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COMMERCE COMMISSION

Decision No. 666

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

David Ferrier and/or New Zealand Woolscourers Limited

and

Cavalier Wool Holdings Limited

and

Godfrey Hirst NZ Limited

The Commission: Paula Rebstock
Denese Bates QC
Gowan Pickering

Summary of Application: Mr David Ferrier himself, or his company New Zealand Woolscourers Limited, has applied for clearance to acquire up to 100% of the wool scouring and wool dumping assets of Godfrey Hirst NZ Limited (Godfrey Hirst); up to 100% of the shares of Cavalier Wool Holdings Limited (Cavalier Wool); and for Cavalier Wool to acquire certain assets, including a wool scour line. The Application also includes the proposed divestment of the wool dumping assets of Godfrey Hirst.

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

Date of Determination: 6 March 2009

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EXECUTIVE SUMMARY

E1. A notice pursuant to s 66(1) of the Commerce Act 1986 (the Act) was registered on 12 December 2008 The notice sought clearance for Mr David Ferrier himself, or his company New Zealand Woolscourers Limited (together the Applicant), to acquire certain assets in Godfrey Hirst NZ Ltd (Godfrey Hirst) and shares in Cavalier Wool Holdings Limited (Cavalier Wool). In addition, the Applicant undertakes to divest the wool dumping assets acquired as part of the proposed acquisition pursuant to section 69A of the Act.

E2. For the purpose of considering this Application**,** the Commission concludes that the relevant markets are those for:

- the North Island market for the supply of wool scouring services (the North Island scouring market);
- the South Island market for the supply of wool scouring services (the South Island scouring market);
- the North Island market for the supply of wool dumping services (the North Island dumping market);
- the South Island market for the supply of wool dumping services (the South Island dumping market); and
- the national market for the purchase and supply of wool grease (the national wool grease market).

E3. The Commission concludes that the likely counterfactual is that in each of the relevant markets, Godfrey Hirst would continue to operate its wool scouring plants (i.e., effectively the status quo).

E4. As part of the wider transaction, the Applicant proposes in the factual to:

- acquire two wool scouring plants (Clifton and Clive) from Godfrey Hirst;
- acquire Godfrey Hirst's four wool dumping businesses;
- acquire 50 shares in Lanolin Trading Co Limited;
- close one scour completely;
- close one of two production lines at the other plant (Clive), and sell the remaining line to Cavalier Wool;
- sell some of the fixed assets from the two ex-Godfrey Hirst plants to New Zealand Wool Services International Limited (NZWSI);
- enter into an underwriting agreement with NZWSI;
- acquire up to 100% of the shares of Cavalier Wool;
- sell the wool dumping assets it acquires from Godfrey Hirst to an independent party in terms of the divestment undertaking; and

- contract to have Godfrey Hirst’s wool scouring requirements carried out by Cavalier Wool.

E5. The Commission concludes that it is satisfied that the proposed acquisition would not have, or would not be likely to have, the effect of substantially lessening competition in the North and South Island scouring markets. The Commission considers that the following factors are likely, when taken together, to provide a sufficient constraint on the combined entity in the relevant markets in the factual:

- the constraint from NZWSI;
- the constraint from potential entry;
- the presence of excess capacity and economies of scale;
- the potential constraint from offshore scouring; and
- the countervailing power of wool merchants.

E6. The Commission further concludes that it is satisfied that the proposed acquisition would not have, or would not be likely to have, the effect of substantially lessening competition in the national grease market or, following the implementation of the divestment undertaking, the North and South Island dumping markets.

E7. The Commission determines to give clearance to the proposed acquisition.

THE PROPOSAL

1. A notice pursuant to section 66(1) of the Commerce Act 1986 (the Act) was registered on 12 December 2008. The notice (the Application) sought clearance for the acquisition by Mr David Ferrier himself, or his company New Zealand Woolscourers Limited – (together the Applicant) to acquire up to 100% of:

   (a) (i) the wool scouring and wool dumping assets of Godfrey Hirst NZ Limited (Godfrey Hirst);[1] and/or

   (ii) the shares in Cavalier Wool Holdings Limited (Cavalier Wool); and/or for

   (b) Cavalier Wool to acquire certain assets and shares, including the 2.4 metre line at Clive (near Napier) and 50 shares in Lanolin Trading Co Limited (Lanolin Trading).

2. In addition, the Applicant undertakes to divest the wool dumping assets acquired as part of the proposed acquisition pursuant to section 69A of the Act.

3. Further details on how the Applicant intends to implement the proposed acquisition are provided in the Factual/Counterfactual section of these reasons (see para 63).

PROCEDURE

4. Section 66(3) of the Act requires the Commission either to give clearance or to decline to give clearance, to the acquisition referred to in a section 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 such that a decision was required by 6 March 2009.

5. The Commission's approach to analysing the proposed acquisition is based on principles set out in the Commission's *Mergers and Acquisitions Guidelines*.[2]

STATUTORY FRAMEWORK

6. Under section 66 of the Act, the Commission is required to consider whether the proposal is, or is likely to have, the effect of substantially lessening competition in a market. If the Commission is satisfied that the proposal would not be likely 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 application. The standard of proof that the Commission must apply in making its determination is the civil standard of the balance of probabilities.[3]

7. The substantial lessening of competition test was considered in Air New Zealand & Qantas v C*ommerce 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

[1] These assets comprise the wool scouring plants located at Clive and Clifton, 50 shares in Lanolin Trading Co Ltd, stock and lanolin, and the wool dumping plants located at Clive,Clifton ,Christchurch and Dunedin.

[2] Commerce Commission, *Mergers and Acquisitions Guidelines*, January 2004.

[3] *Foodstuffs (Wellington) Cooperative Society Limited v Commerce Commission* (1992) 4 TCLR 713-721.

> 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.[4]

8. In determining whether there is a change along the spectrum which is significant, the Commission must identify a real lessening of competition that is more than nominal and not minimal.[5] 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 competition and creation, enhancement or facilitation of the exercise of market power may be taken as being equivalent.

9. 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 given case.

10. 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

11. 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).

12. 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, and may variously consider:

    - existing competition;
    - potential competition;
    - the countervailing market power of buyers; and
    - the ability of suppliers to co-ordinate their pricing in the market.

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[4] *Air New Zealand & Qantas Airways Limited v Commerce Commission* (2004) 11 TCLR 347, Para 42.
[5] *Fisher & Paykel Limited v Commerce Commission* (1990) 2 NZLR 731, 758 and also *Port Nelson Limited v Commerce Commission* (1996) 3 NZLR 554, 563.

13. When an Applicant considers that it is appropriate to undertake to make a structural divestment as part of its application for clearance, section 69A of the Act provides that the Commission may accept such undertakings in writing given by, or on behalf of, an Applicant to dispose of assets or shares. An undertaking given to the Commission is deemed to form part of any clearance given by the Commission.[6]

14. In establishing the likely factual position with the acquisition, the Commission assumes an applicant will be under an obligation to divest the assets or shares which are the subject of the undertaking, on the terms offered by the applicant. The comparison between the factual and the counterfactual will test whether the divestment would, of itself, or in combination with other market conditions, enable the Commission to be satisfied that the proposed acquisition will not have the effect, or likely effect, of substantially lessening competition.

15. Divestments are to some extent uncertain as to their eventual impact on the market. If much rests on the divestment in terms of the future levels of competition in the relevant markets, the Commission must be satisfied that the divested business and assets will be capable of constraining the combined entity in the factual. If the divested business fails or is an ineffective competitor, then a substantial lessening of competition may occur, and consumers will be harmed. Thus it is important for the Commission to consider all the relevant risks associated with a divestment proposal.

16. In order to make this assessment, the Commission will consider:

    - composition risks that the scope of the divestiture package may be too constrained, or not appropriately configured, to attract a suitable purchaser, or may not allow a purchaser to operate effectively and viably in the market;
    - purchaser risks that a suitable purchaser is not available or that the merger parties will dispose to a weak or otherwise inappropriate purchaser; and
    - asset risks that the competitive capability of a divestiture package will deteriorate prior to completion of divestment, for example, through loss of customers or key members of staff.[7]

17. These risk assessments are made and taken into account when establishing the factual and in the competition assessment.

THE PARTIES

David Ferrier/NZ Woolscourers

18. Mr David Ferrier is the sole shareholder and director of NZ Woolscourers, a company that has no current assets but which is the vehicle that may be used to give effect to the above transactions.

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[6]Section 69A(3) of the Commerce Act 1986.

[7] This framework is based on the approach used by the United Kingdom Competition Commission. The Commission recognises that the United Kingdom Competition Commission has greater power to recommend actions (structural and/or behavioural) to be taken by the applicant, to remedy, mitigate or prevent a substantial lessening of competition arising from the acquisition. Nevertheless, the Commission considers that this categorisation of types of risk provides a useful way for the Commission to ensure it has made a thorough assessment of all issues pertinent to the divestment and establishing the factual.

19. Mr Ferrier also has a 7.5% shareholding in Cavalier Wool. This is held through a family trust.

Cavalier Wool

20. The remaining 92.5% of the shares of Cavalier Wool are owned by Cavalier Bremworth Limited (Cavalier Bremworth), which is itself 100% owned by Cavalier Corporation Limited, a publicly listed company.

21. Cavalier Wool, through its 100%-owned subsidiary Cavalier Woolscourers Limited, owns and operates a wool scour near Napier and a wool scour near Timaru . The Hawkes Bay plant scours all of the Cavalier Group's carpet wool requirements. Both of Cavalier Wool's plants also provide commission wool scouring services for independent wool exporters. Commission wool scouring is the term used to describe the contract scouring of wool owned by other parties.

22. Cavalier Wool also ultimately owns a 50% interest in Canterbury Wool Dumpers Limited (the other 50% being owned by Timaru Wool Dumpers Limited), which runs a wool dumping business in Timaru. Wool dumping is the process by which wool is compressed into dense bales with a view to reducing transport costs to a minimum.

23. Cavalier Wool owns one third of the shares of Lanolin Trading (see para 31 for further details about this company).

24. Finally, the Cavalier Group is involved in the manufacture of woollen and wool-blend carpets in New Zealand (through its subsidiaries Cavalier Bremworth and Norman Ellison Carpets Limited).

Godfrey Hirst

25. Godfrey Hirst is a manufacturer of woollen and synthetic carpets in New Zealand. Through subsidiaries, the company owns and operates wool scouring plants at Clive (near Napier) and Clifton (near Invercargill). These scours provide wool scouring services to Godfrey Hirst for its carpet wool requirements as well as commission scouring services for independent wool exporters and other industry participants.

26. Godfrey Hirst also operates four wool dumping businesses (one each at Clifton, Dunedin, Christchurch and Clive). These businesses are the subject of the divestment undertaking included as part of the Application.

OTHER RELEVANT PARTIES

New Zealand Wool Services International Limited (NZWSI)

27. NZWSI is a publicly owned company listed on the New Zealand Exchange's Alternative Market (NZAX). The company is 44% owned by Forresters NZ Limited, a company with ownership links to Timaru businessman, Mr Allan Hubbard.

28. NZWSI operates two businesses. The first is the purchase of wool in New Zealand, primarily for export to a number of overseas countries, including India and China. Secondly, it owns and operates wool scours at Whakatu in Hawkes Bay, and at

Belfast near Christchurch. Most of NZWSI's wool scouring activities relate to the wool that it owns itself. However, it also undertakes commission wool scouring services for some independent wool exporters and other parties. NZWSI informed the Commission that it intends to increase its commission scouring business.

29. As part of the transactions associated with the proposed acquisition, NZWSI will acquire certain fixed assets from the Applicant, comprising various wool scouring machinery and equipment (but not sites), and will enter into an underwriting agreement with the Applicant whereby Cavalier Wool will guarantee a minimum increase in NZWSI's commission scouring volumes, subject to certain terms and conditions being met.

Wool Merchants

30. There are a number of merchants that are involved in the purchase of wool by auction, direct from growers, and in the case of slipe wool,[8] from meat processors for sale to local and overseas customers. These merchants include Segard Masurel (NZ) Ltd (Segard Masurel); J S Brooksbank & Co (A'asia) Ltd (Brooksbank); H Dawson Sons & Co (Wool) NZ) Ltd (H Dawson); and Fuhrmann NZ (1983) Ltd (Fuhrmann). Wool merchants are the major commission customers of wool scourers, but also engage in the sale of greasy (i.e., unscoured) wool.

Lanolin Trading Co Limited (Lanolin Trading)

31. Lanolin Trading, a co-operative, is currently owned in one third shares by Cavalier Wool, Godfrey Hirst and NZWSI. It is involved as agent for its shareholders in the purchase and marketing of wool grease, a by-product of wool scouring. The company sells wool grease predominantly to overseas customers, but also to a small number of New Zealand firms, for use as an input in a wide range of intermediate and final products (e.g., lanolin and lanolin derivatives such as cosmetics).

INDUSTRY BACKGROUND

Overview

32. Wool produced by farmers is sold mainly by auction, with the remainder sold direct to buyers by private treaty. Wool merchants comprise the major purchasers of the wool produced by farmers. Additionally, wool merchants purchase slipe wool.

33. Wool produced in New Zealand is either:

- scoured and used in New Zealand (e.g., for the manufacture of carpet or apparel); or
- scoured and exported as clean wool; or
- exported as greasy wool.

34. On the basis of Meat & Wool New Zealand Economic Service (Meat & Wool) statistics for the 12 months to June 2008, around 75% of wool exports were in scoured form.

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[8] The process of slaughtering sheep for their meat requires each carcass to have the skin removed. This skin offers two by- products - the pelt for leather and the residual wool, known as slipe wool.

35. Wool scoured in New Zealand is used in New Zealand by the two domestic carpet makers (Cavalier Bremworth and Godfrey Hirst), and by other further processors (e.g., apparel manufacturers). Wool that is not required to be scoured is generally sent to a wool dump prior to it being shipped overseas to an end user for scouring and further processing.

36. Wool scouring essentially involves the washing of wool in hot water and detergent to remove the impurities and then drying it. Wool grease is removed during the wool scouring process and is sold separately by Lanolin Trading.

37. Appendix 1 shows the different functional levels in the movement of wool, while Appendix 2 outlines the anticipated 2009 volumes of wool flows in New Zealand.

The New Zealand Wool Industry

38. Approximately 85% of all New Zealand wool is exported. China is the largest destination accounting for around 31% of total wool exported in the 2007/08 year. In 2007/08 approximately 65% of total New Zealand wool exported to China was greasy and the remaining 35% was scoured.[9]

39. Historically, the size of the wool scouring industry has been closely aligned to sheep numbers and the available wool clip. For instance, when the New Zealand sheep flock reached its peak of 70 million in 1982-3, there were numerous scouring operations. However, the decline in sheep numbers to fewer than 35 million at present, accompanied by a significant reduction in the wool clip has resulted in steadily reducing scouring capacity. Currently there are six wool scour plants, three each in the North and South Islands. This compares with around 20 scours operating in the late 1980s/early 1990s.

40. The following companies are currently involved in wool scouring:

- Cavalier Wool (operates two plants - one each at Napier and Timaru);
- Godfrey Hirst (operates two plants - one each at Clive and Invercargill); and
- NZWSI (operates two plants - one each at Whakatu and Christchurch).

41. The acquisition would involve some rationalisation or reduction in New Zealand's total wool scouring capacity. However, there will still be overcapacity and this is discussed further below.

PREVIOUS DECISION

42. The Commission has previously considered wool scouring in *Decision No 587: Godfrey Hirst NZ Limited/Feltex Carpets Limited*, 31 August 2006.

43. That acquisition gave rise to horizontal aggregation in the market for the supply of wool scouring services in the North Island. Godfrey Hirst was granted clearance to acquire Feltex Carpets, in part because the combined entity would face constraint from two large competing scours (Cavalier Wool and NZWSI), both with excess capacity and the ability to expand their capacity.

[9] Page 21 of the Application.

MARKET DEFINITION

Introduction

44. 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."[10]

45. 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 (a SSNIP), 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 increases in price that is sustained for a period of one year.

46. The Commission defines relevant markets in terms of five characteristics or dimensions:

    - the goods or services supplied and purchased (the product dimension);
    - the level in the production or distribution chain (the functional level);
    - the geographic area from which the goods or services are obtained, or within which the goods or services are supplied (the geographic extent); and
    - the temporal dimension of the market, if relevant (the timeframe); and
    - the customer dimension of the market.

47. The Commission first examines the product dimension, followed by the functional, customer and geographic dimensions of the market.

48. The proposed acquisition would give rise to horizontal aggregation in respect of wool scouring services in the North and South Islands. In the absence of the divestment undertaking, the acquisition would result in some minor horizontal aggregation in respect of wool dumping services in the South Island. Additionally, an increased shareholding by the merged entity in Lanolin Trading raises potential vertical issues in respect of wool grease, a by-product of the wool scouring process.

Product/Functional Market Dimensions

49. 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. The degree of demand-side substitutability is influenced by the extent of product differentiation.

Wool Dumping

50. Wool dumping is a specific service comprising the compression of greasy wool into smaller bales. The reduction in transport costs associated with the reduction in

[10] Section 3(1A) of the Commerce Act 1986.

greasy wool volume exceeds the additional costs of dumping, making the process economically viable.

51. The wool dumping assets that are part of the acquisition are specifically and only used for the compression of greasy wool for export.[11] There is no substitute for wool dumping, which constitutes a distinct step in the production chain of greasy wool. For these reasons, the Commission considers that the provision of wool dumping services constitutes a distinct market in both the product and functional dimensions.

Wool Grease

52. Wool grease is a by-product of the wool scouring process. After separation during the scouring process, it is shipped to mostly overseas purchasers for use as an input into the manufacture of a range of products, including lanolin, lanolin derivatives, wool wax acids and wool wax alcohols.

53. As the purchase and supply of wool grease is a distinct step related to the production chain of clean wool and for which there is no substitute, the Commission considers that it forms a distinct market in both the product and functional dimensions.

Wool Scouring

54. In Decision 587 the Commission concluded that it is appropriate to define a discrete market for wool scouring services in terms of both the product and functional dimensions. The Applicant agrees with that conclusion. The Commission remains of the view that the product and functional markets are those for the supply of wool scouring services.

Geographic Market Dimension

55. 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.

Wool Dumping

56. Industry participants advised the Commission that the internal freight costs for wool are high relative to its value, and for that reason the transportation of wool is largely confined to the geographic boundaries of the North and South Islands. Accordingly, for the purpose of this Application, the Commission proposes to delineate separate geographic markets for the dumping of greasy wool in each of the North and South Islands.

Wool Grease

57. Because wool grease is a high value/low volume product it is capable of being transported economically over large distances. For that reason, the Commission

[11] In this respect these assets are not the same as the "wool packaging/pressing"assets that form part of the production line of a New Zealand wool scour. At the end of the scouring process clean wool is also compressed to reduce transport costs.

considers that for the purposes of this Application, it is appropriate to define a national geographic market for the purchase and supply of wool grease.

Wool Scouring

58. The Applicant considers that the proposed acquisition involves overlap in both the North and South Islands because it is of the view that there is some scope for wool to move between the North and South Islands. However, the Applicant concedes that the Acquisition gives rise to similar outcomes in both islands. On that basis the Applicant suggests separate North and South Island markets in its Application.

59. Industry participants have advised the Commission that only small volumes of wool are currently transported across the Cook Strait and that the freight costs render movement of wool between the islands largely uneconomic.

60. In view of these factors, the Commission considers that the conclusion reached in Decision 587 of narrow geographic markets remains appropriate. Accordingly, for the purposes of considering the proposed acquisition, the relevant geographic markets are the North and South Islands.

Conclusion on Market Definition

61. The Commission considers that for the purposes of assessing this Application, the relevant markets are:

- the North Island market for the supply of wool scouring services (the North Island scouring market);
- the South Island market for the supply of wool scouring services (the South Island scouring market);
- the North Island market for the supply of wool dumping services (the North Island dumping market);
- the South Island market for the supply of wool dumping services (the South Island dumping market); and
- the national market for the purchase and supply of wool grease (the national wool grease market).

FACTUAL/COUNTERFACTUAL

62. In reaching a conclusion about whether an acquisition is likely to lead to a substantial lessening of competition, the Commission makes a with and without comparison rather than a before and after comparison. The comparison is between two hypothetical future situations, one with the acquisition (the factual) and one without (the counterfactual).[12] The difference in competition between these two scenarios is then able to be attributed to the impact of the acquisition.

The Factual

63. As part of the transactions surrounding the acquisition, the Applicant proposes in the factual to:

[12] *Air New Zealand & Qantas Airways Limited v Commerce Commission* (2004) 11 TCLR 347, Para 42.

- acquire the two wool scouring plants (Clifton and Clive) currently owned by Godfrey Hirst;
- acquire the four wool dumping businesses currently owned by Godfrey Hirst (one each at Clifton, Dunedin, Christchurch and Clive);
- acquire 50 shares in Lanolin Trading;
- close the Clifton plant completely;
- close one of two production lines at the Clive plant, and sell the remaining line to Cavalier Wool;
- sell some of the fixed assets from the two ex-Godfrey Hirst plants to NZWSI;
- enter into an agreement with NZWSI whereby Cavalier Wool would underwrite a minimum increase in NZWSI's commission scouring volumes, subject to certain terms and conditions being met;
- acquire up to 100% of the shares of Cavalier Wool;
- sell the wool dumping assets it acquires from Godfrey Hirst to an independent party in terms of the divestment undertaking, but retain its interest in the Timaru wool dumping business; and
- contract on "a reasonable commercial endeavours" basis to have Godfrey Hirst's wool scouring requirements carried out by Cavalier Wool for a six year period, subject to Cavalier Wool providing a competitive service.

64. As a result of the Acquisition, Godfrey Hirst would be removed completely as a supplier of wool scouring services in each of the affected wool scouring markets. Godfrey Hirst's wool dumping businesses would also be acquired by an independent party in accordance with the divestment undertaking which forms part of the Application. This is outlined in further detail below.

The Divestment Undertaking

65. As the Applicant undertakes to divest shares or assets, the undertaking forms part of the clearance application. In establishing the factual, the Commission must therefore predict the likely state of the market subsequent to the proposed acquisition and divestment.

66. As outlined in para 16 to make this assessment, the Commission has regard to the categories of composition risk, purchaser risk, and asset risk. These risks are considered with respect to the North Island and South Island dumping markets, as the Applicant has undertaken to divest the wool dumping assets acquired as part of the Acquisition.

67. The Commission considers that the risk framework provides a useful way of identifying the risks that are inherent in divestment undertakings and ensures that the Commission has made a thorough analysis of all factors relevant to the factual.

Overview

68. [ ]

Composition Risks

69. As stated, it is proposed that the Applicant will divest all of the wool dumping assets acquired from Godfrey Hirst to [ ]. The Commission is therefore of the view that the scope of the divestment is sufficiently comprehensive to enable the purchaser to operate effectively and viably in the relevant markets.

Purchaser Risks

70. [ ]

71. The Commission considers that given the proposed divestment of the wool dumping businesses to an independent purchaser with extensive industry experience, the purchaser risk is low.

Asset Risks

72. The main purpose behind the Applicant's divestment of the wool dumping assets is [ ] In both these senses there is no incentive on the Applicant to run down the wool dumping assets.

73. Given that the divestment period is likely to be relatively short and because the assets will be maintained in their existing form, the Commission considers that the asset risks arising from the divestment undertaking are low.

Conclusion on Risks

74. For the reasons outlined above, the Commission concludes that the composition, purchaser and asset risks are minimal.

Counterfactual

75. The counterfactual is the Commission's view of what would be likely to occur if the acquisition being considered were not to proceed. It is the benchmark against which any changes arising from the proposed acquisition is assessed. When making this assessment, the Commission recognises that future scenarios may include either the existing owners continuing to control the target entity, or other parties that are interested in purchasing the target entity if the Applicant's proposed acquisition were not to proceed and the sale to continue.

76. Where there is more than one real and substantial counterfactual, it is not a case of choosing the one that the Commission considers has greater prospects of

occurring.[13] Rather the Commission is to consider each of the possible counterfactuals that are real and substantial possibilities. Each of these real and substantial possibilities becomes a counterfactual against which the factual is to be assessed. The Commission is to then discard those possibilities that have only remote prospects of occurring. This assessment is an evidence based exercise.

77. If each of the counterfactuals is likely (i.e., each of the counterfactuals is not a remote possibility), all likely scenarios must undergo a competition analysis to assess whether a substantial lessening of competition would be likely to arise.

78. Godfrey Hirst advised the Commission that, in the absence of the proposed acquisition, it would continue to operate its wool scouring operations in the previous manner.

79. There has been an ongoing reduction in wool scouring capacity over the past 20 years corresponding to a decline in sheep numbers and wool clip required to be scoured. Based on Meat & Wool forecasts, these trends are expected to continue. However, the closure of wool scours has not kept pace with the reduction in the wool clip, and there is currently considerable excess capacity in the industry. This is detailed further below.

80. The Applicant considers that the increasing level of excess capacity is likely to result in further capacity rationalisation in the affected markets in the next 12-24 months. Nevertheless, for the purposes of the Application, the Applicant has suggested a "status quo" counterfactual, which assumes that the level of existing capacity is unchanged.

81. While the Commission agrees with the Applicant that further rationalisation of the wool scouring industry is likely in the future, the form that such rationalisation would take, without the Acquisition, is unclear. One (or more) of the three existing incumbents could exit the industry, or alternatively continue to operate, but at a reduced capacity.

Conclusion on the Counterfactual

82. The Commission concludes that the likely counterfactual is that in each of the relevant markets, Godfrey Hirst would continue to operate its wool scouring plants (i.e., effectively the status quo). However, the Commission recognises that, without the Acquisition, the industry would, in any event, be ready for rationalisation.

83. If the Commission adopts the status quo as a counterfactual, it does not need to decide on the form of any future rationalisation (without the Acquisition) because the status quo would result in the greatest loss of competition and is the most conservative in respect of the Commission's analysis of the Application.

84. The Commission would need to decide on the form of an industry rationalisation (without the Acquisition) only if it had to revisit the issue because it was unable to grant clearance under a status quo counterfactual.

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[13] *Woolworths Limited v Foodstuffs (Auckland) Limited; Foodstuffs (South Island) Limited; Foodstuffs (Wellington) Co-Operative Society Limited ("Foodstuffs") and Ors* HC WN CIV 2007-485-1255 {29 November 2007}, 118.

COMPETITION ANALYSIS

85. The proposed acquisition would involve horizontal aggregation of market shares in respect of:

- the national wool grease market;
- the South Island wool dumping market; and
- mostly importantly, both of the North Island and South Island scouring markets.

The National Wool Grease Market

86. The acquisition would result in the combined entity increasing its shareholding in Lanolin Trading from 33% to 66%. The Commission has considered whether the increased shareholding is likely to strengthen vertical effects between any markets. In particular, the question arises as to whether the acquisition would provide scope for the combined entity to achieve more favourable payment and trading terms for the wool grease it sells, and/or to limit new entry into the national wool grease market by restricting membership of Lanolin Trading.

87. The Applicant has submitted that regardless of the increased shareholding it will not have any greater voting rights. This is because the constitution of Lanolin Trading prevents any one shareholder from having greater voting rights than any other shareholder.

88. While the Commission agrees with the Applicant that this is a possible outcome, it also considers that the constitution can be interpreted in such a way that could enable the combined entity to increase its voting power in Lanolin Trading, and thereby potentially have a greater influence in the decision making process. Accordingly, for the purposes of the competition analysis, the Commission has adopted a conservative approach, and assumed that the increased shareholding would give the combined entity sufficient influence to control the decision making processes of Lanolin Trading.

89. Control in the decision making process of Lanolin Trading could adversely affect the national market for wool grease by enabling the combined entity to:

- discriminate as to the sale price of wool grease so that it receives a higher price than its competitors; or
- prevent new wool scouring entrants from joining Lanolin Trading.

90. However, in regard to payments that wool scours receive for the wool grease supplied to Lanolin Trading, a pooling system operates. This effectively means that the sellers of all wool grease sold within each quarter receive the same price per kilogram. Accordingly, there is no scope for price discrimination.

91. Further, any new scour operator is eligible for membership of Lanolin Trading, subject to it paying about $50.00 per scour that it owns. Moreover, in the Commission’s view Lanolin Trading as a co-operative is incentivised to attract wool grease supply from all New Zealand wool scours in order to maximise its

bargaining power with its primarily overseas customers. To act otherwise risks undermining the advantages of the company as a single desk seller in its negotiations with overseas purchasers.

92. For these reasons, the Commission is satisfied that the increase in the combined entity's shareholding in Lanolin Trading will not, or would not be likely to have, the effect of substantially lessening competition in this market.

93. This market is not considered in any further detail in these reasons.

Wool Dumping Markets

94. Godfrey Hirst and Cavalier Wool both own wool dumps. However, the Applicant submitted that the divestment undertaking discussed above would avoid aggregation of market share and competition concerns in the wool dumping markets.

95. The Commission agrees that the divestment undertaking means that the factual and the counterfactual are essentially the same with regard to the provision of wool dumping services. The Commission is, therefore, satisfied that the proposed acquisition will not have, or would not be likely to have, the effect of substantially lessening competition in either the North or South Island wool dumping markets.

96. These markets are not considered in any further detail in these reasons.

NORTH AND SOUTH ISLAND SCOURING MARKETS

97. In the Commission's view, the competition issues in respect of the supply of wool scouring services are generic to both the North and South Island geographic markets. The Commission has, therefore, treated them together for the purpose of the competition analysis.

Capacity Utilisation

98. The Applicant submitted that:

> the transaction aims to bring about industry efficiencies by rationalisation based on the removal of substantial, but far from all, excess capacity.

99. This section of the report first assesses the degree of utilisation of wool scouring capacity in the counterfactual and the factual. It then assesses the cost of wool scouring and scale economies that arise in the industry.

100. The Applicant stated that, post acquisition, it would:

- continue operating Godfrey Hirst's North Island plant, but would halve that plant's scouring capacity; and
- close entirely Godfrey Hirst's South Island plant.

101. Meat & Wool estimates that New Zealand sheep numbers and wool clip will decrease significantly in the next few years. To estimate scouring capacities in the factual, the Commission has adopted Meat & Wool's forecasts and has assumed that, compared to 2007/08 figures, the wool clip will decrease in 2009/10 by 8% in

the North Island and by 15% in the South Island before stabilising at those reduced levels.[14]

102. The other assumptions that the Commission has made to estimate capacity utilisation are:

- scours operate 50 weeks a year, 6.5 days a week, 24 hours a day;[15] and
- the combined entity will scour all wool that Godfrey Hirst and Cavalier scoured prior to the proposed acquisition. That is, for the purpose of the estimation, it is assumed that NZWSI will not experience an increase in scouring volumes post acquisition, other than [ ] of additional scouring volume that arises from the combined entity's agreement to underwrite that volume of greasy wool to NZWSI to scour (see discussion in the factual section and also below).

103. Table 1 shows the estimated levels of capacity utilisation with regard to the supply of wool scouring services.

Table 1: Estimated Levels of Scouring Capacity Utilisation in the Factual and Counterfactual

<table>
<tr><th></th><th colspan="2">North Island</th><th colspan="2">South Island</th></tr>
<tr><th>Participant</th><th>Capacity Utilisation in the Counterfactual</th><th>Capacity Utilisation in the Factual</th><th>Capacity Utilisation in the Counterfactual</th><th>Capacity Utilisation in the Factual</th></tr>
<tr><td>Godfrey Hirst</td><td>[ ]%</td><td rowspan="2">[ ]%</td><td>[ ]%</td><td rowspan="2">[ ]%</td></tr>
<tr><td>Cavalier Wool</td><td>[ ]%</td><td>[ ]%</td></tr>
<tr><td>NZWSI</td><td>[ ]%</td><td>[ ]%</td><td>[ ]%</td><td>[ ]%</td></tr>
<tr><td>Industry wide</td><td>[ ]%</td><td>[ ]%</td><td>[ ]%</td><td>[ ]%</td></tr>
</table>

Source: Godfrey Hirst, Cavalier Wool, NZWSI, Commerce Commission analysis

104. As can be seen from Table 1, the Commission calculates that post-acquisition there will be excess capacity of [ ]% in the South Island and [ ]% in the North Island. The corresponding figures are currently [ ]% in the South Island and [ ]% in the North Island. The reason for this is that, post acquisition, Cavalier Wool intends to increase its degree of capacity utilisation by closing a number of scouring lines

[14] These estimates are similiar to estimates provided by the Applicant.

[15] This allows for the changeover times required when switching from one production run to another and for the time to carry out maintenance on machinery.

105. Because of Cavalier Wool's agreement to underwrite some of NZWSI's throughput, post acquisition, NZWSI's degree of capacity utilisation would increase from[ ]% to[ ]% in the North Island, and from [ ]% to [ ]% in the South Island.

Cost of Wool Scouring

106. The Applicant submitted that the removal of excess capacity would enable the combined entity to realise industry efficiencies. This is because a large proportion of wool scouring costs do not vary with throughput, but are fixed. Consequently, higher levels of capacity utilisation would significantly reduce average costs of scouring wool. Industry participants unanimously confirmed the importance of economies of scale with regard to wool scouring.

107. Table 2 below shows the Applicant's estimates of average costs of scouring one kilogram of greasy wool at its North Island and South Island plants.

Table 2: Estimated Costs of Scouring One Kilogram of Greasy Wool (cents per kilogram)

	Degree of Capacity Utilisation			
Plant	**40%**	**60%**	**80%**	**100%**
North Island	[ ]	[ ]	[ ]	[ ]
South Island	[ ]	[ ]	[ ]	[ ]

Source: Cavalier Wool (costs include depreciation and interest)

108. The figures above suggest that the average costs of scouring one kilogram of greasy wool decreases by up to [ ]% as capacity utilisation increases from 80% to 100%. If capacity utilisation increased from 60% to 100%, average costs would decrease by up to [ ]%. Other industry participants submitted similar estimates in this regard.

Existing Competition

109. 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).

110. An examination of concentration in a market can provide a useful indicator 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.

111. Tables 3 and 4 set out the estimated market shares for the firms that supply wool scouring services in the North and South Islands. These figures are based on each of the existing wool scourers' production of greasy wool for the year ending 30 June 2008.

Table 3: Estimated Market Shares for the North Island Scouring Market in 2008

Participant	Tonnes	Share (% approx)
Cavalier Wool	[ ]	[ ]
Godfrey Hirst	[ ]	[ ]
Combined entity	**[ ]**	**[ ]**
NZWSI	[ ]	[ ]
Total	[ ]	100

Source: New Zealand Woolscourers' Association

Table 4: Estimated Market Shares for the South Island Scouring Market in 2008

Participant	Tonnes	Share (% approx)
Cavalier Wool	[ ]	[ ]
Godfrey Hirst	[ ]	[ ]
Combined entity	**[ ]**	**[ ]**
NZWSI	[ ]	[ ]
Total	[ ]	100

Source: New Zealand Woolscourers' Association

112. While the three firm concentration ratio is outside the Commission's safe harbour thresholds, 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.

Competition between Cavalier Wool and Godfrey Hirst

113. Cavalier Wool and Godfrey Hirst are both vertically integrated scourers who scour wool for their own carpet making requirements as well as on a commission basis. They therefore compete strongly to scour the available wool clip.

114. The Applicant and Godfrey Hirst both provided examples of customers switching between Godfrey Hirst and Cavalier Wool. Two examples include:

- [ ]; and
- [ ]

115. The Applicant also submitted that Godfrey Hirst may be aggressive in certain respects but such behaviour relates to the use of wool purchases to leverage scouring of the remainder of the wool being sold by that supplier and "that aggression is irrelevant in terms of pricing."

116. Wool merchants spoken with by the Commission submitted that Cavalier Wool and Godfrey Hirst are currently actively competing for commission scouring business from independent wool merchants in addition to carrying out scouring for their own carpet manufacturing requirements. The practice in many instances has been for wool merchants to spread their scouring requirements between these companies to maintain a degree of competitive tension. For example:

- [ ] stated that Godfrey Hirst contributes to downward pressure on prices by publishing a schedule of prices for comparison; and
- [ ], considered that Cavalier Wool and Godfrey Hirst are fighting for business, always pushing for a bigger share.

117. Having regard to these factors, the Commission considers that the loss of Godfrey Hirst as an independent competitor would remove an important competitive constraint in the factual scenario.

NZWSI

118. As stated previously, at present NZWSI is mostly involved with scouring for its own wool purchase/export business. The company currently has only a limited involvement in commission scouring on behalf of merchants, amounting to around [ ] of its total scouring business.

119. The Commission notes that the largest commission scouring customer of NZWSI is John Marshall & Company Limited,[ ]

120. The Applicant submitted that, post acquisition, NZWSI will constrain Cavalier Wool and that constraint will increase as NZWSI promotes its commission scouring business. It provides the following arguments in support of such claims:

- there is a long standing practice that wool merchants spread their wool scouring requirements across two competing scours to maintain the ability to switch and the threat to switch;
- merchants faced with a price increase are likely to be incentivised to consider and test their options, or alternatively be forced to accept the increase either by reducing their already small margin on wool sales, or increasing price to overseas buyers (which would advantage NZWSI's wool export business). Faced with these outcomes merchants are likely to transfer at least some business to NZWSI;
- a threat by merchants to Cavalier Wool that they would move some of their scouring business to NZWSI would be a potent threat and one that could be readily implemented. The critical importance of volume efficiencies will likely act as a deterrent to Cavalier and incentivise NZWSI to act sensibly and commercially with its commission customers; and
- there are examples of scours owned by a co-operative of exporters or a single exporter like NZWSI attracting commission scouring business from

competing merchants (e.g. Canterbury Woolscourers was from 2004-07 25% owned each by Fuhrmann and Modiano, but commission scouring business for independent merchants accounted for around [ ]% of the total wool scoured).

121. Godfrey Hirst considered that NZWSI represents a viable source for its scouring requirements. Mr Kim McKendrick, CEO of Godfrey Hirst Australia (the parent company of Godfrey Hirst), informed the Commission that "...I would have no hesitation in using New Zealand Wool Services' facilities to scour wool…"

122. As part of the overall transaction, Godfrey Hirst has contracted to use its "reasonable commercial endeavours" to have its scouring requirements carried out by Cavalier Wool for six years, subject to Cavalier Wool providing a competitive service. However, if Cavalier Wool fails to satisfy the terms and conditions of the scouring agreement then Godfrey Hirst has stated [ ]

NZWSI's Incentives to Compete for Commission Scouring

123. The Commission has analysed the incentive and ability of NZWSI to become a competitive constraint on Cavalier Wool, post-acquisition.NZWSI has an incentive to increase its commission scouring business in order to:

- obtain an increased revenue stream from scouring, apart from wool trading which is a risky and low profit business; and
- increase the utilisation of its scouring capacity.

124. While in the year to 30 June 2008 NZWSI had a turnover of about $180m and a profit of about $2.5m per annum, its wool trading business made a loss of $47,000. The overall profit was only as a result of its scouring activities. In view of these circumstances, the Commission is of the view that NZWSI is incentivised to diversify its activities into commission wool scouring which is a more stable and profitable earner.

125. [ ]

126. NZWSI is further incentivised to compete for commission scouring business as the economics for its operations are based on maximising capacity utilisation in order to achieve gains in production efficiencies. As noted above in the discussion on economies of scale effects in wool scouring operations, the average cost of scouring one kilogram of greasy wool decreases by up to [ ]% as scour capacity utilisation increases from 80% to 100%. If capacity utilisation increases from 60% to 100%, the average cost decreases by up to [ ]%.

NZWSI's Ability to Compete for Commission Scouring

127. As mentioned earlier, NZWSI has the ability to, and indeed currently does undertake some commission scouring. As part of the wider transaction, the Applicant has agreed to sell certain ex-Godfrey Hirst scouring assets to NZWSI and

that will enhance NZWSI's ability to further develop its commission scouring business.

128. However, virtually all of the wool merchants spoken with by the Commission expressed a reluctance to use NZWSI, even in the event of a price increase by the combined entity, unless NZWSI ceased its wool trading operations. The reasons put forward were two fold.

129. First, wool merchants compete directly with NZWSI for the purchase of wool and concerns were raised that information about their quantities, wool blends and customer details would be disclosed via any scouring contracts.

130. Secondly, merchants were concerned that any profits that NZWSI earned from scouring their wool would be used to undercut them in the sale of scoured wool to customers and to increase the price NZWSI was able to offer farmers for the purchase of wool.

131. [ ] However, the underwriting agreement between NZWSI and the Applicant does guarantee NZWSI a certain minimum increase in its commission scouring volumes (see paras 133-139 below).

132. The Commission considers that, despite their statements to the contrary, if faced with the actual situation of a scouring price increase by the combined entity, and given their low overall operating margins, wool merchants are likely to respond by switching, or threatening to switch, at least part of their scouring volumes to NZWSI. In this regard, the Commission notes that the Applicant has been advised by [ ] that it has already decided to place some of its volumes with NZWSI.

Underwriting Arrangement between NZWSI and Cavalier Wool

133. As part of the wider transaction, NZWSI has sought, and it has been agreed, that Cavalier Wool will underwrite a minimum increase in NZWSI's commission scouring volumes, subject to NZWSI using "all reasonable commercial endeavours to grow, and thereafter maintain, its Commission scouring business and otherwise carry on its Commission scouring business in accordance with best industry practices."

134. According to the underwriting agreement, [ ] In the event that NZWSI does not achieve the increased throughput, [ ]

135. [ ]

136. The underwriting agreement between NZWSI and Cavalier Wool affects NZWSI's incentives to compete for commission scouring business. On the one hand, the agreement requires NZWSI to compete for new commission scouring business by using all "reasonable commercial endeavours".

137. On the other hand, the underwriting agreement might dampen the company's incentive to compete as vigorously as possible because it would receive the underwritten volumes as long as it uses "all reasonable commercial endeavours".

138. The underwriting agreement might also reduce NZWSI's incentive to compete vigorously as it automatically increases the company's degree of capacity utilisation. In 2008, NZWSI scoured [ ] of greasy wool. Assuming a decline in NZWSI's future scouring throughput of around 12% (in line with the expected decline in New Zealand wool clip in future years), this would reduce the company's throughput to around [ ]. Adding the underwritten scouring volumes of [ ] to that throughput would bring the company to [ ]% capacity utilisation.

139. NZWSI's degree of capacity utilisation post acquisition would limit the company's ability to take on substantial commission scouring in addition to the underwritten volumes, unless the company decided to add extra scouring lines to its existing plants. However, the Commission considers that if NZWSI were to secure sufficient and ongoing scouring business from wool merchants to justify an extra scouring line then there are unlikely to be any major impediments to it installing extra capacity.

Conclusion on Existing Competition

140. The Commission concludes that although NZWSI presently has a limited involvement in commission scouring, it is sufficiently incentivised to develop this business to improve profitability. The installation of the (ex Godfrey Hirst) equipment that it acquires from the Applicant will enhance its ability to undertake commission scouring. In terms of the underwriting agreement it must use "all reasonable commercial endeavours" to obtain new commission scouring customers. Arguably, that term of the agreement would require it to set its scouring prices at levels that would induce switching of customers from Cavalier Wool. NZWSI is likely to be in a position to expand its commission scouring capability if it obtains sufficient new customers to fill its existing limited spare capacity.

141. While the merged entity must accept that some of its existing customers would move to NZWSI in terms of the underwriting agreement, Cavalier Wool would not want this trickle to turn into a torrent as a result of any price increases that Cavalier Wool would impose. In this respect Cavalier Wool will be constrained from raising its prices.

142. Accordingly, the Commission considers that NZWSI is likely to provide some degree of competitive constraint in the factual.

Potential Competition

143. An acquisition is unlikely to result in a substantial lessening of competition in a market if the businesses in that market continue to be subject to real constraints

from the threat of market entry. The Commission's focus is on whether businesses would be able to enter the market and thereafter expand should they be given an inducement to do so, and the extent of any impediments they might encounter should they try.

Conditions of Entry

144. The likely effectiveness of the threat of new entry in preventing a substantial lessening of competition in a market following an acquisition is determined by the nature and effect of market conditions that impede entry.

145. The Commission has identified the following entry conditions that are relevant to the competition analysis of the relevant scouring markets:

- capital, plant, and equipment;
- regulatory requirements, including resource consents;
- technical expertise; and
- economies of scale in conjunction with excess capacity.

<u>Capital, Plant and Equipment.</u>

146. Entry into the wool scouring industry requires, amongst other things, specialised plant and equipment. The Applicant originally stated that new entry could be achieved by the purchase of second hand plant which could be installed for a total cost of approximately $4.5m.

147. However, in a subsequent submission, the Applicant noted that its earlier estimate overstated the costs. It considered that a near new wool scour with up to date technology, could be purchased in the USA for approximately US$250,000. Further, the Applicant also noted that following two recent scour closures in Australia (Jandakot and Goulburn Wool Scour), wool scouring lines and related plant and equipment have now become available for purchase. [ ]

148. The Applicant submitted a model which assessed the cost /benefit of new entry based on the purchase of plant from the closed Jandakot wool scour. It considers that the modelling supports the view that entry using this second hand plant would be relatively easy.

149. The Commission notes that while second hand equipment is readily available from overseas sources, it must be capable of competing effectively with efficient existing New Zealand plants. It must also be capable of processing cross bred wool which is the predominant type of wool produced in New Zealand.

150. The Commission notes that installation of a new 3.0 metre line at Cavalier Wool's Timaru plant cost approximately $[ ]

The Applicant considers that such factors would not be faced by a potential new entrant if it were contemplating entry in the present market situation.

151. The Commission notes that entry on a smaller scale, say using a 2.4 or 2.0 metre plant is likely to be less expensive than a 3.0 metre line, and that such lines are currently used by Godfrey Hirst at each of its two plants, while Cavalier Wool also operates smaller lines at each of its plants. Godfrey Hirst estimates that the cost of purchasing and installing a 2.4 metre line is less than $[ ].

152. The Commission considers that the ready availability of used plant is likely to facilitate entry at much lower fixed costs than was the case previously.

<u>Regulatory Requirements</u>

153. Before undertaking wool scouring activities, a new entrant would be required to obtain a suitable site in compliance with the provisions of the Resource Management Act 1991. The Commission has been advised that there are sites available for wool scouring that have existing resource consents. These include former meat processing plants, such as Oringi in Hawkes Bay. The Applicant has also identified two other sites (one in each island), both of which are considered suitable for use for a wool scour. This includes an empty scouring site directly opposite Cavalier Wool's existing wool scouring site in Hawkes Bay.

154. The Commission was advised that to obtain a resource consent for a greenfields site is likely to be considerably more difficult to obtain and would involve a costly and potentially lengthy process to obtain the relevant consents.

<u>Access to Technical Expertise</u>

155. The Applicant submits that suitable expertise is readily available. The Commission is of the view that such expertise is unlikely to constitute an impediment to new entry.

<u>Economies of Scale/Excess Capacity</u>

156. As noted previously, economies of scale are an important feature of the scouring markets (see paras 106-108 for further details), and their presence provides a strong incentive for wool scourers to maximise their capacity utilisation.

157. The Applicant notes that the wool scouring industry, faced with an ongoing decline in sheep numbers and a consequent reduction in the available wool clip, has been steadily reducing capacity. For instance in 1990 there were around 20 wool scouring plants operating throughout the country, but currently only six plants are left. Regardless, the Applicant considers, and the Commission agrees, that excess capacity would remain post acquisition even after the closure of three scouring lines, as proposed by the Applicant.

158. Wool merchants have been owners of wool scours in the past. However, virtually all merchants spoken to informed the Commission that given the reduction in sheep numbers, a declining wool clip, the existing overcapacity and the costs of setting up they would be reluctant to enter, or re-enter the North Island and South Island wool scouring markets.

159. For example, Mr Peter Crone, Managing Director of John Marshall & Company Ltd when commenting on the likelihood of new entry stated that “The reality is that when you are looking at our wool clip and the falling numbers it is never going to be viable”.

160. [ ] stated in response to a question on what price increase would encourage entry stated that “The way things are now under no circumstances would we be looking at building a scour.”

161. In light of these considerations, the Commission is of the view that economies of scale combined with the current excess capacity would require entry on a substantial scale.

The “LET” Test

162. In order for market entry to be a sufficient constraint, entry of new participants in response to a price increase or other manifestation of market power must be:

- Likely in commercial terms;
- sufficient in Extent to cause market participants to react in a significant manner; and
- Timely, i.e., feasible within two years from the point at which market power is first exercised.

Extent of Entry

163. If it is to constrain market participants, then the threat of entry must be at a level and spread of sales that is likely to cause market participants to react in a significant manner. Entry that might occur at only relatively low volumes, or in localised areas, does not represent a sufficient constraint to alleviate concerns about market power.

164. The Applicant considers that entry would most likely occur using a scouring line with a capacity of around [ ] greasy wool tonnes per annum (i.e., [ ]% of the current total scouring volumes in each of the North and South Islands). However, [ ], was of the view that the minimum breakeven throughput to run a 3.0 metre line is around [ ] greasy wool tonnes per annum.

165. The Commission notes that to attract commission scouring business, a scour must secure sufficient volumes from wool merchant customers. While such merchants have expressed a reluctance to use the commission scouring services of a scour that is owned or part owned by a competitor in wool export markets, the Commission has, nevertheless, been informed of examples of scours owned jointly by rival merchants, and which undertook scouring for other third party merchants. These included Canterbury Woolscourers, currently 100% owned by Cavalier Wool, but which was from 2004 to 2007 25% owned each by Fuhrmann and Modiano, two vigorous wool merchant competitors. Cavalier Wool’s records reveal that in the 2006 year, independent exporters accounted for around [ ]% of total wool scoured by Canterbury Woolscourers.

166. However, [ ]

167. Given the factors outlined above, the Commission concludes that if entry is to be sustainable and effective in this market, it would need to take place on a large scale and for this to occur, the new entrant would need to obtain sales from one or more of the major wool merchants to maximise throughput to obtain the full benefits from economies of scale. Subject to securing sufficient business, this factor is unlikely in the Commission's view to constitute an impediment to entry.

Timeliness of Entry

168. To effectively constrain the exercise of market power, entry must also be timely. If it is to alleviate concerns about a substantial lessening of competition, entry must be feasible within a reasonably short timeframe, which the Commission typically considers to be two years, from the point in which market power is exercised.

169. The Applicant considers that entry could be achieved somewhere between six and eight months. The Commission considers that such timeframes are realistic and accordingly, entry is likely to be achieved within its two year timeframe, subject to the wool scouring site already having a resource consent. Such sites would appear to be available. The Commission considers that greenfields entry would take considerably longer and is unlikely to occur inside two years.

Likelihood of Entry

170. In order to be a constraint on market participants, entry must be likely in commercial terms. An economically rational firm will be unlikely to enter a market unless it has a reasonable prospect of achieving a satisfactory return on investment, including an allowance for any risks involved. The Commission has considered whether entry would be likely if the combined entity were to increase prices by 5% to 10%.

171. The Applicant considers that the most likely candidates for entry are wool merchants. It notes that many of these parties have operated scours previously, and have the expertise to do so again. The Applicant refers to a number of past examples of scours having been owned by a co-operative of exporters. These include Canterbury Woolscourers, which was 25% owned each by Fuhrmann and Modiano; Ferrier Woolscours, which had Fuhrmann, Modiano and Standard Wool (NZ) Ltd as its shareholders; and Seaview Wools Ltd, which was jointly owned by three exporters (Chargeurs, Dewavrin and Modiano).

172. However, none of the merchants contacted expressed any interest in entering or re-entering wool scouring, even if the combined entity were to raise its prices. The reasons given were the decline in the wool clip available, the high capital costs (including environmental costs), and the fact that wool scouring no longer formed a core business for many merchants.

173. The Commission considers that the wool merchants' views on entry, or re-entry, are applicable to the current market circumstances. In the Commission's view, if faced

with a price increase of 5-10% by the combined entity then merchants would be incentivised to either sponsor entry, or to enter themselves. In this respect the Commission considers that the merchants could be induced to enter to preserve the already small margins they have between their costs and their revenue. Compared with the past situation, entry by merchants would now be assisted by the lower capital costs of entry using readily available second hand equipment and the decline in the number of market participants with the associated reduction in New Zealand's total wool scouring capacity.

174. Given the importance to Cavalier Wool that it maintains high capacity utilisation, even the threat of entry may be sufficient to constrain the combined entity. For the reasons outlined above, the Commission considers that entry is likely in the event of a 5% to 10% price increase.

Conclusion on the "LET" Test

175. In view of the factors outlined above, the Commission considers that *de novo* entry into the North Island and South Island scouring markets would be likely, sufficient in extent, and timely.

Conclusion on Potential Competition

176. Considering the conditions of entry collectively and applying the LET test, the Commission concludes that in the factual the combined entity is likely to face some constraint from potential competition.

Constraints from Outside the Market: Scouring in China

177. The competition analysis has focused on the effects of the proposed acquisition on competition in the North and South Island scouring markets. However, there is the potential for the merged entity to be constrained from outside these markets by the possibility of the scouring being carried out offshore.

178. Wool exported in greasy form is scoured overseas. Therefore, the possibility that merchants would divert some or all of their export business from scoured to greasy wool might provide some constraint on the price and service provided by domestic scourers.

179. The Applicant submitted that it would be constrained in the factual because exporters who are currently selling wool scoured in New Zealand into China have available to them the option of shipping greasy wool to China for scouring in China. The Applicant stated that this option would generally only apply to wool that was destined to be processed into manufactured products in China.

180. The Commission notes that this means that Chinese scouring of New Zealand greasy wool would act as a constraint on the merged entity only in respect of 8% of New Zealand's wool production.[16]

[16] The Applicant estimates that around 15% of Zealand wool is processed into manufactured products in New Zealand and the remaining 85% is exported. The Ministry of Agriculture and Forestry (MAF) estimates that of all wool exports, around 28% are destined for China (MAF estimates are based on wool exports measured in value for the year ending 31 March 2008). The Applicant estimates that 65% of wool exported to China is already exported greasy with the balance exported in scoured form. Therefore, the

Commercial Viability of Scouring Offshore: New Zealand Versus China

181. The Applicant submitted that the potential for scouring of New Zealand wool to be carried out in China would represent some constraint on scouring prices in New Zealand. To assess this competitive constraint, the Commission attempted to compare New Zealand scouring prices with Chinese prices. In its analysis, the Commission took into account scouring tariffs, the pressing of greasy and scoured wool, and the cost of sea freight. The Commission's calculations show that scouring wool in China can be less costly than scouring in New Zealand by approximately NZ5 cents/kg.

182. [ ]

183. [ ]

184. [ ]

Conclusion on constraints from offshore scouring

185. As discussed, the potential for scouring in China applies to a limited additional proportion of New Zealand scoured wool exports. For that 8% of New Zealand scoured wool exports, scouring offshore might have some commercial advantages when compared to scouring in New Zealand. However, scouring offshore also has disadvantages such as time delays, logistical issues, and loss of control that make this alternative less attractive. Nevertheless, in spite of these disadvantages, [ ]

proportion of wool currently scoured in New Zealand that would be available for export to China in greasy form is 8% (85% x 28% x 35%)

is investigating the possibility of having some or all of its wool exports scoured in China.

186. While most exporters advised the Commission that offshore scouring would not be a commercially alternative to scouring in New Zealand, even in the event of a 10% increase in New Zealand scouring prices, 65% of New Zealand's wool exported to China is scoured there. The Commission assumes that there must be some commercial advantage otherwise this would not occur and the wool would be scoured in New Zealand and exported in clean form.

187. For these reasons, the Commission considers that the merged entity might be constrained to some extent by the potential for diversion of some of its throughput to overseas scours. However, this constraint is likely to be limited.

Countervailing Power

188. Typically, merchants operate on very low margins between their costs and their revenues. For example, Segard Masurel, which is considered to be one of the more profitable merchants has a margin of 7 cents per kilogram of wool.[17] The margins of most other merchants are believed to be less than 7 cents. Several merchants have already exited the market as a result of their unsatisfactory returns. These include Modiano and Chargeurs.

189. A scouring price increase of 5 to 10 % would equate to about a 3-6 cents per kg increase in the scouring charges. This would reduce the wool merchants' margins by an equivalent amount. The Commission considers that, without the ability to pass on scouring price increases, wool merchants have a strong incentive to exercise any countervailing they might have.

190. The potential for a business to wield market power may be constrained by countervailing power in the hands of its customers. Exercising countervailing power would involve customers switching from one supplier to another, or the credible threat that they might do so. A purchaser would be able credibly to exert such countervailing power if it were large in relation to suppliers, well informed about alternative sources of supply, and readily able to switch from one supplier to another.

Scouring Customers

191. Wool merchants account for a significant proportion of Cavalier Wool's total scouring throughput. There are several large New Zealand wool merchants with a diversified global presence in the wool trade and several are involved in wool scouring in overseas countries. For example, Fuhrmann is a member of the Schneider group, which has a major global presence in wool processing and supply. Fuhrmann also operates scours offshore. Similarly, Brooksbank is a part owner of Elders Australia, which is a major global wool processor and buyer. The Commission therefore considers that wool scouring customers tend to be well

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[17] This calculation is based on Segard Masurel's Annual Report for the year ended to 30 June 2007, which was submitted to the Companies Office, and on the cost of wool at $4.00 per kilogram.

informed in terms of scouring prices and alternative options to scouring in New Zealand.

Ability of customers to switch

192. Wool scouring customers have three options when considering switching their scouring business in response to one scourer increasing its prices. These options are switching to:

- NZWSI; and/or
- an overseas scourer; and/or
- a new entrant, possibly sponsored by the customers.

193. However a potential switcher would be faced with the following difficulties:

- NZWSI would only be able to take on limited additional volumes without increasing its capacity;
- as discussed, the possibility of offshore scouring applies to only 8% of New Zealand's wool exports; and
- an entrant as an alternative is not available immediately.

Conclusion on Countervailing Power

194. The Commission considers that in the factual scenario the countervailing power of wool merchants is likely to be less in the counterfactual. However, given the presence of NZWSI, the possibility of scouring some wool offshore, and the threat of entry, the Commission is of the view that merchants would continue to have the ability to switch, or to credibly threaten to switch, and for that reason would be likely to continue to exercise significant countervailing power in the factual.

Conclusion on Unilateral Effects

195. Overall, the Commission concludes that the constraint likely to be provided by NZWSI, the presence of excess capacity and economies of scale in wool scouring markets, the potential constraint from new entrants and offshore scouring, and the countervailing power of wool merchants, are likely to limit the combined entity from exercising unilateral market power in the factual.

Coordinated Effects

Introduction

196. As well as increasing the scope for the exercise of unilateral market power, an acquisition that significantly increases seller concentration in a market may lead to circumstances where coordination between firms in the market is enhanced. In particular, it can become rational for firms to refrain from initiating price cuts that would be unavoidable in more competitive circumstances, or alternatively to initiate price increases, in the knowledge that their competitors will do likewise. As a result, prices can become higher than they would in a more competitive market.

197. As in its assessment of the potential for an enhancement of the exercise of unilateral market power, the Commission considers existing, potential, and other factors such

as the countervailing power of buyers in assessing the potential for an enhancement of the exercise of coordinated market power between the factual and the counterfactual.

198. The Applicant submitted three principal factors that would preclude any coordination in the factual:

- the presence of excess capacity, coupled with the large marginal gains from increasing throughput (all of which increase the incentives to "cheat");
- the absence of price transparency; and
- the practice of customers to utilise the services of at least two competing wool scourers in order to maximise their negotiating leverage reduces the ability of a scourer to detect cheating.

Analysis of the Ingredients of Coordination

199. In broad terms, effective coordination can be thought of as requiring three ingredients: the possibility of increased profits through coordination; the possibility of detection of non-adherence; and the scope for retaliation.

200. The Commission is of the view that there are factors that are likely to facilitate coordination such as:

- a reduction from three to two in the number of participants in each of the affected geographic markets;
- the removal of Godfrey Hirst which is the participant that in the counterfactual would act as an important influence in respect of any attempt by the market participants to engage in coordinated behaviour;
- there is some degree of industry co-operation (e.g., the NZ Woolscourers' Association prepares industry production figures that may facilitate the sharing of output projections); and
- the presence of the underwriting agreement may lessen the incentive for NZWSI to compete strongly.

201. However, there are also factors that weigh against coordination, such as;

- the presence of excess capacity;
- the importance of economies of scale which incentivises Cavalier Wool and NZWSI to maximise capacity utilisation; and
- entry barriers are unlikely to be so high to preclude new entry (or the threat of new entry).

Conclusion on Coordinated Effects

202. In summary, the Commission considers there are factors that are likely to enhance the scope for coordinated behaviour in the North and South Island scouring markets. However, the presence of excess capacity and economies of scale together with the other alleviating factors outlined above, are likely to sufficiently outweigh the incentives for the market participants to engage in coordinated behaviour.

Accordingly, the Commission concludes that the acquisition is unlikely to increase the scope for coordinated market power such as to substantially lessening competition in the North and South Island scouring markets in the factual.

Economic Modelling

203. The Commission used a game theory approach to model the incentives faced in the factual scenario. The model was developed to offer the most conservative market set up and offered a frictionless market design where wool merchants could shift substantial volumes from the merged entity to either NZWSI and/or offshore for commission scouring. The volumes shifted depended on the capacity available in both options, NZWSI and offshore. The model was developed iteratively with comment sought from the Applicant on the suitability of the underlying assumptions.

204. The model highlights the impact of the underwriting agreement between NZWSI and Cavalier Wool on both companies' incentives to compete. The model indicated that the presence of the volume underwrite incentivised NZWSI to seek a price rise of 10% or more when it had the ability to do so. However, part of the underwriting contract is that NZWSI must use "all reasonable commercial endeavours." Raising prices would likely be contrary to this provision.

205. Moreover, the constraints summarised below in the conclusion section would be likely to prevent the combined entity from raising its prices, post acquisition, above competitive levels.

206. The model also indicates that market co-ordination would be unlikely given the strong incentives for the combined entity to remain competitive. The model also indicates that a moderate price rise by NZWSI (under 10%) was not economic – a price rise by NZWSI would have to be 10% or more. Given the countervailing power of the wool merchants, the Commission considered it unlikely that NZWSI could implement a price rise that would offer economic benefits greater than costs.

Conclusion on the North Island and South Island Scouring Markets

207. The Commission considers that the following factors are likely when taken together to provide a sufficient constraint on the combined entity in the factual:

- the constraint from NZWSI;
- the constraint from potential competition;
- the presence of excess capacity and economies of scale;
- the potential constraint from offshore scouring; and
- the countervailing power of wool merchants.

208. Accordingly, the Commission is satisfied that the proposed acquisition will not have, or would not be likely to have, the effect of substantially lessening competition in the North Island and South Island scouring markets.

OVERALL CONCLUSION

209. Having considered the competition effects in each of the relevant markets, the Commission concludes that is satisfied that the proposed acquisition will not have, or would not be likely to have, the effect of substantially lessening competition in:

- the North Island scouring market;
- the South Island scouring market;
- the North Island dumping market;
- the South Island dumping market; and
- the national wool grease market.

DETERMINATION ON NOTICE OF CLEARANCE

210. Pursuant to section 66(3)(a) of the Commerce Act 1986, the Commission determines to give clearance for the proposed acquisition by Mr David Ferrier himself, or his company New Zealand Woolscourers Limited, to acquire up to 100% of:

(a) (i) the wool scouring and wool dumping assets of Godfrey Hirst NZ Limited (Godfrey Hirst);[18] and/or

(ii) the shares in Cavalier Wool Holdings Limited (Cavalier Wool); and/or for

(b) Cavalier Wool (in which interests related with David Ferrier would have a shareholding giving rise to a substantial degree of influence) to acquire the 2.4 metre line at Clive (near Napier) and land and buildings located at the Clive site, an assignment of the contract for wool scouring with Godfrey Hirst, and 50 shares in Lanolin Trading Co Limited.

211. The clearance is given subject to an amended divestment undertaking dated 3 March 2009 provided by the Applicant to the Commission pursuant to section 69A of the Act (attached as Appendix 3).

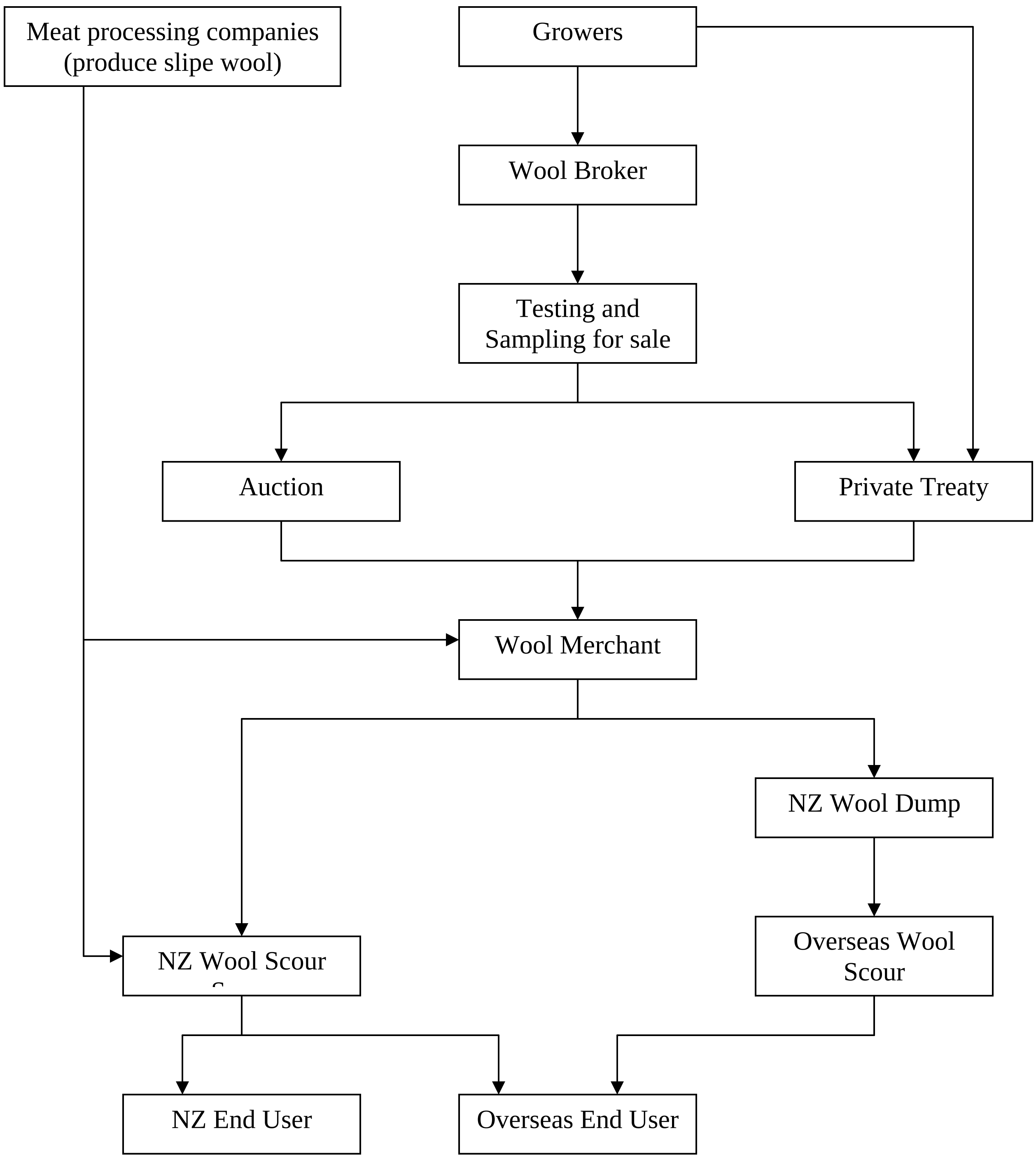
Dated this 6th day of March 2009

Paula Rebstock

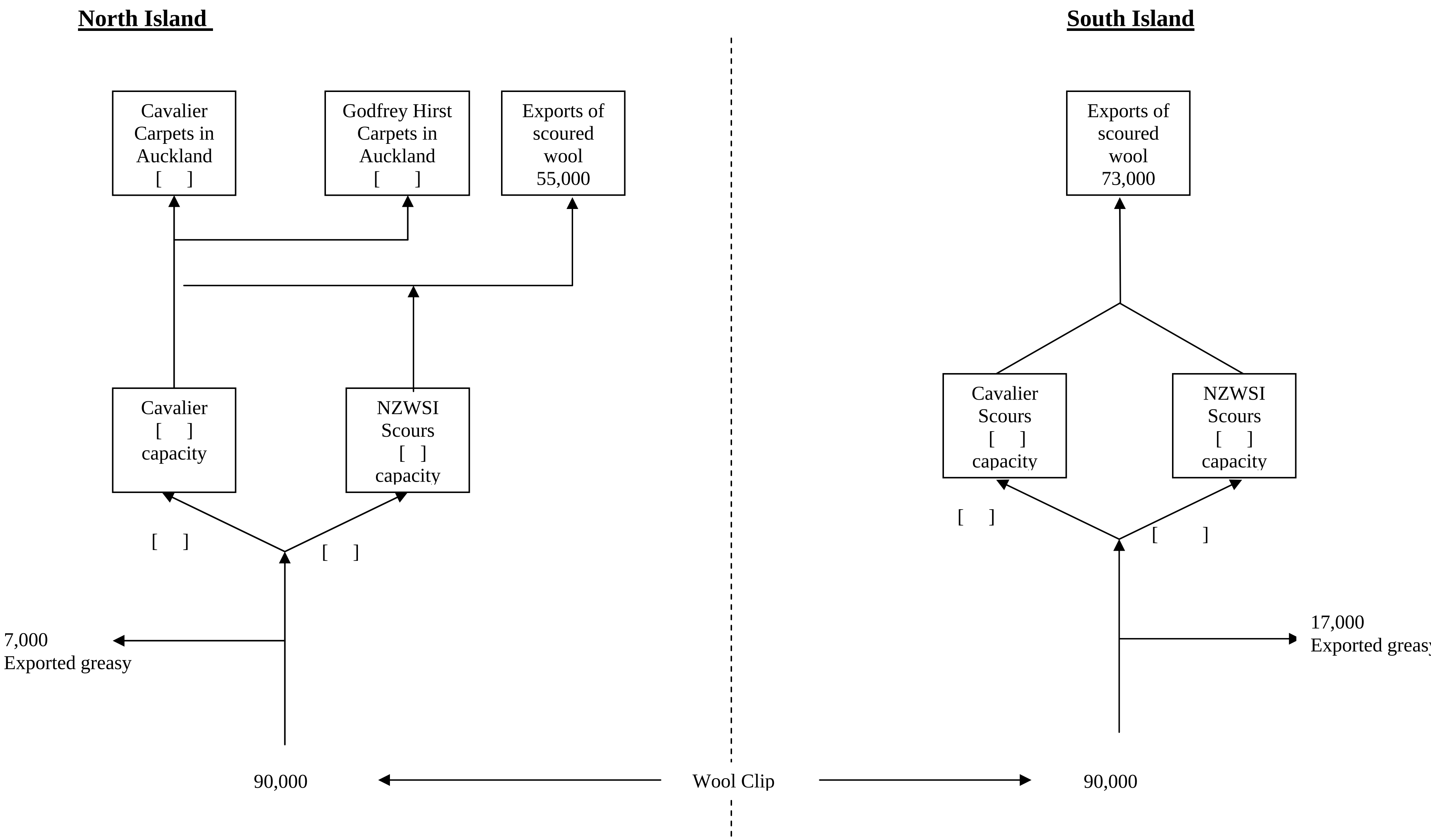
Chair

[18] These assets comprise the wool scouring plants located at Clive, Hawkes Bay, and Clifton, 50 shares in the Lanolin Trading Co Ltd, stock and lanolin, and the wool dumping plants located at Clive, Clifton ,Christchurch and Dunedin

APPENDIX 1 – Flow Diagram of the New Zealand Wool Industry



APPENDIX 2 – Wool Flows in New Zealand in tonnes per annum (2009 estimates)



APPENDIX 3 – Divestment Undertaking

Appendix 1 – Divestment Undertaking

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

1. On 10 December 2008, David Mcdougall Ferrier (the **Applicant**) gave notice to the Commerce Commission (the Commission) pursuant to section 66(1) of the Commerce Act 1986 (the **Act**) seeking clearance for the transaction described in that notice (the **Notice**).

2. Pursuant to section 69A of the Act, in giving a clearance under section 66(1), the Commission may accept a written undertaking given by or on behalf of the person seeking such clearance to dispose of assets or shares specified in the undertaking.

3. Subject to the conditions described in paragraph 5 of this undertaking, the Applicant undertakes to divest, or procure the divestiture of, the four Godfrey Hirst Wool Dumping businesses as listed in schedule 1 of this undertaking (the **Wool Dumping Businesses**) as a going concern to a purchaser which is not an interconnected body corporate (as defined by section 2(7) of the Act) or an associated person (as defined by section 47(3) of the Act) of the Applicant or of Cavalier Wool Holdings Limited, (the **Purchaser**), within six months from the date that the acquisition for which clearance is sought becomes unconditional.

4. Such divestment will proceed by way of an asset transaction and shall include:

   (a) all assets which are necessary to ensure the viability and competitiveness of the Wool Dumping Businesses;

   (b) all licences, permits and authorisations issued by any governmental organisation for the benefit of the Wool Dumping Businesses;

   (c) an assignment of all business contracts that the purchaser wishes to have assigned to it;

   (d) all customer and other records,

   (e) an assignment of the leases of the Christchurch and Dunedin Premises; and

   (f) a lease of that part of the site at Clive, currently occupied by the Clive wool dumping business.

   (the **Assets**).

5. For the avoidance of doubt, the divestment of the Wool Dumping Businesses shall not, *inter alia*, include:

   (g) intellectual property rights which do not contribute to the current operation or are not necessary to ensure the viability and competitiveness of the Wool Dumping Businesses; or

   (h) books and records required to be retained pursuant to any statute, rule or regulation provided that copies of such documents necessary for the Wool Dumping Businesses shall be provided to the Purchaser upon request.

6. Pending divestment, the Applicant will:

   (i) use reasonable endeavours to operate the Wool Dumping Businesses as viable businesses (other than the business operated from Clifton premises);

   (j) preserve the economic viability, marketability and competitiveness of the Wool Dumping Businesses in accordance with good business practice; and

(k) minimise as far as possible any risk of loss of competitive potential for the Wool Dumping Businesses.

7. The provisions of this undertaking are subject to the transaction for which clearance is sought becoming unconditional and to the Commission granting a clearance to the Notice.

DATED this 3RD day of March 2009

Signed:

David Mcdougall Ferrier

Schedule 1: Wool Dumping Assets

Dump	Asset Number	Asset Description	Capacity	
Spare Parts Clifton Dump		Tripack spare ram		$100k new
		Spare Valves		Second-hand
		Pump Parts		Second-hand
		Rams		Second-hand
		Stone Pump		Second-hand
		Spare valves		Second-hand
Clifton Dump	50933	Dump 3 bale Hydraulic	?	1995
Dunedin Dump	51285	Forklift 3 stage		2002
	51286	Forklift 26 ton		2002
	51288	Catsclaw		2002
	51282	Scales		2002
	51283	Dump, 3 bale 560 ton	560t	2002
	51284	Wool presses, double dump		2002
	51293	Sewing machine		2004
	51294	Sewing machine		2004
	51296	Sewing machine		2004
	51295	Washing machine		2004
	56143	Sewing machine		2007
	56151	Sewing machine		2007
	62130	Panasonic Fax Machine		2008
	51298	Desk, reception		2002
	51300	Carpet		2003
	54543	IBM E74R 17" CRT Monitor & Zip		2005
	51299	Printer		2002
	52901	Panasonic Fax/Copier UF490		2004

Dump	Asset Number	Asset Description	Capacity	
Christchurch Dump	59299	New Alarm System - ChCh Dump		2007
	55503	Blinds - CHC Wool Dumpers		2006
	50923	Catsclaw		2000
	50924	Catsclaw (ex RF)		2000
	59926	Forklift TCM FD 3.0		2008
	50909	Hopper 2.0 meter		2000
	50910	Hopper 2.0 meter		2000
	50916	Wool Press (small)		2000
	50917	Wool Press (small)		2000
	50918	Pinch Conveyor		2000
	50919	Wool blender double drum		2000
	54092	Trackgrip decotter		2001
	50921	Dump, 3 bale 560 ton	560t	2000
	50922	Wool Dump		2000
	55378	Dexion Angle Bench & Panel		2006
	55722	CHC Unallocated Asset		2006
	55343	Refrigerator		2006
	55351	2 Tables and 8 Chairs		2006
	50929	Office Building		2001
	50930	Desks		2001
	53559	Panasonic Fax/Copier		2005
	54711	IBM Computer & Screen		2006
Clive Dump	55626	Panasonic Air Conditioner		2006
	50576	Dump 3 bale Hydraulic	500t	2003
	50577	Dump 3 bale Hydraulic	500t	1999
	50779	Weighing machine		1999
	54818	Tarpaulin		2006

Dump	Asset Number	Asset Description	Capacity	
	55327	Tarpaulin #2		2006
	55597	Tarpaulin #3		2006
	55600	Tarpaulin #4		2006
	50743	Forklift clamps		
	50589	Conv press		
	50600	Conv press		
	50624	Blender		
	50628	Pinch elevator		
	50647	Hopper		
	50648	Hopper		
	50704	Electrical		
	50781	Splitting conveyor		
	50814	Conveyor		
	56055	Cotton picker		
	50743	Forklift clamps		
	50589	Conv press		
	50600	Conv press		
	50624	Blender		
	50628	Pinch elevator		
	50647	Hooper		
	50648	Hooper		
	50704	Electrical		
	50781	Splitting Conveyor		
	50814	Conveyor		
	56055	Cotton picker		