Public Version
ISSN NO. 0114-2720
J6436

COMMERCE COMMISSION

Decision No. 520

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

ATLAS GROUP HOLDINGS LIMITED

and

SOUTHWARD ENGINEERING LIMITED

The Commission: Peter JM Taylor
Donal Curtin

Summary of Application: The acquisition by Atlas Group Holdings Limited of all the ordinary shares of Southward Engineering Limited

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

Date of Determination: 4 May 2004

*This decision was amended on 29 June 2004 to correct an error in the application in that at para 1.1 the entity name is "Atlas Group Limited". It should be "Atlas Group Holdings Limited".

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EXECUTIVE SUMMARY

The Proposal

1. A notice pursuant to s 66(1) of the Commerce Act 1986 (the Act) was registered on 8th April 2004. The notice sought clearance for the acquisition by Atlas Group Holdings Limited of all the ordinary shares of Southward Engineering Limited.

Market Definition

2. The Commission concludes that the relevant markets for this acquisition are as follows:
   - the national market for the distribution of stainless steel (the stainless steel market);
   - the national market for the distribution of mild steel (the mild steel market); and
   - the national market for the distribution of aluminium (the aluminium market).

Counterfactual

3. The Commission is of the view that the appropriate counterfactual is [ ]

Competition Analysis

Existing Competition

Mild Steel Market & Aluminium Market

4. The Commission concludes that the proposed acquisition is unlikely to result in a substantial lessening of competition in the mild steel market or the aluminium market due to only minor aggregation resulting from the acquisition and the presence of a number of large existing competitors.

Stainless Steel Market

5. The Commission considers that existing competition is likely to constrain the combined entity post acquisition due to:
   - the presence of five other large competitors ([ ]) that are likely to constrain the combined entity; and
   - the ability of mild steel distributors, as near competitors, to source stainless steel from existing channels to counter any effort by the combined entity to increase prices.

Overall Conclusion

6. The Commission considers that the presence of a number of large competitors [ ] and the ability of other steel and aluminium suppliers, as near competitors, to source other types of steel from existing channels are likely to sufficiently constrain the combined entity.

7. Therefore, the Commission is of the view that the proposed merger is unlikely to give rise to a substantial lessening of competition in the stainless steel, mild steel or aluminium markets.

8. Accordingly, pursuant to section 66(3)(a) of the Commerce Act 1986, the Commission determines to give clearance for the proposed acquisition by Atlas Group Holdings Limited of all the ordinary shares of Southward Engineering Limited.

THE PROPOSAL

1. A notice pursuant to s 66(1) of the Commerce Act 1986 (the Act) was registered on 8th April 2004. The notice sought clearance for the acquisition by Atlas Group Holdings Limited (Atlas) of all the ordinary shares of Southward Engineering Limited (Southward).

PROCEDURE

2. Section 66(3) of the Act requires the Commission either to clear or to decline to clear a notice given under s 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 4th May 2004.

3. 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.

4. The Commission's approach to analysing this proposed acquisition is based on principles set out in the *Commission's Merger and Acquisition Guidelines.*

STATUTORY FRAMEWORK

5. Under s 66 of the Act, the Commission may grant clearances for acquisitions where it is satisfied that the proposed acquisition would not have, or would not be likely to have, the effect of substantially lessening competition in a market. The standard of proof that the Commission must apply in making its determination is the civil standard of the balance of probabilities.[1]

6. The Commission considers that it is necessary to identify a real lessening of competition that is not minimal.[2] Competition must be lessened in a considerable and sustainable way. For the purposes of its analysis, the Commission is of the view that a lessening of competition and creation, enhancement or facilitation of the exercise of market power may be taken as being equivalent.

7. When the impact of market power is expected to be predominantly upon price, for the lessening, or likely lessening, of competition to be regarded as substantial, the anticipated price increase relative to what would otherwise have occurred in the market has to be both material, and able to be sustained for a period of at least two years.

8. Similarly, when the impact of market power is felt in terms of the non-price dimensions of competition such as reduced service, quality or innovation, for there to be a substantial lessening, or likely substantial lessening, of competition, these also have to be both material and sustainable for at least two years.

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[1] Foodstuffs (Wellington) Cooperative Society Limited v Commerce Commission (1992) 4 TCLR 713-722.
[2] See Fisher & Paykel Limited v Commerce Commission (1996) 2 NZLR 731, 758 and also Port Nelson Limited v Commerce Commission (1996) 3 NZLR 554.

ANALYTICAL FRAMEWORK

9. The Commission applies a consistent analytical framework to all its clearance decisions. The first step the Commission takes is to determine the relevant market or markets. As acquisitions considered under s 66 are prospective, the Commission uses a forward-looking type of analysis to assess whether a lessening of competition is likely in the defined market(**s**). Hence, an important subsequent step is to establish the appropriate hypothetical future with and without scenarios, defined as the situations expected:
   - with the acquisition in question (the factual); and
   - in the absence of the acquisition (the counterfactual).

10. The impact of the acquisition on competition is then viewed as the prospective difference in the extent of competition in the market between those two scenarios. The Commission analyses the extent of competition in each relevant market for both the factual and counterfactual scenarios, in terms of:
    - existing competition;
    - potential competition; and
    - other competition factors, such as the countervailing market power of buyers or suppliers.

THE PARTIES

Atlas

11. Atlas is based in Australia and is listed on the Australian Stock Exchange. Atlas distributes stainless steel products, specialty steels and flat rolled aluminium products to a range of industries in New Zealand and Australia. Atlas's total group revenue for the year ended 30 June 2003 was A$281,624,000.

12. Atlas has been operating in New Zealand since 1934 and now employs 53 staff across five branches in Auckland, Wellington, Hamilton, Christchurch and Dunedin. Atlas's steel products and aluminium are sold to manufacturers, who then fabricate those products into a wide range of end products ranging from furniture tubing to wine vats.

Southward

13. Southward is a privately owned New Zealand company that manufactures and distributes stainless steel products, mild steels and aluminium sheet. Southward has been trading in New Zealand since 1936 and now employs 250 staff across its manufacturing and distribution operations. Southward's group revenue for the year ended 30 March 2004 was estimated to be [ ].

14. Southward manufactures stainless steel and light walled carbon steel tube and automotive exhaust systems under the "Southward Engineering" brand. The manufacturing plants are in Auckland and Christchurch.

15. Southward also distributes the above products, as well as, stainless steel products, carbon steel pipe, and flat rolled aluminium sheets to a range of industries in New

Zealand and Australia through its fully owned subsidiary, Stainless Alloys Ltd (Stainless). Stainless has been operating in New Zealand since 1980 and has four branches in New Zealand in Auckland, Hamilton, Wellington and Christchurch.

16. Stainless sells stainless steel products to manufacturers who then fabricate those products into a wide range of end products. Stainless' products are predominately sold to fabricators servicing the dairy and food manufacturing sectors.

OTHER RELEVANT PARTIES

Stainless Steel Distributors

17. There are a number of competing stainless steel distributors. Like Atlas and Southward, these distributors supply stainless steel products to a range of industries in New Zealand. The main distributors are:

- Corus New Zealand Limited (Corus);
- Sandvik New Zealand Limited (Sandvik);
- Mico Metals, a division of Mico Limited (Mico Metals);
- NZ Fasteners Limited (NZ Fasteners)
- Stainless Products Limited (Stainless Products)

Mild Steel Distributors

18. Similarly, there are a large number of competing mild steel distributors. They supply a wide range of mild steel to a range of industries in New Zealand. The main competing distributors include:

- Steel & Tube Holdings Limited (Steel & Tube);
- Fletcher Easysteel, a division of Fletcher Buildings Limited (Fletcher Easysteel)
- Vulcan Steel Limited;
- Kiwi Steel NZ Limited; and
- HJ Asmuss & Co Limited.

Aluminium Distributors

19. There are three other competing aluminium distributors. They supply aluminium products, including aluminium sheets, coil and plate, to a range of industries in New Zealand. The competing distributors include:

- Ullrich Aluminium Co Limited (Ullrich);
- Nalco New Zealand Limited (Nalco); and
- Mico Metals.

Customers

20. Customers of mild steel, stainless steel and aluminium are generally fabricators or manufacturers. Customers the Commission consulted were:

- NDA Engineering Limited; and
- Hendl & Murray Engineering Limited

PREVIOUS DECISIONS

21. The Commission has previously considered the steel industry in the course of a number of clearance applications, namely:

- Decision 376, Fletcher Challenge Steel Products Limited and Steel and Tube Holdings Limited, 4 November 1999 (declined);
- Decision 378, Fletcher Challenge Steel Products Limited and Steel and Tube Holdings Limited, 10 December 1999 (cleared);
- Decision 421, Fletcher Steel Limited and Steel & Tube Holdings Limited, 21 March 2001 (cleared); and
- Decision 427, Steel and Tube Holdings Limited and Fletcher Steel Limited, 27 April 2001 (cleared).

22. On 6th October 1999, Fletcher Steel sought clearance to acquire Steel & Tube. The acquisition resulted in aggregation in a number of steel distribution and processing markets. The majority of Commissioners declined to give clearance in two markets while the minority dissented. The majority and the minority were in agreement in respect of the market definitions. The two markets in question were the national market for the distribution of merchant steel products and the national market for the distribution and processing of steel plate. The majority declined to give clearance due to high market aggregation, insufficient constraint from existing competitors, high barriers to entry and lack of countervailing power from small to medium customers.

23. In December 1999, Fletcher Steel re-applied for clearance with new information and expert reports on the two markets declined by the majority (Decision 378). By a majority of two to one, the Commission reversed its earlier decision in 376 and cleared the merger. The Commission considered that existing competition was sufficient to constrain the combined entity. The Commission also found low barriers to entry as well as evidence of recent entry and expansion. The minority view in Decision 378 was the same as the majority view in 376.

24. Decisions 421 and 427 again considered a proposed merger between Fletcher Steel and Steel & Tube due to the expiration of the clearance period from Decision 378 and a change in the acquisition structure. These Decisions were based largely on the information gathered in Decisions 376 and 378.

INDUSTRY BACKGROUND

25. Steel is an alloy of iron and carbon containing less than 2% carbon with smaller amounts of other elements such as manganese, silicon, phosphorus, sulphur and oxygen.

26. Steel is made by two basic processes - from raw materials including iron ore, limestone and coke along with recycled steel by the blast furnace and basic oxygen furnace method, or from recycled steel via the electric arc furnace method.[3] There are currently more than 3,500 different grades of steel with many different properties - physical, chemical, and environmental, 75% of which have been developed in the last 20 years.[4]

27. An important differentiation in the steel industry is based essentially on the chemistry of the steel. Three main types of steel can be distinguished - carbon steel (mild steel), stainless steel, and special steels. For the purposes of this report there is no need to discuss the special steels any further as no competition issues arise in relation to these types of steel.

Mild Steel

28. Crude steel is formed into semi finished or finished products, which are sold to processors and manufacturers. The semi finished products are steel slabs, billets and blooms. Steel slabs go through further processing to produce hot or cold rolled flat products such as plates, coils or sheets. These products are generally known as mild steel products and are the most commonly used types of steel. Blooms and billets can be further processed to produce hot-rolled long products such as tube, pipe, and bars. Some of these products are also known as mild steel, the others being known as special steels.

29. While mild steel is predominately imported from Asia, Europe and North America, there are two producers of mild steel in New Zealand - New Zealand Steel and Pacific Steel. New Zealand Steel produces 'flat' steel products, slabs, which are formed into plate and coil (mild steel), and 'long' steel products, which are formed into special steel. Pacific Steel produces 'long' steel products, blooms and billets which are formed into reinforcing and special steel products.

Stainless Steel

30. Stainless steel is a low carbon steel that contains 10.5% or more chromium by weight. It is this addition of chromium that gives the steel its stainless, corrosion resisting properties. There are over 60 different stainless steel grades, but about 15 or so are the most commonly used.[5] The chromium content of the steel allows the formation of a rough, adherent, invisible, corrosion-resisting chromium oxide film on the steel surface. If damaged mechanically or chemically, this film is self-healing, providing that oxygen, even in very small amounts, is present. Other alloying elements such as nickel, are added to increase the corrosion resistance, improve the fabrication properties, increase the high temperature performance and improve the machining characteristics.

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[3] International Iron & Steel Institute, http://www.worldsteel.org/understanding/3
[4] International Iron & Steel Institute World Steel in Figures 2003 Edition, http://www.worldsteel.org/figures.php
[5] The Stainless Steel Information Centre, Specialty Steel Institute of North America, http://www.ssina.com/stainless/index.htm

31. Stainless steel is used in many everyday applications in hospitals, food processing, farming, aerospace and in many other areas. Stainless steel is not just one alloy but a series of different compositions designed to provide specific properties and designed for different applications.

Aluminum

32. Aluminium ore, most commonly bauxite, is plentiful and occurs mainly in tropical and sub-tropical areas: Africa, West Indies, South America and Australia. There are also some deposits in Europe. Bauxite is refined into aluminium oxide trihydrate (alumina) and then electrolytically reduced into metallic aluminium. Primary aluminium production facilities are located all over the world, often in areas where there are abundant supplies of inexpensive energy, such as hydro-electric power. Comalco New Zealand exports almost all of its aluminium but the Commission understands that a very small amount is supplied to New Zealand aluminium distributors.[6]

33. Aluminium can be rolled into plate, sheets, or wafer thin foils the thickness of a human hair. The rolling process changes the characteristics of the metal, making it less brittle and more ductile. Aluminium can be extruded by heating it to around 500ºC and pushing it through a die at great pressure to form intricate shapes and sections. Aluminium can be forged by hammering to make stress-bearing parts for aircraft and internal combustion engines.

34. Aluminium has a wide variety of applications including aviation, engines in cars and trucks, as well as the marine industry. It is also used in packaging, construction, electrical and general manufacturing. Aluminium has a number of special properties insofar as it is lightweight, recyclable, soft and ductile, and is highly conductive, thermally and electrically.

Distribution of Stainless Steel, Mild Steel and Aluminum

35. Suppliers of stainless steel, mild steel and aluminium import the majority of their products from overseas mills or through trading houses.

36. New Zealand Steel and Pacific Steel export the majority of their steel but do supply around [ ] tonnes of mild and special steels to New Zealand steel distributors. New Zealand Steel advised the Commission that it supplies some customers direct if it involves very large volumes.

37. The products are stored in large warehouses. Due to its greasy and dirty nature, carbon steel is rarely stored in the same warehouse as "clean" metals such as stainless steel and aluminium. The products are distributed around the country in two ways:

- A centralised distribution system whereby the stock is located in Auckland and then transported via rail or truck to customers throughout New Zealand.
- A series of branches through New Zealand servicing both large and smaller cities.

[6] For example, Comalco supplies a very small amount of aluminium logs to [ ]

38. The centralised distribution system is aimed at customers who require larger amounts of steel for a planned project, while the branch networks are better suited to capturing local customers and "one-off" purchases of smaller amounts.

MARKET DEFINITION

39. 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.

40. For competition purposes, a market is defined to include all those suppliers, and all those buyers, between whom there is close competition, and to exclude all other suppliers and buyers. The focus is upon those goods or services that are close substitutes in the eyes of buyers, and upon those suppliers who produce, or could easily switch to produce, those goods or services. Within that broad approach, the Commission defines relevant markets in a way that best assists the analysis of the competitive impact of the acquisition under consideration, bearing in mind the need for a commonsense, pragmatic approach to market definition.[7]

41. For the purpose of competition analysis, the internationally accepted approach is to assume the 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, would be able to impose at least a small yet significant and non-transitory increase in price, assuming all other terms of sale remain constant (the SSNIP test). The smallest space in which such market power may be exercised is defined in terms of the five dimensions of a market discussed below. The Commission generally considers a SSNIP to involve a five to ten percent increase in price that is sustained for a period of one year.

Product Market

42. Initially, markets are defined for each product supplied by two or more of the parties to an acquisition. For each initial market so defined, the Commission considers whether the imposition of a SSNIP would be likely to be profitable for the hypothetical monopolist. If it were, then all of the relevant substitutes must be incorporated in the market.

43. The greater the extent to which one good or service is substitutable for another, on either the demand-side or supply-side, the greater the likelihood that they are bought and supplied in the same market. The degree of demand-side substitutability is influenced by the extent of product differentiation.

44. 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.

45. 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

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[7] Australian Trade Practices Tribunal, *Re Queensland Co-operative Milling Association*, above note 10; *Telecom Coporation of NZ Ltd v Commerce Commission & Ors* (1991) 3 NZBLC 102,340 (reversed on other grounds).

additional investment in sunk costs, when they are given a profit incentive to do so by a small change in their relative prices.

46. The Applicant's market definition was the national distribution of steel products. This included the distribution of mild steel, stainless steel and aluminium. It is within these three products that aggregation occurs. The Applicant contends that this broad market definition is appropriate given the strong supply side substitutability in the market. The Applicant stated: [8]

> We believe supply side substitutability where the functional dimension of the market is solely distribution is sufficient enough to include the various product lines, both in terms of the form of product (e.g. sheet, plate, pipe, tube) and steel type (carbon, mild, galvanised, stainless). Essentially most steel distributors would be able to expand product lines simply by sourcing from manufacturers or importers additional products and utilising existing distribution channels and spare warehousing capacity.

Supply Side Substitution

47. The supply side substitutability suggested by the Applicant in respect of broader categories of stainless steel, mild steel and aluminium was tentatively confirmed by other suppliers in the industry. Technically, there is little to prevent established mild steel, stainless steel, or aluminium suppliers from distributing another of these metal products.

48. The Commission notes, however, that a distributor of mild steel does not generally also stock stainless steel or aluminium. This is because mild steel is "dirty" and cannot generally be stored in the same warehouse as stainless steel and aluminium. A supplier of mild steel would need to obtain new warehousing space to commence supplying significant volumes of stainless steel or aluminium. In contrast, stainless steel and aluminium, which are "clean", can be stored in the same warehouse. Consequently, there is scope for suppliers to distribute both stainless steel and aluminium. Mico Metals, Atlas and Southward are examples of suppliers who distribute both aluminium and stainless steel.

49. In general, industry participants all agreed that there is some scope for supply side substitutability between stainless steel, aluminium and mild steel in that some can supply more than one of the metals. However, they noted that in practice, suppliers focus on either mild steel, stainless steel or aluminium due to:

- the customer base being specific to the product, a manufacturer using stainless steel rarely purchases mild steel;
- specific industry knowledge in respect of overseas and local contacts;
- technical knowledge in respect of specific metals; and
- stock management and credit facilities.

50. [

[8] Atlas's Public Application (file 6436) at page 7,Paragraph 11.4, http://www.comcom.govt.nz/adjudication/documents/s6667/331677_1.pdf

]

51. On the other hand, the Commission notes that large mild steel distributors are able to source other steel and metal for customers on both a regular and a "one-off" basis. [

]

52. On balance, the Commission considers that there is some scope for supply side substitutability between the supply of stainless steel, mild steel and aluminium.

Demand Side Substitution

53. Mild steel, stainless steel, aluminium and other steels are generally not substitutable from a demand-side perspective, as their form and function are specific for the purpose to which they are used. For example, aluminium used in the construction of planes cannot be substituted with stainless steel or mild steel because aluminium is a uniquely light compound. Mr Ron Murray, Managing Director, Hendl & Murray Engineering Ltd (Hendl), a large stainless steel fabricator, stated that stainless steel is used by dairy and foodstuffs manufacturers for its specific hygienic properties and cannot be substituted by mild steel or aluminium.

54. There are some very limited circumstances where stainless steel, mild steel and aluminium might be used for similar purposes.[9] However, industry participants stated that the price of stainless steel was around three times that of mild steel and indicated that the price of stainless steel would need to rise at least 30% before customers would consider switching to mild steel.

55. While the Commission notes that there is some scope for supply side substitutability between stainless steel, mild steel and aluminium, it considers that defining stainless steel, mild steel and aluminium as separate product markets is appropriate because:
    - of the very limited demand side substitutability between stainless steel, mild steel and aluminium; and
    - if no substantial lessening of competition is found in the narrower market, it is unlikely a substantial lessening of competition exists in the wider market.[10]

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[9] For example, a stairway handrail or furniture tubing could be made from stainless steel, aluminum, or painted mild steel depending on the design requirements.

[10] This approach is supported by a number of Commission decisions including Decision 376 *Fletcher challenge Steel Products Ltd & Steel & Tube Holding Ltd, 4 November 1999,* Decision 463 *Reyrolle Pacific Holdings Limited & VA Tech Reyrolle Pacific Limited 01 July 2002,* Decision 509 *Schneider Electric SA & the Gerard Industry Group of companies, 7 October 2003.*

56. Accordingly, the Commission considers the appropriate product markets are for the supply of:
    - stainless steel;
    - mild steel; and
    - aluminium.

Functional Markets

57. The production, distribution and sale of a product typically occur through a series of functional levels, conventionally arranged vertically in descending order. Generally, the Commission identifies separate relevant markets at each functional level affected by an acquisition, and assesses the impact of the acquisition on each.

58. The Applicant submitted that the functional level of the businesses of Atlas and Southward is distribution.

59. Some very large manufacturers, such as Fisher & Paykel, who require large volumes, have by-passed distributors and imported directly. However, such importing was considered to be rare and confined to very few manufacturers. This was confirmed by customers who advised that it was not feasible to import directly due to the inherent risks associated with importing such as fluctuating exchange rates and transport logistics. Alan Hickman, Contracts Engineer, NDA Engineering Ltd (NDA), for example, noted that he was reluctant to import as he valued the continuity of supply guaranteed by New Zealand distributors.

60. The Commission therefore considers the functional level to be distribution.

Geographic Markets

61. The Commission defines the geographic dimension of a market to include all of the relevant, spatially dispersed sources of supply to which buyers would turn should the prices of local sources of supply be raised.

62. The Applicant submitted that the geographic dimension of the market is national. Distributors advised the Commission that they competed nationally whether it be through the tender process for large projects or via a branch network or sales representatives for "one-off" sales and smaller volumes in smaller regions.

63. The Commission recognises that local customers purchasing small quantities or "one-off" purchases may be unlikely to source metals outside their region due to transport costs. In order to ensure that the proposed acquisition is not likely to affect one specific regional area, the Commission considered the geographic location of the branch networks of stainless steel suppliers.[11] It was found that all of the suppliers of stainless steel have branches in the main centres. Some have wider branch networks while one

[11] Given the small market share that would be held by the combined entity post acquisition in the mild steel and aluminium markets, the Commission has not considered these markets for the purposes of the geographic dimension of the market definition analysis.

only operates out of Auckland. Table 1 illustrates the branch locations of the stainless steel suppliers in New Zealand.

Table 1 Branch locations of stainless steel suppliers

Corus	Mico	Sandvik	NZ Fasteners	Atlas	Southward	Stainless Products
Auckland	Auckland	Auckland	Auckland	Auckland	Auckland	Auckland
Hamilton	Hamilton		Hamilton	Hamilton	Hamilton	
Tauranga	Mt Maunganui					
New Plymouth	New Plymouth		New Plymouth			
Hastings						
	Palmerston		Palmerston			
Wellington	Wellington	Wellington		Wellington	Wellington	
Nelson	Nelson		Nelson			
	Blenheim					
Christchurch	Christchurch	Christchurch	Christchurch	Christchurch	Christchurch	
	Dunedin			Dunedin		
	Invercargill					

64. Atlas, Southward and the other distributors have national reach through their branch networks. The Commission notes that there is only one region, Dunedin, where the number of competitors is limited. However, as Southward does not have a branch located in Dunedin, the competitive environment would not change post acquisition.

65. Accordingly, for the purposes of this Application, the Commission considers the appropriate geographic dimension to be national.

Conclusion on Market Definition

66. The Commission concludes that the relevant markets are:

- The national market for the distribution of stainless steel (the stainless steel market);
- The national market for the distribution of mild steel (the mild steel market); and
- The national market for the distribution of aluminium (the aluminium market).

COUNTERFACTUAL AND FACTUAL

67. In reaching a conclusion about whether an acquisition is likely to lead to a substantial lessening of competition, the Commission makes a "with" and "without" comparison rather than a "before" and "after" comparison. The comparison is between two hypothetical future situations, one with the acquisition (the factual) and one without (the

counterfactual).[12] The difference in competition between these two scenarios is then able to be attributed to the impact of the acquisition.

Factual

68. In the factual scenario the combined entity would operate in the markets defined by the Commission. Several other players including Corus, Mico, Sandvik and NZF will also operate in the markets identified.

69. [ ]

70. [ ]

Counterfactual

71. [ ]

72. The Commission considers that [ ]

73. The Commission is of the view that the more conservative position, for the purposes of competition analysis, [ ]

COMPETITION ANALYSIS

Existing Competition

74. Existing competition occurs between those businesses in the market that already supply the product, and those that could readily do so by adjusting their product-mix (near competitors). Supply-side substitution by near competitors arises either from redeployment of existing capacity, or from expansion involving minimal investment, in both cases involving a delay of no more than one year.

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[12] Commerce Commission, *Decision 410: Ruapehu Alpine Lifts Ltd/Turoa Ski Resorts Ltd (in receivership), 14 November 2000*, paragraph 240, p 44.

75. An examination of concentration in a market can provide a useful indication of the competitive constraints that market participants may place upon each other, providing there is not significant product differentiation. Moreover, the increase in seller concentration caused by a reduction in the number of competitors in a market by an acquisition is an indicator of the extent to which competition in the market may be lessened.

76. The Commission identifies market shares for all significant participants in the relevant market. Market shares can be measured in terms of revenues, volumes of goods sold, production capacities or inputs (such as labour or capital) used.

77. An aggregation that would result in a low concentration level is unlikely to be associated with a substantial lessening of competition in a market. On this basis, indicative safe harbours may be specified.

78. 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%.

79. The Commission recognises that concentration is only one of a number of factors to be considered in the assessment of competition in a market. In order to understand the impact of the acquisition on competition, and having identified the level of concentration in a market, the Commission considers the behaviour of the businesses in the market. Specifically, the Commission seeks to understand the dynamics of the competition that would exist between the remaining firms in the market, compared to what would exist in the absence of the acquisition.

The Mild Steel Market

80. Atlas distribute heavy wall seamless carbon steel pipe that is used for mechanical or hydraulic engineering. Atlas's annual revenue from this product is [ ]. Southward supplies light wall welded seam carbon steel tube and carbon sheet and plate. Southward's annual revenue from these products is [ ]. The total market for the distribution of mild steel is estimated to be [ ]. Post acquisition, the combined entity would account for [ ]% of the market.[13]

81. Given the small market share that would be held by the combined entity and the presence of a number of large suppliers of mild steel, the Commission does not consider the level of aggregation merits further examination in the competition analysis.

[13] These figures reflect the estimated market shares of the combined entity and other competitors in the market based on figures provided by the Applicant and information obtained in the course of the Commission's investigation.

82. The Commission concludes that the proposed acquisition is unlikely to result in a substantial lessening of competition in the mild steel market due to only minor aggregation and the presence of a number of large existing competitors.

The Aluminium Market

83. Atlas's annual revenue from the distribution of its aluminium products is [ ]. Southward also supplies aluminium sheet and its annual revenue from these products is [ ]. The total market for the distribution of aluminium is estimated to be [ ]. Post acquisition, the combined entity would account for [ ]% of the market. The two largest distributors, Ullrich and Mico Metals account for approximately [ ] of the market. Nalco estimates it has about [ ]% of the market.[14]

84. Given the small market share that would be held by the combined entity and the presence of three larger aluminium suppliers, the Commission does not consider the level of aggregation merits further examination in the competition analysis.

85. The Commission concludes that the proposed acquisition is unlikely to result in a substantial lessening of competition in the aluminium market due to only minor aggregation and the presence of a number of large existing competitors.

The Stainless Steel Market

86. The Commission considers the appropriate measure to determine market share in this market is the revenue earned from the sales made of the products represented in the stainless steel market. Table 2 below sets out the estimated market shares of the combined entity and other competitors in the stainless steel market based on figures provided by the Applicant and information obtained in the course of the Commission's investigation.

[14] These figures reflect the estimated market shares of the combined entity and other competitors in the market based on figures provided by the Applicant and information obtained ed in the course of the Commission's investigation. It excludes aluminium imported directly by end users such as cans and cooking foils.

Table 2: Market Shares for the Stainless Steel Distribution Market 2003

[ ]	Company	2003 ($ million)	Market share (%)
[ ]	Corus	[ ]	[ ]
[ ]	Mico Metals	[ ]	[ ]
[ ]	Sandvik	[ ]	[ ]
[ ]	NZ Fasteners	[ ]	[ ]
[ ]	Southward	[ ]	[ ]
[ ]	Atlas	[ ]	[ ]
	COMBINED ENTITY	**[ ]**	**[ ]**
[ ]	Stainless Products	[ ]	[ ]
[ ]	Fletcher Easysteel	[ ]	[ ]
	TOTAL	**[ ]**	**100**

87. Post acquisition, the combined entity would have a combined market share of [ ]%. The current three firm concentration ratio is [ ]%. Post acquisition the three firm concentration ratio would be unaffected. The market shares in the market would be within the Commission's safe harbours guidelines.

88. Market shares are insufficient in themselves to establish whether competition in a market has been lessened. It is the interplay between a number of competition factors, of which seller concentration is only one that has to be assessed in determining the impact of a business acquisition on competition.

89. Post acquisition, the combined entity would be the [ ] largest provider of stainless steel. The combined entity would continue to face strong competition from existing competitors such as Corus, Mico Metals, Sandvik and NZ Fasteners. [ ]

90. [ ]

91. The Commission spoke with NDA and Hendl which are both large customers of Atlas and Southward. Alan Hickman, Contracts Engineer for NDA stated that he considered that post merger there were enough players to maintain healthy competition and that NDA is easily able to switch between stainless steel distributors. Similarly, Ron Murray, Managing Director of Hendl advised the Commission that there was healthy competition and that there are numerous options outside Atlas and Southward.

92. Mild steel distributors, as near competitors, can source stainless steel for customers through existing supply channels which acts as a further constraint on the pricing of the combined entity. [ ]

Conclusion on Existing Competition

93. The Commission considers that existing competition would be likely to constrain the combined entity post acquisition due to:

- the presence of five other large competitors [ ]; and
- the ability of suppliers of mild steel distributors, as near competitors, to source stainless steel from existing channels to counter any effort by the combined entity to increase prices.

94. The Commission concludes that the proposed acquisition is unlikely to result in a substantial lessening of competition in the stainless steel market due to the presence of considerable existing competition.

OVERALL CONCLUSION

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

- The national market for the distribution of stainless steel (the stainless steel market).
- The national market for the distribution of mild steel (the mild steel market).
- The national market for the distribution of aluminium (the aluminium market).

96. The Commission considers that the appropriate counterfactual is [ ]

97. The Commission is satisfied that the proposed acquisition would not have nor would be likely to have the effect of a substantial lessening of competition in the stainless steel market, the mild steel market or the aluminium market due to the constraint on the combined entity that would be provided by existing competition.

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

- stainless steel market;
- mild steel market; and
- aluminium market.

DETERMINATION ON NOTICE OF CLEARANCE

99. Pursuant to section 66(3)(a) of the Commerce Act 1986, the Commission determines to give clearance for the proposed acquisition by Atlas Group Holdings Limited of all the ordinary shares of Southward Engineering Limited.

Dated this 4th day of May 2004

Peter JM Taylor
Division Chair
Commerce Commission