



## COMMERCE COMMISSION

### Decision No. 444

Determination pursuant to the Commerce Act 1986 in the matter of an application for clearance of a business acquisition involving:

**MICO WAKEFIELD LIMITED**

**and**

**MASTERTRADE LIMITED**

**The Commission:** PJM Taylor  
D Bates QC  
DF Curtin

**Summary of Application:** The acquisition by Mico Wakefield Limited or any interconnected body corporate of Mico Wakefield Limited of up to 100% of the shares in; or any or all of the assets of, MasterTrade Limited.

**Determination:** Pursuant to section 66(3)(a) of the Commerce Act 1986, the Commission determines to give clearance for the proposed acquisition.

**Date of Determination:** 6 December 2001

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BRACKETS**

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## THE PROPOSAL

1. On 16 November 2001 the Commission registered a notice pursuant to section 66(1) of the Commerce Act 1986 (the Act), from Mico Wakefield Limited (“Mico” and “the Applicant”) to purchase all of the assets or shares of MasterTrade Limited (“MTL”).

## THE PROCEDURES

2. Section 66(3) of the Act requires the Commission either to clear or to decline to clear a notice given under section 66(1) within 10 working days, unless the Commission and the person who gave notice agree to a longer period. An extension of time was sought by the Commission and agreed to by the Applicant. Accordingly, a decision on the application was required by Friday 7 December 2001.
3. In its application, Mico sought confidentiality for specific aspects of the application. A confidentiality order was made in respect of the information for a period of 20 working days from the Commission’s determination notice. When that order expires, the provisions of the Official Information Act 1982 will apply.
4. The Commission’s determination is based on an investigation conducted by staff.
5. The Commission’s approach is based on principles set out in the Commission’s *Practice Note 4*.<sup>1</sup>

## THE PARTIES

### Mico Wakefield Limited

6. Mico Wakefield is a wholly owned subsidiary of Crane Group Limited (Crane), an Australian publicly listed company. Crane has a controlling interest in Iplex Pipelines NZ Limited (Iplex), a New Zealand company that supplies PVC products to outlets (including a small amount to MasterTrade) for resale. Crane also owns Crane Distribution Limited (trading as Tradelink Plumbing Supplies), an Australian supplier of plumbing products. Tradelink Plumbing Supplies does not sell product in New Zealand.
7. Mico Wakefield is a supplier of plumbing, electrical (trading as Corys Electrical) and metal (and related electrical and plumbing) products. It has 87 branches throughout New Zealand.

### MasterTrade Limited

8. MTL is a wholly-owned subsidiary of electrical and electronics group, PDL, a designer and manufacturer of electrical accessories and AC motor controllers. PDL is a wholly-owned subsidiary of Schneider Electric SA (Schneider). Schneider ultimately owns 100% of PDL Electrical Limited (Wiring Accessories), PDL Electronics (AC Motor

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<sup>1</sup> Commerce Commission, *Practice note 4: The Commission’s Approach to Adjudicating on Business Acquisitions Under the Changed Threshold in section 47 – A Test of Substantially Lessening Competition*, May 2001.

Control) and Parkside Laboratories. The acquisition is of the assets of, or shares in, MTL only.

9. MTL is a supplier of plumbing and electrical products. It has 47 branches throughout New Zealand, focussing on electrical and plumbing products (and related products) and inventory and facilities management. The acquisition is in relation to electrical and plumbing products only.

## **OTHER RELEVANT PARTIES - PLUMBING PRODUCTS**

### **Plumbing World**

10. Plumbing World is a wholly owned New Zealand company that operates as a co-operative. It has 37 stores throughout New Zealand, which specialise in plumbing trade supplies and the retailing of bathroom products.

### **Chesters**

11. Chesters Plumbing and Bathroom Centre is a privately owned NZ company that has six stores located in New Lynn (two), North Shore, Ellerslie, Silverdale and Hamilton. Chesters is a supplier of plumbing products to trade customers and also a retailer of bathroom products to the public.

### **Franklins**

12. Franklins Plumbers and Building Supplies Limited is a privately owned company involved in the supply of plumbing products to the plumbing trade and to the public. Franklins has four stores, all of which are in the Auckland region.

### **Plumbing Plus**

13. Plumbing Plus is a national marketing and buying group comprising a number of independent suppliers of plumbing products. The largest member of the group is Edward Gibbons, which is based in Christchurch and has branches throughout the South Island. Other members of the group include LG Carder Ltd in Auckland and Kealls Plumbing Plus in Palmerston North

## **OTHER RELEVANT PARTIES - ELECTRICAL PRODUCTS**

### **Rexel /Ideal**

14. Rexel and Ideal are the two brand names of Redeal Limited, a wholly owned subsidiary of the Rexel Group, a large international distributor of electrical installation products, which has its headquarters in France. There are 69 Redeal outlets throughout New Zealand.

### **JA Russell Limited**

15. JA Russell is a privately owned company that supplies electrical products to electrical industry users. It has 21 branches, all of which are situated in the North Island, from Taupo north. JA Russell is the largest member of Powerbase Incorporated.

### **Powerbase Incorporated**

16. Powerbase is a group of privately owned and operated electrical merchants with outlets located throughout New Zealand. Powerbase was formed in order for group members to take advantage of the increased marketing, product sourcing and purchasing ability that collective action afforded them. Other participants in the group include Stewarts Electrical Supplies in the Central North Island region, and R Redpath Limited in the South Island.

### **INDUSTRY BACKGROUND**

17. Merchants such as Mico, MTL, and their competitors, typically provide plumbing and electrical products to several types of customers. These include: tradesmen operating small businesses (one to four person operations); large plumbing and electrical contracting firms; large industrials such as Carter Holt Harvey and Norske Skog that require such supplies for plant maintenance; and, to a lesser extent, the ‘do it yourself’ (“DIY”) customer.
18. In recent times, sales of plumbing products to DIY customers have increased, as product range has expanded (largely due to an increase in imported lines), particularly in the ‘front of the wall’ product ranges. ‘Front of the wall’ is a term used particularly in the plumbing industry and includes fittings such as basins, baths, showers, and tapware; those fittings literally found in front of the wall. ‘Behind the wall’ products such as PVC and copper piping are more typically purchased by tradesman and contractors, rather than the DIY customer.
19. Despite recent deregulation of the electrical installation industry, the supply of electrical products is predominantly to electrical tradesmen and contractors. Industry participants have suggested that this is largely due to an aversion on the part of DIY customers to involve themselves with electrical current.

### **MARKET DEFINITION**

20. The Act defines a **market** as:

*. . . a market in New Zealand for goods or services as well as other goods or services that, as a matter of fact and commercial common sense, are substitutable for them.*

21. For the purpose of competition analysis, a relevant market is the smallest space within which a hypothetical, profit-maximising, sole supplier of a good or service, not constrained by the threat of entry, could impose at least a small yet significant and non-transitory increase in price, assuming all other terms of sale remain constant (the ‘*ssnip*

test'). For the purpose of determining relevant markets, the Commission will generally consider a *ssnip* to involve a five percent increase in price for a period of one year.

22. It is substitutability at competitive market prices which is relevant in defining markets. Where the Commission considers that prices in a given market are significantly different from competitive levels, it may be necessary for it to assess the effect of a *ssnip* imposed upon competitive price levels, rather than upon actual prices, in order to detect relevant substitutes.
23. The Commission will seek to define relevant markets in terms of four characteristics or dimensions:
  - the goods or services supplied and purchased (the product dimension);
  - the level in the production or distribution chain (the functional level);
  - the geographic area from which the goods or services are obtained, or within which the goods or services are supplied (the geographic extent); and
  - the temporal dimension of the market, if relevant (the timeframe).
24. The Commission will seek to define relevant markets in a way that best assists the analysis of the competitive impact of the acquisition under consideration. A relevant market will ultimately be determined, in the words of the Act, as a matter of fact and commercial common sense.
25. Where markets are difficult to define precisely, the Commission will initially take a conservative approach. If the proposed acquisition can be cleared on the basis of a narrow market definition, it would also be cleared using a broader one. If the Commission is unable to clear the proposed acquisition on the basis of the narrower market, it will be necessary to review the arguments and evidence in relation to broader markets.

### **Product Dimension**

26. The delineation of relevant markets as a basis for assessing the competitive effects of a business acquisition begins with an examination of the goods or services offered by each of the parties to the acquisition. Both demand-side and supply-side factors are generally considered in defining market boundaries. Broadly speaking, a market includes products that are close substitutes in buyers' eyes on the demand-side, and suppliers who produce, or are able easily to substitute to produce, those product on the supply-side.
27. The Commission takes the view that the appropriate time period for assessing substitution possibilities is the longer term, but within the foreseeable future.<sup>2</sup> The

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<sup>2</sup> In *Tru Tone Ltd v Festival Records Retail Marketing Ltd* [ ] 2 NZLR 351 Smellie J and the Court of Appeal on appeal approvingly quoted an earlier decision of the Commerce Commission in *Edmonds Food Ind Ltd v W F Tucker & Co Ltd* (Decision 21, June 1984) where the Commission had ruled: "A market has been defined as a field of actual or potential transactions between buyers and sellers amongst whom there can be strong substitution, at least in the long run, if given a sufficient price incentive". See also *News Limited v Australian Rugby Football League Limited & Ors* (1996) ATPR at 41,687, where Burchett J stated: "Long term prospects that can be more or less clearly foreseen are, to that extent, a present reality, from the point of view of identifying the constraints upon commercial action. This fact emphasises the importance of the principle . . . that substitution possibilities in the longer run may be very significant for market delineation." Also *Re Tooth & Co Ltd v Tooheys Ltd* (1979) 39 FLR 1 emphasises longer run substitution possibilities.

Commission considers this to be a period of one year, which is the period customarily used internationally in applying the ‘ssnip’ test (see below) to determine market boundaries. The Commission will take into account recent, and likely future, changes in products, relative prices and production technology in the process of market definition.

28. The applicant submits that two markets will be affected by this acquisition:

- The regional markets for the supply of plumbing products; and
- The regional markets for the supply of electrical products.

*Demand-side substitution*

29. Close substitute products on the demand-side are those between which at least a significant proportion of buyers would switch when given an incentive to do so by a small change in their relative prices.

30. Initially, markets are defined for each product supplied by two or more of the parties to an acquisition. Unequivocal substitutes are combined. For each initial market so defined, the Commission will examine whether the imposition of a snip would be likely to be profitable for the hypothetical monopolist. If it were, then all of the relevant substitutes must be incorporated in the market. If not, then the next most likely substitute good or service will be added to the initial market definition and the test repeated. This process continues until a combination of products is found which defines the product dimension of a relevant market, namely, the smallest combination of goods or services for which a snip would be profitable.

31. On the demand-side, the technical viability of one good or service as a substitute for another must be assessed. However, even where another product may technically be suitable as an alternative for the product in question, its price may be so much higher that it may be a poor substitute in an economic sense, at least for the great majority of buyers. In judging economic substitutability between products, the Commission will have regard to relative prices, quality and performance when assessing whether they are, in fact, close substitutes in the eyes of buyers.

32. A number of products fall within the “plumbing products” and “electrical products” definitions respectively.

33. In respect of plumbing products, the Applicant submits and industry participants confirm that plumbing products include:

- cylinders and water heaters;
- brass and copper, Polybute, and galvanised pipe and fittings;
- drain, waste and vent pipes and fittings;
- valves, ballcocks, pumps, lead, solder, pipe insulation, tools and sundries;
- spouting;
- basins, baths, showers, sinks and tubs;



- taps, shower valves and roses;
  - pans, cisterns and seats;
  - vanities;
  - gas appliances, wood fires etc; and
  - associated accessories.
34. The plumbing product range therefore includes front of the wall products and behind the wall products. Industry participants agree that they deal in products that extend to the point of water and/or gas supply.
35. In respect of electrical products, the Applicant submits and industry participants confirm that electrical products include:
- cable;
  - cable protection and repair;
  - data and communications, TV and repair;
  - switchgear;
  - lighting;
  - distribution (fuses, timers, meter boxes, transformers etc);
  - industrial and motor control (sensing and detection, motors, capacitors, starters, indicators/lamps etc);
  - hot water systems and appliances; and
  - hardware (tools, safety and fire-fighting products, fasteners, consumables, connectors, leads/power boards etc).
36. As for plumbing products, the scope of electrical products generally extends beyond the building itself to the point of electrical supply.
37. Many of the products listed above are not substitutable from a demand-side perspective, as their form and function are specific for the purpose to which they are put.
38. For the purposes of this analysis, the Commission therefore intends to adopt the following product definitions:
- plumbing products; and
  - electrical products.

*Undifferentiated/Differentiated Products*

39. In some instances, market definitional problems arise because of the differentiated nature of the goods or services involved in a business acquisition, caused by differing technical specifications, branding, packaging, warranties, distribution channels and other factors.
40. Where a significant group of buyers within a relevant market is likely to be subject to price discrimination, the Commission will consider defining additional relevant markets based on particular uses for a good or service, particular groups of buyers, or buyers in particular geographic areas. In other cases, the primary focus may switch to the extent to which a business acquisition eliminates competition between the products brought together by the acquisition.
41. Apart from front of the wall plumbing products, the majority of products supplied by the market are standardised with price being a minimal differentiator. However, the extent of differentiation is not such as to require close analysis of the extent of substitutability. For the purposes of this application, separate product markets for particular types of plumbing and electrical products will not be defined.
42. The Commission therefore concludes that for the purpose of assessing the competition implications of the proposed acquisition, the appropriate product markets are:
  - the market for the supply of plumbing products; and
  - the market for the supply of electrical products.

**Geographic Extent**

43. The Commission will seek to define the geographical extent of a market to include all of the relevant, spatially dispersed, sources of supply to which buyers can turn should the prices of local sources of supply be raised. For each good or service combination, the overlapping geographic areas in which the parties operate are identified. These form initial markets to which a ssnip is applied. Additional geographic regions are added until the smallest area is determined within which the hypothetical monopolist could profitably impose a ssnip.
44. Generally, the higher the value of the product to be purchased, in absolute terms or relative to total buyer expenditure as appropriate, the more likely are buyers to travel and shop around for the best buy, and the wider the geographic extent of the market is likely to be.
45. Where transport costs are high relative to the final value of a product, a narrower geographic market is more likely to be appropriate. Where product perishability and other similar practical considerations limit the distance that a product may be transported, this may limit the geographic extent of the market. The timeliness of delivery from alternative geographic sources is similarly relevant.
46. Although buyers and sellers of a particular good or service may interact in markets that are apparently local or regional in extent, those markets may themselves overlap and interrelate so as to form a market covering a larger geographical area. In these situations,

the larger market is likely to be the appropriate one for analysing the competitive effects of a business acquisition.

47. The geographical aspect involved in the supply of electrical and plumbing products is similar. Therefore the following discussion is applicable to both.
48. The Applicant submits that regional markets are applicable in this instance, arguing that the majority of sales are made to tradespeople who, by the nature of their work, cover a number of different localities. The Applicant refers to the geographical approach adopted by the Commission in Decision 213 *Fletcher Challenge Limited/New Zealand Forest Products Limited* where the greater Auckland region was identified as a single geographic market in respect of the market for building supplies. The Applicant defines the geographic regions as:
- Northland;
  - Auckland;
  - Waikato/Coromandel;
  - Bay of Plenty;
  - Hawkes Bay (including Gisborne);
  - Manawatu/Taranaki;
  - Wellington/Wairarapa;
  - West Coast (no aggregation)
  - Marlborough/Nelson;
  - Canterbury;
  - Otago; and
  - Southland.
49. The Commission's investigation revealed that whilst the larger contractor is willing to travel greater distances to obtain supplies, the smaller operator is less willing to travel such distances. To this extent, the Commission analysed the aggregation that the proposed merger will give rise to by town/city and found that the market shares in those towns/cities was consistent with the regional figures. The Commission therefore concurs with the Applicant that the geographic markets are regional.

### **Functional Level**

50. The production, distribution and sale of a product typically occurs through a series of functional levels – for example, the manufacturing/import level, the wholesale/distribution level and the retail level. It is often useful to identify the relevant functional level in describing a market, as a proposed business acquisition may affect one horizontal level, but not others.<sup>3</sup> Alternatively, some acquisitions, such as those

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<sup>3</sup> *Telecom Corporation of New Zealand Ltd v Commerce Commission* (1991) 4 TCLR 473, 502 The High Court (Greig J, Shaw WJ, Prof M Brunt) noted: "If we ask what functional divisions are appropriate in any market

involving businesses at different vertical levels, may raise issues related to vertical integration. Generally, the Commission will seek to identify separate relevant markets at each functional level affected by an acquisition and assess the impact of the acquisition on each.

51. The functional aspect of the supply of plumbing and electrical products are similar, therefore the following discussion is applicable to both.
52. In this case, the precise functional market is blurred. Mico and MTL supply plumbing and electrical products to tradespeople at the wholesale level and also to DIY customers at the retail level.
53. While tradespeople generally include in their invoice to clients, separate material and labour components, they are not considered to be resuppliers of plumbing and electrical products in the sense that they purchase at the wholesale level and resell at the retail level.
54. The Commission noted in Decision No.433, *Howard Smith/OPSM Protector* that where a company supplies goods at various functional levels, the functional level appropriate to the market definition is that of supply.
55. The Commission therefore proposes to adopt the functional level of supply in this instance.

### **The Timeframe**

56. Generally, the Commission will view markets as functioning continuously over time. However, where a market is characterised by, for example, infrequent transactions, the Commission may seek to define a separate time dimension as part of its market definition process. Time considerations are also important where there are long-term contracts, and where there are depletable resources.
57. Time dimension is not relevant to the analysis of the regional markets for the supply of general plumbing and electrical products, as transactions are frequent and there are few long-term contracts between suppliers and acquirers.

### **Conclusion on Market Definition**

58. The Commission concludes that the relevant definitions are:
  - The regional markets for the supply of plumbing products (“plumbing products markets”); and
  - The regional markets for the supply of electrical products (“electrical product markets”).

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definition exercise, the answer, ..., must be whatever will best expose the play of market forces, actual and potential, upon buyers and sellers. Wherever successive stages of production and distribution can be co-ordinated by market transactions, there is no difficulty: there will be a series of markets linking actual and potential buyers and sellers at each stage. And again, where pronounced efficiencies of vertical integration dictate that successive stages of production and distribution must be co-ordinated by internal managerial processes, there can be no market.”

## COMPETITION ANALYSIS

### Substantially Lessening Competition

59. Section 47 of the Act prohibits particular business acquisitions. It provides that:

A person must not acquire assets of a business or shares if the acquisition would have, or would be likely to have, the effect of substantially lessening competition in a market.

60. Section 2(1A) provides that substantial means “real or of substance”. Substantial is taken as meaning something more than insubstantial or nominal. It is a question of degree.<sup>4</sup> What is required is a real lessening of competition that is not minimal. The lessening needs to be of such size, character and importance to make it worthy of consideration.<sup>5</sup>
61. Section 3(2) provides that references to the lessening of competition include references to the hindering or preventing of competition.<sup>6</sup>
62. While the Act defines the words “substantial” and “lessening” individually it is desirable to consider the phrase as a whole. For each relevant market, the Commission will assess:
- the probable nature and extent of competition that would exist in a significant section of the market, but for the acquisition (the counterfactual);
  - the nature and extent of the contemplated lessening; and
  - whether the contemplated lessening is substantial.<sup>7</sup>
63. In considering whether the acquisition would have, or would be likely to have, the effect of substantially lessening competition in a market, the Commission will take account of the scope for the exercise of market power, either unilaterally or through co-ordination between firms.
64. When the impact of enhanced market power is expected predominantly to be upon price, the anticipated price increase relative to what would otherwise have occurred in the market has to be both material, and able to be sustained for a period of at least two years, for the lessening, or likely lessening, of competition to be regarded as substantial. Similarly, when the impact of increased market power is felt in terms of the non-price dimensions of competition, these also have to be both material and able to be sustainable

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<sup>4</sup> *Commerce Commission v Port Nelson Ltd* (1995) 6 TCLR 406, 434; *Mobil Oil Corporation v The Queen in Right of NZ* 4/5/89, International Centre for Settlement of Investment Disputes, Washington DC, International Arbitral Tribunal ARB/87/2 (paras 8.2, 19, 20).

<sup>5</sup> *Dandy Power Equipment Ltd v Mercury Marina Pty Ltd* (1982) ATPR 40-315, 43-888; *South Yorkshire Transport Ltd v Monopolies & Mergers Commission* [ ] 1 All ER 289.

<sup>6</sup> For a discussion of the definition see *Commerce Commission v Port Nelson Ltd*, supra n 6, 434.

<sup>7</sup> See *Dandy*, supra n 5, pp 43–887 to 43-888 and adopted in New Zealand: *ARA v Mutual Rental Cars* [ ] 2 NZLR 647; *Tru Tone Ltd v Festival Records Retail Marketing Ltd* [ ] 2 NZLR 352; *Fisher & Paykel Ltd v Commerce Commission* [ ] 2 NZLR 731; *Commerce Commission v Carter Holt Harvey*, unreported, High Court, Auckland, CL 27/95, 18/4/00.

for at least two years for there to be a substantial lessening, or likely substantial lessening, of competition.

### **The Counterfactual**

65. The Commission will continue to use a forward-looking, counterfactual, type of analysis in its assessment of business acquisitions, in which two future scenarios are postulated: that with the acquisition in question, and that in the absence of the acquisition (the counterfactual). The impact of the acquisition on competition can then be viewed as the difference between those two scenarios. It should be noted that the status quo cannot necessarily be assumed to continue in the absence of the acquisition, although that may often be the case. For example, in some instances a clearly developing trend may be evident in the market, in which case the appropriate counterfactual may be based on an extrapolation of that trend.
66. The present state of competition in a market can be referred to in order to illuminate the future state of the market where there is a range of possible scenarios should a merger not proceed.<sup>8</sup>
67. MTL advised the Commission staff [

] The Commission therefore  
proposes to use the status quo as the counterfactual.

### **Potential Sources of Market Power**

68. Two types of market situation conducive to the exercise of substantial unilateral market power are now considered. These involve making the distinction between undifferentiated and differentiated product markets. That distinction may also have a bearing on the scope for co-ordinated behaviour in a market.
69. In undifferentiated product markets, where buyers make their purchases largely on the basis of price, and the production capacities of firms are an important element in competition, a business acquisition may have the potential to substantially lessen competition when the combined entity has acquired a market share below that required for dominance. This is especially likely in circumstances where the rivals of the combined entity cannot easily expand production to offset its output contraction within a one year time frame.<sup>9</sup> The inability of rivals to expand may result either from their facing binding capacity constraints, or because additional capacity is significantly more expensive to operate.
70. In differentiated products markets, where the product offerings of different firms vary, and in which buyers make their purchase decisions on the basis of product characteristics as well as of price, the products of firms are by definition not perfect substitutes for each other. The substitutability between products will vary depending upon differences in their various characteristics, which may include their physical specifications, brand

<sup>8</sup> *Stirling Harbour Services Pty Ltd v Bunbury Port Authority* (2000) ATPR 41 at paras 113 & 114.

<sup>9</sup> See, for example, Roger D Blair and Amanda K Esquibel, "The Roles of Areeda, Turner and Economic Theory in Measuring Monopoly Power" (1996) *Antitrust Bulletin*, 781, especially pp 791-95.

image, associated services and location of sale. In simple terms, differentiated products can be thought of as being arranged in a “chain of substitutes”, where those in adjacent positions in the chain tend to be close substitutes, and those positioned further apart are less close substitutes.

71. The supply-side characteristics of differentiated products markets are important, as the potential market power of the combined entity may be offset by the actions of rivals. However, rivals may not be able to offer a competitive constraint where they are unable either to re-position their products closer to that of the combined entity to replace the lost localised competition, or to strengthen the promotion of existing products. A further possible constraint would be lost if it were not possible for new products to be added through new entry.
72. The Commission considers that in the present application, the product range offered by suppliers is not so differentiated as either to cast doubt on there being single, well defined markets as described above, or to require a special analysis with fully differentiated product markets.

### **Conclusion – Competition Analysis Principles**

73. The Act prohibits business acquisitions that would be likely to have the effect of substantially lessening competition in a market. The Commission makes this assessment against a counterfactual of what it considers would be likely to happen in the absence of the acquisition. In the present case the counterfactual is considered to be the status quo. A substantial lessening of competition is taken to be equivalent to a substantial increase in market power. A business acquisition can lead to an increase in market power by providing scope either for the combined entity to exercise such power unilaterally, or for the firms remaining in the market to co-ordinate their behaviour so as to exercise such power.
74. In broad terms, a substantial lessening of competition cannot arise from a business acquisition where there are sufficient competitive constraints upon the combined entity. The balance of this Decision considers and evaluates the constraints that might apply in the previously defined markets under the following headings:
  - existing competition;
  - potential competition from entry; and
  - other competition factors.

## **ANALYSIS OF EXISTING COMPETITION**

### **Introduction**

75. One consequence of a merger between competitors is that the number of firms competing in a market is reduced or, put another way, concentration is increased. This raises the possibility that competition in the market may be substantially lessened through the exercise of unilateral or coordinated market power. These are the subject of the analysis in this section.

## Scope for Unilateral Market Power

### *Introduction*

76. An examination of concentration in a market post-acquisition can provide a useful guide to the constraints that market participants may place upon each other, including the combined entity. Both structural and behavioural factors have to be considered. However, concentration is only one of a number of factors to be considered in the assessment of competition in a market. Those other factors are considered in later sections, as noted above.
77. Market shares can be measured in terms of revenues, volumes of goods sold, production capacities or inputs (such as labour or capital) used. All measures may yield similar results in some cases. Where they do not, the Commission may, for the purposes of its assessment, adopt the measure which yields the highest level of market share for the combined entity. The Commission considers that this will lead to an appropriately conservative assessment of concentration, and that the factors which lead to the other different market share results are more appropriately considered elsewhere during the assessment of the acquisition.<sup>10</sup>
78. In determining market shares, the Commission will take into account the existing participants (including ‘near entrants’), inter-firm relationships, and the level of imports. This is followed by a specification of the Commission’s ‘safe harbours’, an estimation of market shares, and an evaluation of existing competition in the market. Each of these aspects is now considered in turn.

## The Plumbing Products Markets

### *Existing Participants*

79. There are numerous competitors in each of the regional markets. In particular, Plumbing World and the Plumbing Plus group are vigorous competitors in the plumbing products markets. In addition, Chesters poses significant competition in the region from Hamilton north, and Franklins has a strong presence in the Auckland region.
80. Participants at all levels of the plumbing industry advised the Commission that there is strong competition in the markets for the supply of plumbing products.

### *Inter-firm Relationships*

81. Companies that are part of the same corporate grouping, or that have similar strong relationships, cannot be relied upon to provide an effective competitive constraint to one another. Other less formal relationships between companies may also give rise to limitations on the extent of rivalry between them. Relationships between persons in the relevant market and other businesses may also affect rivalry in a market.

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<sup>10</sup> For example, where market share measured in terms of capacity produces a significantly lower share of the market in the hands of participants than a measure in terms of sales volumes, the constraint on a combined entity from that unemployed capacity might be taken into account when identifying near entrants or the constraint from new market entry. In some cases, the model of market power being used may influence the choice as to which market share measure is used.



82. Although some suppliers of plumbing products are members of industry associations, their ability to influence the industry is limited.

#### *Imports*

83. In markets where imports are present, the Commission will consider whether actual competition from imported products is the equivalent to that from domestic supply. In undertaking this evaluation, the Commission will take into account the existence of any limits on quantities of imported product (the price elasticity of supply), and the effects on trade of various factors. Imports channelled through the parties to an acquisition, or persons associated with them, will be added to their domestic production in assessing market share, rather than being treated as independent sources of supply.
84. Potential imports may also provide a constraint on domestic suppliers, however the Commission considers that imports are not relevant to this analysis of the plumbing products markets.

#### *Safe Harbours*

85. Once the relevant market has been defined, the participants have been identified, and their market shares estimated, the Commission's 'safe harbours' can be applied. Under these safe harbours, a business acquisition is considered unlikely to substantially lessen competition in a market where, after the proposed acquisition, either of the following situations exist:
- where the three-firm concentration ratio (with individual firms' market shares including any interconnected or associated persons) in the relevant market is below 70%, the combined entity (including any interconnected or associated persons) has less than in the order of a 40% share; or
  - where the three-firm concentration ratio (with individual firms' market shares including any interconnected or associated persons) in the relevant market is above 70%, the market share of the combined entity is less than in the order of 20%.
86. As noted below, market shares by themselves are insufficient to establish whether competition in a market has been lessened. Other relevant issues are discussed in later sections.

#### *Market Shares*

87. The Commission proposes to use comparative annual turnover figures as its primary measure of market share and concentration.
88. The Applicant provided to the Commission aggregated national figures for the plumbing products market, and those for the aforementioned regions. Aggregated national shares for the plumbing products market are shown in Table 1 below:

**Table 1 – Estimated National Market Shares for the Plumbing Products Market**

<b>Company</b>	<b>Turnover (\$m)</b>	<b>Market Share (%)</b>
Plumbing World	[ ]	[ ]
Mico Wakefield	[ ]	[ ]
MasterTrade	[ ]	[ ]
Chesters	[ ]	[ ]
Franklins	[ ]	[ ]
Plumbing Plus and Other Independents	[ ]	[ ]
Hardware Stores	[ ]	[ ]
<b>Total</b>	<b>[ ]</b>	<b>100</b>
<b>Current 3-Firm Concentration Ratio</b>		[ ]
<b>Post-Merger 3-Firm Concentration Ratio</b>		[ ]
<b>Mico/MTL</b>		[ ]

89. The current three firm concentration is [ ]. Post merger, the three firm concentration ratio would be [ ] with the merged entity having a [ ] share. These figures are outside the Commission's safe harbours.
90. The Commission has also analysed regional figures for plumbing products. Areas where post-merger market shares would fall outside the safe harbours are Hawkes Bay [ ], Wellington [ ], Marlborough [ ], Otago [ ], and Southland [ ].
91. The following tables show the relative market shares held by participants in those regions:

**Table 2 – Estimated Market Shares for the Hawkes Bay Plumbing Products Market**

<b>Company</b>	<b>Turnover (\$m)</b>	<b>Market Share (%)</b>
Mico Wakefield	[ ]	[ ]
MasterTrade	[ ]	[ ]
Plumbing World	[ ]	[ ]
Plumbing Plus	[ ]	[ ]
Others	[ ]	[ ]
<b>Total</b>	<b>[ ]</b>	<b>[ ]</b>
<b>Current 3 Firm Concentration Ratio</b>		[ ]
<b>Post-Merger 3 Firm Concentration Ratio</b>		[ ]
<b>Mico/MTL</b>		[ ]

**Table 3 – Estimated Market Shares for the Wellington Plumbing Products Market**

<b>Company</b>	<b>Turnover (\$m)</b>	<b>Market Share (%)</b>
Mico Wakefield	[ ]	[ ]
MasterTrade	[ ]	[ ]
Plumbing World	[ ]	[ ]
Plumbing Plus	[ ]	[ ]
Others	[ ]	[ ]
<b>Total</b>	[ ]	[ ]
<b>Current 3 Firm Concentration Ratio</b>		[ ]
<b>Post-Merger 3 Firm Concentration Ratio</b>		[ ]
<b>Mico/MTL</b>		[ ]

**Table 4 – Estimated Market Shares for the Marlborough Plumbing Products Market**

<b>Company</b>	<b>Turnover (\$m)</b>	<b>Market Share (%)</b>
Mico Wakefield	[ ]	[ ]
MasterTrade	[ ]	[ ]
Plumbing World	[ ]	[ ]
Plumbing Plus	[ ]	[ ]
Others	[ ]	[ ]
<b>Total</b>	[ ]	[ ]
<b>Current 3 Firm Concentration Ratio</b>		[ ]
<b>Post-Merger 3 Firm Concentration Ratio</b>		[ ]
<b>Mico/MTL</b>		[ ]

**Table 5 – Estimated Market Shares for the Otago Plumbing Products Market**

<b>Company</b>	<b>Turnover (\$m)</b>	<b>Market Share (%)</b>
Mico Wakefield	[ ]	[ ]
MasterTrade	[ ]	[ ]
Plumbing World	[ ]	[ ]
Plumbing Plus	[ ]	[ ]
Others	[ ]	[ ]
<b>Total</b>	[ ]	[ ]
<b>Current 3 Firm Concentration Ratio</b>		[ ]
<b>Post-Merger 3 Firm Concentration Ratio</b>		[ ]
<b>Mico/MTL</b>		[ ]

**Table 6 – Estimated Market Shares for the Southland Plumbing Products Market**

<b>Company</b>	<b>Turnover (\$m)</b>	<b>Market Share (%)</b>
Mico Wakefield	[ ]	[ ]
MasterTrade	[ ]	[ ]
Plumbing World	[ ]	[ ]
Plumbing Plus	[ ]	[ ]
Others	[ ]	[ ]
<b>Total</b>	[ ]	[ ]
<b>Current 3 Firm Concentration Ratio</b>		[ ]
<b>Post-Merger 3 Firm Concentration Ratio</b>		[ ]*
<b>Mico/MTL</b>		[ ]

\*Aggregated market shares were provided for smaller participants, as such the post-merger three firm ratio is likely to be less than [ ]

92. The data in Tables 2 to 6 show that the respective markets will be concentrated post-merger. The post-merger three firm concentration ratios are above [ ] in each instance with the merged entity having between [ ] to [ ] market share. These percentages fall outside the Commission's safe harbours.
93. As already noted, market shares are insufficient in themselves to establish whether competition in a market has been lessened. It is the interplay between a number of competition factors, of which seller concentration is only one that has to be assessed in determining the impact of a business acquisition on competition. Other competition factors include entry conditions; the presence of an aggressive, innovative or maverick firm; countervailing power of buyers or suppliers; rapid innovation in the market; and others. These are considered for the relevant market in subsequent sections.

*State of Existing Competition*

94. The acquisition would result in the merged entity becoming the largest provider of plumbing products with a national aggregated market share of [ ]%. Despite this, the merged entity would face strong competition from existing participants in the market.
95. Plumbing World has around [ ] market share on a national basis, [ ] The Plumbing Plus group has around [ ] market share, [ ]
96. In each of the regional markets analysed in tables 2-6 above, there is at least one significant competitor that would provide a constraint on the merged entity. Smaller independent companies also have a presence in these markets.
97. All plumbing industry participants interviewed consider the plumbing products markets to be highly competitive.

*Conclusions – Unilateral Market Power*

98. The merged entity would be constrained by current competition. In all regional markets, the merged entity faces strong competition from Plumbing World and/or members of the Plumbing Plus group, with smaller independents also having a presence.

**Scope for the Exercise of Coordinated Market Power***Introduction*

99. A business acquisition may lead to a change in market circumstances such that coordination between the remaining firms either is made more likely, or the effectiveness of pre-acquisition coordination is enhanced. Firms that would otherwise compete may attempt to coordinate their behaviour in order to exercise market power by restricting their joint output and raising price. In extreme cases, where all firms in the market are involved and coordination is particularly effective, they may be able to behave like a collective monopolist. Where not all firms are involved, and market share in the hands of the collaborators is reduced, coordinated market power becomes more difficult to exercise because of competition from the independent firms in the market.
100. In broad terms, successful coordination can be thought of as requiring two ingredients: ‘collusion’ and ‘discipline’. ‘Collusion’ involves the firms individually coming to a mutually profitable expectation or agreement over coordination; ‘discipline’ requires that firms that would deviate from the understanding are detected and punished (thereby eliminating the short-term profit to be gained by the firm from deviating).
101. When assessing the scope for coordination in the market during the consideration of a business acquisition, the Commission will evaluate the likely post-acquisition structural and behavioural characteristics of the relevant market or markets to test whether the potential for coordination would be materially enhanced by the acquisition. The intention is to assess the likelihood of certain types of behaviour occurring, and whether these would be likely to lead to a substantial lessening of competition.

### *Collusion*

102. “Collusion” involves firms in a market individually coming to a mutually profitable expectation or agreement over coordination. Both explicit and tacit forms of such behaviour between firms are included.
103. The structural and behavioural factors that are usually considered to be conducive to collusion are set out in the left-hand column in Table 9. The significance of these is explained more fully in the Commission’s *Practice Note 4*. The right-hand column of the table then assesses the extent to which those factors are present, or are likely to be enhanced post-merger, in the plumbing products market. A high proportion of ‘yes’ responses would suggest that the market was particularly favourable to ‘collusion’; a high proportion of ‘no’ responses the reverse.

**Table 7 - Testing the Potential for ‘Collusion’ in the Plumbing Products Market**

<b>Factors conducive to collusion</b>	<b>Presence of factors in the market</b>
High seller concentration	Yes- the three firm concentration in some regions exceeds prescribed safe harbours.
Undifferentiated product	Yes –the range of products supplied to the market is largely undifferentiated.
New entry slow	No – entry can be effected relatively quickly.
Lack of fringe competitors	No – there are a number of fringe competitors with the ability to quickly expand supply given the necessary incentive.
Price inelastic demand curve	No – demand for plumbing products is reasonably elastic.
Industry’s poor competition record	No –no problems apparent.
Presence of excess capacity	No – excess capacity is not relevant in this instance.
Presence of industry associations/fora	Yes - but with limited influence.

104. On analysis of the large number of negative responses in Table 7 above, the Commission is satisfied that the potential for collusion in the plumbing products market is minimal. Accordingly, the Commission has found it unnecessary to determine the potential for discipline in the plumbing products markets.

### *Conclusions – Co-ordinated Market Power*

105. The Commission concludes that the scope for the exercise of co-ordinated market power in the plumbing products markets would not be enhanced by the acquisition.

### **Conclusions – Existing Competition**

106. The Commission considers that existing competition will alleviate any concerns of unilateral power being exercised by the merged entity

107. Furthermore, the Commission considers that the scope for the exercise of coordinated market power would not be enhanced by the acquisition.

## **CONSTRAINTS FROM MARKET ENTRY**

### **Introduction**

108. A business acquisition is unlikely to result in a substantial lessening of competition in a market if behaviour in that market continues to be subject to real constraints from the threat of market entry.

109. Where barriers to entry are clearly low, it will not be necessary for the Commission to identify specific firms that might enter the market. In other cases, the Commission will seek to identify likely new entrants into the market.

110. The Commission will consider the history of past market entry as an indicator of the likelihood of future entry. The Commission is also mindful that entry often occurs on a relatively small scale, at least initially, and as such may not pose much of a competitive constraint on incumbents within the relevant time frame.

### **Barriers to Entry**

111. The likely effectiveness of the threat of new entry in constraining the conduct of market participants, following a business acquisition that might otherwise lead to a substantial lessening of competition in a market, is determined by the nature and height of barriers to entry into that market.

112. The Commission considers that, for the purpose of considering this issue, a barrier to entry is best defined as an additional or significantly increased cost or other disadvantage that a new entrant must bear as a condition of entry. In evaluating the barriers to entry into a market, the Commission will generally consider the broader 'entry conditions' that apply, and then go on to evaluate which of those constitute entry barriers.

113. It is the overall obstacle to entry posed by the aggregation of the various barriers that is relevant in determining whether entry is relatively easy or not, and therefore whether or not potential entry would prevent a substantial lessening of competition.

114. For entry to act as an antidote to a substantial lessening of competition stemming from a business acquisition, it must constrain the behaviour of the combined entity and others in the market.

115. A new entrant would face few barriers to entry. The Applicant submits that establishing a physical presence requires minimal expense. Furthermore, the Applicant contends that an outlet stocking plumbing products would require \$[ ] to commence operations, and can be staffed with as little as [ ] people. Industry participants varied in their estimate of start-up costs but generally agreed that a small operator could commence operations with minimal capital input. A new entrant might require small commercial premises, however market participants advised the Commission that in the past, some new entrants have commenced operation from their own garages.

116. Access to a buying group, such as Plumbing Plus, enables some of the smaller market players to attract volume discounts. However, industry participants suggest that the pricing discounts attached to volume are not large enough to represent a barrier to entry. [ ] In addition, a small competitor can often compete on price due to lower overheads.

*The “LET” Test*

*Likelihood of Entry*

117. The Applicant and other industry participants stated, that competition from expansion by existing plumbing products suppliers is as likely as greenfields entry.
118. There are no significant impediments preventing a current or new entrant from expanding operations, and indeed several participants such as Chesters and Edward Gibbon have expanded into new regions recently. [ ]

119. [ ]

120. Furthermore, participants in the plumbing products market advised the Commission that the threat of new entry into localised areas from tradespeople is very real. One example of such entry is Kealls Plumbing Plus in Palmerston North, which has around [ ] of the market share in that city. The Commission is therefore satisfied that entry into the plumbing products supply market is more than a mere possibility and is likely.

*Extent of Entry*

121. Whilst entry as a small scale plumbing products merchant is not difficult, it is more onerous to set up a national plumbing products chain. However, as mentioned above, the national chains face the very real threat of new entry in localised areas by small operators.

*Timeliness of Entry*

122. The Applicant contends that there are approximately 200 hardware stores nation-wide which could quickly secure a significant share of the plumbing products market in response to the necessary incentive. A small number of building supply chains already have specialist plumbing supply departments in some of their stores. [ ]
123. A new entrant from within New Zealand or from Australia could enter the plumbing products markets quickly and with relative ease. Supply from manufacturers/importers is readily available and there appears to be no exclusive supply arrangements between wholesalers/importers and the distributors of plumbing products. Entry could be effected in fewer than three months with the implementation of a physical store.



### *Conclusions on Barriers to Entry*

124. The Commission concludes that there are minimal barriers to entry such that expansion or new entry is likely to be deterred. Potential competition is likely to provide constraint on the merged entity, and the industry as a whole.

## **OTHER COMPETITION FACTORS**

### **Elimination of a Vigorous and Effective Competitor**

125. The Commission does not consider MTL to be markedly different from any other firm in the plumbing products markets. Given the other constraints listed above, MTL's removal from the market is unlikely to have a disproportionate effect on competition in the markets.

### **Constraint from Buyers or Suppliers**

126. The potential for a firm to wield market power may be constrained by countervailing power in the hands of its customers, or alternatively, when considering buyer (oligopsony or monopsony) market power, its suppliers. In some circumstances, it is possible that this constraint may be sufficient to eliminate concerns that a business acquisition may lead to a substantial lessening of competition.

127. Where a combined entity would face a purchaser or supplier with a substantial degree of market power in a market affected by the acquisition, the Commission will consider whether that situation is such as to constrain market participants to such an extent that competition is not substantially lessened.

128. Industry participants advised that there are very few written contracts between suppliers of plumbing products and their clients, and that it is very easy for an acquirer to switch suppliers. They also stated that many of their clients hold accounts with several competitors in the market.

129. It is the Commission's view that the acquirers of plumbing products have a high degree of countervailing power, and that this would constrain the merged entity.

130. In addition, industry participants advised that there is ample competition and product availability at the manufacture/import level for the merged entity to be constrained by suppliers.

### **Efficiencies**

131. The Commission recognises that there may be circumstances where efficiencies are relevant to an application for clearance.<sup>11</sup> In the context of a business acquisition, the

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<sup>11</sup> In *Fisher & Paykel*, considered under s 27, the Court held that in assessing "substantial lessening of competition", a net approach to assessing anti-competitive effects was required: "The majority correctly accepted that it had to 'net out' the pro and anti-competitive effects and that, if it could be shown that the net effect of the EDC was to promote competition, then there could be no substantial lessening of competition." *Fisher & Paykel v Commerce Commission* [ ] 2 NZLR 731 at 740. See also: *Commerce Commission v Port Nelson*, supra n 6,433; *Shell (Petroleum Mining) Company Ltd v Kapuni Gas Contracts Ltd*, (1997) 7 TCLR 463, 531.

combined entity might be able to make efficiency gains that are not obtainable by other means, such that its unit cost of production would decline. This could result in the entity reducing its price below that obtaining prior to the acquisition, even though with the acquisition it would otherwise be considered to have substantially lessened competition, and would be able to raise price above costs.

132. Where the applicant can make a sound and credible case that such efficiencies will be realised, that they cannot be realised without the acquisition, and that they will enhance competition in the relevant market, the Commission will include them in the broader analysis of all of the competitive effects of the acquisition in the course of assessing whether or not competition is likely to be substantially lessened. However, the Commission envisages that efficiency claims of the required magnitude and credibility will only very rarely overturn a finding that competition would otherwise be substantially lessened.
133. The Applicant has not argued that efficiencies are relevant to this application for clearance. The Commission does not consider that it is necessary to form a view on efficiency gains in the context of this application.

#### *Conclusion on the Regional Markets for the Supply of Plumbing Products*

134. The Commission has considered the probable nature and extent of competition that would exist in the markets for plumbing products but for the acquisition.
135. The proposed acquisition would result in the merged entity obtaining a market share in some regions that falls outside the Commission's safe harbour guidelines.
136. The Commission has considered the nature and extent of the contemplated lessening, in terms of the competitive constraints that would exist following the merger from:
- existing competition;
  - potential competition from entry; and
  - other competition factors.
137. The Commission is satisfied that the proposed acquisition would not have, nor would be likely to have, the effect of substantially lessening competition in the regional markets for the supply of plumbing products.

#### **The Electrical Products Market**

##### *Existing Participants*

138. There are numerous competitors in each of the regional markets. In particular, Rexel and Powerbase outlets offer strong competition to the proposed merged entity in the electrical products markets. There are also a number of independent suppliers of electrical products.
139. Participants at all levels of the electrical products industry advised the Commission that the electrical products market is highly competitive. In addition, it was the general view of market participants that New Zealand has an excess of suppliers. By comparison, they

noted that Australia has half the ratio of electrical product suppliers to electrical contractors as New Zealand.

#### *Inter-firm Relationships*

140. Companies that are part of the same corporate grouping, or that have similar strong relationships, cannot be relied upon to provide an effective competitive constraint to one another. Other less formal relationships between companies may also give rise to limitations on the extent of rivalry between them. Relationships between persons in the relevant market and other businesses may also affect rivalry in a market.
141. Electrical supply industry participants are limited to Associate Member status of the Electrical Contractors Association of New Zealand (“ECANZ”). This means that they have no voting rights but can attend ECANZ meetings and functions. Market participants stated that they had limited ability to influence the industry.

#### *Imports*

142. As in the analysis for the plumbing products markets, the Commission is of the view that imports are not relevant in this instance.

#### *Market Shares*

143. Again, the Commission proposes to use comparative annual turnover figures as its primary measure of market share and concentration.
144. Relevant market participants have provided to the Commission aggregated national figures for the electrical products market, and those for the aforementioned regions. Aggregated national shares are shown in Table 8 below:

**Table 8 – Estimated National Market Shares for the Electrical Products Market**

<b>Company</b>	<b>Turnover (\$m)</b>	<b>Market Share (%)</b>
Mico Wakefield	[ ]	[ ]
MasterTrade	[ ]	[ ]
Rexel/Ideal	[ ]	[ ]
JA Russell and other PowerBase members	[ ]	[ ]
Other Independents	[ ]	[ ]
Hardware Stores	[ ]	[ ]
<b>Total</b>	<b>[ ]</b>	<b>100</b>
<b>Current 3 Firm Concentration Ratio</b>		[ ]
<b>Post-Merger 3 Firm Concentration Ratio</b>		[ ]
<b>Mico/MTL</b>		[ ]

145. The current three-firm concentration is [ ]. Post-merger, the three-firm concentration ratio would be [ ] with the merged entity having a [ ] share. These figures are outside the Commission's safe harbours.
146. Commission staff have analysed regional markets for the supply of electrical products and found that the region in which the greatest aggregation of market share would occur is Southland. Table 9 sets out the relative turnover and market share figures for electrical products in Southland:

**Table 9 – Estimated Market Shares for the Southland Electrical Products Market**

<b>Company</b>	<b>Turnover (\$m)</b>	<b>Market Share (%)</b>
Mico Wakefield	[ ]	[ ]
MasterTrade	[ ]	[ ]
Rexel	[ ]	[ ]
McCulloch (PB)	[ ]	[ ]
Clive Wilson	[ ]	[ ]
<b>Total</b>	<b>[ ]</b>	<b>[ ]</b>
<b>Current 3 Firm Concentration Ratio</b>		[ ]
<b>Post-Merger 3 Firm Concentration Ratio</b>		[ ]
<b>Mico/MTL</b>		[ ]

147. The current three firm concentration is [ ]. Post-merger, the three firm concentration ratio would be [ ] with the merged entity having a [ ] share. These figures are outside the Commission's safe harbours.

148. As already noted, market shares are insufficient in themselves to establish whether competition in a market has been lessened. The other competition factors noted above are considered in subsequent sections for the relevant market.

*State of Existing Competition*

149. The acquisition would result in the merged entity becoming the biggest supplier of electrical products with a national aggregated market share of [ ]. Despite this, the merged entity would face strong competition from other participants in the market.
150. Rexel and Ideal combined under the Redeal Group currently has around [ ] market share of the aggregated national electrical products market. The Powerbase group has around [ ] and a national presence through its independent members. In particular, JA Russell (Taupo-North), Stewarts Electrical Supplies (Palmerston North), and R Redpath Ltd (South Island) are strong competitors in their respective regions.
151. In the Southland market, the Powerbase group member McCulloch offers strong competition with a market share of [ ]. In addition, Rexel has a market share of [ ].
152. All electrical industry participants interviewed consider the electrical products markets to be highly competitive due to the high ratio of suppliers to contractors, and as such, consider the merged entity would have very limited ability to increase prices.

*Conclusions – Unilateral Market Power*

153. The merged entity will be constrained by current competition. In all regional markets, the merged entity faces strong competition from Redeal outlets and/or members of the Powerbase group, with smaller independents also having a presence.

**Scope for the Exercise of Coordinated Market Power**

*Collusion*

**Table 10 - Testing the Potential for ‘Collusion’ in the Electrical Products Market**

<b>Factors conducive to collusion</b>	<b>Presence of factors in the market</b>
High seller concentration	Yes - the 3-firm concentration in the Southland region exceeds prescribed safe harbours.
Undifferentiated product	Yes – the range of products supplied to the market is largely undifferentiated.
New entry slow	No – entry can be effected relatively quickly.
Lack of fringe competitors	No – there are a number of fringe competitors with the ability to quickly expand supply given the necessary incentive.
Price inelastic demand curve	No – demand for plumbing products is reasonably elastic.
Industry’s poor competition record	No – no problems apparent.
Presence of excess capacity	No – excess capacity is not relevant in this instance.

Factors conducive to collusion	Presence of factors in the market
	instance
Presence of industry associations/fora	Yes - but with limited influence.

154. On analysis of the large number of negative responses in Table 10 above, the Commission is satisfied that the potential for collusion in the electrical products market post-acquisition is minimal. As such, the Commission has found it unnecessary to determine the potential for discipline in the electrical products market.

*Conclusions – Co-ordinated Market Power*

155. The Commission has determined that the scope for the exercise of co-ordinated market power in the electrical products markets would not be enhanced by the acquisition.

**Conclusions – Existing Competition**

156. The Commission considers that existing competition will be sufficient to constrain the merged entity.

157. Furthermore, the Commission considers that the scope for the exercise of co-ordinated market power would not be enhanced by the acquisition.

**CONSTRAINTS FROM MARKET ENTRY**

**BARRIERS TO ENTRY**

158. A new entrant would face few barriers to entering the electrical products markets. The Applicant submits that establishing a physical presence requires minimal expense. The Applicant contends that an outlet stocking electrical products would require \$[ ] to commence operations, and can be staffed with as little as [ ] people. Industry participants interviewed confirmed that entry into the electrical products markets would require minimal outlay. A new entrant might require small commercial premises, however market participants advised the Commission that in the past, some new entrants have commenced operations from their own garage.

159. The Commission understands that, providing credit requirements are met, manufacturers/importers are willing to supply new entrants with electrical products. Access to a buying group, such as Powerbase, enables some of the smaller market players to attract volume discounts. However, industry participants suggest that the pricing discounts attached to volume are not large enough to represent a barrier to entry.  
[

] In addition, the small competitor can often compete on price due to lower overheads.

*The “LET” Test**Likelihood of Entry*

160. The Applicant and other industry participants stated that competition from expansion by existing electrical products suppliers is as likely as greenfields entry. There are no impediments to a current participant from expanding operations, and indeed participants such as JA Russell have expanded into new regions recently.

161. [

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162. Current competitors in the electrical products market advised the Commission that there is a very real threat of new entry to localised areas from electrical tradespeople. The Applicant cites David Fraser’s success in the electrical products market as an example of the ease with which entry and expansion can occur. Mr Fraser founded Fraser Electrical and grew his electrical products business to some 30 stores. He sold this business to Pacific Dunlop and over the next seven years established a new business in direct competition with his previous business. In 1997 he sold that business to Rexel.

163. In addition, the Applicant submits that there are approximately 200 hardware stores nation-wide which could quickly secure a significant share of the electrical products market in response to the necessary incentive.

164. The Commission is therefore satisfied that entry into the electrical products markets is more than a mere possibility and is likely.

*Extent of Entry*

165. Whilst entry as a small-scale electrical products merchant is not difficult, it is more onerous to set up a national electrical products supply chain. However, as mentioned above, the national chains face the very real threat of new entry in localised areas by small operators who are able to compete on price due to their relatively low overheads.

*Timeliness of Entry*

166. A new entrant could enter the electrical products markets quickly and with relative ease. Supply from New Zealand sources is readily available and there appears to be no exclusive supply arrangements between wholesalers/importers and the distributors of electrical products. Small-scale entry could be effected in fewer than three months with the implementation of a physical store.

*Conclusion on the LET Test*

167. The Commission concludes that the various components of the LET test are satisfied.

*Conclusion on Barriers to Entry*

168. The Commission concludes that there are no barriers to entry likely to deter expansion or new entry to the electrical products markets. Potential competition is likely to provide constraint on the merged entity, and the industry as a whole.

**OTHER COMPETITION FACTORS**

169. The same considerations apply to the elimination of a vigorous and effective competitor, the constraint provided by buyers or suppliers, and efficiencies in the electrical products market, as for the plumbing products market above.

*Conclusion on the Regional Markets for the Supply of Electrical Products*

170. The Commission has considered the probable nature and extent of competition that would exist in the market for electrical products but for the acquisition.

171. The proposed acquisition would result in the merged entity obtaining a market share in one particular region that falls outside the Commission's safe harbour guidelines.

172. The Commission has considered the nature and extent of the contemplated lessening, in terms of the competitive constraints that would exist following the merger from:

- existing competition;
- potential competition from entry; and
- other competition factors.

173. The Commission is satisfied that the proposed acquisition would not have, nor would be likely to have, the effect of substantially lessening competition in the regional markets for the supply of electrical products.

**OVERALL CONCLUSION**

174. The Commission is therefore satisfied that the proposed acquisition would not have, nor would be likely to have, the effect of substantially lessening competition in the following markets:

- The regional markets for the supply of plumbing products.
- The regional markets for the supply of electrical products.



**DETERMINATION ON NOTICE OF CLEARANCE**

175. Accordingly, pursuant to section 66(3)(a) of the Commerce Act 1986, the Commission determines to give clearance for Mico Wakefield Limited or any interconnected body corporate of Mico Wakefield Limited to acquire up to 100% of the shares in; or any or all of the assets of, MasterTrade Limited.

Dated this 6<sup>th</sup> day of December 2001

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PJM Taylor  
Commissioner