

Statement of Preliminary Issues

Taranaki By-Products / Lowe Corporation

26 February 2021

Introduction

1. On 9 February 2021, we registered an application from Taranaki By-Products Limited seeking clearance for it, or an interconnected body corporate (the Applicant), to acquire up to 100% of the shares in Tuakau Proteins Limited, Hawkes Bay Protein Limited and Jackson Transport Limited (the Proposed Acquisition).¹ The Applicant already owns shares in these three companies.
2. The Commission will give clearance if it is satisfied that the Proposed Acquisition will not have, or would not be likely to have, the effect of substantially lessening competition in a market in New Zealand.
3. This statement of preliminary issues sets out the issues we currently consider to be important in deciding whether or not to grant clearance.²
4. We invite interested parties to provide comments on the likely competitive effects of the Proposed Acquisition. We request that parties who wish to make a submission do so by close of business on **12 March 2021**.

The parties

The Applicant

5. The Applicant (directly and via subsidiaries) owns shares in entities that provide animal rendering and associated services to meat processors and farmers in the North Island. These entities include Taranaki By-Products Limited (Taranaki By-Products) and Glenninburg Holdings Limited (Glenninburg).

The Targets

6. Tuakau Proteins Limited (Tuakau Proteins), Hawkes Bay Protein Limited (Hawkes Bay Protein) and Jackson Transport Limited (JTL) are companies active in the animal

¹ A public version of the application is available on our website at:
<http://www.comcom.govt.nz/businesscompetition/mergers-and-acquisitions/clearances/clearances-register/>

² The issues set out in this statement are based on the information available when it was published and may change as our investigation progresses. The issues in this statement are not binding on us.

rendering industry. Tuakau Proteins and Hawkes Bay Protein each provide animal rendering services, while JTL provides transport services to renderers.

7. These companies are currently joint ventures between the Applicant and Lowe Corporation Limited or its related entity, Graeme Lowe Proteins Limited (together, Lowe). Outside of these joint ventures, Lowe's main businesses in the wider meat industry are involved in the tanning and processing of hides, skins and pelts.³
8. The current ownership structure of each of the three joint venture companies is set out in Table 1 below.

Table 1: Ownership structure of the joint ventures

Tuakau Proteins	Hawkes Bay Protein	JTL
Glenninburg 49.9%	Taranaki By-Products 50.1%	Taranaki By-Products 50%
Graeme Lowe Protein Limited 50.1%	Lowe 49.9%	Lowe 50%

Source: The Applicant

The Proposed Acquisition

9. Under the Proposed Acquisition it is proposed that:
 - 9.1 Taranaki By-Products will acquire up to 100% of the shares in Hawkes Bay Protein and up to 100% of shares in JTL; and
 - 9.2 Glenninburg will acquire up to 100% of the shares in Tuakau Proteins.

Our framework

10. Our approach to analysing the competition effects of the proposed acquisition is based on the principles set out in our Mergers and Acquisitions Guidelines.⁴ As required by the Commerce Act 1986 (the Act), we assess mergers and acquisitions using the substantial lessening of competition test.
11. 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).⁵ This allows us to assess the degree by which the proposed acquisition might lessen competition.

³ Clearance application from Taranaki By-Products at [106].

⁴ Commerce Commission, *Mergers and Acquisitions Guidelines*, July 2019. Available on our website at www.comcom.govt.nz.

⁵ *Commerce Commission v Woolworths Limited* (2008) 12 TCLR 194 (CA) at [63].

12. If the lessening of competition resulting from the proposed acquisition is likely to be substantial, we will not give clearance. When making that assessment, we consider, among other matters:
- 12.1 constraint from existing competitors – the extent to which current competitors compete and the degree to which they would expand their sales if prices increased;⁶
 - 12.2 constraint from potential new entry – the extent to which new competitors would enter the market and compete if prices increased; and
 - 12.3 the countervailing market power of buyers – the potential constraint on a business from the purchaser’s ability to exert substantial influence on negotiations.

Market definition

13. We define markets in the way that we consider best isolates the key competition issues that arise from the Proposed 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 Act, as a matter of fact and commercial common sense.⁷
14. As noted above, all three joint ventures are involved in the rendering industry in the North Island.
- 14.1 Taranaki By-Products, Hawkes Bay Protein and Tuakau Proteins all own operations in the North Island that render animal materials (or inputs) into finished products (or outputs) such as meat and bone meal and tallow.
 - 14.2 JTL is a Taranaki-based transport company that primarily provides transport services to the rendering industry in the North Island.
15. The Applicant has submitted that the only relevant overlap that arises as a result of the Proposed Acquisition relates to inputs into rendering services.⁸ These input services can vary based on the type of animal material to which the rendering service relates, and the geographic region where the service is provided. In this regard, the Applicant submitted that markets relevant to the consideration of the Proposed Acquisition are for the provision of toll and direct collection rendering services to customers for:⁹
- 15.1 bovine material in the upper North Island;

⁶ References to price increases in this document should be taken to include a reduction in quality, service or innovation.

⁷ Section 3(1A); See also *Brambles v Commerce Commission* (2003) 10 TCLR 868 at [81].

⁸ Clearance application from Taranaki By-Products at [102].

⁹ *Ibid.*

- 15.2 mixed animal material in the upper North Island;
 - 15.3 poultry material in the upper North Island;
 - 15.4 bovine material in the lower North Island;
 - 15.5 mixed animal material in the lower North Island;
 - 15.6 ovine material in the lower North Island; and
 - 15.7 poultry material in the lower North Island.
16. The Applicant considers that renderers receive significantly higher prices from having single-species processing lines and so, unlike in the past, renderers do not tend to switch their processing lines between different species.¹⁰ The processing of mixed animal material has also declined in recent times.
 17. We will consider whether the provision of rendering services varies between the different animal species and the extent to which renderers can and do switch their production lines between the material from different animals.
 18. We will also consider the geographic scope for any rendering service and the extent to which the existing rendering service providers in the North Island compete with one another.
 19. Finally, we will consider whether rendering customers requiring a ‘toll’ service are different to those requiring ‘direct’ collection and, if so, whether rendering services provided to toll customers comprise a separate market from services provided to direct collection customers.
 - 19.1 Under a toll service, the provider renders the customer’s animal material for a fee, with the customer retaining ownership of the material throughout the rendering process. In this scenario, the rendering provider acts as seller.
 - 19.2 Under a direct collection service, renderers collect, and take ownership of, the animal material from animal processors or farmers. The benefit to the processor or farmer is that they are no longer responsible for the animal material that they would otherwise have had to dispose of. In this scenario, the rendering provider acts as buyer.

Without the acquisition

20. The Applicant considers the status quo is the appropriate counterfactual in this case.¹¹ We will consider the evidence on whether the without-the-acquisition scenario is best characterised by the status quo or whether the counterfactual may

¹⁰ For example, the Applicant considers the rendering of bovine material should be limited to ante and post-mortem veterinary inspected bovine material: clearance application from Taranaki By-Products at [43] and [52].

¹¹ Clearance application from Taranaki By-Products at [25].

be something other than the status quo. For example, we will test whether there are buyers, other than the Applicant, for the shares in the three joint ventures.

21. We also note that Taranaki By-Products (via Glenninburg) acquired the North Island rendering assets of Wallace Group GP Limited in 2020. The Commission is, separately, investigating whether this acquisition is likely to have substantially lessened competition in any market in breach of section 47 of the Act. In assessing the Proposed Acquisition, the Commission will consider the likely ownership of these assets in both the factual and counterfactual.

Preliminary issues

22. The focus of our investigation will be to consider whether the Proposed Acquisition would be likely to substantially lessen competition in the relevant market (or markets) by assessing whether horizontal unilateral effects might result from the Proposed Acquisition.
23. We will also consider whether any coordinated effects and/or conglomerate/vertical effects might result from the Proposed Acquisition.

Unilateral effects: would the merged entity be able to profitably raise prices by itself?

24. Unilateral effects arise when a firm merges with a competitor that would otherwise provide a significant competitive constraint (particularly relative to remaining competitors) such that the merged firm can profitably increase price above the level that would prevail without the merger without the profitability of that increase being thwarted by rival firms' competitive responses. A merger could also reduce competition if one of the merging firms was a potential or emerging competitor.
25. The question that we will be focusing on is would any loss of competition enable the Applicant to profitably raise prices or reduce quality or innovation of any relevant rendering service by itself?¹²
26. While this question relates to the Applicant as a seller, we are also considering rendering markets where the Applicant acts as a buyer. In buying markets, the unilateral effects of a merger can be slightly different than in a selling market as the concerns tends to be whether a buying firm can decrease prices. In this case, in assessing any market where the Applicant is a buyer, the references below to price increases should be read as references to price decreases.
27. The Applicant considers that the Proposed Acquisition would not be likely to substantially lessen competition in any relevant rendering service market.

¹² For ease of reference, we only refer to the ability of the merged entity to "raise prices" from this point on. This should be taken to include the possibility that the merged entity could reduce quality or innovation, or worsen an element of service or any other element of competition, ie, it could increase quality-adjusted prices.

- 27.1 Post acquisition, the Applicant would own the only two rendering plants in the upper North Island (one in Tuakau and one in Waitoa) that are not associated with a vertically integrated meat processor. However, the Applicant considers the two plants are not close competitors because the Tuakau plant currently only renders bovine material while the Waitoa plant only renders poultry and mixed animal material.¹³
- 27.2 Post acquisition, the Applicant would own two rendering plants in the lower North Island (one in Napier and one in Hawera) as well as having a shareholding in a third plant (Kakariki). The Applicant considers that the Proposed Acquisition would not impact on competition in any relevant lower North Island market because it only involves an increase in shareholding in the Napier plant and this is the only plant in the North Island that currently renders ovine material. As such, the Napier plant does not compete with Taranaki By-Products (or any other independent rendering service provider) in the North Island.¹⁴
28. In the relevant rendering services market(s), we will consider:
- 28.1 the degree of competitive constraint that Lowe, via its shareholdings in the three joint ventures, is likely to impose on the Applicant and any of its related rendering operations in the counterfactual. To the extent that any constraint is material, we will assess whether the competition lost between the merging parties could be replaced by rival competitors;
- 28.2 remaining competitive constraints: the degree of constraint that existing competitors would impose on the merged entity;
- 28.3 entry and expansion: how easily rivals could enter and/or expand; and
- 28.4 countervailing power: whether customers, in particular meat and poultry processors, have special characteristics that would enable them to resist a price increase by the merged entity.

Coordinated effects: does the Proposed Acquisition make coordination more likely?

29. A merger can substantially lessen competition if it increases the potential for the merged entity and all or some of its remaining rivals to coordinate their behaviour and collectively exercise market power such that output reduces and/or prices increase across the market. Unlike a substantial lessening of competition, which can arise from the merged entity acting on its own, coordinated effects require some or all of the firms in the market to be acting in a coordinated way.

¹³ Clearance application from Taranaki By-Products at [37-69].

¹⁴ Clearance application from Taranaki By-Products at [70-92].

30. The Applicant submitted that there is no risk of coordinated effects from the Proposed Acquisition because it does not result in any significant aggregation or integration in any relevant market.¹⁵
31. We will assess whether the Proposed Acquisition would make coordination more likely, more complete or more sustainable. As part of our assessment we will consider whether any of the relevant markets are vulnerable to coordination, and whether the Proposed Acquisition would change the conditions in the relevant markets.

Vertical and conglomerate effects: would the merged entity be able to foreclose rivals?

32. A merger between suppliers (or buyers) who are not competitors but who operate in related markets can result in a substantial lessening of competition due to vertical or conglomerate effects. This can occur where a merger gives the merged entity a greater ability or incentive to engage in conduct that prevents or hinders rivals from competing effectively (which we refer to as ‘foreclosing rivals’).
33. The Applicant submitted that there is no risk of conglomerate and/or vertical effects from the Proposed Acquisition because of the presence of numerous participants throughout the rendering supply chain.¹⁶
34. We will assess whether the Proposed Acquisition would be likely to give the merged entity the ability and incentive to foreclose rivals. In particular, we will consider whether:
- 34.1 the merged entity would have control over an important input;
 - 34.2 the merged entity would have the incentive to impede its rivals by refusing to supply the input or only supplying at a higher price; and
 - 34.3 such behaviour would substantially lessen competition.

Next steps in our investigation

35. The Commission is currently scheduled to make a decision on whether or not to give clearance to the Proposed Acquisition by **8 April 2021**. However, this date may change as our investigation progresses.¹⁷ In particular, if we need to test and consider the issues identified above further, the decision date is likely to extend.
36. As part of our investigation, we will be identifying and contacting parties that we consider will be able to help us assess the preliminary issues identified above.

¹⁵ Clearance application from Taranaki By-Products at [111-125].

¹⁶ Ibid at [111-125].

¹⁷ 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.

Making a submission

37. If you wish to make a submission, please send it to us at registrar@comcom.govt.nz with the reference 'Taranaki By-Products/Lowe' 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 on **12 March 2021**.
38. Please clearly identify any confidential information contained in your submission and provide both a confidential and a public version. We will be publishing the public versions of all submissions on the Commission's website.
39. 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, in circumstances where disclosure would unreasonably prejudice the supplier or subject of the information.