Statement of Preliminary Issues

Fletcher Building / Higgins

29 February 2016

Introduction

1. Fletcher Building Holdings New Zealand Limited (Fletcher Building) is proposing to acquire Higgins Group Holdings Limited (Higgins), and up to 50% of the shares in Horokiwi Quarries Limited (HQL). The transaction excludes Higgins' ready-mix concrete business, which includes joint ventures in ready-mix concrete.

2. On 18 February 2016, the Commerce Commission registered an application from Fletcher Building seeking clearance for the proposed acquisition.[1]

3. The Commission will give clearance if it is satisfied that the acquisition will not have or would not be likely to have, the effect of substantially lessening competition in a market in New Zealand.

4. This Statement of Preliminary Issues outlines the key competition issues we currently consider to be important in deciding whether or not to grant clearance.[2]

5. We invite interested parties to comment on the likely competitive effects of the proposed acquisition, and request that parties who wish to make a submission do so by **Monday 14 March 2016**.

The parties

6. Fletcher Building Holdings New Zealand Limited is a wholly owned subsidiary of Fletcher Building Limited, a NZX and ASX listed company primarily involved in the manufacture and distribution of building materials and in residential and commercial construction. Fletcher Building has operations in New Zealand, Australia, Asia, Europe and the USA.

7. Higgins is a privately owned New Zealand company that provides civil construction services and is a manufacturer of construction products such as aggregates.

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1 The public version of the application is available on our website at: http://www.comcom.govt.nz/business-competition/mergers-and-acquisitions/clearances/clearances-register/detail/926

2 The issues highlighted in this statement are based on the information available at the time of publication and may change as our assessment of the application for clearance progresses. Therefore, the issues highlighted in this statement are not binding on us.

8. HQL operates three quarries in the Wellington region (Horokiwi, Fitzroy Bay and Hutt River). HQL is a joint venture between Higgins and Fulton Hogan Limited, each having a 50% share.

Our framework

9. Our approach to analysing the competition effects of the proposed acquisition is based on the principles set out in our Mergers and Acquisitions Guidelines.[3] As required by the Commerce Act 1986, we assess mergers using the substantial lessening of competition test.

10. We determine whether an acquisition is likely to substantially lessen competition in a market by comparing the likely state of competition if the acquisition proceeds (the scenario with the acquisition, often referred to as the factual), with the likely state of competition if the acquisition does not proceed (the scenario without the acquisition, often referred to as the counterfactual).[4]

11. We define markets in the way that we consider best isolates the key competition issues that arise from the acquisition. In many cases this may not require us to precisely define the boundaries of a market. A relevant market is ultimately determined, in the words of the Commerce Act, as a matter of fact and commercial common sense.[5]

12. We compare the extent of competition in each relevant market both with and without the acquisition. This allows us to assess the degree by which the proposed acquisition might lessen competition. If the lessening is likely to be substantial, we will not give clearance to the proposed acquisition. When making that assessment, we consider, among other matters:

    12.1 existing competition – the degree to which existing competitors compete;

    12.2 potential competition – the extent to which existing competitors would expand their sales or new competitors would enter the market and compete effectively if prices were increased; and

    12.3 the countervailing market power of buyers – the potential for a business to be sufficiently constrained by purchaser's ability to exert substantial influence on negotiations.

Preliminary issues

13. We will investigate whether the proposed acquisition is likely to substantially lessen competition in the relevant markets by focusing on the unilateral, coordinated and vertical effects that might result from this acquisition. In particular, we will consider:

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3 Commerce Commission, *Mergers and Acquisitions Guidelines*, July 2013. Available on our website at www.comcom.govt.nz

4 *Commerce Commission v Woolworths Limited* (2008) 12 TCLR 194 (CA) at [63].

5 Section 3(1A). See also *Brambles v Commerce Commission* (2003) 10 TCLR 868 at [81].

13.1 the closeness of competition between the merging parties in each market affected by the acquisition;

13.2 the degree to which existing competitors provide competitive constraints;

13.3 the ability for new suppliers to enter or for existing suppliers to expand in each market affected by the acquisition;

13.4 the ability of customers to exert substantial influence on the price and other terms the merged entity would charge;

13.5 whether the merged firm would have the ability and/or the incentive to foreclose its competitors; and

13.6 whether the acquisition is likely to increase the ability of Fletcher Building and all or some of its remaining competitors to coordinate their behaviour.

Areas of overlap

14. Fletcher Building submitted that any overlap in activities with Higgins would be in the manufacture and supply of aggregates. Furthermore, it submitted that while both parties undertake construction services, there is little overlap in this area due to Fletcher Building's focus on the construction of vertical structures (bridges and tunnels etc.) and Higgins' focus on the construction of horizontal surfaces such as roads.

15. We will consider whether Fletcher Building and Higgins have a material overlap in any markets affected by the acquisition. However, our current competition concerns are focused on the aggregates markets.

Market definition

16. With respect to aggregates, in its application Fletcher Building identified six relevant regional markets for the manufacture and wholesale supply of aggregates. The regional markets identified are:

16.1 North Waikato;

16.2 Napier;

16.3 Manawatu-Whanganui;

16.4 Kapiti;

16.5 Wellington; and

16.6 Christchurch.

17. As part of our investigation, we will consider the scope of regional geographic aggregate markets.

18. In addition, we will consider whether there are separate markets for different types of aggregates or end use product markets and we will consider whether there are separate customer markets for aggregates.

Closeness of competition

19. Fletcher Building submits that much of Fletcher Building and Higgins aggregate production is used in their respective downstream operations. However, as part of our investigation, we will consider the closeness of competition between Fletcher Building and Higgins in each of the relevant markets identified.

Existing competition from other suppliers

20. Fletcher Building submits that in each geographic market there are existing competitors whose quarries will continue to constrain the proposed merged party from being able to raise prices.

21. We will consider the extent to which existing competitors in each geographic market are able to provide a competitive constraint on the merged entity. Factors we will consider in making this assessment include:

    21.1 the types of aggregates competing quarries can supply and their substitutability with aggregates supplied by the merged party; and

    21.2 the capacity of competing quarries, including length of resource consents.

22. We will also assess whether there are any major costs or other impediments, involved in customers switching between aggregate supplier and the likely impact of the acquisition on their ability to switch.

Entry and expansion

23. On aggregates, Fletcher Building submits that access to alluvial deposited aggregates provides an easy entry into the market in some of the regions.

24. We will assess whether entry (or expansion of an existing supplier) would be of likely, of sufficient extent and occur in a timely fashion to prevent a substantial lessening of competition in each region. Our assessment will include the considering the length of time it takes to obtain resource consents, and length of time resource consents are likely to be granted for.

Foreclosure

25. Fletcher Building submits that there are a number of viable alternatives for the supply of aggregates, ready-mix concrete and other inputs such that Fletcher Building will not have the ability to foreclose downstream competitors active in infrastructure construction and road projects.

26. We will assess whether competitors to the proposed merged entity in downstream markets, such as road maintenance, are able to easily switch to alternative suppliers of inputs such as aggregates or able to self-supply.

Countervailing power

27. We will consider whether purchasers of downstream activities such as civil construction and road maintenance have countervailing power and are able to sufficiently constrain the merged entity from profitably increasing prices or reducing the quality of its services.

Coordinated effects

28. Fletcher Building submits that the aggregates markets do not currently show signs of coordinated conduct and the acquisition would not remove any features that currently prevent coordination, or introduce new features that might provide an incentive for coordination.

29. We will consider whether the merger increases the potential for the proposed merged entity and all or some of its competitors to coordinate their behaviour and collectively exercise market power such that output or quality reduces, and/or prices increase, across the markets.

30. We will also assess:

    30.1 whether the market is vulnerable to coordination; and

    30.2 whether the merger is likely to change the conditions in the market so that coordination is more likely, more complete or more sustainable.

Next steps in our investigation

31. The Commission is currently aiming to make a final decision on whether or not to give clearance to the merger by **3 May 2016.** However, this date may change as our investigation progresses.[6]

32. As part of our investigation, we will be identifying and contacting parties we consider will be able to help us assess the preliminary issues identified above.

Making a submission

33. If you wish to make a submission, please send it to us at registrar@comcom.govt.nz with the reference Fletcher Building/Higgins in the subject line of your email, or by mail to The Registrar, PO Box 2351, Wellington 6140. Please do so by close of business **Monday 14 March 2016**.

34. All information we receive is subject to the Official Information Act 1982 (OIA), under which there is a principle of availability. We recognise, however, that there may be good reason to withhold certain information contained in a submission under the OIA. For example, if disclosure would unreasonably prejudice the supplier or subject of the information. In assessing the confidentiality of information contained in

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[6] The Commission maintains a clearance register on our website at http://www.comcom.govt.nz/clearances-register/ where we update any changes to our deadlines and provide relevant documents.

submissions for the purposes of publication on our website, we intend to apply an approach that is consistent with the OIA.