to the ability of large customers to impose a credible threat by seeking alternative suppliers.

394. On the other hand, small to medium sized customers all stated that they believed that they had little to no countervailing power. They stated that they were unlikely to import products due to the:

- large volumes required to mitigate freight costs; and
- difficulties in storing and managing large stock piles of a wide range of braces and brackets.

395. In the supply of non-software-supported brackets and braces used in prefabricated construction, the Commission found that the larger fabricators have strong countervailing power, and the small to medium sized customers have limited countervailing power

Conclusion on SLC in Supply of Non-software-supported Brackets and Braces

396. In the supply of non-software-supported braces and brackets used in prefabricated construction, the Commission considers that there would be a loss of existing competition, as the merged entity would become the only supplier of brackets and braces. However, the Commission considers that post acquisition, barriers to entry are moderate, there is scope for potential entry from [ ] who can provide the required "one stop shop" of products, and the large customers of the merged entity are likely to have a significant degree of countervailing power. Consequently, the Commission concludes that the merger is unlikely to lead to a substantial lessening of competition in the supply of non-software-supported brackets and braces used in prefabricated construction.

Truss Making Machinery

Existing Competition

397. In the supply of truss making machinery, there is some vertical aggregation in the supply of manual presses and jigs. Pryda manufactures and distributes manual jigs and presses. MiTek does not manufacture any jigs and presses but purchases the machinery from New Zealand which it then distributes to customers along with other bundled products. Therefore, there is horizontal aggregation at the distribution level.

398. Table 8 shows MiTek and Pryda's sales of jigs and presses.

Table 8: MiTek and Pryda Sales for the Supply of Jigs and Presses

	Forecast 2003		2002		2001	
	Total Sales $	**%**	**Total Sales $**	**%**	**Total Sales $**	**%**
MiTek	[ ]	[ ]	[ ]	[ ]	[ ]	[ ]
Pryda	[ ]	[ ]	[ ]	[ ]	[ ]	[ ]
Total	**[ ]**	**[ ]**	**[ ]**	**[ ]**	**[ ]**	**[ ]**

Source: MiTek and Pryda

399. The table above shows market share by sales. However market share by volume would be more indicative of MiTek and Pryda's activities in the supply of truss making machinery. Market shares based on volume were not obtained. However, the Commission understands that an average piece of machinery would cost around $40,000, suggesting that the number of units sold by either MiTek or Pryda would be around [ ].

400. Post-acquisition, the merged entity appears to be the main supplier of manual jigs and presses. It is likely that MiTek would cease purchasing jigs from New Zealand Welders in Auckland as well as purchases of presses from North Hydraulics and Industrial Maintenance Engineers. However, these companies also supply manual jigs and presses directly to fabricators and are likely to be alternative suppliers post acquisition.

401. The Commission also found that some truss making machinery could be purchased in the second hand market. [ ].

402. The Commission also found that some specialised truss making machinery could be imported. For example, [ ].

403. However, some industry participants raised concerns that the merger would result in fabricators having to purchase machinery that can read only from MiTek and Pryda software. For example, [

].

404. On the other hand, [

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405. The Commission notes that because of Pryda's activities in the supply of truss making machinery, post-acquisition, the merged entity would be vertically integrated to a greater extent and thus could be in a stronger position to sell its own machinery as a bundled offer, as is currently done overseas (see paragraph 194).

406. However, on balance of probabilities, it appears that, post-acquisition, fabricators would have alternative suppliers of presses and jigs. They would also continue to have the same number of suppliers of automated saws.

Conclusion on Existing Competition

407. In the supply of truss making machinery, the Commission considers that there is sufficient existing competition to prevent there being a substantial lessening of competition. There are alternative suppliers of jigs and presses, and automated saws can continue to be purchased from Spida or MangoTech. Further, there is a second hand market for manual truss making machinery and in some cases, machinery could be imported, although it may be more expensive and specialised.

408. As the Commission considers that there would be sufficient existing competition in the supply of truss making machinery, it has therefore not considered potential competition.

Conclusion on SLC in Truss Making Machinery

409. The Commission concludes that the proposed acquisition is unlikely to result in a substantial lessening of competition in the supply of truss making machinery due to sufficient existing competition being maintained.

Software-supported Products for Flat Roofs and Flooring

Existing Competition

410. In the supply of software-supported products for flat roofs and flooring there are various suppliers for competing products. These products and suppliers include the following:

- metal webs, supplied by MiTek (Posi-Strut) and Pryda (Long Reach);
- LVLs supplied by Carter Holt Harvey;
- I-beams supplied by Fletchers New Zealand and Nelson Pine; and
- timber webs (the software to design the timber webs is supplied by MiTek and Pryda but fabricators use timber "off-cuts" to make the actual timber webs).

411. Table 9 shows that the combined entity would have a market share of [ ] in the supply of software-supported products for flooring. The suppliers of I-beams and LVL suppliers would have a market share of [ ]. However, these market shares do not include the use of the same software-supported products which are also used in flat roofs. Given that flat roofs are rarely built, it is unlikely that the market shares would be significantly higher.

Table 9: Market Shares in the Supply of Software-supported Products used in Flooring

Supplier	Engineered Floors ($m)	Market Share
MiTek	[ ]	[ ]
Pryda	[ ]	[ ]
Combined Entity	**[ ]**	**[ ]**
I-beam and LVL suppliers	[ ]	[ ]
Others	[ ]	[ ]
Total	[ ]	[ ]

Source: MiTek estimates

412. Post acquisition, the merged entity would be the only supplier of software-supported metal webs, and the only supplier of software that is capable of designing timber webs. Table 10 shows MiTek sales of metal webs over the past three years. Pryda have just introduced a range of metal webs for floor trusses and consequently it does not have any sales history.

Table 10: MiTek's Revenue From Sales of Metal Webs

Forecast 2003	2002	2001
[ ]	[ ]	[ ]

413. [ ]:

[

].

414. MiTek estimate that the share of I-beam and LVL products used in flooring has [ ] over the last two years. [

].

415. Further, [

].

416. Some industry participants [ ] and said that the use of metal webs has been declining over recent years and that the use of LVL and I-Beams has significantly increased. [ ] commented that it believed that LVL beams were used by the vast majority of builders and that metal and timber webs were generally only used for specialised flat roofs.

417. In contrast, some industry participants had a preference for metal webs because they were light and easy to use.

418. Therefore it appears that the decision to choose metal webs or LVLs and I-beams depends on the builder's preference.

Conclusion on Existing Competition

419. The Commission considers that there would be sufficient existing competition post acquisition in the supply of software-supported products for flat roofs and floors. This is because, in the event of any price increases, customers could switch to LVL or I beams which are supplied by Carter Holt Harvey and Fletchers/Nelson Pine respectively.

420. The Commission considers that there is sufficient existing competition in the supply of software supported products for flat roofs and flooring, and has therefore not considered potential competition.

Conclusion on SLC in Software-supported Products for Flat Roofs and Flooring

421. The Commission considers that there is unlikely to be a substantial lessening of competition in the supply of software-supported products for flat roofs and flooring as there would be sufficient competition provided from competing products.

OVERALL CONCLUSION

422. The Commission has considered the probable nature and extent of competition that would exist in the following relevant markets:

- the national supply of general fasteners;
- the national supply of software-supported connector plates;
- the national supply of non-software-supported brackets used in prefabricated construction;
- the national supply of non-software-supported braces used in prefabricated construction;
- the national supply of truss making machinery; and
- the national supply of software-supported products for flat roofs and flooring;

423. [

]. The Commission therefore considers that the appropriate counterfactual is the Pryda and Reid businesses being acquired by a party that does not raise competition concerns.

424. The Commission has considered the nature and extent of the contemplated lessening of competition in each of the relevant markets.

425. 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:

- constraint posed by existing competition;

- ease of entry by potential competitors; and
- countervailing power by large purchasers.

General Fasteners

426. In the supply of general fasteners, there is a minor aggregation. Further, there are several existing suppliers of general fasteners, including imports. Consequently, the Commission considers that there is unlikely to be a substantial lessening of competition in the supply of general fasteners.

Software-supported Connector Plates

427. In the supply of software-supported connector plates, the Commission concludes that compared with the counterfactual where Pryda remains as an effective competitor, the merger would result in a loss of existing competition, as it would reduce the number of suppliers from two to one. As the sole supplier, the merged entity would have a 100% market share and could potentially limit the number of software licences available to fabricators, in order to raise prices.

428. The Commission considers that potential entry into the supply of software-supported connector plates is insufficient to provide competition to the merged entity. Barriers to entry are high and it appears that entry from [ ] may be likely and timely, but it would be insufficient in extent to prevent the merged entity from raising prices or reducing the quality of product or service. This is because the extent of entry would be affected by the [ ], also there are difficulties in persuading fabricators to switch, as well as a need to gain economies of scale and to provide the same level of guarantee and on-going technical and engineering support as the combined entity.

429. Further, given the limited extent of any likely entry, the large fabricators would have limited countervailing power to prevent the merged entity from raising prices or reducing the quality of product and service supplied.

430. The Commission concludes that the merger is likely to lead to a substantial lessening of competition in the supply of software-supported connector plates. In addition, to the substantial lessening of competition in the supply of software-supported connector plates, the Commission is concerned that the merged entity would be able to leverage its market power in this market and tie-in sales of other related products, namely braces, brackets and truss making machinery, with sales of software-supported connector plates.

Non-software-supported Brackets and Braces

431. In the supply of non-software-supported brackets, and non-software-supported braces, used in prefabricated construction, the Commission concludes that there would be a loss of existing competition, as the merged entity would become the only supplier. However, the Commission considers that post-acquisition, given that barriers to entry are moderate, there would be scope for potential entry from [ ] which could provide the required "one stop shop" of products, and the large customers of the merged entity are likely to have countervailing power. Consequently, the Commission concludes that the merger is unlikely to lead to a substantial lessening of competition in the supply of non-software supported brackets and braces used in prefabricated construction.

Truss Making Machinery

432. In the supply of truss making machinery, the Commission considers that there would be sufficient existing competition to prevent there being a substantial lessening of competition. There are alternative suppliers of jigs, presses, and automated saws that would continue to be purchased from Spida or MangoTech. Further, there is a second-hand market for manual truss-making machinery. In some cases, machinery could be imported, although it may be more expensive and specialised. The Commission considers that there is sufficient existing competition in the supply of truss-making machinery, and has therefore not considered the scope for potential competition.

Software-supported products for Flat roofs and Flooring

433. The Commission considers that there is unlikely to be a substantial lessening of competition in the supply of software-supported products for flat roofs and flooring, as there would be sufficient competition provided from competing products.

Conclusion

434. 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 following markets.

- the national supply of general fasteners;
- the national supply of non-software-supported brackets used in prefabricated construction;
- the national supply of non-software-supported braces used in prefabricated construction;
- the national supply of truss making machinery; and
- the national supply of software-supported products for flat roofs and flooring.

435. However the Commission is not satisfied that the proposed acquisition would not have, nor would be likely to have, the effect of substantially lessening competition in the supply of software-supported connector plates due to the lack of existing and potential competition and the lack of countervailing power.

DETERMINATION ON NOTICE OF CLEARANCE

Pursuant to section 66(3) (b) of the Commerce Act 1986, the Commission determines to decline the proposed acquisition of MiTek New Zealand ("MiTek") or its related company, MiTek Australia Limited, of the assets and liabilities of Pryda New Zealand ('Pryda") and Reid New Zealand ("Reid") which are operating divisions of Nylex (New Zealand) Limited.

Dated this 13th day of November 2003

Peter JM Taylor
Division Chair
Commerce Commission

APPENDIX ONE

FABRICATOR MOVEMENTS OVER THE LAST 10 YEARS

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