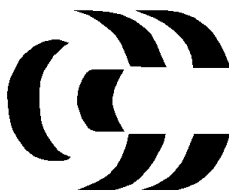


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## COMMERCE COMMISSION

### Commerce Commission

### Decision No. 346

Determination pursuant to the Commerce Act 1986 in the matter of an application involving:

**KROMA COLOUR PRINTS LIMITED**

and

**ZANDA LABORATORIES LIMITED**

**The Commission:** K M Brown

**Summary of Proposed Acquisition:** Acquisition by Kroma Colour Prints Limited of 100% of the share capital in Zanda Laboratories Limited.

**Determination:** Pursuant to s 66(3)(a) of the Act, the Commission determines to give clearance for the proposed acquisition

**Date of Determination:** 10 March 1999

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## **THE PROPOSED ACQUISITION**

- 1 Pursuant to section 66(1) of the Commerce Act 1986 (the Act), Kroma Colour Prints Limited (Kroma) gave notice to the Commission on 24 February 1999 (the application) seeking clearance for the proposed acquisition by it of 100% of the share capital in Zanda Laboratories Limited (Zanda)

## **THE PARTIES**

### **Kroma**

- 2 Kroma has its registered office in Auckland, and it provides photo finishing services from six sites in New Zealand to retailers and consumers throughout New Zealand. The company commenced business in 1976.
- 3 The shares in Kroma are held by individuals, mainly in joint shareholdings of three people. Each of the seven largest joint shareholdings accounts for about 11 % of the shares.

### **Zanda**

- 4 Zanda, which was formed in 1987, was owned until recently by Mr L E Riddle of Canterbury, but was then acquired by Kodak New Zealand Limited. The company, which trades as "Jumbo Prints", provides photo finishing services from eight sites in New Zealand.

## **PROCEDURES**

- 30 The application was registered by the Commission on 24 February 1999. Section 66(3) of the Commerce Act requires that the Commission, within 10 working days after the date of registration of the application, or such longer period agreed by the Commission and the applicant, gives, or declines to give, a clearance for the acquisition. The tenth working day after the registration of the application was 10 March 1999.
- 6 Kroma advised the Commission that it did not seek a confidentiality order for the fact of the application, but that it did require one for some of the information contained in the application. A Confidentiality Order was made in respect of certain information for a period of 20 working days from the Commission's determination. When the order expires, the provisions of the Official Information Act 1992 will apply.
- 7 The Commission's determination is based on an investigation conducted by Commission staff and their subsequent advice to the Commission.

## **THE INVESTIGATION**

- 8 In the course of their investigation of the proposed acquisition, Commission staff have discussed the application with a number of parties, including:
  - Viko New Zealand Limited, Auckland
  - Langwood Corporation Limited, Christchurch

- The Pharmacy Guild of New Zealand, Wellington,
- Hanimex (N.Z.) Limited, Auckland
- Postie Photos, Christchurch
- Photopost, Taupo
- Photo Finishing Systems Limited, Auckland

9 In addition, staff obtained further information from Kroma.

## **MARKET DEFINITION**

### **Introduction**

10 The purpose of defining a market is to provide a framework within which the competition implications of a business acquisition can be analysed. The relevant markets are those in which competition may be affected by the acquisition being considered. Identification of the relevant markets enables the Commission to examine whether the acquisition would result, or would be likely to result, in the acquisition or strengthening of a dominant position in terms of s 47(1) of the Act, in any market.

11 Section 3(1A) of the Act provides that:

... the term 'market' is a reference to a market in New Zealand for goods and services as well as other goods and services that, as a matter of fact and commercial common sense, are substitutable for them.

12 The Commission's Business Acquisition Guidelines provide information on how the Commission approaches the task of market definition.<sup>1</sup> A brief discussion of this approach follows.

13 Markets are defined in relation to product type, geographical extent, and functional level. The boundaries of the product and geographical markets are identified by considering the extent to which buyers are able to substitute other products or across geographical regions in response to a change in relative prices of the products concerned. A market is the smallest area in which all such substitution possibilities are encompassed. It is in this area that a hypothetical monopoly supplier could exert market power.

14 A properly defined market will include products which are regarded by buyers or sellers as being not too different ('product' dimension), and not too far away ('geographical' dimension). A market defined in these terms is one within which a hypothetical profit-maximising sole supplier of a product could impose at least a small yet significant and *non-transitory* increase in price (the "*ssnip*" test), assuming other terms of sale remain unchanged. It will also include those suppliers currently in production who are likely, in the event of such a *ssnip*, to shift promptly to offer a suitable alternative product, or offer their product to alternative acquirers.

15 Markets are also defined in relation to functional level. Typically, the production, distribution, and sale of products proceeds through a series of vertical functional

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<sup>1</sup> Commerce Commission, *Business Acquisition Guidelines* 1996, pp 11-16

levels, so the functional levels affected by the application have to be determined as part of the market definition. For example, that between manufacturers and wholesalers might be called the “manufacturing market”, while that between wholesalers and retailers is usually known as the “wholesaling market”. Functional levels are sometimes combined.

### **Product Market**

- 16 Kroma has defined the product market as “photo-processing and finishing for retailers and consumers of amateur photography”. Kroma provided a copy of a USA District Court Decision (U.S. v Eastman Kodak Co. 853 F.Supp 1454 (WDNY 1994) which concluded that the relevant product market definition for that case was “amateur colour negative film”. While this definition is of interest, the Commission must reach its own conclusion on market definition.
- 17 In a determination on a section 66 application in December 1996 (Kodak/Chromatek), the Commission accepted that photo finishing services for professional photographers (such as those producing wedding photographs and portraits) constituted a separate market. It was found that many firms provide these services. The Commission continues to view these services as constituting a separate market.
- 18 Amateur photographers who wish to have their films processed normally use one of three methods.
- 19 The traditional method was for consumers to leave the films with a retailer who is an agent for one of the wholesale film processors (of which Kroma, Jumbo and Viko are presently the largest), and then collect the processed photographs from that retailer. Pharmacies have been the main retail agents for the wholesalers, but some other retailers now provide this service. Courier services are used to bring the films to the wholesaler, and the photographs back to the retailer.
- 20 The second method is for consumers to leave their films with a mini-lab which undertakes the processing on the premises. Mini-labs are usually stand-alone businesses located in retail shopping districts with high foot traffic, but a few are located in large retail stores. There are about 500 mini-labs in New Zealand.
- 21 Third, consumers may post the films to processors which specialise in postal business. These firms generally provide free post envelopes for this purpose. The envelopes may be sent to consumers by direct mail, or they may be available in outlets such as supermarkets. The photographs are returned to the consumer by mail.
- 22 There are some minor variations on these three methods. In some cases consumers might themselves deliver their films to a wholesale processor who happens to be conveniently located. In some other cases retailers who act as agents may use a mini-lab rather than a wholesaler for the processing.
- 23 As the Eastman Kodak decision quoted above noted, the selection by consumers of the method by which they will have their films processed involves a trade-off between the considerations of time, convenience and price. While mini-labs can offer one-hour processing (some advertise a 30 minute service), retail agencies such as

pharmacies usually offer overnight service, or in some cases, same day service. Postal services require longer periods, such as “5 working days”. While prices appear to vary considerably, particularly for mini-labs, price is generally inversely related to the speed of service. Thus, one hour service at mini-labs might be offered at \$16.95 to \$18.95 per roll of 24 exposures. Kroma states that some Auckland mini-labs charge prices as low as \$12.50 to \$12.95 for this service. Overnight service from retail agents is often available at \$9.95 per roll of 24. Postal service is available at \$8.95 per roll, plus \$1.50 for return postage and handling, for rolls of up to 36 exposures.

- 24 In the Commission’s view, the avenues open to consumers for photo processing are substitutes, and these avenues constitute a single product market.

### **Geographic Market**

- 25 Kroma has defined the geographic market as national.
- 26 While mini-labs normally serve only their immediate locality, mini-labs are located throughout New Zealand. Some mini-labs are organised under banner groups which operate in many localities. The wholesale processors operate on a national basis though their agents who are located throughout New Zealand. Photopost, the largest postal processing service, provides a national coverage. The Commission concludes that the market is a national one.

### **Conclusion on Market Definition**

- 27 The Commission concludes that the relevant market is the New Zealand market for photo processing and finishing for retailers and consumers of amateur photography.

## **COMPETITION ANALYSIS**

### **Competition Analysis Overview**

- 28 Section 66(3) of the Act, when read in conjunction with s 47(1) of the Act, requires the Commission to give clearance for a proposed acquisition if it is satisfied that the proposed acquisition would not result, and would not be likely to result, in a person acquiring or strengthening a dominant position in a market. If the Commission is not so satisfied, clearance must be declined.
- 29 Section 3(9) of the Act states that a person is in a “dominant position” in a market if:
- ... a person as a supplier or an acquirer of goods or services either alone or together with an interconnected or associated person is in a position to exercise a dominant influence over the production, acquisition, supply, or price of goods or services in that market ...
- 30 That section also states that a determination of dominance shall have regard to:
- market share, technical knowledge and access to materials or capital;
  - the constraint exercised by competitors or potential competitors; and
  - the constraint exercised by suppliers or acquirers.

- 31 In reaching a view on whether a person is in a position to exercise a dominant influence in a market, the Commission considers the foregoing non-exhaustive factors and any other relevant matters that may be found in a particular case.
- 32 In the Commission's view, as expressed in the Business Acquisition Guidelines 1996 (p.17), a dominant position in a market is generally unlikely to be created or strengthened where, after the proposed acquisition, either of the following situations exist:
- the merged entity (including any interconnected or associated persons) has less than in the order of a 40% share of the relevant market;
  - the merged entity (including any interconnected or associated persons) has less than in the order of a 60% share of the relevant market and faces competition from at least one other market participant having no less than in the order of a 15% market share.
- 33 In *Port Nelson Ltd v Commerce Commission* {1996} 3 NZLR 554, the Court of Appeal approved the following dominance standard, adopted by McGechan J in the High Court:

... dominance involves more than "high" market power; more than mere ability to behave "largely" independently of competitors; and more than power to effect "appreciable" changes in terms of trading. It involves a high degree of market *control*. (emphasis in original).

- 34 Each of the relevant markets is considered below to assess whether the proposed merger might lead to the acquisition or strengthening of a dominant position.

### **Market Shares**

- 35 The photo processing industry does not pool its figures of the number of films processed, and there are no other official figures on the volume of production. Kroma estimated that 7.5 million rolls of film are processed each year in New Zealand, that 65% of this work is undertaken by mini-labs, and that the remaining 35% is processed by the wholesalers and postal providers. Kroma provided more detailed estimates of the market shares of individual operators.
- 36 Estimates given to the Commission by other market participants are in line with those provided in the application, and the Commission accepts Kroma's figures as providing a reasonable indication of market shares.
- 37 The effect of the proposal would be to increase Kroma's share of the relevant market from [ ] to [ ], a level which is well within the first of the safe harbours described in the Commission's Business Acquisition Guidelines.

### **Conditions for Entry and Expansion**

- 38 Mini-labs. Kroma states that used mini-lab equipment can be obtained for \$50,000 to \$80,000, and that new equipment would cost from \$100,000 to \$300,000. Information obtained by the Commission from other sources suggests that these price

ranges are reasonable estimates, although used equipment is available from as little as \$10,000 upwards. Used equipment originates both from equipment which was originally imported into New Zealand new, and imported used equipment. Used equipment appears to be regularly available. The price ranges for mini-lab equipment suggest that the level of entry costs to this segment of the market are unlikely to be a barrier, and this appears to be confirmed by the rapid expansion in the number of mini-labs to the present estimate of 500. There are indications that mini-labs may be installed in a wider range of retail outlets, thereby increasing the competition for their services.

- 39 Wholesalers. Kroma notes that Jumbo expanded from processing [ ] rolls a year to [ ] rolls in four years, a very rapid rate of increase. Kroma further notes that QFL, an Australian organisation, commenced business in Auckland in December 1998 and now serves 20 retail outlets. While the number of photo processing wholesalers is not large, these two recent examples suggest that expansion by existing participants and by new entrants is feasible.
- 40 Postal operators. While the turnaround time required for postal service is a limiting factor, postal operators provide a budget priced service. For consumers whose requirements are not time-sensitive, services provided by post appear capable of expansion. The main requirement for processors offering a postal service is to have their free post envelopes distributed widely to likely users.

### **Summary**

- 41 In the Commission's view the relatively low market share which would result from the proposal, and the relative ease of entry into the market, particularly for mini-labs, mean that the merged entity would be significantly constrained by its competitors, the other wholesalers, particularly Viko, and by the mini-lab and postal operators.
- 42 The Commission therefore concludes that the proposed acquisition would not result, and would not be likely to result, in any person acquiring or strengthening dominance in any market in terms of section 47(1) of the Act.

### **CONCLUSION**

- 43 The Commission has considered the impact of the proposal in the New Zealand market for photo processing and finishing for retailers and consumers of amateur photography.
- 44 Having regard to the factors set out in section 3(9) of the Commerce Act and all the other relevant factors, the Commission is satisfied that the proposal would not result, or would not be likely to result, in (the applicant) or any other person acquiring or strengthening a dominant position in a market.



## **DETERMINATION ON NOTICE OF CLEARANCE**

- 45 Accordingly, pursuant to section 66(3)(a) of the Commerce Act 1986, the Commission gives clearance for the acquisition by Kroma Colour Prints Limited of 100% of the share capital in Zanda Laboratories Limited.

Dated this .....day of March 1999

K M Brown  
Member