COMMERCE ACT 1986: BUSINESS ACQUISITION
SECTION 66: NOTICE SEEKING CLEARANCE

Date: 19 November 2007

The Registrar
Market Structure Group
Commerce Commission
PO Box 2351
WELLINGTON

Pursuant to s66(1) of the Commerce Act 1986 notice is hereby given seeking **clearance** of a proposed business acquisition.

OVERVIEW

1. A merger is proposed between Provenco Group Limited ("**Provenco**") and Cadmus Technology Limited ("**Cadmus**"), both New Zealand listed public companies.

2. Provenco and Cadmus operate in highly competitive and dynamic technology markets locally and offshore. These markets are dominated by much larger global competitors. The objective behind the merger is to scale up their businesses to:

   2.1. expand their operations overseas in competition with those same large global players, and

   2.2. enhance their ability to adapt to changing competitive conditions through the emergence of new technologies and business models.

3. The businesses of Provenco and Cadmus are similar to an extent but have significant differences and operate in different market segments. The area of overlap lies predominantly in the provision of electronic payment systems (although "payments" is estimated by Provenco to be approximately only **[ ]** of its total business, just one part of its offer to retailers). Specifically, both companies are device vendors of EFTPOS terminals and so the appropriate market definition for these purposes is that for the supply of EFTPOS terminals in New Zealand.

4. Cadmus is the only New Zealand manufacturer and exporter of its own terminals whereas Provenco is a supplier of imported terminals manufactured by much larger global players referred to above (eg, Hypercom). Other device vendors in New Zealand supplying terminals manufactured overseas include Quest, Viaduct, Ingenico, Tech Trans (NZ) Limited, DPS and EFTPOS New Zealand Limited ("**ENZ**" - owned by ANZ National bank. Other banks also direct a range of terminals to their end user customers).

5. The business of supplying terminals is commonly stratified into segments, described as "Enterprise" (largest users, such as supermarket chains and oil companies), "Commercial" (retail groups), "SME" (small to medium enterprises) and "Mass Market" (small traders). It is said that the volume business for terminals is in the bottom end but the volume of actual transactions is in the top end.

6. The Enterprise and Commercial segments (including businesses such as oil companies, retail chains, and the like) are quite different from the other segments. They are characterised by large and sophisticated end users prepared to look further afield for their requirements of complex technology packages with a range of features over their entire operations. All oil companies and one of the two supermarket chains, for instance, are controlled offshore and increasingly selection and sign-off occur offshore. As a result, BP uses the same terminals as in Australia (Quest), pursuant to the common trans-Tasman approach whereby business secured in Australia will include New Zealand as an "add-on", as does Woolworths. Caltex/Chevron, Wesfarmers, DFS and Reading Cinemas are also examples where local product offerings have been selected by trans-Tasman businesses.

7. The SME and Mass Market segments, on the other hand, are characterised by more straightforward EFTPOS terminal packages and range of suppliers accordingly. In the SME and Mass Market segments, a merchant (retailer, service, hospitality etc) often obtains EFTPOS by asking its bank. In this sector terminal supply is vendor agnostic; the terminal supplied by the bank is accepted by the merchant in the bundle offered (because the merchant wants settlement of credit and debit card transactions and does not care whose terminal is supplied). Equally, in New Zealand, a large proportion of users are supplied by re-sellers, or dealers, who obtain devices from vendors (primarily Provenco) and re-sell them to users in the SME and Mass Market segments with other products/services.

8. Cadmus primarily sells direct to the Mass Market and SME segments whereas Provenco's direct marketing focus is primarily on Enterprise and Commercial (approximately **[ ]** of its non-wholesale business). Provenco does compete with Cadmus through its out-bound call centre operation called Netco which does direct business into the bottom two segments. The largest part of Provenco's business is, however, supplying terminals to dealers (approximately **[ ]** of its business) who re-sell into those segments.

9. ENZ (owned by ANZ National) is a significantly vertically integrated competitor and has the advantage of Bank parent backing which can exercise control of its percentage share of merchant business (it is believed the other banks are also able to influence their respective shares). It is the second largest supplier of terminals in New Zealand (just behind Provenco and ahead of Cadmus), and growing. By virtue of its position as a substantial issuer of credit cards, as an acquirer of merchant transactions and as well as being the owner of one of the two switches in New Zealand, it is uniquely placed to grow its volume of terminal supplies to the detriment of both applicants. ANZ National have approximately 40% of the acquiring market in New Zealand.

10. There is an accelerating trend worldwide (and locally) for terminals to become commoditised, forming only a minor part of a technology solutions package that may include POS ("Point of Sale") hardware and software, system support, telecoms (whereby EFTPOS can be bundled with provision of telco broadband services) and related products and services. The price for terminals has been declining significantly over the last five years (see table in Appendix 1), and this is now merchant expectation. Margins on terminals have deteriorated, and will continue to do so, as a result, and the ability to charge for a value proposition depends on innovating and supplying other features. Local manufacture has been further pressured by the strong New Zealand dollar, making imports cheaper.

11. There is no cross-over between the applicants in market segments. Competition in the market for the supply of EFT terminals and related products and services will not be lessened as a result of the merger, because:

11.1. Provenco is only a supplier of terminals manufactured offshore. **[ ]** its contract with Hypercom is currently exclusive **[**

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11.2. As evidenced by the proliferation of new suppliers in recent years, there are sufficient other terminal suppliers able to supply users in competition with the merged entity. There are no significant barriers to entry. There is a degree of homogenisation of aspects of terminal standards globally, such as EMV and PCI compliance and other features, which facilitates further expansion or entry by global suppliers.

11.3. At the top end of the market, not only are there credible alternatives, but the customers themselves (particularly trans-Tasman organisations) have countervailing power. A number of large local users of terminals are also Australian owned and can and do introduce their own terminal suppliers to their New Zealand operations. There are examples of local relationships being lost to a competitor used by the Australian parent company. At the mass-market end, competition is varied.

11.4. The current pressures driving down terminal pricing will not diminish. Overseas trends (followed in New Zealand) are that terminals have become commoditised, with the hardware squeezed and value being created in software and add-ons.

11.5. The dealers are not exclusive to any device vendor.

11.6. ENZ is and will continue to be a strong, active, vertically integrated competitor, bundling acquiring services with terminals so as to increase the number of merchants signed up to ANZ National's network. It already represents approximately 40% of the acquirer market (ANZ National currently forward all terminal leads directly to ENZ).

11.7. There is increasing competition from new business models in the way payments are made and who is providing the services, including telcos bundling terminals as loss leaders with telco packages. That is likely to increase with emerging technologies and as businesses up and down the supply chain also inhabit space occupied by device vendors.

11.8. There is a degree of market power residing in the major banks generally, able to influence the terminals market through ETSL (specifications, sunset dates, certifications and implementations of new compliance standards). There is always an opportunity for the Banks to adopt the same model of EFTPOS supply themselves as is the practice in Australia. Indeed, this was the origin of ANZ's move into EFTPOS with the purchase of ENZ in 2000.

11.9. It is unlikely that the merged entity could itself attempt to exercise market power, without losing market share. Nor would the market structure created appear likely to have the characteristics whereby non-coordinated or coordinated effects would occur. The presence of ENZ, large global participants, a range of differentiated service offerings (often bundled) and the many permutations of business models and customer relationships count against it.

12. By virtue of their status as listed public companies and the apparent aggregation in supply of terminals, this application is being made out of responsibility and an abundance of caution. However, the applicants are firmly of the view that the merger would not lessen competition in any market and that, in fact, it is a highly desirable transaction which will improve the competitiveness of two New Zealand based companies in the face of global competition.

PART I: TRANSACTION DETAILS

1. **THE BUSINESS ACQUISITION**

1.1. Clearance is sought for a merger transaction whereby Cadmus and Provenco will amalgamate pursuant to Part XIII of the Companies Act 1993, in terms set out in the conditional Merger Implementation Agreement executed by them.

2. **PERSON GIVING NOTICE**

2.1. This notice is given by:

Cadmus Technology Ltd
182-190 Wairau Road
Glenfield
AUCKLAND

Provenco Group Ltd
25 College Hill
Ponsonby
AUCKLAND

2.2. All correspondence and notices in respect of this application should be directed in the first instance to:

Matthew Dunning
Barrister
Park Chambers
PO Box 5844
Wellesley Street
Auckland

Ph: (09) 379 9780
Fax: (09) 377 0361

3. **CONFIDENTIALITY**

3.1. Confidentiality is sought in respect of all items deleted from the public copy of this application ("**confidential information**") and identified in square brackets.

3.2. A confidentiality order is sought under s 100 of the Commerce Act 1986 ("**Act**") for the confidential information, and confidentiality is claimed under section 9(2)(b)(ii) of the Official Information Act 1982 on the grounds that the information is commercially sensitive and valuable information which is confidential to the participants, and disclosure of it is likely to give unfair advantage to competitors and/or unreasonably prejudice the commercial position of the participants.

3.3. The participants request that they be notified of any request made to the Commission for release of any of their confidential information, and that the Commission seeks their views as to whether the information remains confidential and commercially sensitive, at the time responses to such requests are being considered.

4. DETAILS OF THE PARTICIPANTS

4.1. Cadmus is a listed public company with a market capitalisation of approximately $40 million. It designs, develops and implements electronic point-of-sale payment solutions for merchant businesses in New Zealand and overseas. It is the only New Zealand manufacturer and exporter of payment terminals. Further information can be obtained from its website: www.cadmustechnology.com.

4.2. Provenco is also a listed public company, with a market capitalisation of approximately $80 million. It is a supplier of technology to businesses in New Zealand and overseas, founded in EFTPOS and payment solutions but now extending across a range of technology applications for the retail environment. Its diverse operations range from forecourt solutions for oil companies, payment technology and EFTPOS in the domestic New Zealand market, retail technology for the Australian market and distribution of retail, bar-coding and mobile and wireless technology in Asia-Pacific. Approximately only **[ ]** of its business is in "payments" as such. Further information can be obtained from its website: www.provenco.com.

5. INTERCONNECTED AND ASSOCIATED PARTIES

5.1. Nil.

6. BENEFICIAL INTERESTS

6.1. Neither of the participants currently holds any interests in the other.

7. LINKS BETWEEN COMPETITORS

7.1. There are currently no links between either of the participants.[1]

8. CROSS DIRECTORSHIPS

8.1. There are currently no cross-directorships.

9. BUSINESS ACTIVITIES OF EACH PARTICIPANT

9.1. See section 4 above, and details at the respective websites.

10. REASONS FOR THE PROPOSAL

10.1. The markets in which the participants compete are global, with many large players. Like many companies developed in the small domestic New Zealand market, they need to attain global significance to survive. New Zealand is also a well saturated, mature market with relatively flat growth[2], whereas globally the

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[1] Cadmus was once a dealer, re-selling Hypercom products sourced from Provenco, but then developed its own product and moved away accordingly. It still re-sells some Hypercom product sourced from Provenco.

[2] New Zealand has the highest incidence of EFTPOS terminals to head of population in the world, with one terminal for every 34 people at the end of 2005: "Banking in New Zealand" (Fourth Edition), New Zealand Bankers Association, page 15.

terminal supply market is forecast to grow significantly, particularly in emerging economies of Eastern Europe and Asia-Pacific. Both companies seek to scale up their businesses to improve their international competitiveness for this reason. While they are innovative, successful companies in the domestic space, both have struggled to achieve any consistent profitability. They have grown to the point where they need critical mass to achieve outcomes offshore and to enhance their ability to adapt to changing competitive conditions. The higher New Zealand dollar is a major reason that the imported cost of terminals is lower. Foreign competitors benefit from much larger production scale. To combat this, greater scale is necessary to reduce manufacturing costs at the same time as increasing total returns from the manufacturers margin and increasing competitiveness. As well as gaining new offshore markets, [

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10.2. The New Zealand developed and manufactured Cadmus products combined with the expertise and network of Provenco, and their complementary technology solutions, will assist global expansion. There will be synergies across the different end user spaces each company presently individually markets to, savings in research and development and other costs.

PART II: IDENTIFICATION OF MARKETS AFFECTED

11. MARKET DEFINITION

11.1. Activity in respect of which the applicants overlap is in the New Zealand payments markets, through the provision of EFTPOS terminals, and supporting products and services, for electronic transactions.[3] Cadmus manufactures its own brand of terminal (and is the only New Zealand company to do so) whereas Provenco imports Hypercom, Keycorp and Thales terminals from overseas manufacturers.

11.2. In broad terms, payment "products" include cash, credit and debit payment cards, paper instruments and electronic. Payment channels include electronic, "over the counter" and rapidly growing internet.[4]

11.3. Players in payment markets include:

(a) the banks (as issuers and acquirers of debit and credit card transactions and facilitators of other payment methods, and providers of merchant services whereby credit and debit card transactions are facilitated and settled. In Australia, all major banks also supply EFTPOS terminals),

(b) payment "scheme" providers (ie, credit and debit card companies) including Visa, Mastercard, Amex, Diners, store cards and others,

(c) interchange, clearance and settlement system (ISL, owned collectively by banks),

(d) retail payment processing and switching (ETSL, owned by 4 major banks, and EFTPOS New Zealand Limited ("**ENZ**"), owned by ANZ bank: see Commission Decision No 507, *ANZ/NBNZ*)[5],

(e) "transacters" (merchants and others, and their customers), and

(f) device vendors (as well as "dealers" or resellers) such as Cadmus and Provenco which supply EFTPOS terminals (the devices through which a customer's card is "swiped") to merchants and others for electronic transactions to occur.[6]

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3 For a sufficiently accurate overview of the history and developing trends in EFTPOS in New Zealand, see http://en.wikipedia.org/wiki/Eftpos#New_Zealand.

4 See Australian Government Paper: "Exploration of Future Electronic Payments Market" (June 2006). On 9 May 2007, Payment Express was certified as the first IP/broadband certified terminal allowing EFTPOS transactions to be transmitted securely over the internet. Merchant IP Services (MIPS) is another alternative.

5 The industry is not neatly demarcated and different players often occupy multiple positions. ENZ is an example of this, see link http://www.eftpos.co.nz/gs_paymentprocess.html.

6 There could well be another category emerging; "third party switching (mainly loyalty and some financial) for value added applications". This is yet another example of how the market(s) are fragmenting (players including Smartpay (NZX:SPY), eazipay, DPS, evolution, Transactor). These players are presenting new offers overlapping the existing terminal market (they often include terminals) and are an increasing competitive force.

Also relevant participants (and emerging competitors) are telecommunications networks through which electronic transactions operate.

11.4. On one view of it, Cadmus and Provenco compete in just one part of an overall payment solutions market which includes all forms of payment and their respective channels referred to in 11.2 above. However, it is acknowledged that a more conservative approach would be appropriate in the first instance, and any constraint from other elements taken into account in the competition analysis.

11.5. Central to what both companies provide in the way of EFTPOS payment solutions is the hardware, ie EFTPOS terminals (including, and without which they would not operate as intended, their integral software). Accordingly, it is suggested that the appropriate market definition for these purposes is that for the manufacture or importation for supply of EFTPOS terminals in New Zealand.[7]

HORIZONTAL AGGREGATION

11.6. Provenco is only an importer/distributor and its role as a supplier of terminals derives entirely from its distribution arrangements with overseas manufacturers. Aggregation as a result of the proposed merger is on the face of it, therefore, potentially less permanent (as a matter of market structure) since continuation in that role is not entirely within its control.

11.7. Of the terminals it imports, those from Hypercom are imported pursuant to an exclusive distribution arrangement (dated 4 May 1996). However, that contract:

(a) **[**

(b)

(c)

7 Conceptually, because a significant portion of Provenco's business involves the supply of terminals to dealers for resale to end users, the market could appear to be divisible further: into a manufacturing/wholesale channel market and a retail (end users) market. However, such a distinction in the market definition is not particularly useful to the analysis nor determinative of any different outcome to the competition analysis. First, if there is a separate "wholesale" functional market, there is little or no aggregation (because Cadmus does not operate the same way as Provenco in this regard) so no serious examination of such a market would be required. Secondly, the ongoing availability of terminals in a competitive supply market post-merger is the fundamental question, the answer to which affects all purchasers equally, whether dealers or end users.

(d)

11.8. **[**

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12. DIFFERENTIATED PRODUCT MARKETS

12.1. To an extent: see 13.1 below.

13. NATURE OF DIFFERENTIATION

13.1. At the end user level, differentiation occurs through the packages of product/service/support offered . Technical specifications, and functionality, of hardware (and its attendant software) differ between suppliers, as does the level of service/support provided and other “add ons” (eg, bundled with telecommunications). In addition, like many complex technology markets with a number of participants, firms target and succeed in different business segments (for instance, Provenco has developed particular expertise in respect of forecourt retail solutions for oil companies. Cadmus does not offer a product in this sector in New Zealand).

13.2. However, in terms of the market definition above the same ultimate functionality is competed for and provided by all device vendors: an ability for users to conduct transactions with card holders electronically. Accordingly, for the purposes of the current analysis the EFTPOS terminal based payment solution packages supplied by Cadmus and Provenco would be viewed as substitutable for others in the market.

14. VERTICAL INTEGRATION

14.1. The merged entity will operate at the same levels as the participants do now. The proposal will not result in any material vertical integration effects.

15. PREVIOUS ACQUISITIONS AND COMMISSION NOTIFICATIONS

15.1. None applicable.

PART III: CONSTRAINTS ON MARKET POWER BY EXISTING COMPETITION

16. EXISTING COMPETITORS IN MARKET

16.1. As noted, all other suppliers in the market apart from Cadmus are importers of terminals manufactured overseas. There are numerous such manufacturers but by far the three largest (in order of size based on estimated sales of terminals in 2006: see table in Card Technology article, Appendix 2) are:

(a) Verifone (USA): 2,500,000.

(b) Ingenico (France): 2,200,000.

(c) Hypercom (USA): 800,000.

(Cadmus, in contrast, is reported in that articles as having sold approximately 27,000 terminals, locally and overseas, in the same period). Consolidation has occurred over recent years (Verifone acquired Lipman, and in July 2007 Ingenico announced negotiations to buy Sagem[8]), and appears likely to continue.

16.2. These brands are all present in New Zealand, as well as the following:

(a) Keycorp.

(b) Thales (via Keycorp).

(c) Intellect.

(d) Quest.

(e) Dione Lipman (owned by Verifone).

(f) Sagem (new entry via Keycorp).

16.3. Both Cadmus and Provenco supply their terminals direct to end users in different segments of the market, but a significant proportion of Provenco's business (approximately **[ ]**) is with dealers (or other re-sellers, such as banks), who then supply the terminals to end users (usually with other service "add-ons") in competition with Cadmus and Provenco and others. It is estimated that there are approximately at least 60 to 80 such dealers (Cadmus was itself one, originally). They are non-exclusive to any device vendor.[9]

16.4. The market tends to be stratified into segments, from Enterprise (largest users, such as supermarket chains and oil companies), Commercial (retail groups/chains), Small to Medium Enterprises (SME) down to "Mass Market"

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8 See http://bvcontent.verifone.com/VeriFone/Attachment/20070917/Verifone_Taxi,%20Investor's%20Business%20Daily.pdf and sample excerpts/publications in Appendix 2.

9 See for example: http://www.eftpos-specialists.co.nz/products.htm; http://store.viaductnz.co.nz/catalog/; http://www.eftpos.co.nz/bs_terminals.html; http://www.eftco.co.nz/

(small traders). It is said that the volume business for terminals is in the bottom end but the volume of actual transactions is in the top end. Cadmus primarily sells (direct) to the Mass Market and SME. It has virtually no custom in the top end Enterprise and Commercial segments. Provenco, on the other hand, focuses its direct sales (and, hence, customer relationships) on Enterprise and Commercial segments which deliver **[ ]** of its business. With **[ ]** of its business to "wholesale" customers, the remaining **[ ]** of its business is in competition with Cadmus and all the other direct to customer EFTPOS suppliers through its out-bound call centre operation called Netco which does direct business into the bottom two segments.

16.5. Terminals can be either sold outright (for approximately $1,400.00) or "leased" (typically for around $9 per week, but up to $12 to $15). The exact proportion between the two is not known exactly, due to the range of end user suppliers, but it is estimated that approximately 70% of terminals in New Zealand are leased. Many dealers hold "books" of customers to whom they lease terminals. Contracts are typically for a term of 36 to 48 months, with forced re-contracting or upgrades at the end of each term providing an opening for being contested by competitors. This had its genesis in the use of finance companies which would facilitate the Rental Agreement – allowing the Dealer to receive income and cash at the time of contracting. Dealers with stronger capital structure also rent the terminals direct and obtain better margins through not involving a middle man.

16.6. As security standards change, merchants are required to up-grade their terminal.[10] To compete for this up-grade business a number of pricing options are available:

(a) Deferred payment. The customer signs a new contract and receives the up-grade hardware but does not start to pay for it until the old contract expires. This is similar to the mass retail offers of "no payment for twelve months".

(b) Contract buy-out. Towards the conclusion of an existing contract term the customer signs a new contract with a new supplier who pays the remaining balance on the old contract. This is similar to the account credits Vodafone and Telecom provide if a customer moves from one network to the other.

(c) Free terminal. For some customers, they are eligible for a free terminal if they run a number of applications. The primary example of this is merchants who sell a lot of prepaid mobile phone top up vouchers will receive a free terminal.

[10] For instance, merchants who do not use an EMV certified terminal after 31 December 2007 will be liable for any fraud committed through use of their terminals.

16.7. Quite apart from specific upgrade instances, leased contracts come up for renewal at different times and there is a constant state of churn driven by high levels of telesales contact from the large number of direct EFTPOS suppliers competing for the business. This does not occur just at the end of a contract either: competitors approach users all the time with offers designed to make switching worthwhile (including innovative packages bundling other services, such as telecommunications or banking services).

16.8. It is difficult to obtain precise measurements of market shares. It is possible to estimate the total number of existing terminals in use (from information published by the NZ Bankers Association:[11] 125,000 terminals in 2006 and connection data with ETSL: 100,000 terminals. So, approximately 20%, or 25,000 terminals, are also connected through ENZ). However, that figure is more of contextual interest than specific relevance: it does not of itself reflect current shares of business and the customer relationships driving ongoing sales. Ongoing sales reflect "churn" of the existing terminal base (influenced by previous sales, service and lease relationships, among other things) plus whatever new users emerge.[12] It is estimated that "sales" in the financial year to June 2007 numbered approximately **[ ]** terminals (comprising replacement and new).

16.9. Current market participants and available brands in the market are provided in the following table.

Table 1: Vendors and brands

Vendor	Manufacturer
Provenco www.provenco.com	Hypercom, Keycorp, Thales (direct & through dealers)
Cadmus www.cadmus.co.nz	Cadmus
ENZ www.eftpos.co.nz	Verifone, Keycorp, Hypercom, Ingenico
TTL www.ttlnz.co.nz	Verifone
Skyzer www.skyzer.co.nz	Ingenico
DPS www.dps.co.nz	Verifone
Dealers	Hypercom (via Provenco), Keycorp, Verifone, Ingenico
Westpac	Preferred supplier agreements with Provenco and TTL
Quest www.questpaymentsystems.com	Quest

11 NZ Bankers Association: http://www.nzba.org.nz/Public%20Payment%20Statistics%202006.htm

12 Many new users will obtain their terminals through their bank, along with other products and services.

16.10. Shares of direct to end user/customer relationships are estimated to be as set out in the following table.

Table 2: Estimated share of sales to end users – past 12 months

Provenco	**[ ]**
Cadmus	**[ ]**
ANZ National	**[[13]]**
Independent re-sellers and banks (excluding ANZ National)	**[[14]]**

It is likely that post merger shares will be less than the combined total of both participants, due to some business inevitably being lost in the process.[15]

17. CONDITIONS TO EXPANSION BY EXISTING COMPETITORS

17.1. Barriers to entry or expansion are insignificant. For a terminal to be used in New Zealand, it is required only to be:

(a) suitably certified to the satisfaction of the banking system. Previously, New Zealand had its own hardware standard, but is now moving to an international standard whereby a Pin Entry Device is required to be PCI certified,[16]

(b) EMV certified (L1 hardware and L2 software). EMV is the global standard for chip card technology,

(c) approved by the New Zealand Bankers' Association,[17]

(d) able to "talk" to the two New Zealand switches. This requires operating software (different for ETSL and ANZ but becoming similar under the EMV standard requirement currently being introduced), and

(e) Telepermitted for the New Zealand market.

13 **[ ]** out of this **[ ]** is directed to ENZ, owned by ANZ National.

14 **[ ]** out of this **[ ]** is estimated to be Hypercom brand terminals currently supplied via Provenco.

15 See recent promotional pamphlet circulated by Skyzer, using Ingenico terminals, as an example: attached in Appendix 2.

16 PCI PED (Payment Card Industry PIN Entry Device) is an updated requirement for manufacturers that sell PIN pads and terminals with internal PIN pads. It is a standard testing process that combines one set of standards for each of the PCI members (Visa, Mastercard and JCB), helping ensure cardholder security and providing faster time-to-market for financial institutions. After 31 December 2007, device manufacturers may no longer sell PIN entry devices for PIN-based transactions that do not comply with this standard.

17 The New Zealand Bankers' Association, together with ETSL and ENZ, developed the EFTPOS standards to ensure the ongoing integrity and robustness of the EFTPOS payment system. The EFTPOS standards were implemented in May 2006.

17.2. In respect of each of the above:

(a) PCI PED certification is common worldwide and coupled with the hardware. The move to this standard makes it easier for overseas terminals to be imported. Previously it might not have been worthwhile, for such a small market, for an overseas manufacturer to obtain what was hitherto a specific New Zealand hardware certification. Now, they will already have the requisite standard.

(b) Similarly, EMV certification is global. Having already complied overseas, it is now easier for an overseas manufacturer to comply in New Zealand.

(c) Approval from the NZBA is straightforward, if the other requirements are met.

(d) Each terminal provider manages the development of their terminal software from potentially multiple sources (in-source and/or out-source).[18] It costs approximately $300,000.00 to $400,000.00 and takes approximately six months for software to be developed for a terminal. ETSL and ENZ are open for anyone to write terminal software to connect to their switches. The introduction of EMV standards means that terminal architecture with EMV compliant software overseas can be adapted more easily into the New Zealand environment.

(e) Obtaining a Telepermit is straightforward, with standardisation of communication protocols.

Existing participants in New Zealand already meet these standards.

18. EXAMPLES OF EXPANSION BY EXISTING COMPETITORS

18.1. See next section.

19. CONDITIONS INFLUENCING EXPANSION

19.1. The market is highly competitive. Expansion opportunities are sought and taken advantage of by a varied range of competitors at all times. ENZ in particular is motivated to increase its terminal base by virtue of ANZ National's role as issuer and acquirer in payment card markets, and owner of a switch.

19.2. Relationships with end users are closely protected by dealers so that ongoing service and renewal opportunities are maintained. Dealers provide an important channel to market due to their customer relationships and sales/support resources. The merged entity is unlikely to want to forego that channel lightly (when other device vendors are likely to want to increase their share of it and will replace existing terminals given the opportunity).

18 Verifone, for instance, has its software developed out of India. Once created for the architecture of a particular terminal, the software can be used with minimal or no further adaptation up and down the model family based on that architecture or platform.

19.3. Other business models, such as telco bundling, and use of internet, are emerging. It is inconceivable that the price of Cadmus or Hypercom branded terminals could be raised post-merger, or that their supply would be restricted. If either was attempted, the inevitable result would be loss of business to competing brands as dealers and suppliers sought each other out. The merger of itself is likely to provide an opportunity for competitors to try and substitute themselves (which Ingenico, at least, has already begun: refer recent pamphlet to dealers promoting Skyzer with Ingenico products, in Appendix 2).

20. TIME TO INCREASE SUPPLY

20.1. The time taken to increase supply would be short.

21. EXTENT OF CONSTRAINT BY POSSIBLE COMPETITIVE RESPONSE

21.1. Significant.

22. CONCLUSIONS ON CONSTRAINT BY EXISTING COMPETITION ON EXERCISE OF UNILATERAL MARKET POWER

22.1. There is every reason to believe that current constraints in the market will continue.

23. MARKET CHARACTERISTICS FACILITATING OR IMPEDING COORDINATION

23.1. By virtue of the varied range of participants, including a multitude of dealers and the vertically integrated ENZ, coordination is highly unlikely.

Table 1: Scope for co-ordinated market power

Feature	Comment
High seller concentration	No: range of large and small participants, high international presence, including one vertically integrated significant competitor (ENZ).
Differentiated product	Not so much in respect of terminals per se, but is in respect of supply of packages to end users.
Static production technology	No: highly dynamic and innovative.
Speed of new entry	High.
Fringe competitors	Yes, numerous and diverse offerings.
Acquisition of an unusually vigorous or effective competitor	No.
Price elastic market demand	Reasonably, subject to product/service differentiation.
History of co-ordinated conduct	No.
Countervailing power of acquirers	Large users, and dealers, provide constraint.
Existence of excess capacity	Not applicable.
Industry associations/fora	Not from the point of view of terminal suppliers (but banks have).

24. CHARACTERISTICS POST-ACQUISITION AS TO MONITORING/ENFORCEMENT OF COORDINATED BEHAVIOUR

24.1. The same factors which do not facilitate co-ordination apply equally to monitoring/enforcement.

Table 2: Detection of deviation from co-ordination

Feature	Comment
Seller concentration	No.
Frequent sales	Yes, and mixture of different product/service offerings and of new sales and renewal of sales under leases.
Vertical integration	ENZ is vertically integrated/interconnected at many levels. Cadmus is, and the merged entity therefore also will be, vertically integrated into manufacturing.

Growth in demand	Stable in NZ (but growth globally)
Cost similarities	No.
Multi market contact	No.
Price transparency	No. Very difficult to obtain data about competitors.

Table 3: Ability to retaliate

Credibility of threats to abandon collusion	N/A.
Availability of excess capacity	Not applicable (although overseas manufacturers could effectively “dump” onto New Zealand market).
Profit incentive from collusion	N/A.
Ability to disadvantage by dumping in deviator’s allocated section of market	N/A.

25. **EVIDENCE OF PAST OR CURRENT COORDINATION**

25.1. The applicant is not aware of any past or current co-ordination.

26. **CONCLUSIONS ON CONSTRAINT BY EXISTING COMPETITION ON CO-ORDINATION**

26.1. There is no evidence to suggest that the markets, which presently are not co-ordinated in these terms, will become so post-acquisition.

PART IV: CONSTRAINTS ON MARKET POWER BY POTENTIAL COMPETITION

Sufficient competitive constraint will continue to be provided by existing competitors, and so the remainder of the application is, strictly, not required. However, for completeness (and because there is evidence of new entry) the following responses are also provided.

27. **CONDITIONS OF ENTRY**

27.1. Conditions to entry identified in section 17.1 above are not onerous for international terminal suppliers and a number have entered over recent years (eg, Thales, Sagem, Nurit, Skyzer/Ingenico).

27.2. In addition, there are no barriers to entry by those competing for end users.

28. **POTENTIAL NEW ENTRANTS**

28.1. Blue Bamboo and EFT Networks have recently announced an intention to expand into Australia and New Zealand (see Appendix 2. Also: Perceptions, using Nurit terminals: http://www.perceptions.co.nz/eftpos.php). Other examples of potential new entrants include large players in adjacent markets. These include:

(a) the non-ANZ National banks which could follow the ANZ National in duplicating the Australian model,

(b) the three major telco/cellco's in New Zealand which are believed to be actively pursuing or considering the bundling or cross-selling of EFTPOS with their own offers,

(c) Micros, the global POS hardware vendor which has a strong vertical market share in New Zealand hospitality and is launching a vertically integrated hardware and software suite including payment for the first time.

29. **CONDITIONS INFLUENCING ENTRY**

29.1. As above.

30. **TIMELINESS OF ENTRY**

30.1. Little time is required, no more than six months.

31. **LIKELIHOOD OF ENTRY**

31.1. As the examples show, it is occurring all the time.

32. **EXTENT OF ENTRY**

32.1. Sufficient.

33. **CONDITIONS INFLUENCING *DE NOVO* ENTRY**

33.1. See above.

34. **TIME FOR *DE NOVO* ENTRY TO OCCUR**

34.1. See above.

35. **CONCLUSION ON POTENTIAL ENTRY**

35.1. Potential entry is also sufficient competitive constraint.

PART V: OTHER POTENTIAL CONSTRAINTS

36. SUPPLIERS

36.1. In respect of Hypercom, and its distribution contract with Provenco, see section 11.7 above.

37. OWNERSHIP OF SUPPLIERS

37.1. As above.

38. CONSTRAINTS ON MARKET POWER BY THE CONDUCT OF SUPPLIERS

38.1. **[**

]

39. ACQUIRERS

39.1. Dealers and banks have countervailing power, for reasons set out above.

40. OWNERSHIP OF ACQUIRERS

40.1. Banks, and numerous owners of dealers.

41. CONSTRAINTS ON MARKET POWER BY THE CONDUCT OF ACQUIRERS

41.1. As set out above, vis-à-vis dealers and banks. See section 19.2. Our major banks are Australian-owned, and familiar with terminal providers in Australia, which they could introduce in New Zealand. The merged entity would have neither the incentive nor the ability to squeeze out dealers. It does not have the ability or commercial incentive to do so now, and nothing would change. The merged entity does not have the customer relationships the dealers do, throughout the country, and would risk losing a significant portion of its business if it attempted to bypass them, because they would simply obtain terminals from Ingenico, or Verifone, or one of the other suppliers.

Appendix 1

Declining terminal prices

Year	Average monthly rental charges ($/mth)	% decline
2003	**[ ]**	
2004	**[ ]**	**[ ]**
2005	**[ ]**	**[ ]**
2006	**[ ]**	**[ ]**
2007	**[ ]**	**[ ]**

(average reduction of **[ ]** across the period)

Appendix 2

Market/competitor material

This Notice is given by:

Provenco Group Limited and Cadmus Technology Limited

The companies hereby confirm that:

- all information specified by the Commission has been supplied;
- all information known to the applicants which is relevant to the consideration of this application has been supplied; and
- all information supplied is correct as at the date of this application.

The companies undertake to advise the Commission immediately of any material change in circumstances relating to the application/notice.

Dated this 19th day of November 2007

Signed by Chris Morrison (Provenco) and Anthony Howard (Cadmus)

Chris Morrison Anthony Howard

We are directors of Provenco and Cadmus respectively and are duly authorised to make this notice.