

Statement of Preliminary Issues

Beijer / Realcold

26 August 2015

Introduction

1. On 12 August, the Commerce Commission received an application from B100 Limited, a newly incorporated subsidiary of the Swedish refrigeration group Beijer Ref AB (Beijer), to acquire the business and assets of Realcold Limited (Realcold).
2. 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/867>
3. This Statement of Preliminary Issues outlines the key competition issues we currently consider will be important in deciding whether or not to grant clearance. 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.
4. We invite interested parties to make comment on the likely competitive effects of the proposed acquisition and request that parties who wish to make a submission do so by **7 September 2015**.

The transaction and the parties

5. Beijer recently entered the New Zealand market through its acquisition of Patton Limited (Patton), an assembler and distributor of commercial refrigeration, air conditioning, and condensation equipment. Patton has branches and assembly facilities in New Zealand, Australia and Thailand, with New Zealand corporate headquarters in Auckland.
6. Realcold is based in Auckland, and also assembles and distributes commercial refrigeration and air conditioning equipment in New Zealand. It has 10 branches across New Zealand and has operations in Australia.
7. Both companies are wholesale suppliers of refrigeration and air conditioning products, with their main customers being refrigeration and air-conditioning installers.

Our framework

8. As required by the Commerce Act 1986, we assess whether an acquisition of shares is likely to result in a substantial lessening of competition. How we assess this is set out in our Mergers and Acquisitions Guidelines.¹
9. We ask 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).²
10. A tool used to assess competitive effects is market definition. Market definition provides a framework to help identify and assess the close competitive constraints the merged firm would likely face.³ A market is defined in the Commerce Act as a market in New Zealand for goods or services as well as other goods or services that are substitutable for them as a matter of “fact and commercial common sense”.⁴
11. We define markets in the way that we consider best isolates the key competition issues that arise from the merger. In many cases this may not require us to precisely define the boundaries of a market.
12. We analyse the extent of competition in each relevant market both with and without the acquisition to determine whether the acquisition would be likely to substantially lessen competition.
13. When making that assessment, we consider, among other matters:
 - 13.1 Existing competition – the degree to which existing competitors compete.
 - 13.2 Potential competition – the extent to which existing competitors would expand their sales or new competitors would enter and compete effectively if prices were increased.
 - 13.3 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.

¹ Commerce Commission, *Mergers and Acquisitions Guidelines*, July 2013. Available on our website at www.comcom.govt.nz

² *Commerce Commission v Woolworths Limited* (2008) 12 TCLR 194 (CA) at [63].

³ *Commerce Commission v New Zealand Bus Limited* (2006) 11 TCLR 679 (HC), at [123]. *Brambles New Zealand Ltd v Commerce Commission* (2003) TCLR 868 (HC) at [137].

⁴ Similarly, the courts have said that “[t]he boundaries of the market are defined by substitution between one product and another and between one source of supply and another, in response to changing prices”. See *Commerce Commission v New Zealand Bus Limited* (HC), above n 3 at [123] citing *Re Queensland Co-operative Milling Association Ltd* (1976) ATPR 40-012 at 17,247.

Preliminary issues

14. We will assess whether the proposed acquisition is likely to substantially lessen competition in the relevant markets by focusing on the unilateral and coordinated effects that might result from this acquisition. In particular, we will consider:
 - 14.1 whether there is a single differentiated product market for the importation and wholesale supply of refrigerants, refrigeration components, refrigeration equipment, high wall split air conditioning units and air conditioning components;
 - 14.2 the closeness of competition between the merging parties and other suppliers;
 - 14.3 the ability for new suppliers to enter or for existing suppliers to expand, by extending the range and geographic coverage of their operations;
 - 14.4 the ability of customers to exert substantial influence on the price the merged entity charges and on other terms; and
 - 14.5 whether the merger is likely to increase the ability of the merged entity and all or some of its remaining competitors to coordinate their behaviour on price or any other dimension of competition.

Market definition

15. Beijer submitted that the relevant markets where the parties overlap are in the national market for the importation and wholesale supply of:
 - 15.1 refrigerants;
 - 15.2 refrigeration components;
 - 15.3 refrigeration equipment;
 - 15.4 high wall split air-conditioning units; and
 - 15.5 air-conditioning components.
16. On refrigeration equipment, Beijer submitted that both parties undertake the assembly of refrigeration equipment, marketed under their own brands (pre-assembled) and also design and manufacture refrigeration equipment to suit customer specific requirements (bespoke). However, in the application, Beijer indicated that suppliers can readily switch between supplying pre-assembled and bespoke refrigeration equipment such that a single refrigeration equipment market would be appropriate when analysing the proposed merger.
17. We will consider:

- 17.1 whether separate markets exist for refrigeration equipment (pre-assembled and bespoke);
- 17.2 whether separate markets exist for refrigeration components and air-conditioning components (unique, universal);
- 17.3 whether the supply of refrigerants, refrigeration components and air-conditioning components are tied to the sale of refrigeration equipment and air-conditioning units;
- 17.4 the various customer types and characteristics, including their size (large installers, local tradespeople), requirements (pick-up, courier, one-stop shop) and attributes (specialists versus general tradespeople);
- 17.5 the role of warranties on refrigeration equipment and air-conditioning units and their interplay with the trade in refrigeration components, refrigerants and air-conditioning components; and
- 17.6 the geographic dimension by exploring the role of local outlets and assessing whether a national market is appropriate.

Existing competition

- 18. Beijer submitted that post-acquisition it will continue to face strong competition from firms who operate in the same market. Competitors it has identified include:
 - 18.1 BOC and Nuplex Specialities in the refrigerants market;
 - 18.2 Heatcraft New Zealand in the refrigeration equipment and refrigeration components market;
 - 18.3 BDT and Fujitsu in the air-conditioning units market; and
 - 18.4 Hollyoakes and Smooth-Air in the air-conditioning components market.
- 19. Our investigation will focus on the closeness of competition between the merging parties, and between the merging parties and other competitors. In doing so, we will consider whether the merged entity would be effectively constrained from raising its prices above the competitive level, or reducing the quality of its services by the existing competition.
- 20. We will also assess whether there are any major costs or other impediments (such as rebates) involved in customers switching between wholesale suppliers and the likely impact of the acquisition on their ability to switch.

Potential competition

21. Beijer submitted that, due to there being no regulatory barriers or supply constraints, combined with products being interchangeable, existing wholesale suppliers could readily expand. This combined with the prospect of entry by offshore wholesale suppliers such as Actrol/Reece from Australia who could use Reece plumbing stores as its shop front would, in Beijer's view, provide a further competitive constraint on the merged entity.
22. We will assess whether entry by new competitors or expansion by existing competitors is likely, of sufficient extent and would occur in a timely fashion to prevent a substantial lessening of competition.

Countervailing power

23. We will consider whether the countervailing power of customers will be able to sufficiently constrain the merged entity from profitably increasing prices or reducing the quality of its services, including for instance by switching wholesale suppliers or by passing wholesale suppliers entirely and self-supplying.

Coordinated effects

24. Beijer submitted that the conditions necessary for effective and sustainable coordinated behaviour are not present in the market for the importation and wholesale supply of: refrigerants, refrigeration components, refrigeration equipment, high wall split air conditioning units and air conditioning components.
25. We will consider whether the merger increases the potential for the 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.
26. We will also assess:
 - 26.1 whether the market is vulnerable to coordination; and
 - 26.2 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

27. We are currently aiming to make our decision by **7 October 2015**. However, this date may change as the investigation progresses.
28. To keep up to date with any changes to our deadline and to find relevant documents, visit our clearance register on our website at <http://www.comcom.govt.nz/clearances-register/>
29. As part of our investigation, we will identify the parties we believe will provide the best information to help us assess the preliminary issues identified above. We will be contacting those parties over the next few weeks.

30. We also invite submissions from any other parties who consider they have information relevant to our consideration of this matter. If you wish to make a submission, please email it to us at registrar@comcom.govt.nz with the reference Beijer/Realcold in the subject line of your email, or post it to us at The Registrar, PO Box 2351, Wellington 6140 by close of business **7 September 2015**. Please clearly identify any confidential information contained in the submission and provide contact details.
31. 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.