ISSN NO. 0114-2720
J4527
PUBLIC VERSION

COMMERCE COMMISSION

# Decision No. 427

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

**STEEL AND TUBE HOLDINGS LIMITED**

**and**

**FLETCHER STEEL LIMITED**

**The Commission:** M J Belgrave
M N Berry
P R Rebstock

**Summary of Application:** The acquisition by Steel and Tube Limited of up to 100% of the shares of Fletcher Steel Limited.

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

**Date of Determination:** 27 April 2001

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## THE PROPOSAL

1. On 5 April 2001, the Commerce Commission ("the Commission") registered a notice pursuant to section 66(1) of the Commerce Act 1986 ("the Act"), in which clearance was sought by Steel and Tube Holdings Limited ("Steel & Tube") to acquire up to 100% of Fletcher Steel Limited ("Fletcher Steel").
2. The Commission recently considered a similar acquisition in Decision 421 (21 March 2001). Decision 421 gave clearance to Fletcher Steel Limited to acquire up to 100% of the shares in Steel and Tube Holdings.

## THE PROCEDURES

3. The notice was registered on 5 April 2001. Section 66(3) of the Act requires the Commission either to clear or decline to clear a notice given under section 66(1) within 10 working days, unless the Commission and the person who gave notice agree to a longer period. A four day extension was sought by the Commission and agreed to by the applicant. Accordingly, a decision was due on 27 April 2001.
4. In its application, Steel & Tube did not seek confidentiality for fact of the application or for any material within its application.
5. The Commission's determination is based on an investigation by its staff. The Commission has also relied on information gathered for Decision 421. Commission staff contacted the following parties during the current investigation:
   - Asmuss Steel
   - Vulcan Steel
   - Steel Plus (United Industries)
   - OneSteel
   - Smorgon Steel
6. The Commission also sought further information from the applicant.

## THE PARTIES

### Steel & Tube

7. Steel & Tube is a publicly listed company involved in the merchandising, processing, and manufacture of a range of steel products. Further details are contained within Decision 421.

*OneSteel*

8. Steel & Tube's major shareholder is OneSteel, an Australian listed company, which holds 50.01% of the shares. OneSteel has four divisions; distribution, market mills, Whyalla Steelworks, and Steel & Tube Holdings. They are involved in the manufacture and distribution of a full range of long steel products in Australia.
9. The Whyalla steel mill produces around 1.2 million tonnes of raw steel annually. About 65% of that product is transferred to OneSteel's market mills in billet form for further processing. The balance is converted to finished products in the Whyalla Rolling Mill.

10. OneSteel also has another steel mill in Sydney, which produces around 500,000 tonnes of steel billets from scrap metal. Approximately 180,000 tonnes is manufactured into finished products on-site, while the remainder is transported to other OneSteel mills for further processing.

11. OneSteel has steel processing plants in Newcastle and Brisbane, which receive steel in billet form and manufacture them into finished steel products. The goods produced at these mills include hollows, merchant bar, angles, and reinforcing bar.

12. OneSteel exports to markets in North Asia, South East Asia, the US, Europe, and New Zealand. It has a turnover of around $3 billion.

### Fletcher Steel

13. Fletcher Steel is a subsidiary of Fletcher Building, which is a publicly listed company. Fletcher Steel distribution operations are similar to Steel & Tube's. Further details are contained within Decision 421.

14. Fletcher Steel also operates a steel-rolling mill in Auckland, which trades as Pacific Steel. It produces "long" products from this mill including merchant steel products and reinforcing bar, for the domestic and international markets. There has been significant media speculation that this mill will be closed to satisfy potential buyers of Fletcher Steel.

## MARKET DEFINITION

15. The relevant markets in Decision 421 were as follows:

- the national market for the distribution of merchant steel products;
- the national market for the distribution and fabrication of reinforcing steel;
- the national market for the distribution and processing of steel plate products;
- the national market for the distribution and processing of steel coil products;
- the national market for the manufacture and distribution of domestic roofing products; and,
- the national market for the manufacture and distribution of industrial roofing products.

16. Although these markets will be affected, the Commission is of the view that there is no material difference to the acquisition considered and cleared in Decision 421. For this reason, the Commission will not consider these markets further

17. In addition to the distribution markets, there is aggregation at the production functional level of the market by virtue of OneSteel's supply of steel into New Zealand. This is illustrated in Appendix 1.

18. Both OneSteel and Pacific Steel only produce "long products"[1], therefore the relevant production/importation markets are:

- The national market for the production or importation of merchant steel products; and,
- The national market for the production or importation of reinforcing steel.

[1] Industry players typically refer to steel products as being either "long" or "flat". Long products include structural products, angles, merchant bar, reinforcing bar, hollow sections, pipe and so forth. Flat products include plate and coil products.

## COMPETITION ANALYSIS

### Introduction

19. The competition analysis assesses competition in the relevant markets in order to determine whether the proposed acquisition would not result, or would not be likely to result, in an acquisition or strengthening of **dominance**.

20. Competition in a market is a broad concept. It is defined in section 3(1) of the Commerce Act as meaning "workable or effective competition". In referring to this definition the Court of Appeal said:[2]

> "That encompasses a market framework which participants may enter and in which they may engage in rivalrous behaviour with the expectation of deriving advantage from greater efficiency."

21. Section 3(9) of the Commerce Act states:

> "For the purposes of sections 47 and 48 of this Act, a person has … a dominant position in a market if that person as a supplier … of goods and services, is or are in a position to exercise a dominant influence over the production, acquisition, supply, or price of goods or services in that market and for the purposes of determining whether a person is … in a position to exercise a dominant influence over the production, acquisition, supply, or price of goods or services in a market regard shall be had to-
>
> (a) The share of the market, the technical knowledge, the access to materials or capital of that person or those persons:
> (b) The extent to which that person is … constrained by the conduct of competitors or potential competitors in that market:
> (c) The extent to which that person is … constrained by the conduct of suppliers or acquirers of goods or services in that market."

*The Dominance Test*

22. Section 47(1) of the Commerce Act prohibits certain business acquisitions:

> "No person shall acquire assets of a business or shares if, as a result of the acquisition, -
> (a) That person or another person would be, or would be likely to be, in a dominant position in a market; or
> (b) That person's or another person's dominant position in a market would be, or would be likely to be, strengthened."

23. The test for dominance has been considered by the High Court. McGechan J stated:[3]

> "The test for 'dominance' is not a matter of prevailing economic theory, to be identified outside the statute."
>
> …
>
> "Dominance includes a qualitative assessment of market power. It involves more than 'high' market power; more than mere ability to behave 'largely' independently of competitors; and more than power to effect 'appreciable' changes in terms of trading. It involves a *high degree of market control*."

24. Both McGechan J and the Court of Appeal, which approved this test,[4] stated that a lower standard than "a high degree of market control" was unacceptable.[5] The Commission has acknowledged this test:[6]

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[2] *Port Nelson Limited v Commerce Commission* (1996) 3 NZLR 554, 564-565
[3] *Commerce Commission v Port Nelson Ltd* (1995) 5 NZBLC 103,762 103,787 (HC)

> "A person is in a dominant position in a market when it is in a position to exercise a high degree of market control. A person in a dominant position will be able to set prices or conditions without significant constraint by competitor or customer reaction."

25. The Commission's *Business Acquisitions Guidelines* state:

> "A person is in a dominant position in a market when it is in a position to exercise a high degree of market control. A person in a dominant position will be able to set prices or conditions without significant constraint by competitor {or} customer reaction."
>
> …
>
> "A person in a dominant position will be able to initiate and maintain an appreciable increase in price or reduction in supply, quality or degree of innovation, without suffering an adverse impact on profitability in the short term or long term. The Commission notes that it is not necessary to believe that a person will act in such a manner to establish that it is in a dominant position, it is sufficient for it to have that ability." (p21)

26. The role of the Commission in respect of an application for clearance of a business acquisition is prescribed by the Commerce Act. Where the Commission is satisfied that the proposed acquisition would not result, or would not be likely to result, in an acquisition or strengthening of a dominant position in a market, the Commission must give a clearance. Where the Commission is not satisfied, clearance is declined.

27. The Commission applies the dominance test in the following competition analysis.

*Market Concentration*

28. An examination of concentration in a market provides an indication of whether a merged firm may or may not be constrained by others participating in the market, and thus the extent to which it may be able to exercise market power.

29. The *Business Acquisitions Guidelines* specify certain "safe harbours" which can be used to assess the likely impact of a merger in terms of s 47 of the Act -

> "In the Commission's view, a dominant position in a market is generally unlikely to be created or strengthened where, after the proposed acquisition, either of the following situations exist:
>
> the merged entity (including any interconnected or associated persons) has less than in the order of a 40% share of the relevant market;
>
> the merged entity (including any interconnected or associated persons) has less than in the order of a 60% share of the relevant market and faces competition from at least one other market participant having no less than in the order of a 15% market share." (p 17)

30. These safe harbours recognise that both absolute levels of market share and the distribution of market shares between the merged firm and its rivals is relevant in considering the extent to which the rivals are able to provide a constraint over the merged firm. The Commission went on to state that:

> "Except in unusual circumstances, the Commission will not seek to intervene in business acquisitions which, given appropriate delineation of the relevant market and measurement of shares, fall within these safe harbours."

31. Although, in general, the higher the market share held by the merged firm, the greater the probability that dominance will be acquired or strengthened (as proscribed by s 47 of the

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[4] *Commerce Commission v Port Nelson Ltd* (1996) 5 NZBLC 104,142 104,161 (CA)

[5] *Commerce Commission v Port Nelson Ltd* (1995) 5 NZBLC 103,762 103,787 (HC) and *Commerce Commission v Port Nelson Ltd* (1996) 5 NZBLC 104,142 104,161 (CA)

[6] *Business Acquisition Guidelines*, Section 7

Act), market share alone is not sufficient to establish a dominant position in a market. Other factors intrinsic to the market structure, such as the extent of rivalry within the market and constraints provided through market entry, also typically need to be considered and assessed.

32. Market share for the merged entity has been assessed in table 1 and 2 below.

**Table 1:**
**Estimated Market Share for the National Market for the Production or Importation of Merchant Steel Products**

| Firm | Tonnage | Market Share |
|---|---|---|
| Pacific Steel | [ ] | [ ] |
| OneSteel (imported) | [ ] | [ ] |
| **Sub-Total** | [ ] | [ ] |
| BHP NZ | [ ] | [ ] |
| Smorgon Steel | [ ] | [ ] |
| Imports | [ ] | [ ] |
| **Total** | [ ] | 100 |

33. The majority of this market is supplied by imports, while a small contribution is made by BHP NZ and Pacific Steel. The imports come mainly from Australia and Asia, including Korea, Japan, Taiwan, Singapore, and India. The associated companies will account for around [ ] of the market. Although, this is a reasonable share of the market, most of this is purchased by the merging entities. Second-tier players in general do not purchase significant amounts from OneSteel. Options remain open for competitors if they choose not to source from OneSteel. These options include Smorgons in Australia, and Asian steel mills. Given the relatively small quantities purchased by New Zealand steel merchants these steel mills could easily meet an increase in demand.

34. In addition, industry parties have advised that there is little real aggregation because Pacific Steel and OneSteel differ in the particular gauges and types of merchant products they produce. OneSteel tends to supply heavy structural steel, and hollows, whereas Pacific Steel produces light gauge merchant steel, such as angles and flats. The association of OneSteel and Pacific Steel is, therefore, unlikely to impact on the market to any significant extent.

35. Given the above facts, the Commission is satisfied the acquisition will not result, or be likely to result, in any person creating or strengthening a dominant position in this market.

**Table 2:**
**Estimated Market Share for the National Market for the Production or Importation of Reinforcing Steel**

| Firm | Tonnage | Market Share (%) |
|---|---|---|
| Pacific Steel | [ ] | [ ] |
| OneSteel | 0 | 0 |
| **Sub-Total** | [ ] | [ ] |
| Imports | [ ] | [ ] |
| **Total** | [ ] | 100 |

36. OneSteel has advised it does not supply any reinforcing steel to the New Zealand market. It advised that this is because [ ]. Steel merchants have advised that imports can be obtained from Japan and Thailand that meet the building standards.

37. OneSteel has advised the Commission that it could enter the market with a [ ] investment of around [ ]. The Commission, therefore, recognises OneSteel is a potential entrant to this market, would be removed if the acquisition were to go ahead.

38. However, given that there are mills in Japan and Thailand that already supply reinforcing steel to the market, they are likely to provide more of a constraint than OneSteel. Therefore, even if Pacific Steel was dominant in this market, the removal of OneSteel as a potential competitor is not considered sufficient to have strengthened that position. The Commission is thus satisfied the acquisition would not result in any person creating or strengthening a dominant position in this market.

39. In addition to its application, Steel and Tube has made further submissions in which it agrees with the conclusions reached by the Commission in previous decisions, notably Decision 376 and 378. The submissions also express the applicant's view on the production/importation level of the market. The submissions include the following points:

    - That the second-tier players at the distribution level are credible and effective competitors;
    - Barriers to entry in the distribution level are not insurmountable and, therefore, potential entry will offer some constraint to the merged entity; and,
    - Imports from a range of sources will continue to be available and provide alternatives to the merged entity.

## CONCLUSION

40. The Commission has considered the likely effects of the acquisition in the following markets:

- the national market for the distribution of merchant steel products;
- the national market for the distribution and fabrication of reinforcing steel;
- the national market for the distribution and processing of steel plate products;
- the national market for the distribution and processing of steel coil products;
- the national market for the manufacture and distribution of domestic roofing products;
- the national market for the manufacture and distribution of industrial roofing products;
- the national market for the production or importation of merchant steel products; and,
- the national market for the production or importation of reinforcing steel.

41. Having regard to the various elements of section 3(9) of the Act, and all other relevant factors, the Commission is satisfied that the proposal would not result, or would not be likely to result, in any person acquiring or strengthening a dominant position in any market.

## DETERMINATION ON NOTICE OF CLEARANCE

42. Accordingly, pursuant to section 66(3)(a) of the Commerce Act 1986, the Commission determines to give clearance for the proposed acquisition by Steel and Tube Holdings Limited, or any interconnected body, of up to 100% of the shares in Fletcher Steel Limited.

Dated this 27th day of April 2001

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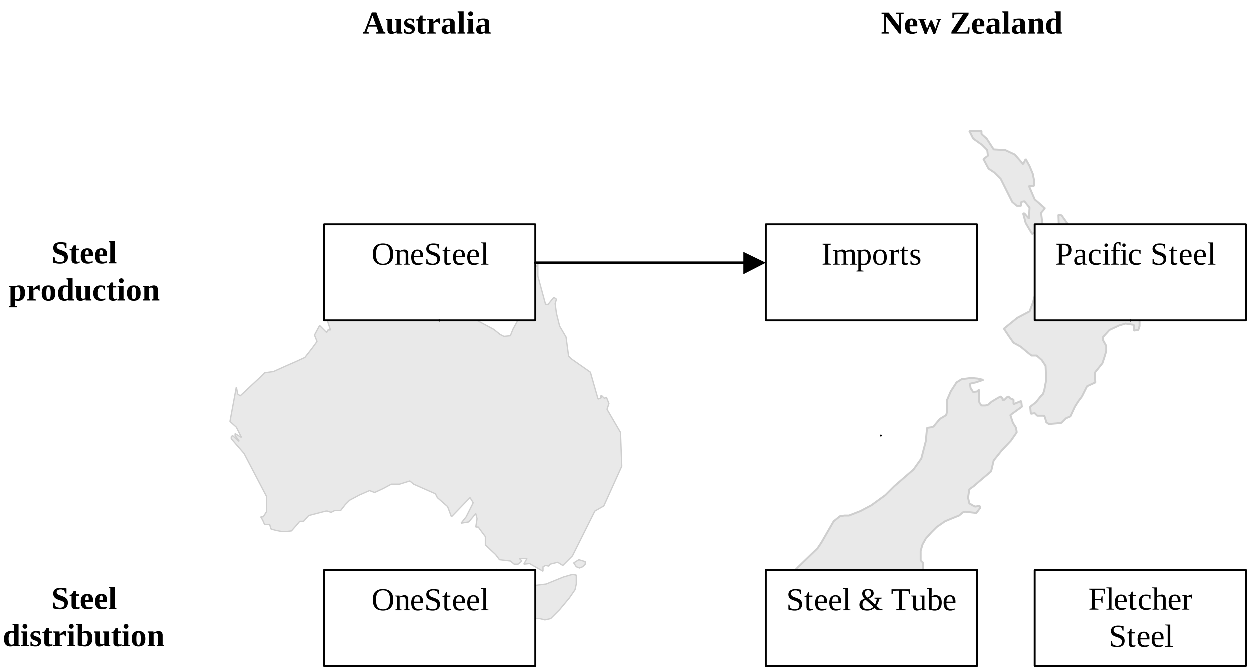
M J Belgrave
Chair

APPENDIX A


Australia
New Zealand
Steel production
OneSteel
Imports
Pacific Steel
Steel distribution
OneSteel
Steel & Tube
Fletcher Steel