



COMMERCE COMMISSION

Decision No. 589

Determination pursuant to the Commerce Act 1986 in the matter of an application for Proposal

CRBF LIMITED

and

CARTER HOLT HARVEY LIMITED

The Commission: Paula Rebstock
Denese Bates QC
Peter J M Taylor

Summary of Application: CRBF Limited seeks clearance to acquire shares and assets owned by Carter Holt Harvey Limited, relating to forestry estates located in Northland, Auckland, central North Island and Nelson.

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

Date of Determination: 05 October 2006

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EXECUTIVE SUMMARY

1. A notice pursuant to s 66 (1) of the Commerce Act 1986 (the Act) was registered on 10 August 2006. The notice sought clearance for the acquisition of shares and assets owned by Carter Holt Harvey Limited (CHH), relating to forestry estates located in Northland, Auckland, the CNI region, and Nelson by CRBF Limited (CRBF).
2. CRBF is a newly created timber investment fund, advised by GFP for the special purpose of acquiring the estates being sold by CHH. GFP is a TIMO which presently manages forestry estates in Northland, the Nelson/Marlborough region, and a small forestry estate in the CNI region. Accordingly, the Commission's analysis focussed upon the impact of the acquisition on the markets for the production and supply of:
 - the production and supply of pulplogs in Northland, for the periods 2006–2008, 2009–2013, and 2014–2018;
 - the production and supply of unpruned sawlogs in Northland, for the periods 2006–2008, 2009–2013, and 2014–2018;
 - the production and supply of pruned sawlogs in Northland and Auckland, for the periods 2006–2008, 2009–2013, and 2014–2018;
 - the production and supply of pulplogs in Nelson/Marlborough, for the periods 2006–2008, 2009–2013, and 2014–2018;
 - the production and supply of unpruned sawlogs in Nelson/Marlborough, for the periods 2006–2008, 2009–2013, and 2014–2018; and
 - the production and supply of pruned sawlogs in Nelson/Marlborough, for the periods 2006–2008, 2009–2013, and 2014–2018.
3. CHH's forestry asset sale is a bidding process, and the Commission understands that there are a number of other interested parties, including Hancock Natural Resource Group, Inc., [] and [].
4. The Commission considers that the counterfactual is that CHH will be acquired by a third party that does not presently have a major interest in New Zealand forestry.
5. In respect of the Northland region, the Commission considers that the combined entity will continue to face a degree of constraint from existing competitors in the pulplog markets and the pruned sawlog markets. Whilst the Commission is of the view that this is also the case for the Northland unpruned sawlog markets during the 2006-2008 and 2014-2018 time periods, the Commission considers that a supply deficit is likely to diminish this constraint during the 2009-2013 time period.
6. Based on current export volumes, the Commission considers that it is unlikely that existing competitors will expand through diversion from export in any of the relevant Northland markets.
7. In the Northland pulplog and pruned sawlog markets, the Commission considers that acquirers of pulplogs and pruned sawlogs are also likely to act as a constraint upon the combined entity in the factual scenario, because of the excess supply of logs and the limited number of outlets for these logs.

8. Regarding the Northland unpruned sawlog market, the Commission considers that acquirers of unpruned sawlogs are likely to act as a constraint, to some extent, during the 2006-2008 and 2013-2018 time periods, due to the excess supply of unpruned sawlogs. However, the Commission considers that the supply deficit is likely to diminish this constraint during the 2009-2013 time period.
9. The Commission considers that the combined entity is unlikely to have an enhanced scope to exercise unilateral market power in the Northland unpruned sawlog market during the 2009-2013 time period, because:
 - the combined entity must continue harvesting unpruned sawlogs [];
 - the combined entity is unlikely to reduce the volume of unpruned sawlogs sold on the spot market, by holding back harvest, []; and
 - the combined entity is incentivised to continue harvesting and competing to dispose of its unpruned sawlogs during the 2009-2013 time period due to the overall surplus supply of unpruned sawlogs anticipated for the 2014-2018 time period in the Northland region.
10. The Commission considers that the scope for coordinated market power is unlikely to be enhanced in the Northland unpruned sawlog market during the 2009-2013 time period, as Matariki and Crown Forestry are incentivised to continue harvesting and competing to dispose of unpruned sawlogs because []. Furthermore, small woodlots, which tend to increase harvest to take advantage of higher log prices, would also be incentivised to harvest and compete against the combined entity.
11. The Commission also considers that the large number of fringe competitors also limits the scope for coordinated behaviour in the factual scenario for the Northland unpruned sawlog market during the 2009-2013 time period.
12. Turning to the Nelson/Marlborough region, the Commission considers that the termination of the Nelson JV creates the potential for two potential counterfactual scenarios and three potential factual scenarios to arise in respect of GFP's forestry holdings.
13. The Commission considers that each of the two counterfactual scenarios is equally likely to occur. The Commission adopts the second scenario as the counterfactual scenario, as it considers that if no competition concerns arise from adopting the second scenario as the counterfactual scenario (in which the Applicant would have the smallest market share), it is unlikely that competition concerns will arise from adopting the first scenario as the counterfactual scenario.
14. Likewise, the Commission considers that each of the three factual scenarios is equally likely to occur. The Commission adopts the third scenario as the factual scenario, as it considers that if no competition concerns arise from adopting the third scenario as the factual scenario (in which the Applicant would have the greatest market share), it is unlikely that competition concerns will arise from adopting the first or second scenarios as the factual scenario.

15. In order to alleviate any competition concerns relating to the Nelson/Marlborough log markets, CRBF has given an undertaking to the Commission, such that [], GFP will retain its interest in the Nelson JV and divest the CHH forestry assets to a third party [].
16. The Commission considers that GFP would be able to find an independent buyer, and therefore successfully divest itself of the CHH forestry estate. The divestment would preserve the CHH forestry estate as a competitor to GFP in the Nelson/Marlborough log markets, and as such, it would not result in any material difference between the factual and the counterfactual.
17. The Commission is therefore satisfied that the proposed acquisition would not have, or would not be likely to have, the effect of substantially lessening competition in any market.

GLOSSARY**Terms**

CNI	Central North Island.
Forest Management Company	A business that is contracted by forest owners (including TIMOs) to carry out the day-to-day administration of the forest owner's strategic forest plan. Activities may include planting, silviculture, harvesting, transportation and sale of logs.
LVL	Laminated Veneer Lumber, an engineered wood product which is used as an alternative to solid lumber and steel in the construction industry.
LVL Plant	A plant which processes structural-grade unpruned sawlogs into LVL.
MDF	Medium Density Fibreboard, a type of reconstituted board product.
MDF Plant	A plant which processes industrial-grade unpruned sawlogs into MDF.
Pruned Sawlog	Used in the production of furniture, mouldings and other appearance grade timber.
Pulplog	Pulplog is sourced from the top section of the tree, including branches, and is used in the production of pulp and paper
Pulpmill	A plant which processes pulplogs into pulp and paper products.
Sawmill	A plant which processes unpruned sawlogs and pruned sawlogs into timber.
SNI	Southern North Island.
Stumpage Contractor	A business or individual that is contracted by a forest owner or forest management company to undertake harvesting activities. These activities may include cutting, transportation and log sales.
TIMO	Timber Investment Management Organisation, an organisation that develops and manages international timberland portfolios on behalf of investment groups
Unpruned Sawlog	Used for packaging (industrial grades) and construction (structural grades).

Parties

Ahead Lumber	Ahead Lumber Limited; sawmill
CHH	Carter Holt Harvey Limited; land/forest owner, sawmill, pulpmill
Crofts	Croft Pole Distributors Limited; sawmill
Crown Forestry	Crown Forestry Group; land/forest owner
Flight	Flight Timbers Limited; sawmill
GMO RR	Grantham Mayo and Otterloo Renewable Resources; TIMO, forest owner
GFP	Global Forest Partners LP; TIMO, forest owner
Goldpine	Goldpine Industries Limited; sawmill
Hancock	Hancock Natural Resource Group Inc; TIMO, forest owner
Juken	Juken Nissho; forest/land owner, MDF plant, LVL plant, sawmill
MAF	Ministry of Agriculture and Forestry; government
Mangakahia JV	Mangakahia Forest Joint Venutre; land/forest owner
Matariki	Matariki Forests; forest owner
Marusumi	Marusumi Whangarei Company Limited; pulplog acquirer/exporter
Nelson JV	Nelson Forests Joint Venture; land/forest owner
NFML	Northland Forest Managers Limited; forest manager
NPI	Nelson Pine Industries; land/forest owner, pulpmill, LVL plant, MDF plant
PF Olsen	PF Olsen and Company Limited; forest manager
Rosvall	Rosvall Sawmill Limited; sawmill
South Pine	South Pine (Nelson) Limited; sawmill
Stillwater Lumber	Stillwater Lumber Limited; sawmill
Taylor's Timber	Taylor's Timber & Joinery Limited; sawmill
TFML	Tasman Forest Management Limited; forest manager
Thames Timber	Thames Timber Limited; sawmill
Waimea	Waimea Sawmillers Limited; forest/land owner, sawmill
Weyerhaeuser	Weyerhaeuser New Zealand Inc; land/forest owner

THE PROPOSAL

1. A notice pursuant to s 66 (1) of the Commerce Act 1986 (the Act) was registered on 10 August 2006. The notice sought clearance for the acquisition of shares and assets owned by Carter Holt Harvey Limited (CHH), relating to forestry estates located in Northland, Auckland, the central North Island (CNI) region and Nelson by CRBF Limited (CRBF).

PROCEDURE

2. Section 66(3) of the Act requires the Commission either to clear or to decline to clear the acquisition referred to in a s 66(1) notice within 10 working days, unless the Commission and the person who gave notice agree to a longer period. An extension of time was agreed between the Commission and the Applicant. Accordingly, a decision on the application was required by 5 October 2006.
3. The Applicant sought confidentiality for specific aspects of the application. A confidentiality order was made in respect of the information for up to 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 approach to analysing the proposed acquisition is based on principles set out in the Commission's Mergers and Acquisitions Guidelines.¹

STATUTORY FRAMEWORK

5. Under s 66 of the Act, the Commission is required to consider whether the proposal will, or would be likely to have the effect of substantially lessening competition in the market. If the Commission is satisfied that the proposal is unlikely to substantially lessen competition then it is required to grant clearance to the application. Conversely if the Commission is not satisfied it must decline. The standard of proof that the Commission must apply in making its determination is the civil standard of the balance of probabilities.²
6. The substantial lessening of competition test was considered in *Air New Zealand & Qantas v Commerce Commission*, where the Court held;

We accept that an absence of market power would suggest there had been no substantial lessening of competition in a market but do not see this as a reason to forsake an analysis of the counterfactual as well as the factual. A comparative judgement is implied by the statutory test which now focuses on a possible change along the spectrum of market power rather than on whether or not a particular position on that spectrum, i.e. dominance has been attained. We consider, therefore, that a study of likely outcomes, with and without the proposed Alliance, provides a more rigorous framework for the comparative analysis required and is likely to lead to a more informed assessment of competitive conditions than would be permitted if the inquiry were limited to the existence or otherwise of market power in the factual.³
7. In determining whether there is a change along the spectrum which is significant the Commission must identify a real lessening of competition that is not minimal.⁴ Competition must be lessened in a considerable and sustainable way. For the purposes of its analysis the Commission is of the view that a lessening of

¹ Commerce Commission, *Mergers and Acquisitions Guidelines*, January 2004.

² *Foodstuffs (Wellington) Cooperative Society Limited v Commerce Commission* (1992) 4 TCLR 713-722.

³ *Air New Zealand & Qantas Airways Ltd v Commerce Commission*, unreported HC Auckland, CIV 2003 404 6590, Hansen J and K M Vautier, Para 42.

⁴ *Fisher & Paykel Limited v Commerce Commission* (1996) 2 NZLR 731, 758 and also *Port Nelson Limited v Commerce Commission* (1996) 3 NZLR 554.

competition and creation, enhancement or facilitation of the exercise of market power may be taken as being equivalent.

8. When the impact of market power is expected to be predominantly upon price, for the lessening, or likely lessening, of competition to be regarded as substantial, the anticipated price increase relative to what would otherwise have occurred in the market has to be both material, and ordinarily able to be sustained for a period of at least two years or such other time frame as may be appropriate in any give case.
9. Similarly, when the impact of market power is felt in terms of the non-price dimensions of competition such as reduced services, quality or innovation, for there to be a substantial lessening, or likely substantial lessening of competition, these also have to be both material and ordinarily sustainable for at least two years or such other time frame as may be appropriate.

ANALYTICAL FRAMEWORK

10. The Commission applies a consistent analytical framework to all its clearance decisions. The first step the Commission takes is to determine the relevant market or markets. As acquisitions considered under s 66 are prospective, the Commission uses a forward-looking type of analysis to assess whether a lessening of competition is likely in the defined market(s). Hence, an important subsequent step is to establish the appropriate hypothetical future with and without scenarios, defined as the situations expected:
 - with the acquisition in question (the factual); and
 - in the absence of the acquisition (the counterfactual).
11. The impact of the acquisition on competition is then viewed as the prospective difference in the extent of competition in the market between those two scenarios. The Commission analyses the extent of competition in each relevant market for both the factual and the counterfactual, in terms of:
 - existing competition;
 - potential competition; and
 - other competition factors, such as the countervailing market power of buyers or suppliers.

THE PARTIES

CRBF

12. CRBF is a newly created timber investment fund, advised by GFP for the special purpose of acquiring the estates being sold by CHH.
13. GFP is a TIMO. In New Zealand its portfolio includes forestry estates held by four different investment vehicles:
 - GTI6 has a 100% shareholding in the 1,500 ha Tauhara Forest in the CNI; and 50% shareholding in the 22,000 ha Mangakahia JV in Northland. The other 50% shareholding of the Mangakahia JV is owned by CHH.
 - NZ2 has a 100% shareholding in Scolly Forest, which is a forest estate of approximately 1,800 ha in Marlborough; a 75% shareholding in the 10,000 ha Madaket estate in the CNI; and a 75% shareholding in the 6,401 ha Mahoe Forest in Northland.

- NZ3 has a 25% shareholding in the Mahoe Forest; and a 25% shareholding in the Madaket estate.
- NZ1 holds a 49% shareholding in the Nelson JV⁵. The Nelson JV has a net stocked area of approximately 61,000 ha of forestry estate scattered throughout the Nelson/Marlborough region, as well as a pruned sawmill located at Kaituna⁶.

CHH

14. Rank Group Investments Limited purchased CHH in March 2006. CHH is a wood fibre products company and carries on business activities in forests, wood products, pulp and paper, packaging and building supplies. CHH is Australasia's leading forest products company and one of the largest forest product companies in the Southern Hemisphere.
15. CHH has a number of forests throughout New Zealand, including significant forestry estates in the CNI, as well as:
 - CHH's Northland forestry estate, which comprises 35,000 ha of forests located in the far North, Whangarei and North Auckland. CHH is 50% shareholder in, and manager of, the Mangakahia JV.
 - the Nelson/Marlborough CHH forestry estate, which comprises four forest blocks located in the proximity of Nelson and Motueka: Waimea ([] ha); Hira ([] ha); Moutere ([] ha); and Baigent ([] ha).

OTHER PARTIES

Northland

Matariki

16. Matariki is a joint venture company between Rayonier Inc, the Rosenberg Real Estate Equity Fund (RREEF) and Australian Mutual Provident (AMP). Rayonier is a US-based TIMO that manages 25,000 ha of forest in Northland.

Crown Forestry

17. Crown Forestry manages the Crown's interest in a number of commercial forests and forestry-related leases. The Crown has 25 forests geographically spread throughout New Zealand's North Island, five of which are located in Northland: Parengarenga A and 3G Forests, which are located north of Kaitaia; Onepu Forest, which is located near Kaitaia; Pouto 2F Forest, which is located south of Dargaville; and Waipoua Forest, which is located west of Kaikohe. Crown Forestry's Northland forests total 8,300 ha.

PF Olsen

18. PF Olsen is a forest management company that manages 130,000 ha of plantation forest for individual and corporate clients throughout New Zealand.
19. In Northland, PF Olsen manages [] ha, comprising of [] ha of small woodlots and [] ha of Crown Forestry estate. Of its small woodlots, its largest clients are []. Most of PF Olsen's

⁵ The Nelson JV is an unincorporated arrangement between Weyerhaeuser (51%) and investors from North America and Europe (49%) advised by GFP.

⁶ Kaituna is located near Blenheim.

remaining Northland customers are farmers and land trusts that on average hold [] ha of forest each.

NFML

20. NFML is a forest management company, which manages [] ha of plantation forest for individuals and corporate clients in Northland and Coromandel. NFML manages approximately [] ha of forest in Northland, which includes the [] ha it manages for Crown Forestry.

Nelson/Marlborough

Weyerhaeuser

21. Weyerhaeuser New Zealand acts as forest manager on behalf of the Nelson JV, of which it is a 51% shareholder.
22. Weyerhaeuser also manages [] ha of forest land in the Nelson/Marlborough region on behalf of private woodlot owners.

Matariki

23. In the Nelson/Marlborough region, Matariki manages 1,800 ha of forest located in the Marlborough Sounds.

NPI

24. NPI is a wholly-owned subsidiary of Sumitomo Forestry Group; it owns 3,300 ha of forest throughout the Nelson/Marlborough region; and a MDF plant and a LVL plant in Nelson.

TFML

25. TFML is a forest management company that manages [] ha of plantation forest for private owners and Maori Trusts in the Nelson/Marlborough region.

ASSOCIATION

26. Section 47(2) provides that, for the purposes of s 47(1), a reference to a person includes two or more persons that are interconnected or associated. Sections 47(3) and (4) stipulate that two or more corporate entities are associated if one, either directly or indirectly, is able to exert a substantial degree of influence over the activities of the other. The Commission is of the view that, in this context, a substantial degree of influence means being able to bring real pressure to bear on the decision-making process of the other.
27. In coming to a view on association, the Commission must consider each case on its particular facts.⁷ Among the factors the Commission usually takes into account in determining association are the:
- nature and extent of ownership links between the companies;
 - presence of overlapping directorships;
 - rights of one company to appoint directors of another; and
 - nature of other shareholder agreements and links between the companies concerned.

⁷ *Commerce Commission v New Zealand Bus Ltd* (2006) CIV 2006-485-585, para 212.

28. The Commission also considers the interaction between these various factors. For example, the Commission assesses the nature and extent of the communications between persons, the apparent influence of one person on the key strategic decisions of the other⁸. The question the Commission has to answer is whether two or more enterprises can, for the purposes of commerce and competition, be regarded as one⁹.
29. The Applicant advised the Commission that GFP will have responsibility for [] the selection of investment and the management of CRBF, under the supervision of CRBF's board of directors.
[]
[]
30. NZ1 is a wholly-owned subsidiary of RII New Zealand Properties I, Inc. (RII), []
[]
[]
31. As GFP has a substantial involvement in the management of the funds, the Commission considers that the entities are related.
32. The Applicant submitted that documents for the respective funds and fiduciary obligations under United States securities law preclude GFP from treating different investment funds as "related" entities.
33. The fund documents are in the form of agreements between GFP and the funds' shareholders. The Commission is of the view that these parties' interests may be aligned toward acting in concert to exploit any jointly held market power. Consequently, the Commission could not be satisfied that a transaction that solely relied on agreements between these parties would not result in a substantial lessening of competition.
34. Given the respective roles of GFP in NZ1 and CRBF it is the Commission's view that GFP, NZ1 and CRBF can be regarded as one person for the purposes of s 47(1).

INDUSTRY BACKGROUND

35. New Zealand's planted production forests covered an estimated 1.81 million ha as at 1 April 2005. The total standing timber volume (growing stock) is estimated to be 400 million m³ with an average forest stand age (area weighted) of 13.9 years¹⁰.
36. Current plantation forests in New Zealand are dominated by radiata pine (which accounts for 89% by area planted nationally, 97% in Northland, and 90% in the Nelson/Marlborough region). The other species of note is Douglas fir (6% nationally), with the remainder a mix of eucalyptus and other hardwoods.

⁸ Decision 388, *New Zealand Seafood Investments Limited and Basuto Investments Limited*, Para 16 – 24.

⁹ Decision 278, *Air New Zealand Limited and Ansett Holdings Limited and Bodas Pty Limited*, Para 180 – 182.

¹⁰ MAF, *National Exotic Forest Description as at 1 April 2005*.

37. Seventy percent of New Zealand's forest area is in the North Island, which is in turn divided into six forestry regions – Northland, Auckland, CNI, East Coast, Hawke's Bay and SNI¹¹.

Northland Forestry Region

38. The Northern region contains approximately 204,000 ha of plantation forests, of which 97% is radiata pine. The remainder is largely comprised of hardwood species such as eucalyptus and acacia. The main forested areas within the Northland region lie between Kaikohe in the north and Dargaville in the south. Other forests are located along the west coast north of Auckland, and in the far north, near Kaitaia. Processing capacity in the area is concentrated around Whangarei and Marsden Point¹².

Nelson/Marlborough Forestry Region

39. The climate and soils in the Nelson/Marlborough region are recognised for producing trees with a higher wood density, which is valued for its stiffness and strength. The main forested areas within the Nelson/Marlborough region lie to the southwest of Nelson (toward Murchison), and along the Wairau Valley, west of Blenheim. Other forests are scattered throughout the Marlborough Sounds¹³.

Log Production

40. The quality of logs from plantation grown trees is influenced by several factors: generic selection, silviculture practice, site selection and rotation age. Log quality is generally a function of size (diameter and length), shape (straightness, roundness and taper). Branch-related features such as size and distribution, and improvements achieved by pruning are also important features.
41. Wood basic density is also an important indicator of wood quality. This is a measure of the mass of dry wood substance per unit volume of green timber and is an important indicator of wood strength. In New Zealand, the Northland and Auckland regions produce high-density wood, the CNI produces medium density wood, whilst regions further south produce lower density wood¹⁴.
42. If trees are pruned, the core of the wood containing defects can be restricted to a relatively small cylinder in the butt log (the first log produced from the tree). Thinning will promote rapid growth of clearwood outside the knotty core. In this situation, clear timber or veneer is produced instead of grades containing knots. Pruning is normally conducted in years five to ten of the tree's growth; however, this is also dependent on the forest location.
43. The outerwood of a radiata pine tree is referred to as mature wood. It is mainly sapwood, has a higher density, fewer knots and narrower growth rings. It is used as high quality structural timber, as clear lengths for furniture and decorative boards. The corewood or juvenile wood is mainly heartwood, is of lower density, and is less stable than the outerwood. It is used in industrial packaging,

¹¹ MAF, *NEFD National and Regional Wood Supply Forecasts*, 2000, p 19.

¹² CFK, *Resources of Northern Forests*, June 2007.

¹³ MAF, *Nelson/Marlborough Forest Industry and Wood Availability Forecasts*, 2006.

¹⁴ http://www.insights.co.nz/products_processes_tc.asp

as low strength structural timber and in reconstituted products such as MDF and particle board¹⁵.

44. Log quality is a more important issue to the solid wood processing industry than it is to reconstituted wood industries. This is because the economics of log conversion in solid wood processing are dependent on log size and shape. The grade of timber produced is a function of the defects present.
45. The specifications for domestic log grades are outlined below in Table 1.

Table 1: Domestic Log Grade Specifications

Log Grade	Log Type	Small end Diameter (mm)	Maximum Knot (mm)
P1	Pruned	400+	0
P2	Pruned	300-399	0
S1	Unpruned	400+	60
S2	Unpruned	300-399	60
S3	Pruned or unpruned	200-299	60
L1	Unpruned	400+	140
L2	Unpruned	300-399	140
L3	Unpruned	200-299	140
Pulp	Unpruned	100	N/a

Source: MAF

46. Pruned sawlogs are generally distinguished on the basis of external characteristics. Internal quality characteristics such as the defect core are not included in the specifications. The quality and potential value of pruned logs can vary greatly, depending on the silvaculture regime¹⁶.

Log Supply

47. The log supply industry is characterised by several different strategic groups of competitors. The first group involves large vertically integrated companies, which are involved in forest ownership and log production, log trading, and downstream wood processing facilities. CHH is the only remaining business that falls within this group since the sale of the Fletcher Challenge Forests' (FCF) forestry estates.
48. The next group is also characterised by a vertically integrated structure. However, the scale of business operations is considerably smaller than that of the first group, and these businesses are generally net purchasers of logs. This group includes Juken in Northland, and NPI and Flight in the Nelson/Marlborough region.
49. The next strategic group is characterised by forest ownership or management on a large scale, with no downstream processing activities. This group is a mixture of smaller privately owned or publicly listed companies and large foreign owned TIMOs. The main function of these organisations is the overall strategic management of forest ownership and log production. TIMOs in this group

¹⁵ New Zealand Pine Remanufacturers Association, *New Zealand Pine User Guide* (Neilson Scott Limited, 1996) 10.

¹⁶ Ibid 5-19.

include GFP, Weyerhaeuser and Matariki. Harvest managers, such as NFML and TFML, are also included in this group.

50. The next group consists of fragmented, smaller scale forests in private ownership. Owners include farmers with woodlots and other private individuals with small blocks of plantation forests, as well as forestry estates owned by bodies such as government and Maori land trusts. Harvest managers are frequently involved in the operational management of these woodlots.

Log Processors

51. In the Northland region, the highest concentration of processing facilities is located in close proximity of Whangarei. In Nelson/Marlborough, the highest concentration of processing facilities is located in close proximity of Nelson.

Pulplog Processors

52. There is one major processor of pulplogs in each of the Nelson/Marlborough Northland regions.
53. In Northland, Marusumi manufactures [] m³ per year of woodfibre, which it exports to its parent company in Japan. The woodfibre consists of [] % pulplogs, which is processed by Marusumi's woodchipping facility in Whangarei. The other [] % consists of woodchip that Marusumi purchases from sawmilling operations in the Northland region.
54. In the Nelson/Marlborough region, NPI processes [] m³ per year of pulplogs, of which [] % is sourced from its own forests.

Unpruned Sawlog Processors

55. Both the Northland and Nelson/Marlborough regions are characterised by a large number of sawmills that process unpruned sawlogs. Both regions have two large sawmills that process in excess of 200,000 m³ per year of unpruned sawlogs, and a handful of medium-sized sawmills that process 50,000-200,000 m³ per year of unpruned sawlogs.
56. In the Northland region, TDC and CHH's LVL plant are the largest processors of unpruned sawlogs. Both of these mills have advised the Commission that they [].
57. Other large processors in the Northland region include Crofts and Ahead Lumber.
[]
58. CHH Eve's Valley and NPI's LVL plant are the largest processors of unpruned sawlogs in the Nelson/Marlborough region. Other large processors in the Nelson/Marlborough region include Goldpine, Waimea, Flight, South Pine and Taylors Timber.

Pruned Sawlog Processors

59. In the Northland region, Rosvall, TDC and Thames Timber are the most significantly-sized processors of pruned sawlogs.
60. Weyerhaeuser's Kaituna sawmill is the largest processor of pruned sawlogs in the Nelson/Marlborough region. Other processors in the Nelson/Marlborough region are considerably smaller, their combined processing capacity is

approximately [] of Weyerhaeuser's. These processors include Flight Timber, Southwood, Stillwater Lumber and Taylors Timber.

PREVIOUS COMMISSION DECISIONS

61. The Commission previously considered the market for the supply of logs in Nelson/Marlborough region in Decision 342, when Weyerhaeuser applied for clearance to acquire CHH's 28,000 ha forestry estate in the Nelson/Marlborough region in 1999.
62. At this time Weyerhaeuser was party to the Nelson JV with UBS Brinson Resource Investments¹⁷. In Decision 342, the proposed acquisition was assessed under the dominance test, and the Commission concluded that it was not satisfied the proposal would not result, or would not be likely to result, in any person acquiring or strengthening a dominant position in any market.
63. The Commission has not previously assessed any mergers or acquisitions relating to the Northland forestry markets.
64. The Commission's previous decisions relating to the forestry industry have mainly involved the CNI region¹⁸. The Commission's most recent forestry decision, Decision 588¹⁹, related to the CHH forestry assets located within the CNI. The Commission considered the markets for:
 - the production and supply of pruned sawlogs in the CNI, Auckland and Hawke's Bay for the periods 2006-2010, 2011-2015 and 2016-2020;
 - the production and supply of unpruned sawlogs in the CNI, for the periods 2006-2010, 2011-2015 and 2016-2020; and
 - the production and supply of pulplogs in the CNI, for the periods 2006-2010, 2011-2015 and 2016-2020.
65. The Commission concluded that the acquisition would not have, or be likely to have, the effect of substantially lessening competition in any market, as the combined entity would continue to face constraint from existing competitors, and acquirers of logs. The Commission also concluded that neither the scope for unilateral market power nor the scope for coordinated market power were likely to be enhanced in the factual scenario.

¹⁷ GFP acquired the assets of UBS Brinson Resource Investments in September 2003.

¹⁸ Decision 426, *Carter Holt Harvey Limited and Central North Island Forestry Partnership*, July 2001; Decision 468, *Fletcher Challenge Forests Limited and Central North Island Forestry Partnership*, August 2002; and more recently, Decision 588, *Hancock Natural Resource Group Inc and Carter Holt Harvey Limited*, September 2006.

¹⁹ Decision 588 related to the same CHH assets as the current Application; however, the area of aggregation in Decision 588 was the CNI region.

MARKET DEFINITION

66. 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.”²⁰
67. For the purpose of competition analysis, the internationally accepted approach is to assume the 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 would be able to impose at least a Small yet Significant and Non-transitory Increase in Price, assuming all other terms of sale remain constant (the SSNIP test). The smallest space in which such market power may be exercised is defined in terms of the dimensions of the market discussed below. The Commission generally considers a SSNIP to involve a five to ten percent increase in price that is sustained for a period of one year.
68. The Commission seeks to define relevant markets in a way which best assists the analysis of the competitive impact of the acquisition under consideration. In this instance, the common activity of the two parties is the production and supply of logs.
69. The Applicant submitted that the relevant markets are:
- the production and supply of unpruned sawlogs in Northland, for the periods 2006–2008, 2009–2013, 2014–2018, and 2019-2023;
 - the production and supply of pruned sawlogs in Northland, for the periods 2006–2008, 2009–2013, 2014–2018, and 2019-2023;
 - the production and supply of pulplogs in Northland, for the periods 2006–2008, 2009–2013, 2014–2018, and 2019-2023;
 - the production and supply of unpruned sawlogs in Nelson/Marlborough, for the periods 2006–2008, 2009–2013, 2014–2018, and 2019-2023;
 - the production and supply of pruned sawlogs in Nelson/Marlborough, for the periods 2006–2008, 2009–2013, 2014–2018, and 2019-2023; and
 - the production and supply of pulplogs in Nelson/Marlborough, for the periods 2006–2008, 2009–2013, 2014–2018, and 2019-2023.

Product Market

70. The greater the extent to which one good or service is substitutable for another, on either the demand-side or supply-side, the greater the likelihood that they are bought and supplied in the same market.
71. 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.
72. Close substitute products on the supply-side are those between which suppliers can easily shift production, using largely unchanged production facilities and little or no additional investment in sunk costs, when they are given a profit incentive to do so by a small change to their relative prices.

²⁰ S 3(1) of the Commerce Act 1986.

73. The Applicant submitted that the Commission has a well-developed approach to market definition in respect of the forestry industry²¹, and accepts the Commission's previous analysis of the relevant market dimensions.
74. In Decision 588 the Commission explored features of the production of logs in considering the appropriate product market dimension, including species of tree and range of grades of logs.
75. In terms of species, the Commission noted that the ownership spread pertaining to the non-radiata species is not materially different from that of radiata pine, and concluded that it was not necessary to distinguish between the species when assessing the competitive impact of the proposed acquisition being considered.
76. In respect of log grades, the Commission recognised that although the supply of different grades of logs is linked, pulplogs and sawlogs have distinct uses. Furthermore, sawlogs can be distinguished between pruned and unpruned logs, again on the basis of different demand characteristics.
77. On the demand-side, there would appear to be little substitution between these broad classes of logs. Pulplogs tend to be younger, smaller, and less dense, and therefore are often not suitable for the production of sawn timber. Furthermore, unpruned sawlogs are not considered to be close substitutes for pruned sawlogs. The presence of knots in unpruned sawlogs renders them unsuitable for the appearance-based products that are usually manufactured from pruned sawlogs.
78. The Commission considers that for the purposes of assessing the competition implications of the proposed acquisition, the product markets as defined in Decisions 426, 468 and 588 remain valid, in that there are separate product dimensions for pulplogs, unpruned sawlogs, and pruned sawlogs.

Conclusion on Product Markets

79. The Commission concludes that for the purpose of assessing the competition implication of the proposed acquisition, the appropriate product markets are those which were defined in Decisions 426 and 468:
 - the market for the production and supply of pulplogs;
 - the market for the production and supply of unpruned sawlogs; and
 - the market for the production and supply of pruned sawlogs.

Functional Markets

80. There are a number of functional levels that relate to the forestry sector, including the production and supply of various grades of raw logs, the processing of those logs (e.g., into timber or pulp and paper), and the distribution of the processed product (e.g., through building supply chains)²².
81. The proposed acquisition involves aggregation at the forestry level. The Commission concludes, for the purposes of the current application, that the relevant functional market is therefore the production and supply of unpruned sawlogs, pruned sawlogs and pulplogs.

²¹ Specifically referencing Decisions 426 and 468.

²² There may be various levels of (vertical) integration between these functional levels, as is the case where an entity owns pulpmill as well as a forestry estate. The proposed acquisition involves some vertical disintegration, with CHH selling its forestry estate.

Geographic Markets

82. The Commission defines the geographic dimension of a market to include all of the relevant, spatially dispersed sources of supply to which buyers would turn should the prices of local sources of supply be raised.
83. In Decisions 426 and 468, the Commission defined the geographic dimensions as the CNI for pulplogs and unpruned sawlogs, and the CNI, Hawkes Bay, and Auckland for the higher value pruned sawlogs. In Decision 342, the Commission defined the relevant geographic market as being the Nelson/Marlborough region.
84. In context of the current application, the main areas of potential aggregation are in the Northland and Nelson/Marlborough regions. The Commission has therefore considered the relevant geographic dimensions of the supply of logs in these regions.
85. In the forestry sector, processing capacity is often concentrated in close proximity to major forests. In Northland, approximately half of the processing facilities are located near Whangarei, with other processors located further north, near Kerikeri, as well as south, near Auckland and Coromandel. The main processing centre for the Nelson/Marlborough region is Nelson/Richmond, although there are a number of other mills located near Blenheim.
86. In assessing the relevant geographic market for the supply of each log type, the Commission has considered the inland transport cost of shifting logs relative to the median value of each log type. A SSNIP of 10% applied to a pruned sawlog price of \$130/m³ results in a price increase of \$13/m³. Similarly, for unpruned sawlogs, a SSNIP would result in an increase of approximately \$7/m³, while for pulplogs the price increase would be approximately \$4/m³.
87. Faced with an increase in log prices of the above magnitude, the ability of a customer purchasing logs to switch to an alternative source of supply from another region will depend on the additional transport costs of shipping in logs from further away.

Northland

88. A number of Northland sawmills advised the Commission that the area from which they generally source logs extends down to Auckland. Crofts²³ advised the Commission that it purchases unpruned sawlogs from a region that encompasses Kaitaia to the north and Auckland to the south. Crofts said it would cost an additional \$15/m³ to transport logs sourced south of Auckland²⁴.
89. TDC advised the Commission that it sources unpruned sawlogs from as far south as Woodhill Forest²⁵, although it does not purchase logs from south of Auckland as the relatively high transportation cost does not make this an economically viable option.
90. The Commission notes that there is some evidence that suggests higher value pruned sawlogs are sourced from a broader catchment area, which extends down to encompass forests located south of Auckland. Rosvall advised the

²³ Crofts' processing facility is located near Whangarei.

²⁴ This additional transport cost of \$15/m³ is significantly higher than the SSNIP applied to pulplogs and unpruned sawlogs, and just higher than the SSNIP applied to pruned sawlogs.

²⁵ Woodhill Forest is located near Kumeu, north-west of Auckland city.

Commission that pruned sawlogs can be economically transported up to 200 km, and purchases some of its pruned sawlogs from as far south as Waiuku.

91. Crown Forestry informed the Commission that its trucking costs in Northland range from \$[]/m³ per km to \$[]/m³ per km. A long haul, such as from Parengarenga Forest to Whangarei²⁶, would cost of \$[]/m³ per km. A shorter distance over which Crown Forestry would transport its logs, from Waipoua Forest to Whangarei²⁷, would cost \$[]/m³ per km.
92. The transportation cost per kilometre tends to decline as the distance carried increases^{28 29}. It is likely that the costs associated with loading and unloading trucks at either end of the journey are relatively high, with such costs being independent of the journey length.
93. The immediate area in which aggregation would occur as a result of the proposed acquisition lies predominantly within a 100 km radius of Whangarei, encompassing the Mangakahia JV, as well as a number of CHH forested areas that form part of the sale estate³⁰.
94. In the event that a SSNIP was applied in respect of logs produced within this area, processors may be able to respond by sourcing logs from more distant suppliers, as long as the additional transport costs were less than the price increase. Based on a cost of \$0.12/m³ per km, purchasers faced with a SSNIP could source pulplogs from an additional 35 km, unpruned logs from an additional 60 km, and pruned logs from an additional 110 km beyond the area of aggregation.
95. In the context of the current application, these distances would indicate that if a SSNIP is imposed, it would be economic for a processor located in the Whangarei region to transport pulplogs over a total distance of up to 135 km, unpruned sawlogs up to 160 km, and pruned sawlogs up to 210 km.
96. These distances are consistent with what industry participants indicated to the Commission in terms of existing wood flows throughout the Northland region and the distance at which it becomes no longer efficient to source logs. As noted earlier, a number of parties processing unpruned logs in Whangarei source logs from a catchment region that extends to Auckland in the south³¹, whereas pruned sawlog processors in Whangarei source logs from a catchment region that extends to Waiuku in the south³².
97. On some occasions, pulplogs have been railed from Northland to the CNI region in order to meet the demand of CHH's Kinleith mill. However the Commission is of the view that this is the exception rather than the rule.
98. The above analysis is summarised in Figure 1 below. The smaller shaded circle represents areas located within 160 km of Whangarei. Whangarei is taken as the epicentre of the main processing capacity in Northland, although sawmills located on the boundary of the shaded circle may be able to source logs from

²⁶ Parengarenga Forest to Whangarei is approximately 220 km.

²⁷ Waipoua Forest to Whangarei is approximately 110 km.

²⁸ Decision 426, paragraph 63.

²⁹ The Commission discussed back-loading in greater detail in Decision 588.

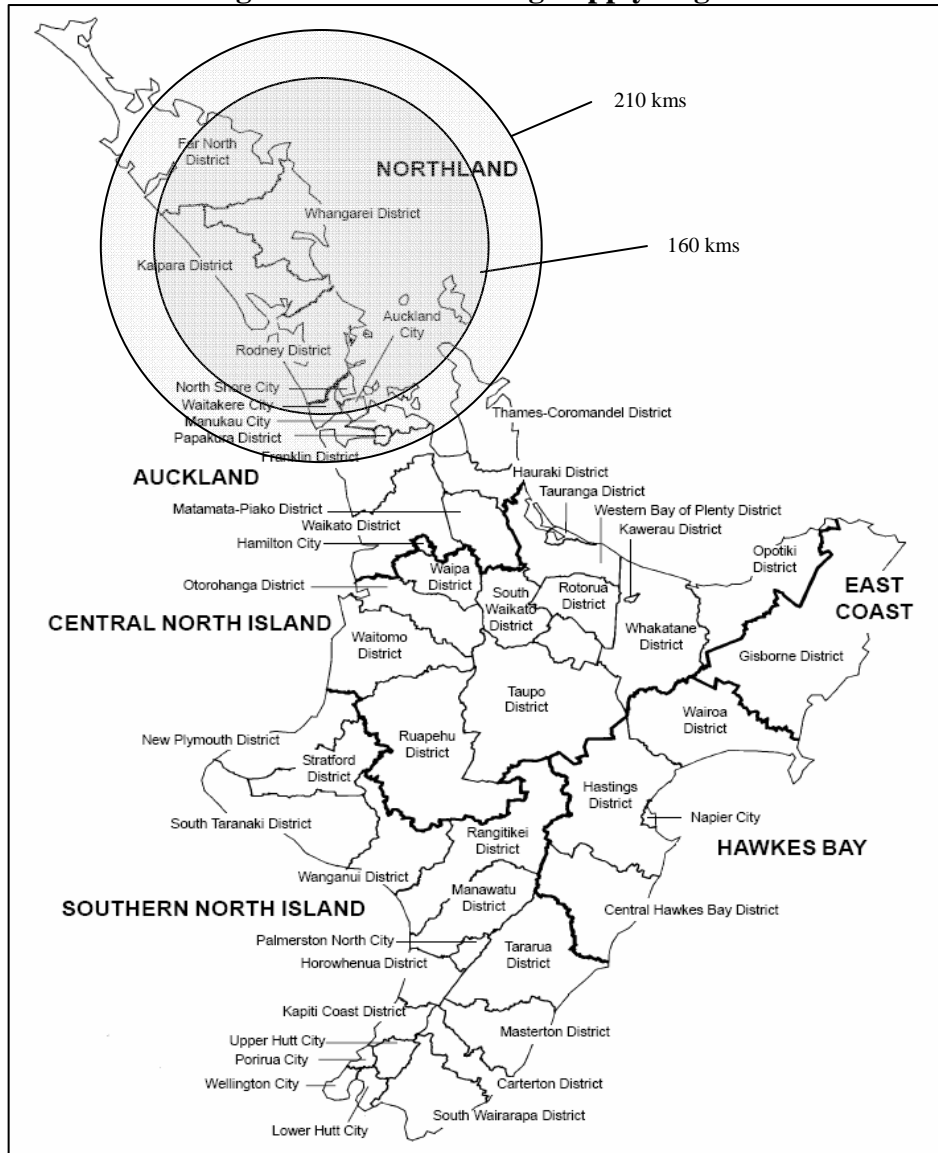
³⁰ The sale estate also includes Woodhill forest and smaller forest blocks in the far north.

³¹ The distance from Whangarei to Auckland is 165 km.

³² The distance from Whangarei to Waiuku is 230 km.

other regions³³. The shaded circle approximates the area within which it is most economically feasible to transport pulplogs and unpruned sawlogs in response to a SSNIP applied to pulplogs and unpruned sawlogs. This indicates that the Northland forestry region is the appropriate economic market for pulplogs and unpruned sawlogs.

Figure 1: Northland Log Supply Region



Source: MAF

99. The larger circle represents a distance of 210 km from Whangarei, and approximates the area within which higher value pruned sawlogs can be sourced. This boundary includes the Northland forestry region and extends south to include forests that lie south of Auckland. The Commission is of the view that it is unlikely that the Coromandel forests would be included within this boundary because of the logistics of transporting the logs down the peninsula and across to Auckland.

³³ For example, the Anderson & O’Leary structural sawmill at Whenuapai.

Nelson/Marlborough

100. In Decision 342, the Commission defined a market for the supply of logs in the Nelson/Marlborough region. The Commission noted that the volume of logs flowing from the West Coast region into Nelson/Marlborough was relatively small when compared with the total volume of Nelson/Marlborough production and demand.
101. The Commission notes that, on the demand side, the processing facilities in the Nelson/Marlborough region tend to be primarily located near Nelson and Motueka. This reflects the location of the largest forested area of the Nelson/Marlborough region, which lies within an 80 km radius of Nelson.
102. Sawmills such as Waimea, NPI and South Pine advised the Commission that the Nelson/Marlborough region is distinct from the surrounding regions of the South Island, and that there is minimal wood flow from Canterbury into Nelson/Marlborough. Sawmills remarked that although there are some volumes flowing between the West Coast region and Nelson/Marlborough, these volumes are not significant. The Commission notes that whilst Weyerhaeuser sells some of its logs to West Coast region sawmills³⁴, the majority of its logs are sold to processors in Nelson and Blenheim.
103. Given the concentration of customer demand for logs, and the location of the main forests, the Commission has considered the forested area near Nelson and Motueka as being the smallest area in which a hypothetical monopolist might be able to exert market power, and has therefore applied a SSNIP in respect of this area³⁵.
104. In the event that a SSNIP was introduced in respect of logs produced within this area, processors may be able to respond by switching to logs from more distant suppliers as long as the additional transport costs were less than the price increase. As discussed in the context of the Northland region, the Commission considers that based on a cost of \$0.12/ m³ per km, purchasers faced with a SSNIP could source pulplogs from an additional 35 km, unpruned logs from an additional 60 km, and pruned logs from an additional 110 km beyond the area of aggregation.
105. These distances would indicate that if a SSNIP were to be introduced, it would be economic for a processor located in Nelson to transport pulplogs over a total distance of approximately 120 km, unpruned sawlogs 140 km, and pruned sawlogs 200 km.
106. These boundaries suggest that it would be economic to transport pruned sawlogs over greater distances than for unpruned sawlogs and pulplogs, indicating that a broader pruned sawlog market may be appropriate. However, the Commission considers that it is unlikely that a wider boundary would make any substantial difference. Beyond the Nelson/Marlborough region, the next major forestry regions are the Canterbury region and the West Coast region wood supply catchments. These regions lie more than 300 km from Nelson, and are therefore unlikely to represent a significant supply-side alternative in the event that a SSNIP is applied.

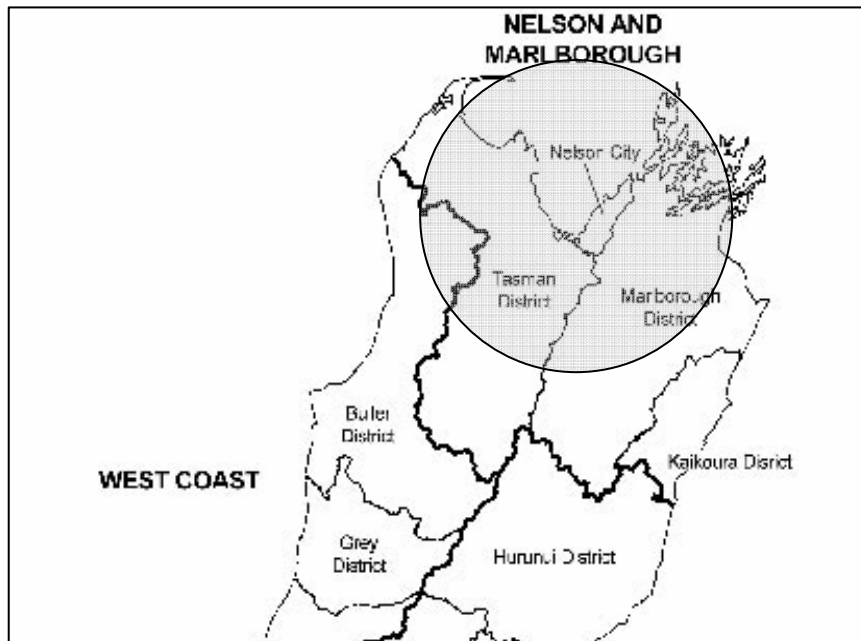
³⁴ Weyerhaeuser has long-term supply contracts for pruned sawlog processors (Inangahua, International Panel and Westco Lagen) located in the West Coast region.

³⁵ The resulting price increases are discussed in paragraph 86 above.

107. The distances calculated above are consistent with information provided to the Commission in terms of existing wood flows within the Nelson/Marlborough region.
108. NPI advised that it prefers to source pulplogs from Nelson forests close to its MDF plant, due to the low value of pulplogs and the relative cost of transporting pulplogs from Marlborough.
109. Waimea, which processes unpruned sawlogs, advised the Commission that its suite of suppliers includes [], which manages some forests located in Marlborough.
110. TFML and Matariki advised the Commission that they use barges to transport logs sourced from Marlborough Sounds, where there is limited road access, to processors in Nelson³⁶. Matariki advised the Commission that logs from its Queen Charlotte Forest are transported to Nelson by truck, via Port Underwood Road, as well as by barge. Matariki sometimes barges logs directly to Nelson; however, it most commonly barges logs to Havelock, where the logs are transferred to trucks for transportation to Nelson. The Commission notes that the cost to barge logs tends to be more expensive than road transport³⁷, although this additional cost is offset to some extent by Transit New Zealand subsidies.
111. Weyerhaeuser advised the Commission that its Kaituna sawmill in Blenheim sources the greater proportion of its pruned sawlogs from the Nelson JV. Weyerhaeuser uses backloading to reduce transport costs: a truck that is used to deliver pruned sawlogs to Kaituna sawmill will transport pulplogs from Weyerhaeuser's Marlborough forests to Picton or Nelson on the return trip.
112. The above analysis is summarised in Figure 2 below. Nelson is taken as the epicentre of the main processing capacity in Nelson/Marlborough. The shaded circle represents the approximate area within which it is economically feasible to transport logs in response to a SSNIP. This indicates that the Nelson/Marlborough forestry region is the appropriate economic market for pulplogs, unpruned sawlogs and pruned sawlogs.

³⁶ Logs destined for export are barged to Port Marlborough at Picton.

³⁷ Matariki advised the Commission that it costs an additional \$[]/m³ to barge logs from its Queen Charlotte Forest, as compared to the cost of transporting the logs over Port Underwood Road. \$[]/m³ of this is subsidised by Transit New Zealand's Alternative to Roads Programme.

Figure 2: Nelson/Marlborough Log Supply Region

Source: MAF

Conclusion on Geographic Markets

113. The Commission considers that for the purpose of assessing the competition implications of the proposed acquisition, the appropriate markets are:

- the market for the production and supply of pulplogs in Northland;
- the market for the production and supply of unpruned sawlogs in Northland;
- the market for the production and supply of pruned sawlogs in Northland and Auckland;
- the market for the production and supply of pulplogs in Nelson/Marlborough;
- the market for the production and supply of unpruned sawlogs in Nelson/Marlborough; and
- the market for the production and supply of pruned sawlogs in Nelson/Marlborough.

Temporal Dimension

114. The Commission typically views markets as operating continuously over time. However, temporal considerations may be important where depletable resources are involved, as is the case with forestry, where production depends substantially on the level of planting that occurred years before the harvesting of the trees takes place. For example, radiata pine, which accounts for around 89% of New Zealand's plantation forests, takes up to 30 years to reach an age at which it is economic to harvest. Therefore, each firm's potential production will depend on the age structure of its forests, and its market share can vary over time.

115. The Commission understands that there is reasonably low substitutability on the demand- and supply-side between timber harvested in different periods, although forest owners may be able to accelerate or defer harvest by some years.

Acceleration of harvesting levels may be constrained by the loss of value in cutting a younger tree. Deferral of harvesting may be less problematic (due to the resultant increase in value of the ageing forest), but later harvesting results in more heavily discounted cash-flows.

116. In Decisions 426, 468 and 588, the Commission considered it appropriate to define distinct temporal dimensions within the relevant markets.
117. The Applicant submitted that the relevant timeframes are 2006-2008, 2009-2013, 2014-2018 and 2019-2023³⁸.
118. There are a number of factors that affect wood flow forecasts, including log prices and market demand³⁹. These conditions are highly variable and cannot be easily predicted. Industry participants advised the Commission that for these reasons, the industry tends to base its projections on current market conditions.
119. The Commission relies upon relatively accurate wood flow forecasts in its assessment of the competition implications of the proposed acquisition. Industry participants advised the Commission that the further into the future that the harvest is projected, the higher degree of speculation is involved in the projection, and therefore the less certainty as to the accuracy of the projected harvest level. To this end, the Commission has not included the 2019-2023 time period in its assessment of the likely competition implications of the proposed acquisition.

Conclusion on Market Definition

120. The Commission concludes that the relevant markets are:

- the production and supply of pulplogs in Northland, for the periods 2006–2008, 2009–2013, and 2014–2018;
- the production and supply of unpruned sawlogs in Northland, for the periods 2006–2008, 2009–2013, and 2014–2018;
- the production and supply of pruned sawlogs in Northland and Auckland, for the periods 2006–2008, 2009–2013, and 2014–2018;
- the production and supply of pulplogs in Nelson/Marlborough, for the periods 2006–2008, 2009–2013, and 2014–2018;
- the production and supply of unpruned sawlogs in Nelson/Marlborough, for the periods 2006–2008, 2009–2013, and 2014–2018; and
- the production and supply of pruned sawlogs in Nelson/Marlborough, for the periods 2006–2008, 2009–2013, and 2014–2018.

COUNTERFACTUAL AND FACTUAL

121. In reaching a conclusion about whether an acquisition is likely to lead to a substantial lessening of competition, the Commission makes a comparative judgement considering the likely outcomes between two hypothetical situations,

³⁸ Timeframes submitted by the Applicant are based on those which were used in the report Resources of the Northern Forests, June 2004, which was prepared for the Enterprise Northland Forests Group by CFK.

³⁹ E.g., In Decision 588, [] held back harvest in order to increase the average cutting age, in order to meet market demand for stronger, stiffer wood.

one with the acquisition (the factual) and one without (counterfactual).⁴⁰ The difference in competition between these two scenarios is then able to be attributed to the impact of the acquisition.

Northland

Factual

122. As discussed previously, CRBF⁴¹ and CHH currently each hold a 50% shareholding of the 22,000 ha Mangakahia JV⁴². In addition, GFP owns [] ha of forestry estates scattered throughout Northland.
123. The Commission considers that in the factual scenario, the combined entity would own and manage the entire 22,000 ha Mangakahia JV; CHH's 35,000 ha of Northland forestry estate; and its existing [] ha of forestry estates in the Northland region. Post-acquisition, the combined entity's total forestry estate in the Northland region would be [] ha.

Counterfactual

124. CRBF Limited is one of a number of bidders for CHH's forestry assets. The Commission was advised by CHH that the other bidders involved are:
- Hancock⁴³;
 - []; and
 - [].
125. The Commission considers the relevant counterfactual to be that the CHH forestry assets would be acquired by a third party that does not presently have a major interest in New Zealand forestry.

Nelson/Marlborough

126. In the Nelson/Marlborough region, CRBF⁴⁴ currently has a forestry holding of [] ha. This forestry holding consists of its [] ha forest in Marlborough and the 64,000 ha Nelson JV.
127. In respect of the proposed acquisition, the Commission considers the relevant counterfactual to be that the CHH forestry assets would be acquired by a third party that does not presently have a major interest in New Zealand forestry.
128. The Nelson JV []. It was put up for sale in February 2006; however, the sale was unsuccessful []. Accordingly, the Nelson JV rejected all bids. Because the joint venture has been terminated, the participants must determine another means of disposing of the joint venture assets.
129. In respect of GFP's forestry holdings, the Commission considers that the disposal of the Nelson JV generates the possibility for two different scenarios to arise in the counterfactual scenario:

⁴⁰ *Air New Zealand & Qantas Airways Ltd v Commerce Commission (No.6)*, unreported HC Auckland, CIV 2003 404 6590, Hansen J and KM Vautier, Para 42.

⁴¹ Through its parent company, GFP.

⁴² CHH acts as the forest manager for the Mangakahia JV.

⁴³ Decision 588, *Hancock Natural Resource Group Inc. and Carter Holt Harvey Limited*, September 2006.

⁴⁴ Through its parent company, GFP.

- GFP and Weyerhaeuser will divide the Nelson JV⁴⁵. GFP will own and manage [] ha of forestry estate in the Nelson/Marlborough region, comprising: its [] ha forest in Marlborough and its 32,000 ha share in the Nelson JV; or
- GFP will continue its current involvement in the Nelson JV, either as a result of purchasing Weyerhaeuser's shareholding or by entering into a new JV with a third-party. GFP will continue to own and manage [] ha of forestry estate in the Nelson/Marlborough region.

130. The Commission considers that each of these scenarios is equally likely to occur in the counterfactual scenario. However, the Applicant would have a smaller market share in the second scenario than the first scenario. To this extent, the Commission considers that for the purpose of assessing this application, if no competition concerns arise from adopting the second scenario as the counterfactual, it is unlikely that competition concerns will arise from adopting the first scenario as the counterfactual.

131. The Commission therefore considers that the appropriate counterfactual scenario in this instance is the second scenario, in which GFP will continue its current involvement in the Nelson JV and will continue to own and manage [] ha of forestry estate in the Nelson/Marlborough region.

132. In respect of GFP's forestry holdings, the Commission considers that the disposal of the Nelson JV generates the possibility for three different scenarios to arise in the factual scenario:

- GFP will sell its stake in the Nelson JV to a third party. GFP would own and manage of [] ha in the Nelson/Marlborough region, comprising: its [] ha forest in Marlborough and the 27,000 ha CHH forestry estate;
- GFP and Weyerhaeuser will partition the Nelson JV⁴⁶. GFP would own and manage [] ha of forestry estate in the Nelson/Marlborough region, comprising: its [] ha forest in Marlborough, its 32,000 ha share in the Nelson JV, and the 27,000 ha CHH forestry estate; or
- GFP will retain its interest in the Nelson JV, either through a new joint venture with a third party or full ownership of the Nelson JV. GFP would own and manage [] ha of forestry estate in the Nelson/Marlborough region, comprising: its [] ha forest in Marlborough, the 64,000 ha Nelson JV and the 27,000 ha CHH forestry estate.

⁴⁵ GFP advised the Commission that it has no interest in becoming a vertically-integrated forestry operator. The Commission therefore considers that in this scenario, the most likely division of assets will be an equal split of the Nelson JV forestry estate between Weyerhaeuser and GFP, and Weyerhaeuser will retain the Kaituna sawmill.

⁴⁶ GFP advised the Commission that it has no interest in becoming a vertically-integrated forestry operator. The Commission therefore considers that in this scenario, the most likely division of assets will be an equal split of the Nelson JV forestry estate between Weyerhaeuser and GFP, and Weyerhaeuser would retain the Kaituna sawmill.

133. The Commission considers that each of these scenarios is equally likely to occur in the factual scenario. However, the Applicant would have the greatest market share in the third scenario, in comparison to the first and second scenarios. To this extent, the Commission considers that for the purpose of assessing this application, if no competition concerns arise from adopting the third scenario as the factual, it is unlikely that competition concerns will arise from adopting the first or second scenarios as the factual.
134. The Commission therefore considers that the appropriate factual scenario in this instance is the third scenario, in which GFP will continue its current involvement in the Nelson JV and will continue to own and manage [] ha of forestry estate in the Nelson/Marlborough region as well as the 27,000 ha CHH forestry estate.
135. In the third scenario, GFP would have a significantly larger forestry holding, and therefore market share, than it currently does. In order to alleviate any competition concerns, GFP has given the Commission an undertaking that [], GFP will retain its interest in the Nelson JV and divest the CHH forestry assets to a third party [].
136. In assessing the viability of the divestment undertaking, the Commission has evaluated the likelihood of CRBF being able to dispose of the CHH forestry estates (purchaser risk⁴⁷).
137. GFP advised the Commission that [] have registered an interest in acquiring portions of the CHH forestry assets that GFP may not wish to retain post-acquisition, including the Nelson/Marlborough forestry estates.
138. Other parties spoken to by the Commission also signalled an interest in purchasing the CHH forestry estate in Nelson/Marlborough. [] advised the Commission that they would be interested in acquiring some or all of the CHH forestry estate should a divestment occur. [] explained that the CHH forestry estate is an attractive prospect because it consists of four discrete forests which could be divided and sold individually.
139. To this end, the Commission is of the view that GFP would be able to find an independent buyer, and therefore successfully divest itself of the CHH forestry estate. The divestment would preserve the CHH forestry estate as a competitor to GFP in the Nelson/Marlborough log markets, and as such, it would not result in any material difference between the factual and the counterfactual.
140. Accordingly the Commission considers that the proposed acquisition would not have, or would not be likely to have, the effect of substantially lessening competition in the markets for:
- the production and supply of pulplogs in Nelson/Marlborough, for the periods 2006–2008, 2009–2013, and 2014–2018;
 - the production and supply of unpruned sawlogs in Nelson/Marlborough, for the periods 2006–2008, 2009–2013, and 2014–2018; and

⁴⁷ Purchaser risks are risks that a suitable purchaser is not available or that the merger parties will dispose to a weak or otherwise inappropriate purchaser; Decision 545, Gallagher Holdings Limited and Tru-Test Corporation Limited, p 3.

- the production and supply of pruned sawlogs in Nelson/Marlborough, for the periods 2006–2008, 2009–2013, and 2014–2018.

141. The Commission therefore considers that it is not necessary to examine Nelson/Marlborough log markets in the competition analysis below.

COMPETITION ANALYSIS

Northland Region

Pulplog Markets

Existing Competition

142. Existing competition occurs between those businesses in the market that already supply the product, and those that could readily do so by adjusting their product-mix (near competitors).
143. An examination of concentration in a market can provide a useful indication of the competitive constraints that market participants may place upon each other, providing there is not significant product differentiation. Moreover, the increase in seller concentration caused by a reduction in the number of competitors in a market by an acquisition is an indicator of the extent to which competition in the market may be lessened.
144. A business acquisition is considered unlikely to substantially lessen competition in a market where, after the proposed acquisition, either of the following situations exist:
- 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 persons or associated persons) has less than in order of 40% share; or
 - 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%.
145. The Applicant submitted that the combined entity would continue to face constraint from existing competitors. In addition, the combined entity would be constrained by diversion of pulplogs from export.
146. The Commission has gathered information from the Applicant and other relevant parties, and has used this to estimate market shares for the pulplog markets as set out in Table 2. The Applicant's market shares are displayed as CRBF. CRBF's market share figures include wood flows from existing Northland GFP forestry estates.

Table 2: Future Wood Flows for Pulplogs in the Northland Region

Forest Owner/Manager	Wood flow: Average volume per year					
	2006-2008		2009-2013		2014-2018	
	(000 m ³)	%	(000 m ³)	%	(000 m ³)	%
CRBF	[]	[]%	[]	[]%	[]	[]%
CHH	[]	[]%	[]	[]%	[]	[]%
<i>Combined Entity</i>	[]	[]%	[]	[]%	[]	[]%
Matariki	[]	[]%	[]	[]%	[]	[]%
PF Olsen	[]	[]%	[]	[]%	[]	[]%
Crown Forestry	[]	[]%	[]	[]%	[]	[]%
NFML	[]	[]%	[]	[]%	[]	[]%
Other	[]	[]%	[]	[]%	[]	[]%
Total Northland supply	[]	100%	[]	100%	[]	100%

Source: Industry participants

147. The market shares in Table 2 relate to the production and supply of pulplogs in the Northland region. The combined entity has the largest volume of wood flow in Northland across all time periods; its greatest competitor in the pulplog markets is [].
148. Small woodlots also make up a significant proportion of pulplogs in the Northland markets, particularly during the 2006-2008 and 2014-2018 time periods. This is due to the relatively high volume of pulplogs projected for harvest from small woodlots and the uncommitted nature of these logs - all woodlot logs flow directly into the Northland pulplog market, as none of it is tied into long-term contracts.
149. A number of these woodlots are administered by forest managers such as PF Olsen and NFML. Harvest contractors aggregate harvest from a number of different sources, providing a single point of sale for a proportion of the small woodlot pulplogs in the Northland region. Accordingly, PF Olsen and NFML's market shares are presented separately from other small woodlots.
150. The remaining owners of small woodlots in the Northland are numerous and fragmented. A CFK report⁴⁸ examining the Northland forests states that woodlot owners, which hold less than 40 ha each, are the second largest ownership group in the Northland region⁴⁹.
151. In Decision 588, the Commission considered that any degree of constraint posed by small woodlots was likely to be of a lesser magnitude than that of larger forestry operators in the CNI pulplog markets, due to the disjointed nature of woodlots, and their variability in harvest.
152. Industry participants advised the Commission that it is unlikely that small woodlots in the Northland region would exhibit the same inconsistency in

⁴⁸ CFK, *Resources of the Northern Forests*, June 2004, p 6-7.

⁴⁹ The CFK report also goes on to discuss forest ownership by land area, whereby small woodlots make up 17% of forest ownership by land area, and large forestry companies make up 72% of forest ownership by land area.

harvest levels, as it is generally anticipated that Northland is subject to an industry-wide harvest increase over the next ten years, and as such, woodlot owners are incentivised to maintain cutting at projected harvest levels.

153. For this reason the Commission considers that, for the purposes of assessing the competition implications of the proposed acquisition, the ability for small woodlots to exert constraint upon the combined entity is unlikely to be diminished by variability in supply⁵⁰.
154. In Decision 426, 468 and 588, the Commission considered the extent to which wood flows were committed to particular uses⁵¹, and therefore the extent by which the combined entity would be able to control or influence the flow of wood to parties, such as independent sawmills.
155. For the purpose of assessing the competition implications of the proposed acquisition, the Commission considers that it is only residual wood flows that could be controlled or influenced by the merged entity. That is, wood flows that are committed to long-term contracts⁵² are not contestable in the market for pulplogs in Northland.
156. Juken, a vertically-integrated forestry operator, was unable to furnish the Commission with its harvest information within the required time period. For this reason, Juken has not been included in the Northland pulplog markets market share tables. The Commission considers that the absence of this information is not detrimental to its ability to accurately assess the likely competition implications of the proposed acquisition, as Juken is not a supplier or purchaser of pulplogs in the Northland region: the pulplogs processed by its MDF and LVL plants in Kaitaia are sourced entirely from Juken's forests.
157. The market shares for residual wood flows for the pulplog markets are set out in Table 3 (Appendix 1).
158. Table 3 indicates that in the 2006-2008 time period, prior to the acquisition, CRBF has a market share of [] % of residual supply, with a three-firm concentration ratio of [] %. Post-acquisition, the combined entity would have a market share of [] % and the three-firm concentration would be [] %, which is within the Commission's safe harbour guidelines.
159. In the 2009-2013 time period, prior to the acquisition, CRBF has a market share of [] % with a three-firm concentration ratio of [] %. Post-acquisition, the combined entity would have a market share of [] % and the three-firm concentration would be [] %. This falls outside of Commission's safe harbour guidelines.
160. In the 2014-2018 time period, prior to the acquisition, CRBF has a market share of [] % with a three-firm concentration ratio of [] %. Post-acquisition, the combined entity would have a market share of [] % and the three-firm

⁵⁰ The fragmented nature of small woodlots remains a consideration.

⁵¹ Such as self-supply for the case of vertically integrated forestry operators and long-term supply contracts.

⁵² Logs purchased on the spot market are acquired by quarterly negotiation for volume and price. For the purposes of assessing the competition implications of the proposed acquisition, the Commission considers that a long-term contract is a supply commitment between a forest operator and a sawmill for a time period longer than three months.

concentration would be [] %; this is outside of the Commission's safe harbour guidelines.

161. The Commission recognises that concentration is only one of a number of factors to be considered in the assessment of competition in a market. In order to understand the impact of the acquisition on competition, and having identified the level of concentration in a market, the Commission considers the behaviour of the businesses in the market.
162. The combined entity is the greatest contributor of residual wood flow into the Northland pulplog markets across all time periods. The combined entity's market share increases uniformly across all time periods, [].
163. In the 2006-2008 and 2009-2013 time periods, the combined entity's greatest competitor is [], and to a lesser extent, [].
164. [] remains the combined entity's greatest competitor in the 2014-2018 time period, although [].
165. [] is not a significant competitor to the combined entity in the 2014-2018 time period. [].
166. In Decision 588, the Commission considered that the large volumes of pulplogs committed under long-term supply contracts and the harvest conditions in the CNI region, meant that a diligent assessment of the pulplog market should consider demand requirements.
167. In respect of the current application, the Commission considers that the unique structure of the pulplog markets in the Northland region renders a detailed analysis of supply and demand unnecessary. Marusumi is the only purchaser of pulplogs in the Northland region. Furthermore, the Commission notes that there is an excess supply of pulplogs in the Northland region across all time periods, such that Marusumi is not reliant on the combined entity for its supply of pulplogs.

Expansion through Diversion from Export

168. The Applicant submitted that the combined entity would be constrained by the potential diversion of pulplogs from export by existing competitors in the factual scenario.
169. In Decision 426, the Commission considered that the combined entity would be constrained by diversion of pulplogs destined for export back into the domestic market. More recently, in Decision 588, the Commission considered that, based on current pulplog export levels, it was unlikely that existing competitors would expand through diversion from export in the factual scenario.
170. Post acquisition, the combined entity will export the greatest volume of pulplogs in the Northland region. [].
171. The only other forest manager that exports pulplogs from Northland is []; however, the volumes exported by [] are negligible in comparison to the volumes exported by the combined entity.

172. There are a number of factors that affect the incentive to export pulplogs, including foreign exchange rates and global log prices. These conditions are highly variable and cannot be easily predicted. For these reasons, the Commission considers that it cannot speculate as to the likelihood of future export volumes of pulplogs in the Northland markets, and bases its assessment on the current levels of export.

Conclusion on Expansion through Diversion from Export

173. The Commission considers that, based on current pulplog export levels, it is unlikely that existing competitors would expand through diversion from export in the factual scenario.

Merger Simulation

174. In considering the likely impact of the proposed acquisition, the Commission has undertaken some simulation work, based on a Cournot model of competition⁵³. The Commission considers that a Cournot model is appropriate for the purpose of assessing the current application as the products under consideration are relatively homogeneous. In addition, the assumption that competitors' output remains constant is consistent with indications that log supply is relatively inelastic.
175. In order to run the simulation, the Commission used the residual supply market shares for each of the time periods under consideration. Utilisation of the residual supply market shares is considered appropriate as the residual supply market shares eliminate minimum volumes contained in long-term supply contracts, which are unlikely to be impacted upon in the event that the combined entity was able to exercise market power. The Commission used log prices provided by MAF⁵⁴.
176. To consider the effects of the proposed acquisition, the Commission has modeled two scenarios for each market. The first scenario considers the price effect where supply from small woodlots (which accounts for [] % - [] % of residual supply) is aggregated and treated as a single entity. The second scenario disaggregates this share to reflect the more fragmented nature of this source of supply⁵⁵.
177. The result of the simulation indicates that the proposed acquisition could lead to an increase in pulplog prices of 1.8% p.a. over 2006-2008 (0.8% if "Others" is disaggregated); 4.2% p.a. over 2009-2013 (1.8%); and 4.0% p.a. over 2014-2018 (1.7%).
178. Merger simulation can provide a helpful guide in assessing the possible pricing impact of an acquisition. The Commission notes that the merger simulation is only one element of its analysis of the competition implications of the proposed acquisition. The merger simulation takes no account of qualitative factors that will typically be relevant, such as countervailing power of acquirers. The Commission has considered these issues separately as part of this decision.

⁵³ The Cournot model used can be found at <http://csgb.ubc.ca/ccpp/simulation/>

⁵⁴ Specifically, the price for each type of log delivered to the mill, and averaged over the last four quarters was used. For pulplogs, the price used is \$44 per m³; for unpruned sawlogs, the price is \$72 per m³ (an average of industrial and structural grades); and for pruned sawlogs, the price used is \$122 per m³.

⁵⁵ Specifically, the "Others" share is divided by 10.

179. The modelling undertaken indicates that the upper bound of any price increase resulting from the proposed acquisition is likely to be less than approximately 4% in the Northland pulplog markets.

Conclusion on Merger Simulation

180. The Commission considers that the result of the merger simulation is consistent with the Commission's view regarding existing competition, that is, the combined entity would continue to face some degree of constraint from large forestry operators, such as Matariki and Crown Forestry, as well as small woodlots in the factual scenario.

Conclusion on Existing Competition

181. The Commission considers that existing competitors, such as Matariki, Crown Forestry, and small woodlots, would likely provide a degree of constraint on the combined entity in the factual scenario.
182. The Commission considers that, based on current pulplog export levels, it is unlikely that existing competitors would expand through diversion from export in the factual scenario.
183. The Commission considers that the result of the merger simulation is consistent with the Commission's view regarding existing competition, that is, the combined entity would continue to face some degree of constraint from large forestry operators, such as Matariki and Crown Forestry, as well as small woodlots in the factual scenario.
184. Accordingly, the Commission concludes that post-acquisition, the combined entity would be likely to face a degree of constraint from existing competition in the market for the production and supply of pulplogs in the Northland region for the 2006-2008, 2009-2013 and 2014-2018 time periods.

Countervailing Power

185. Marusumi is a monopsonist in the Northland pulplog markets. It only has one long-term supply contract, which is a rolling annual contract⁵⁶ with [] to supply [] m³ of pulplogs per year.
186. Marusumi told the Commission that it maintains a suite of suppliers from which it sources pulplogs. Presently its main suppliers include forestry operators such as [], harvest managers such as [] and log exporters such as [].
187. Industry participants advised the Commission that there is presently an excess of supply of pulplogs in the Northland region, which is a result of the limited processing capacity, and therefore demand, for pulplogs. [] told the Commission that it predicts that Northland's current surplus of pulplogs will only grow as the Northland wood flows increase over the next eight years.
188. [] advised the Commission that at present, it is unable to find an outlet for the pulplogs harvested from its Northland forests and it is leaving its harvested pulplogs on the forest floor. [] said it prefers to sell its pulplogs, as leaving the pulplogs in the forest means forfeiting potential profit. It occasionally supplies Marusumi when market conditions are favourable

⁵⁶ Under this contract, price and volume are negotiated quarterly.

whereby the price fetched for its pulplogs justifies the cost of harvest and transportation of the pulplogs.

189. In addition, [] told the Commission that the cost of transportation relative to the low value of pulplogs makes selling the pulplogs in an alternative market, such as the CNI, unfeasible. Similarly, presently [] does not export significant volumes from its Northland forests, because the current export prices means that it is not cost effective to transport pulplogs to the closest port.
190. The Commission considers that the range of pulplog producers, coupled with the excess supply of pulplogs and the limited number of pulplog outlets in the Northland region gives Marusumi, as an acquirer of pulplogs, an advantageous position in terms of countervailing power.

Conclusion on Countervailing Power

191. The Commission considers that Marusumi, an acquirer of pulplogs, would likely act as a constraint on the combined entity in the factual scenario, because of the excess supply of pulplogs and the limited number of pulplog outlets in the Northland region.
192. Accordingly, the Commission concludes that post-acquisition, the combined entity would likely be constrained by acquirers of pulplogs in the market for the production and supply of pulplogs in Northland for the 2006-2008, 2009-2013 and 2014-2018 time periods.

Conclusion on Pulplog Markets

193. The Commission considers that existing competitors, such as Matariki, Crown Forestry, and small woodlots, would likely provide a degree of constraint on the combined entity in the factual scenario.
194. The Commission considers that, based on current pulplog export levels, it is unlikely that existing competitors would expand through diversion from export in the factual scenario.
195. The Commission considers that the result of the merger simulation is consistent with the Commission's view regarding existing competition, that is, the combined entity would continue to face some degree of constraint from large forestry operators, such as Matariki and Crown Forestry, as well as small woodlots in the factual scenario.
196. The Commission considers that Marusumi, an acquirer of pulplogs, would likely act as a constraint on the combined entity in the factual scenario, because of the excess supply of pulplogs and the limited number of pulplog outlets in the Northland region.
197. Accordingly, the Commission concludes that the proposed acquisition would not have, or would not be likely to have, the effect of substantially lessening competition in the market for the production and supply of pulplogs in Northland for the 2006-2008, 2009-2013 and 2014-2018 time periods.

Unpruned Sawlog Markets

Existing Competition

198. The Applicant submitted that the combined entity would continue to face constraint from existing competitors in the factual scenario. In addition, the combined entity would be constrained by diversion from export.
199. The Commission has gathered information from the Applicant and other relevant parties, and has used this to estimate market shares for the unpruned log markets, as set out in Table 4. The Applicant's market shares are displayed as CRBF. CRBF's market share figures include wood flows from existing Northland GFP forestry estates.

Table 4: Future Wood Flows for Unpruned Sawlogs in Northland

Forest Owner/Manager	Wood flow: Average volume per year					
	2006-2008		2009-2013		2014-2018	
	(000 m ³)	%	(000 m ³)	%	(000 m ³)	%
GFP	[]	[]%	[]	[]%	[]	[]%
CHH	[]	[]%	[]	[]%	[]	[]%
<i>Combined Entity</i>	[]	[]%	[]	[]%	[]	[]%
Matariki	[]	[]%	[]	[]%	[]	[]%
PF Olsen	[]	[]%	[]	[]%	[]	[]%
Crown Forestry	[]	[]%	[]	[]%	[]	[]%
NFML	[]	[]%	[]	[]%	[]	[]%
Other	[]	[]%	[]	[]%	[]	[]%
Total Northland supply	[]	100%	[]	100%	[]	100%

Source: Industry participants

200. The market shares in Table 4 relate to the production and supply of unpruned sawlogs in Northland. The combined entity has the largest volume of wood flow in Northland across all time periods; the second largest contributor of unpruned sawlogs into the Northland markets is [].
201. As discussed in the context of the pulplog markets, the Commission considers that the ability for small woodlots to exert constraint upon the combined entity is unlikely to be diminished by variability in supply⁵⁷.
202. As discussed in the context of the pulplog markets, the Commission considers, for the purpose of assessing the competition implications of the proposed acquisition, only residual wood flows can be controlled or influenced by the combined entity. That is, wood flows that are committed to long-term contracts are not contestable in the market for unpruned sawlogs in Northland.
203. The market shares for residual wood flows for the unpruned markets are set out in Table 5 (Appendix 1).
204. Table 5 indicates that in the 2006-2008 time period, prior to the acquisition, CRBF has a market share of [] % of residual supply, with a three-firm

⁵⁷ Although the fragmented nature of small woodlots remain a consideration.

concentration ratio of [] %. Post-acquisition, the combined entity would have a market share of [] % and the three-firm concentration would be [] %, which is within the Commission's safe harbour guidelines.

205. In the 2009-2013 time period, prior to the acquisition, CRBF has a market share of [] % with a three-firm concentration ratio of [] %. Post-acquisition, the combined entity would have a market share of [] % and the three-firm concentration would be [] %, which is outside the Commission's safe harbour guidelines.
206. In the 2014-2018 time period, prior to the acquisition, CRBF has market share of [] % with a three-firm concentration ratio of [] %. Post-acquisition, the combined entity would have a market share of [] % and the three-firm concentration would be [] %. This falls outside of the Commission's safe harbour guidelines.
207. The combined entity is the largest contributor of residual unpruned sawlogs into the Northland region across all time periods.
208. The combined entity's largest competitor across all time periods is []. [] harvest levels decrease slightly from the 2006-2008 time period to the 2009-2013 time period; however, its market share remains uniform [].
209. [] is the next largest competitor in both the 2006-2008 and 2009-2013 time periods, although it is not a significant competitor to the combined entity during the 2014-2018 time period, [].
210. In Decision 588, the Commission included an assessment of the demand requirements for unpruned sawlogs in its analysis of existing competition. The Commission considers that this approach remains appropriate in the context of the proposed acquisition.
211. []
212. For the purpose of assessing demand requirements, the Commission has not included wood flows that are tied into long-term contracts, as these volumes are not contestable. Table 6 shows the residual demand, post-acquisition, in the Northland unpruned sawlog markets.

Table 6: Future Residual Demand for Unpruned Sawlogs in Northland

Sawmill	Wood flows: Average volume per year					
	2006-2008		2009-2013		2014-2018	
	(000 m ³)	%	(000 m ³)	%	(000 m ³)	%
CHH	[]		[]		[]	
Less contracted supply	[]		[]		[]	
CHH Residual Demand	[]	[]%	[]	[]%	[]	[]%
TDC	[]		[]		[]	
Less contracted supply	Matariki	[]		[]		[]
TDC Residual Demand	[]	[]%	[]	[]%	[]	[]%
Crofts	[]		[]		[]	
Less contracted supply	[]		[]		[]	
Crofts Residual Demand	[]	[]%	[]	[]%	[]	[]%
Ahead Lumber	[]		[]		[]	
Less contracted supply	[]		[]		[]	
Ahead Lumber Residual Demand	[]	[]%	[]	[]%	[]	[]%
[]	[]		[]		[]	
Less contracted supply	[]		[]		[]	
[] Residual Demand	[]	[]%	[]	[]%	[]	[]%
Other Residual Demand	[]	[]%	[]	[]%	[]	[]%
Total Northland Demand	[]		[]		[]	
Total Northland Residual Demand	[]	100%	[]	100%	[]	100%

Source: Industry participants

213. Table 6 shows that there is a significant increase in the demand for unpruned sawlogs from the 2006-2008 time period to the 2009-2013 time period.
[

].

214. CHH advised the Commission that its new sawmill, known in the industry as “Big Foot”, will have a processing capacity of [] m³ of unpruned sawlogs from [], which will increase to [] m³ per year by [].

215. The Commission has made a conservative evaluation of the demand for the Northland unpruned sawlog markets and included the projected demand volumes for [], as well as those for [] in Table 6 and Table 7.

216. Table 7 shows the relationship between residual demand and supply for the Northland pulplog markets.

Table 7: Future Residual Supply and Demand for Unpruned Sawlogs in Northland

	Wood flows: Average volume per year					
	2006-2008		2009-2013		2014-2018	
Residual Supply						
Forest Owner/Manager	(000 m³)	%	(000 m³)	%	(000 m³)	%
Combined Entity	[]	[]%	[]	[]%	[]	[]%
Matariki	[]	[]%	[]	[]%	[]	[]%
PF Olsen	[]	[]%	[]	[]%	[]	[]%
Crown Forestry	[]	[]%	[]	[]%	[]	[]%
Northland Forest Managers	[]	[]%	[]	[]%	[]	[]%
Other	[]	[]%	[]	[]%	[]	[]%
Total Northland Residual Supply	[]	100%	[]	100%	[]	100%
Residual Demand						
Sawmill	(000 m³)	%	(000 m³)	%	(000 m³)	%
CHH	[]	[]%	[]	[]%	[]	[]%
Crofts	[]	[]%	[]	[]%	[]	[]%
A&L	[]	[]%	[]	[]%	[]	[]%
TDC	[]	[]%	[]	[]%	[]	[]%
[]	[]	[]%	[]	[]%	[]	[]%
Other	[]	[]%	[]	[]%	[]	[]%
Total Northland Residual Demand	[]	100%	[]	100%	[]	[]%
Total Northland Excess Residual Supply	[]		[]		[]	

Source: Industry participants

217. An assessment of residual demand and supply shows that supply is in excess of demand in the Northland unpruned sawlog market during the 2006-2008 and 2014-2018 time periods.
218. Although there is a projected harvest increase throughout the 2009-2013 time period, there is a shortfall in supply due to the increased processing capacity, and therefore demand, during this time period. The Commission considers that this supply deficit will likely result in diminished constraint by existing competitors and an increase in the price of unpruned sawlogs.
219. The Commission notes that because the projected increase in processing capacity is likely to occur whether or not the proposed acquisition goes ahead, there is likely to be a supply deficit, and therefore a price increase, for unpruned sawlogs in both the factual and the counterfactual.
220. The Commission must therefore examine as to whether the combined entity has enhanced scope in the factual scenario to exercise market power and raise the price of unpruned sawlogs to supra-competitive levels. The Commission considers the combined entity's ability to exercise unilateral market power and coordinated market power in the 2009-2013 time period separately as part of this decision.

Expansion through Diversion from Export

221. The Applicant submitted that the combined entity would be constrained by the diversion of unpruned sawlogs from export by existing competitors in the factual scenario.
222. In Decision 588, the Commission considered there was sufficient evidence, in the form of fluctuating volumes of exported unpruned sawlogs, to suggest that it

was likely that existing competitors would expand to some degree through diversion from export in the factual scenario.

223. Most of the larger forestry operators in the Northland region do not export significant volumes of unpruned sawlogs. [] only export very small volumes of unpruned sawlogs, and [] does not export any unpruned sawlogs. [] advised the Commission that its export volumes are relatively low because export log prices are not sufficient to absorb the additional transportation cost of moving unpruned sawlogs from its Northland forests to the port.
224. The only other forest manager that exports significant volumes of unpruned sawlogs from Northland is []; however, the volumes exported by [] are negligible in comparison to the volumes exported by the combined entity.

Conclusion on Expansion through Diversion from Export

225. The Commission considers that, based on current unpruned sawlog export levels, it is unlikely that existing competitors would expand through diversion from export in the factual scenario.

Merger Simulation

226. In order to run the simulation, the Commission used the residual supply market shares for each of the time periods under consideration. Utilisation of the residual supply market shares is considered appropriate as the residual supply market shares eliminate minimum volumes contained in long-term supply contracts, which are unlikely to be impacted upon in the event that the combined entity was able to exercise market power. The Commission used log prices provided by MAF⁵⁸.
227. To consider the effects of the proposed merger, the Commission has modelled two scenarios for each market. The first scenario considers the price effect where supply from small woodlots (which accounts for []% - []% of residual supply) is aggregated and treated as a single entity. The second scenario disaggregates this share to reflect the more fragmented nature of this source of supply.⁵⁹
228. The results of the simulation conducted by the Commission in respect of the unpruned sawlog markets indicates that the proposed acquisition could lead to an increase in unpruned log prices of 1.8% p.a. over 2006-2008 (0.8% if “Others” is disaggregated); 2.0% p.a. over 2009-2013 (0.9%); and 2.6% p.a. over 2014-2018 (1.1%).
229. Merger simulation can provide a helpful guide in assessing the possible pricing impact of an acquisition. The Commission notes that the merger simulation is only one element of its analysis of the competition implications of the proposed acquisition. The merger simulation takes no account of qualitative factors that will typically be relevant, such as countervailing power of acquirers. The Commission has considered these issues separately as part of this decision.

⁵⁸ Specifically, the price for each type of log delivered to the mill, and averaged over the last 4 quarters was used. For pulplogs, the price used is \$44 per m³; for unpruned sawlogs, the price is \$72 per m³ (an average of industrial and structural grades); and for pruned sawlogs, the price used is \$122 per m³.

⁵⁹ Specifically, the “Others” share is divided by 10.

230. The modelling undertaken indicates that the upper bound of any price increase resulting from the proposed acquisition is likely to be less than approximately 3% in the Northland unpruned sawlog markets.

Conclusion on Merger Simulation

231. The Commission considers that the result of the merger simulation is consistent with the Commission's view regarding existing competition, that is, the combined entity would continue to face some degree of constraint from large forestry operators, such as Matariki and Crown Forestry, as well as small woodlots in the factual scenario.

Conclusion on Existing Competition

232. The Commission considers that existing competitors, such as Matariki and Crown Forestry, and small woodlots, would likely provide a degree of constraint on the combined entity in the factual scenario for the 2006-2008 and 2014-2018 time periods.
233. The Commission considers that this degree of constraint is likely to be diminished by an unpruned sawlog supply deficit in the 2009-2013 time period.
234. The Commission considers that, based on current unpruned sawlog export levels, it is unlikely that existing competitors would expand through diversion from export in the factual scenario.
235. The Commission considers that the result of the merger simulation is consistent with the Commission's view regarding existing competition, that is, the combined entity would continue to face some degree of constraint from large forestry operators, such as Matariki and Crown Forestry, as well as small woodlots in the factual scenario.
236. Accordingly, the Commission concludes that post-acquisition, the combined entity would be likely to face some degree of constraint from existing competition in the market for the production and supply of unpruned sawlogs in the Northland region for the 2006-2008 and 2014-2018 time periods.

Countervailing Power

237. TDC and CHH are the largest purchasers of unpruned sawlogs, and account for [] % of the demand for unpruned sawlogs in the Northland region.
238. TDC advised the Commission that it purchases unpruned sawlogs from [] different suppliers, although this does not include [] and it only sources a limited volume of unpruned sawlogs from [].
239. TDC uses its suite of suppliers to mitigate risks associated with price and supply. For example, five years ago TDC sourced [] % of its unpruned sawlogs from [], but following an attempt by the supplier to increase prices by \$10/m³, TDC reduced this volume to [] %. In addition, TDC said that it has the flexibility to adjust its processing to accommodate the availability of unpruned sawlogs.
240. []
241. []

].

242. Smaller sawmills spoken to by the Commission also advised that they also use a suite of suppliers in order to strengthen their bargaining power when negotiating prices with suppliers. [] advised the Commission that it sources [] % of its unpruned sawlogs from CHH, and the remaining [] % is sourced from a range of smaller forestry operators, including [] and small woodlots.
243. [] said that it can easily adjust volumes amongst its suppliers, and in the event that the combined entity raised its prices, it could source additional volumes from smaller suppliers.
244. All sawmills spoken to by the Commission expressed concerns regarding their ability to source sufficient volumes of unpruned sawlogs, given an expected increase in processing capacity, and therefore demand, during the 2009-2013 time period.
245. [] advised that it is concerned that its ability to negotiate prices may be diminished by an inability to source additional volumes from smaller suppliers. [] expects that the supply of unpruned sawlogs from smaller suppliers will be absorbed by larger sawmills, such as CHH and TDC.

Conclusion on Countervailing Power

246. The Commission considers that acquirers of unpruned sawlogs would likely act as a constraint on the combined entity in the factual scenario, during the 2006-2008 and 2014-2018 time periods due to the excess supply of unpruned sawlogs in the Northland region.
247. The Commission considers that a supply deficit is likely to be detrimental to acquirers' ability to constrain the combined entity during the 2009-2013 time period.
248. Accordingly, the Commission concludes that post-acquisition, the combined entity would be likely to be constrained by acquirers of unpruned sawlogs in the market for the production and supply of unpruned sawlogs in Northland for the 2006-2008 and 2014-2018 time periods.

Unilateral Market Power

249. Once existing and potential competition and other competition factors have all been considered, the Commission is in a position to draw a conclusion as to whether the proposed acquisition would result in circumstances where there would be a substantial lessening of competition in the relevant market or markets, or, equivalently, whether circumstances would be such as to lead to the 'creation, enhancement or facilitation of the exercise of market power' in those markets. It is the creation of the potential for a business to exercise market power that is the focus of the analysis, rather than whether or not the market power would actually be exercised should it be obtained.
250. The Commission considers that the ability for CRBF to raise the price of unpruned sawlogs sourced from its own Northland forests is present in both the factual and the counterfactual, and it is therefore not necessary to explore this scenario further.
251. The Commission will explore the combined entity's scope to exercise unilateral market power in terms of its ability to raise the price of unpruned sawlogs

harvested from the CHH forestry estate to supra-competitive levels in the factual scenario.

252. In Decision 588, the Commission considered that the most likely method in which the combined entity would exercise unilateral market power would be by holding back harvest in order to shorten supply and increase log prices in the CNI region. The Commission considered that it would not be rational for the combined entity to hold back harvest in the CHH forests [] because of the limited harvest window for radiata, reduced return on investment and the logistical difficulties of harvesting older trees.
253. []
-].
254. As discussed in its assessment of existing competition in the Northland unpruned sawlog markets, the Commission considers that there is likely to be a supply deficit, and therefore a price increase during the 2009-2013⁶⁰ time period. The Commission notes that because of a predicted harvest increase, there is a significant surplus of unpruned sawlogs in the Northland region during the 2014-2018 time period.
255. To this end, the Commission considers that its previous assessment of the ability to defer harvest in the CHH forests remains valid for the purposes of the current acquisition.
256. In either case, the combined entity must continue harvesting the CHH forests []
⁶¹.
257. Furthermore, the Commission notes that the volume of unpruned sawlogs sold on the spot market during the 2009-2013 time period is negligible: [] % of the unpruned sawlogs harvested are non-contestable []; and another [] % of the harvest is destined for export⁶². For these reasons, the combined entity's residual supply market share is only [] % greater in the factual than the counterfactual.
258. To this end, the Commission considers that it is unlikely that the combined entity will have an enhanced scope for unilateral market power in the factual scenario in the Northland unpruned sawlog market during the 2009-2013 time period.

Conclusion on Unilateral Market Power

259. The Commission considers that the combined entity must continue harvesting unpruned sawlogs during the 2009-2013 time period

⁶⁰ It is likely that there will be a price increase for unpruned sawlogs in both the factual and the counterfactual, as the supply deficit is essentially a result of increased processing capacity in the Northland region during the 2009-2013 time period.

⁶¹ []

⁶² As the Commission has previously ascertained, it is possible that the combined entity may be able to divert unpruned sawlogs from export. This would result in the combined entity raising its total market share for residual supply by [] %.

- [] in the factual scenario.
260. In addition, the Commission considers that the combined entity is unlikely to reduce the volume of unpruned sawlogs sold on the spot market, by holding back harvest,
[]].
261. Furthermore, the Commission considers that the combined entity is incentivised to continue harvesting and competing to dispose of its unpruned sawlogs in the factual scenario during the 2009-2013 time period, due to the overall surplus supply of unpruned sawlogs anticipated for the 2014-2018 time period in the Northland region.
262. Accordingly, the Commission concludes that the scope for unilateral market power is unlikely to be enhanced by the proposed acquisition in the market for the production and supply of unpruned sawlogs in the Northland region for the 2009-2013 time period.

Coordinated Market Power

263. The Commission is of the view that where an acquisition materially enhances the prospects for any form of coordination between businesses in the market, the result is likely to be a substantial lessening of competition.
264. In broad terms, effective co-ordination can be thought of as requiring three ingredients: collusion, the ability to detect any deviation from the coordinated behaviour, and the ability to retaliate and punish the deviating firm.
265. There are a number of factors that may indicate that collusion is possible. Unpruned sawlogs are generally undifferentiated, production technology is static, new entry is extremely slow, and competitors may be constrained in their attempts to respond to any coordinated attempt to raise prices, due to the difficulties in accelerating the rate at which forests are harvested⁶³.
266. Post-acquisition, there are few large suppliers of unpruned sawlogs in the Northland region – the combined entity, Matariki and Crown Forestry.
267. Matariki and Crown Forestry are the combined entity's greatest competitors in the 2009-2013 time period. Both Matariki and Crown Forestry have []⁶⁴. The Commission considers that because of [], Matariki and Crown Forestry are incentivised to continue harvesting and competing against the combined entity to dispose of their unpruned sawlogs in the factual scenario.
268. Fringe competitors, in the form of small woodlots, collectively account for almost [] of residual wood flow during the 2009-2013 time period. Several industry participants, such as [] advised the Commission that small woodlots tend to harvest in order to take advantage of higher log prices. As such, the Commission considers that it is likely that small woodlots would also be

⁶³ The Commission discussed this in detail in Decision 588. Difficulties include the requirement for sophisticated infrastructure, as well as limitations associated with harvesting younger trees.

⁶⁴

[]].

incentivised to harvest and compete against the combined entity to dispose of their unpruned sawlogs during the 2009-2013 time period.

269. Furthermore, the large number of fringe competitors⁶⁵ acts as an additional constraint on the ability of players to co-ordinate their behaviour during the 2009-2013 time period.

Conclusion on Coordinated Market Power

270. The Commission considers that Matariki and Crown Forestry are incentivised to continue harvesting and competing to dispose of unpruned sawlogs in the factual scenario during the 2009-2013 time period, because of their []. Furthermore, small woodlots, which tend to increase harvest to take advantage of higher log prices, would also be incentivised to harvest and compete against the combined entity.
271. Furthermore, the Commission considers that the large number of fringe competitors also limits the scope for coordinated behaviour in the factual scenario during the 2009-2013 time period.
272. Accordingly, the Commission concludes that the scope for coordinated behaviour is unlikely to be enhanced by the proposed acquisition in the market for the production and supply of unpruned sawlogs in the Northland region for the 2009-2013 time period.

Conclusion on Unpruned Sawlog Markets

273. The Commission considers that in the factual scenario, the combined entity will continue to face some degree of constraint from existing competitors in the 2006-2008 and 2014-2018 time periods. This degree of constraint is likely to be diminished, due to a supply deficit, during the 2009-2013 time period.
274. Based on current unpruned sawlog export levels, the Commission considers that it is unlikely that existing competitors would expand through diversion from export in the factual scenario.
275. The Commission considers that the result of the merger simulation is consistent with the Commission's view regarding existing competition, that is, the combined entity would continue to face some degree of constraint from large forestry operators, such as Matariki and Crown Forestry, as well as small woodlots in the factual scenario.
276. The Commission considers that acquirers of unpruned sawlogs are also likely to constrain the combined entity, to some degree, in the 2006-2008 and 2014-2018 time periods, when there is a surplus supply of unpruned sawlogs. The Commission considers that this degree of constraint is likely to be diminished due to a supply deficit during the 2009-2013 time period.
277. The Commission considers that the combined entity is unlikely to have enhanced scope to exercise unilateral market power during the 2009-2013 time period because:
- the combined entity must continue harvesting unpruned sawlogs [];

⁶⁵ Including harvest managers PF Olsen and NFML, as well as small, independently owned and harvested woodlots.

- the combined entity is unlikely to reduce the volume of unpruned sawlogs sold on the spot market, by holding back harvest, []; and
- the combined entity is incentivised to continue harvesting and competing to dispose of its unpruned sawlogs during the 2009-2013 time period due to the significant surplus supply of unpruned sawlogs anticipated for the Northland region in the subsequent 2014-2018 time period.

278. The Commission considers that the scope for coordinated market power is unlikely to be enhanced during the 2009-2013 time period as Matariki and Crown Forestry are incentivised to continue harvesting and competing to dispose of unpruned sawlogs in the factual scenario during the 2009-2013 time period, because of their [].

Furthermore, small woodlots, which tend to increase harvest to take advantage of higher log prices, would also be incentivised to harvest and compete against the combined entity. The Commission also considers that the large number of fringe competitors also limits the scope for coordinated behaviour in the factual scenario during the 2009-2013 time period.

279. Accordingly, the Commission concludes that the proposed acquisition would not have, or would not be likely to have, the effect of substantially lessening competition in the market for the production and supply of unpruned sawlogs in Northland the 2006-2008, 2009-2013 and 2014-2018 time periods.

Pruned Sawlog Markets

Existing Competition

280. The Applicant submitted that the combined entity would continue to face constraint from existing competitors in the Northland and Auckland pruned sawlog markets in the factual scenario. In addition, the combined entity would be constrained by diversion from export of pruned sawlogs.

281. The Commission has gathered information from the Applicant and other relevant parties, and has used this to estimate market shares for the pruned log markets, as set out in Table 8. The Applicants market shares are displayed as CRBF. CRBF's figures include wood flows from GFP's existing Northland forestry estates.

Table 8: Future Wood Flows for Pruned Sawlogs in the Northland Region

Forest Owner/Manager	Wood flow: Average volume per year					
	2006-2008		2009-2013		2014-2018	
	(000 m ³)	%	(000 m ³)	%	(000 m ³)	%
CRBF	[]	[]%	[]	[]%	[]	[]%
CHH	[]	[]%	[]	[]%	[]	[]%
<i>Combined Entity</i>	[]	[]%	[]	[]%	[]	[]%
Matariki	[]	[]%	[]	[]%	[]	[]%
PF Olsen	[]	[]%	[]	[]%	[]	[]%
Crown Forestry	[]	[]%	[]	[]%	[]	[]%
NFML	[]	[]%	[]	[]%	[]	[]%
Other	[]	[]%	[]	[]%	[]	[]%
Total Northland supply	[]	100%	[]	100%	[]	100%

Source: Industry participants

282. The market shares in Table 8 relate to the production and supply of pruned sawlogs in the Northland region. The Commission considers that the market for the production and supply of pruned sawlogs in the Northland and Auckland region extends further south than the pulplog and unpruned sawlog markets; however, the harvest volumes from these southern forests⁶⁶ are not expected to be significant⁶⁷ and subsequently have not been included in Table 8.
283. The combined entity has the largest volume of wood flow in Northland in the 2006-2008 and 2014-2018 time periods. [] has the largest harvest volume in Northland in the 2009-2013 time period.
284. Small woodlots account for a significant share of the Northland and Auckland pruned sawlog markets. As discussed in the context of the pulplog and unpruned sawlog markets, the Commission considers that the ability for small woodlots to exert constraint upon the combined entity is unlikely to be diminished by variability in supply⁶⁸.
285. In Decision 588, the Commission considered that the ability for small woodlots to exert constraint upon the combined entity was likely to be diminished in the pruned sawlog markets because of inconsistency in log quality. None of the Northland and Auckland pruned sawlogs processors spoken to by the Commission indicated that they had concerns with the quality of small woodlot pruned sawlogs. For this reason, in the context of the Northland and Auckland pruned sawlog markets, the Commission considers that the ability for small woodlots to exert constraint upon the combined entity is unlikely to be diminished by log quality.
286. The market shares for residual wood flows for the pruned markets are set out in Table 9 (Appendix 1).
287. Table 9 indicates that in the 2006-2008 time period, presently CRBF has a market share of [] % with a three-firm concentration ratio of [] %. Post-acquisition, the combined entity would have a market share of [] % and the three-firm concentration would be [] %. This falls within the Commission's safe harbour guidelines.
288. In the 2009-2013 time period, presently CRBF has a market share of [] % with a three-firm concentration ratio of [] %. Post-acquisition, the combined entity would have a market share of [] % and the three-firm concentration ratio would be [] %. This is inside the Commission's safe harbour guidelines.
289. In the 2014-2018 time period, presently CRBF has a market share of [] % with a three-firm concentration ratio of [] %. Post-acquisition, the combined entity would have a market share of [] % and the three-firm concentration would be [] %. This falls within the Commission's safe harbour guidelines.
290. [] is the combined entity's greatest competitor in the 2006-2008 time period.

⁶⁶ Crown Forestry's Waiuku forest is projected to produce [] m³ of pruned sawlogs per year, Matariki's Whitford and Onewhero forests are projected to produce approximately [] m³ of pruned sawlogs per year.

⁶⁷ The Auckland forests have the potential to add an additional [] m³ of pruned sawlogs per year, which equates to approximately [] % of the total pruned sawlog supply for the Northland and Auckland region.

⁶⁸ Although the fragmented nature of small woodlots remains a consideration.

291. [] has the greatest market share in the pruned sawlog market during the 2009-2013 time period. [] are also significant competitors during this time period.
292. [] market shares [] in the 2014-2018 time period []. The combined entity's greatest competitor is [], whose market share is []. All other competitors [].
293. As with the pulplog and unpruned sawlog markets, the Commission considers that for the purpose of assessing the competition implications of the proposed acquisition, a diligent assessment of the pruned sawlog markets should consider demand requirements.
294. Table 10 shows the residual demand volumes of pruned sawlogs in Northland and Auckland across all time periods.
295. Few sawmills that process pruned sawlogs in the Northland and Auckland region have long-term contracts for pruned sawlogs⁶⁹.

⁶⁹ Generally, sawmills that have long-term contracts tend to process significant volumes of pruned sawlogs. Smaller sawmills advised the Commission that price and volume negotiations tend to be based on long-term relationships with the forest operators.

Table 10: Residual Demand for Pruned Sawlogs in the Northland and Auckland Region

Sawmill	Woodflow: Average volume per year					
	2006-2008		2009-2013		2014-2018	
	(000 m ³)	%	(000 m ³)	%	(000 m ³)	%
Rosvall	[]		[]		[]	
Less contracted supply	[]		[]		[]	
Rosvall Residual Demand	[]	[]%	[]	[]%	[]	[]%
TDC	[]		[]		[]	
Less contracted supply Matariki	[]		[]		[]	
TDC Residual Demand	[]	[]%	[]	[]%	[]	[]%
Thames Timber	[]		[]		[]	
Less contracted supply []	[]		[]		[]	
Matariki	[]		[]		[]	
Thames Timber Residual Demand	[]	[]%	[]	[]%	[]	[]%
Other Residual Demand	[]	[]%	[]	[]%	[]	[]%
Total Northland and Auckland Demand	[]		[]		[]	
Total Northland and Auckland Residual Demand	[]	100%	[]	100%	[]	100%

Source: Industry participants

296. Table 10 shows that the main purchasers of pruned sawlogs in Northland and Auckland are Rosvall and TDC. Rosvall purchases all of its pruned sawlogs on the spot market, from a variety of suppliers including []. TDC also employs this strategy, sourcing its pruned sawlogs from [] different suppliers, including [].
297. Thames Timber, which is located to the south of the Northland region, sources [] % of its pruned sawlog requirements from forests located within the Northland region.
298. Table 11 shows the relationship between residual demand and supply for the Northland and Auckland pruned sawlog markets.

Table 11: Future Residual Supply and Demand for Pruned Sawlogs in Northland and Auckland

	Wood flow: Average volume per year					
	2006-2008		2009-2013		2014-2018	
Residual Supply						
Forest Owner/Manager	(000 m ³)	%	(000 m ³)	%	(000 m ³)	%
Combined Entity	[]	[]%	[]	[]%	[]	[]%
Matariki	[]	[]%	[]	[]%	[]	[]%
PF Olsen	[]	[]%	[]	[]%	[]	[]%
Crown Forestry	[]	[]%	[]	[]%	[]	[]%
NFML	[]	[]%	[]	[]%	[]	[]%
Other	[]	[]%	[]	[]%	[]	[]%
Total Northland Residual Supply	[]	100%	[]	100%	[]	100%
Residual Demand						
Sawmill	(000 m ³)	%	(000 m ³)	%	(000 m ³)	%
Rosvall	[]	[]%	[]	[]%	[]	[]%
TDC	[]	[]%	[]	[]%	[]	[]%
Thames Timber	[]	[]%	[]	[]%	[]	[]%
Other	[]	[]%	[]	[]%	[]	[]%
Total Northland Residual Demand	[]	[]%	[]	100%	[]	100%
Total Northland Excess Residual Supply	[]		[]		[]	

Source: Industry participants

299. Table 11 shows that residual supply will exceed demand across all three time periods. Furthermore, as previously discussed, processors of pruned sawlogs in Northland would also be able to source volumes of pruned sawlogs from South Auckland forests⁷⁰.
300. The volume of excess supply is significantly greater than the combined entity's supply volume. The Commission considers that there is sufficient excess supply in the Northland region such that purchasers of pruned sawlogs would not be dependent on the combined entity for supply.

Expansion through Diversion from Export

301. The Applicant submitted that the combined entity would face constraint from the diversion of pruned sawlogs from export by existing competitors in the factual scenario.
302. Pruned sawlogs are used for the manufacture of appearance-grade end-products. In Decision 588, the Commission considered that high-value pruned sawlogs have the potential to fetch greater prices overseas after value-added processing. This is because in general, sawlogs have a shelf-life of approximately two days before sap-stain sets in. The long-haul shipping required to transport sawlogs to New Zealand's largest export markets in the northern hemisphere means that the pruned sawlogs are likely to become devalued during transit. For these reasons, pruned sawlogs are not commonly exported from New Zealand.
303. In addition, there is not a significant demand for valuable sawlogs overseas. Presently the largest demand is from Asia, for unpruned sawlogs.

⁷⁰ The South Auckland forests have the potential to meet [] % of the demand requirement for pruned sawlogs in the Northland and Auckland region.

304. In the context of the Northland pruned sawlog markets, the Commission is aware that small volumes of pruned sawlogs are exported infrequently. However, for the purposes of assessing the competition implications of the proposed acquisition, the Commission considers that the volume of pruned sawlogs exported are not significant in comparison to the total volume of pruned sawlog production and supply in the Northland and Auckland region.

Conclusion on Expansion through Diversion from Export

305. The Commission considers that, based on current pruned sawlog export levels, it is unlikely that existing competitors would expand through diversion from export in the factual scenario.

Merger Simulation

306. In order to run the simulation, the Commission used the residual supply market shares for each of the time periods under consideration. Utilisation of the residual supply market shares is considered appropriate as the residual supply market shares eliminate minimum volumes contained in long-term supply contracts, which are unlikely to be impacted upon in the event that the combined entity was able to exercise market power. The Commission used log prices provided by MAF⁷¹.
307. To consider the effects of the proposed merger, the Commission has modeled two scenarios for each market. The first scenario considers the price effect where supply from small woodlots (which accounts for [] % - [] % of residual supply) is aggregated and treated as a single entity. The second scenario disaggregates this share to reflect the more fragmented nature of this source of supply.⁷²
308. The results of the simulation conducted by the Commission in respect of the unpruned sawlog markets indicates that the proposed acquisition could lead to an increase in pruned log prices of 1.0% p.a. over 2006-2008 (0.4% if “Others” is disaggregated); 0.9% p.a. over 2009-2013 (0.4%); and 1.4% p.a. over 2014-2018 (0.6%).
309. Merger simulation can provide a helpful guide in assessing the possible pricing impact of an acquisition. The Commission notes that the merger simulation is only one element of its analysis of the competition implications of the proposed acquisition. The merger simulation takes no account of qualitative factors that will typically be relevant, such as countervailing power of acquirers. The Commission has considered these issues separately as part of this decision.
310. The modelling undertaken indicates that the upper bound of any price increase resulting from the proposed acquisition is likely to be less than approximately 1% in the Northland pruned sawlog markets.

Conclusion on Merger Simulation

311. The Commission considers that the result of the merger simulation is consistent with the Commission’s view regarding existing competition, that is, the combined entity would continue to face some degree of constraint from large

⁷¹ Specifically, the price for each type of log delivered to the mill, and averaged over the last 4 quarters was used. For pulplogs, the price used is \$44 per m³; for unpruned sawlogs, the price is \$72 per m³ (an average of industrial and structural grades); and for pruned sawlogs, the price used is \$122 per m³.

⁷² Specifically, the “Others” share is divided by 10.

forestry operators, such as Matariki and Crown Forestry, as well as small woodlots in the factual scenario.

Conclusion on Existing Competition

312. The Commission considers that existing competition, such as Matariki, Crown Forestry, and small woodlots, would likely provide a degree of constraint on the combined entity in the factual scenario.
313. The Commission considers that, based on current export volumes, it is unlikely that either large forestry operators, or small woodlots, would expand through diversion from export in the factual scenario.
314. The Commission considers that the result of the merger simulation is consistent with the Commission's view regarding existing competition, that is, the combined entity would continue to face some degree of constraint from large forestry operators, Matariki and Crown Forestry, as well as small woodlots in the factual scenario.
315. Accordingly, the Commission concludes that post-acquisition, the combined entity would be likely to face some degree of constraint from existing competition in the market for the production and supply of pruned sawlogs in the Northland region for the 2006-2008, 2009-2013 and 2014-2018 time periods.

Countervailing Power

316. The main purchasers of pruned sawlogs in Northland are Rosvall, TDC and Thames Timber, which combined purchase approximately [] % of the residual supply of pruned sawlogs in Northland.
317. All sawmills spoken to by the Commission advised that there is a surplus of pruned sawlogs in the Northland region, which is expected to increase as harvest levels increase over the next ten years. The Commission notes that the surplus⁷³ is such that acquirers of pruned sawlogs are not reliant upon the combined entity for supply in any of the time periods.
318. Presently, TDC acquires [] % of its pruned sawlogs from CHH. TDC advised the Commission that it has the flexibility to adjust its processing volumes to accommodate unfavourable market conditions. TDC advised the Commission that it is not concerned about the proposed acquisition because in [].
319. Thames Timber's location, on the boundary between the CNI and Northland regions, means that it can readily source pruned sawlogs from either region. Presently, it sources [] % of its pruned sawlog requirements from the Northland region: [] from the CHH's Woodhill forest; [] from Matariki's Mahurangi and Topuni forests; and the remaining [] is sourced from small woodlots.
320. Both TDC and Thames Timber have long-term supply contracts. Under these contracts, prices are negotiated monthly, using a formula that references US/NZ exchange rate, end-product price, and quality of the pruned sawlog.
321. Although Rosvall sources all of its pruned sawlogs on the spot market, it also uses a suite of suppliers between which it compares prices during negotiation time.

⁷³ As described by Table 10.

322. [] advised the Commission it is in a good bargaining position when negotiating price and supply with forest owners because there is a surplus of pruned sawlogs and few large processors of pruned sawlogs in the Northland and Auckland region.

Conclusion on Countervailing Power

323. The Commission considers that acquirers of pruned sawlogs, such as Rosvall and TDC, would likely constrain the combined entity in the factual scenario, because of the excess supply and the limited number of outlets for pruned sawlogs in the Northland region.
324. Accordingly, the Commission concludes that post-acquisition, the combined entity would likely be constrained by acquirers of pruned sawlogs in the market for the production and supply of pruned sawlogs in Northland for the 2006-2008, 2009-2013 and 2014-2018 time periods.

Conclusion on Pruned Sawlog Markets

325. The Commission considers that large forestry operators, such as Matariki and Crown Forestry, as well as small woodlots, would likely provide a degree of constraint on the combined entity in the factual scenario.
326. The Commission considers that, based on current export volumes, it is unlikely that existing competitors would expand through diversion from export in the factual scenario.
327. The Commission considers that the result of the merger simulation is consistent with the Commission's view regarding existing competition, that is, the combined entity would continue to face some degree of constraint from large forestry operators, Matariki and Crown Forestry, as well as small woodlots in the factual scenario.
328. The Commission considers that acquirers of pruned sawlogs, such as Rosvall and TDC, would likely constrain the combined entity in the factual scenario, because of the excess supply and the limited number of outlets for pruned sawlogs in the Northland and Auckland region.
329. Accordingly, the Commission concludes that the proposed acquisition would not have, or would not be likely to have, the effect of substantially lessening competition in the market for the production and supply of pruned sawlogs in Northland and Auckland for the 2006-2008, 2009-2013 and 2014-2018 time periods.

CONCLUSION

330. The Commission has considered the probable nature and extent of competition that would exist, subsequent to the proposed acquisition, in:
- the production and supply of pulplogs in Northland, for the periods 2006–2008, 2009–2013, and 2014–2018;
 - the production and supply of unpruned sawlogs in Northland, for the periods 2006–2008, 2009–2013, and 2014–2018;
 - the production and supply of pruned sawlogs in Northland and Auckland, for the periods 2006–2008, 2009–2013, and 2014–2018;

- the production and supply of pulplogs in Nelson/Marlborough, for the periods 2006–2008, 2009–2013, and 2014–2018;
 - the production and supply of unpruned sawlogs in Nelson/Marlborough, for the periods 2006–2008, 2009–2013, and 2014–2018; and
 - the production and supply of pruned sawlogs in Nelson/Marlborough, for the periods 2006–2008, 2009–2013, and 2014–2018.
331. The Commission considers that the counterfactual is that CHH will be acquired by a third party that does not presently have a major interest in New Zealand forestry
332. In respect of the Northland region, the Commission considers that the combined entity will continue to face a degree of constraint from existing competitors in the pulplog markets and the pruned sawlog markets. Whilst the Commission is of the view that this is also the case for the unpruned sawlog markets during the 2006-2008 and 2014-2018 time periods, the Commission considers that a supply deficit is likely to diminish this constraint during the 2009-2013 time period.
333. Based on current export volumes, the Commission considers that it is unlikely that existing competitors will expand through diversion from export in any of the relevant Northland markets.
334. In the Northland pulplog and pruned sawlog markets, the Commission considers that acquirers of pulplogs and pruned sawlogs are also likely to act as a constraint upon the combined entity in the factual scenario, because of the excess supply of logs and the limited number of outlets for these logs.
335. Regarding the Northland unpruned sawlog market, the Commission considers that acquirers of unpruned sawlogs are likely to act as a constraint, to some extent, during the 2006-2008 and 2013-2018 time periods, due to the excess supply of unpruned sawlogs. However, the Commission considers that the supply deficit is likely to diminish this constraint during the 2009-2013 time period.
336. The Commission considers that the combined entity is unlikely to have an enhanced scope to exercise unilateral market power in the Northland unpruned sawlog market during the 2009-2013 time period, because:
- the combined entity must continue harvesting unpruned sawlogs
[
];
 - the combined entity is unlikely to reduce the volume of unpruned sawlogs sold on the spot market, by holding back harvest,
[
]; and
 - the combined entity is incentivised to continue harvesting and competing to dispose of its unpruned sawlogs during the 2009-2013 time period, due to the significant surplus supply of unpruned sawlogs anticipated for the subsequent 2014-2018 time period in the Northland region.
337. The Commission considers that the scope for coordinated market power is unlikely to be enhanced in the Northland unpruned sawlog market during the 2009-2013 time period, as Matariki and Crown Forestry are incentivised to

continue harvesting and competing to dispose of unpruned sawlogs because []. Furthermore, small woodlots, which tend to increase harvest to take advantage of higher log prices, would also be incentivised to harvest and compete against the combined entity in the factual scenario.

338. The Commission also considers that the large number of fringe competitors also limits the scope for coordinated behaviour in the factual scenario in the Northland unpruned sawlog market during the 2009-2013 time period.
339. Turning to the Nelson/Marlborough region, the Commission considers that the termination of the Nelson JV creates the potential for two potential scenarios to arise in the counterfactual, and three potential scenarios to arise in the factual, in terms of GFP's forestry holdings.
340. The Commission considers that each of the two counterfactual scenarios is equally likely to occur. The Commission adopts the second scenario as the counterfactual scenario, as it considers that if no competition concerns arise from adopting the second scenario as the counterfactual scenario (in which the Applicant would have the smallest market share), it is unlikely that competition concerns will arise from adopting the first scenario as the counterfactual scenario.
341. Likewise, the Commission considers that each of the three factual scenarios is equally likely to occur. The Commission adopts the third scenario as the factual scenario, as it considers that if no competition concerns arise from adopting the third scenario as the factual scenario (in which the Applicant would have the greatest market share), it is unlikely that competition concerns will arise from adopting the first or second scenarios as the factual scenario.
342. In order to alleviate any competition concerns relating to the Nelson/Marlborough log markets, CRBF has given an undertaking to the Commission, such that [], GFP will retain its interest in the Nelson JV and divest the CHH forestry assets to a third party [].
343. The Commission considers that GFP would be able to find an independent buyer, and therefore successfully divest itself of the CHH forestry estate. The divestment would preserve the CHH forestry estate as a competitor to GFP in the Nelson/Marlborough log markets, and as such, it would not result in any material difference between the factual and the counterfactual.
344. The Commission is therefore satisfied that the proposed acquisition would not have, or would not be likely to have, the effect of substantially lessening competition in any market.

DETERMINATION ON NOTICE OF CLEARANCE

345. Pursuant to section 66(3) (a) of the Commerce Act 1986, the Commission determines to give clearance for the proposed acquisition by CRBF Limited of shares and assets owned by Carter Holt Harvey Limited, relating to forestry estates located in Northland, Auckland, the CNI and Nelson.

Dated this 5th day of October 2006



Paula Rebstock

Chair

Commerce Commission

APPENDIX 1

Table 3: Future Residual Wood Flows for Pulplogs in Northland

Forest Owner/Manager		Wood flow: Average volume per year					
		2006-2008		2009-2013		2014-2018	
		(000 m ³)	%	(000 m ³)	%	(000 m ³)	%
CRBF		[]		[]		[]	
	Less contracted supply	[]		[]		[]	
	Less exports	[]		[]		[]	
	CRBF Residual Supply	[]	[]%	[]	[]%	[]	[]%
CHH		[]		[]		[]	
	Less contracted supply Marusumi	[]		[]		[]	
	Less exports	[]		[]		[]	
	CHH Residual Supply	[]	[]%	[]	[]%	[]	[]%
<i>Combined Entity</i>		[]		[]		[]	
	<i>Less contracted supply Marusumi</i>	[]		[]		[]	
	<i>Less exports</i>	[]		[]		[]	
	Combined Entity Residual Supply	[]	[]%	[]	[]%	[]	[]%
Matariki		[]		[]		[]	
	Less contracted supply TDC	[]		[]		[]	
	Less exports	[]		[]		[]	
	Matariki Residual Supply	[]	[]%	[]	[]%	[]	[]%
PF Olsen		[]		[]		[]	
	Less contracted supply	[]		[]		[]	
	Less exports	[]		[]		[]	
	PF Olsen Residual Supply	[]	[]%	[]	[]%	[]	[]%
Crown Forestry		[]		[]		[]	
	Less contracted supply	[]		[]		[]	
	Less exports	[]		[]		[]	
	Crown Forestry Residual Supply	[]	[]%	[]	[]%	[]	[]%
NFML		[]		[]		[]	
	Less contracted supply	[]		[]		[]	
	Less exports	[]		[]		[]	
	NFML Residual Supply	[]	[]%	[]	[]%	[]	[]%
	Other Residual Supply	[]	[]%	[]	[]%	[]	[]%
Total Northland Supply		[]		[]		[]	
Total Northland Residual Supply		[]	100%	[]	100%	[]	100%

Source: Industry participants

Table 5: Future Residual Wood Flows for Unpruned Sawlogs in Northland

Forest Owner/Manager	Wood flow: Average volumes per year					
	2006-2008		2009-2013		2014-2018	
	(000 m ³)	%	(000 m ³)	%	(000 m ³)	%
CRBF	[]		[]		[]	
Less contracted supply	[]		[]		[]	
Less exports	[]		[]		[]	
CRBF Residual Supply	[]	[]%	[]	[]%	[]	[]%
CHH	[]		[]		[]	
Less internal demand []	[]		[]		[]	
[]	[]		[]		[]	
Less contracted supply []	[]		[]		[]	
Less exports	[]		[]		[]	
CHH Residual Supply	[]	[]%	[]	[]%	[]	[]%
<i>Combined Entity</i>	[]		[]		[]	
<i>Less contracted supply []</i>	[]		[]		[]	
[]	[]		[]		[]	
[]	[]		[]		[]	
<i>Less exports</i>	[]		[]		[]	
Combined Entity Residual Supply	[]	[]%	[]	[]%	[]	[]%
Matariki	[]		[]		[]	
Less contracted supply TDC	[]		[]		[]	
Less exports	[]		[]		[]	
Matariki Residual Supply	[]	[]%	[]	[]%	[]	[]%
PF Olsen	[]		[]		[]	
Less contracted supply	[]		[]		[]	
Less exports	[]		[]		[]	
PF Olsen Residual Supply	[]	[]%	[]	[]%	[]	[]%
Crown Forestry	[]		[]		[]	
Less contracted supply	[]		[]		[]	
Less exports	[]		[]		[]	
Crown Forestry Residual Supply	[]	[]%	[]	[]%	[]	[]%
NFML	[]		[]		[]	
Less contracted supply	[]		[]		[]	
Less exports	[]		[]		[]	
NFM Residual Supply	[]	[]%	[]	[]%	[]	[]%
Other Residual Supply	[]	[]%	[]	[]%	[]	[]%
Total Northland supply	[]		[]		[]	
Total Northland Residual Supply	[]	100%	[]	100%	[]	100%

Source: Industry participants

Table 9: Future Residual Wood Flows for Pruned Sawlogs in Northland

Forest Owner/Manager	Wood flow: Average volume per year					
	2006-2008		2009-2013		2014-2018	
	(000 m ³)	%	(000 m ³)	%	(000 m ³)	%
CRBF	[]		[]		[]	
Less contracted supply	[]		[]		[]	
Less exports	[]		[]		[]	
CRBF Residual Supply	[]	[]%	[]	[]%	[]	[]%
CHH	[]		[]		[]	
Less contracted supply Thames Timber	[]		[]		[]	
Less exports	[]		[]		[]	
CHH Residual Supply	[]	[]%	[]	[]%	[]	[]%
<i>Combined Entity</i>	[]		[]		[]	
<i>Less contracted supply Thames Timber</i>	[]		[]		[]	
<i>Less exports</i>	[]		[]		[]	
Combined Entity Residual Supply	[]	[]%	[]	[]%	[]	[]%
Matariki	[]		[]		[]	
Less contracted supply TDC	[]		[]		[]	
Thames Timber	[]		[]		[]	
Less exports	[]		[]		[]	
Matariki Residual Supply	[]	[]%	[]	[]%	[]	[]%
PF Olsen	[]		[]		[]	
Less contracted supply	[]		[]		[]	
Less exports	[]		[]		[]	
PF Olsen Residual Supply	[]	[]%	[]	[]%	[]	[]%
Crown Forestry	[]		[]		[]	
Less contracted supply	[]		[]		[]	
Less exports	[]		[]		[]	
Crown Forestry Residual Supply	[]	[]%	[]	[]%	[]	[]%
NFML	[]		[]		[]	
Less contracted supply	[]		[]		[]	
Less exports	[]		[]		[]	
NFML Residual Supply	[]	[]%	[]	[]%	[]	[]%
Other Residual Supply	[]	[]%	[]	[]%	[]	[]%
Total Northland Supply	[]		[]		[]	
Total Northland Residual Supply	[]	100%	[]	100%	[]	100%

Source: Industry participants

APPENDIX 2

DIVESTMENT UNDERTAKING PURSUANT TO SECTION 69A OF THE COMMERCE ACT 1986

1. This divestment undertaking ("**Undertaking**") is made pursuant to section 69A of the Commerce Act ("**Act**"). The Undertaking is made in support and forms part of the notice by CRBF Limited ("**CRBF**") dated 29 August 2006 seeking clearance under section 66(1) of the Act, and in replacement of any and all previous undertakings provided.
2. CRBF is a newly created closed-end timber investment fund managed by the US timber investment organisation, Global Forest Partners LP ("**GFP**"), that is seeking to purchase certain forest properties currently being offered for sale by Carter Holt Harvey Limited ("**CHH**") in the Nelson, Central North Island and Northland regions of New Zealand
3. [RIL New Zealand Forests I, Inc., _____ international business company ("**NZ1**") is a closed-end timber investment fund entirely unrelated to CRBF except that NZ1 is managed by GFP.] NZ1 holds an undivided 49% interest in the forests and sawmill business known as the Nelson Joint Venture ("**Nelson JV**") located in the Nelson and Marlborough regions of the South Island and comprising a total of [63,873] stocked ha. Nelson Forest Products Limited ("**NFP**"), a subsidiary of Weyerhaeuser Company, owns the remaining 51% undivided interest, with Weyerhaeuser New Zealand Inc ("**WNZI**"), another subsidiary of Weyerhaeuser Company, acting as the operating manager. Neither NFP, WNZI nor any other Weyerhaeuser entity has any economic or other business relationship with NZ1.
- 4.
5. CRBF undertakes to the Commerce Commission that _____ CRBF will, if it is the successful purchaser in terms of paragraph 2 above, within _____ of completion of

the acquisition for which clearance is sought unreservedly divest the forest it acquires from CHH in the Nelson/Motueka area comprising the following four blocks: Waimea (5,868 ha), Hira (3,663 ha), Moutere (10,692 ha) and Baigent (6,315 ha).]

DATED this ^{3rd} day of October 2006

Signed for and on behalf of CRBF by its duly authorised attorney pursuant to a power of attorney in that regard:



Michael J Edgar
Director of Asia Pacific Investments
Global Forest Partners LP