
AGGREGATE INDUSTRIES
RESPONSE TO UPDATED ISSUES STATEMENT

CONTENTS

SECTION	PAGE
1. INTRODUCTION AND SUMMARY	3
2. ECONOMIC OUTLOOK.....	5
3. PROFITABILITY	6
4. MARKET DEFINITION	7
5. THEORY OF HARM 1: HIGH LEVELS OF CONCENTRATION AND BARRIERS TO ENTRY MEAN THAT THE SUPPLIERS CAN EXERCISE UNILATERAL MARKET POWER	10
6. THEORY OF HARM 2: COORDINATION BETWEEN PRODUCERS REDUCES OR PREVENTS COMPETITION.....	14
7. THEORY OF HARM 3: VERTICAL INTEGRATION AND EXCLUSIONARY BEHAVIOUR.....	17
8. POLICY AND REGULATION.....	18
9. CONCLUSION.....	19

1. INTRODUCTION AND SUMMARY

1.1 Aggregate Industries (*AI*) broadly agrees with a number of the preliminary views expressed by the Competition Commission (*CC*) in the Updated Issues Statement. At the hearing on 10 December the Chairman noted that the *CC*'s focus has “*turned away from rmx*” and that the “*approach on aggregates is, so to speak, to keep it in mind but again not to focus on it as much as we expect to focus on cement*”. Given the findings in the Updated Issues Statement, *AI* submits that there is no cause for the *CC* to investigate the aggregates or ready mix concrete (*rmx*) markets further.

1.2 *AI* is not surprised that the *CC* finds aggregates suppliers making low returns on capital employed and *rmx* suppliers making negative returns on capital employed.

1.3 The construction industry continues to suffer from the severe downturn that affected the UK economy at the end of 2008. The Government continues to reduce spend on infrastructure as part of its austerity measures: public sector net investment has fallen by 8% since 2007/08¹. Likewise, for the private sector, the Office for Budget Responsibility notes that, “*Set against weaker global prospects, ongoing uncertainty in the euro area and a tighter outlook for credit conditions, we have revised down our forecast for business investment growth since March.*”²

1.4 Construction output is at its lowest level for more than 10 years³. This has had a significant impact upon the demand for aggregates and *rmx*, which remains at its lowest level for the past 20 years. In the third quarter of this year, sales of crushed rock were down 4%, sand and gravel 11% and *rmx* 9%, against the same period last year⁴. At the same time, energy, raw material and regulatory costs have all risen.

1.5 Customers for aggregates are exerting significant pressure on returns as they have a choice of a number of suppliers and suppliers have excess capacity. According to the *CC*'s own analysis, over 90% of job sites have a choice of more than five suppliers and demand for aggregates over the last 5 years has fallen by over 25%⁵. *AI*'s own analysis confirms this result. As the *CC* has observed in its case studies, there is fierce competition for the remaining demand.

1.6 *Rmx* customers, likewise, have access to a number of alternative suppliers. More than 85% of *AI*'s *rmx* sales by volume are delivered to locations in which customers have a choice of three or more suppliers within an 8 mile radius. Furthermore the *CC* finds a lack of barriers to entry and that existing suppliers can expand output with ease. At a time when demand for *rmx* has fallen by approximately 35% in the last 5 years⁶, *rmx* returns have been placed under substantial pressure.

¹ HM Treasury, Public Sector Databank. Public Sector net investment was £29.1bn in 2007/08 and £26.7bn in 2011/12

² Economic and Fiscal Outlook Report, December 2012

³ Construction Products Association press release (November 2012)

⁴ Mineral Products Association (*MPA*) press release (October 2012)

⁵ *MPA* statistics

⁶ *MPA* statistics

1.7 In such fragmented markets, suffering a severe downturn in demand, tacit co-ordination in aggregates and rmx does not seem to be a credible concern. The features of the aggregates and rmx markets do not support co-ordination, namely: variation in competitive conditions between local markets; the low levels of concentration; the bi-lateral nature of negotiations with customers; the size and diversity of the customer base; the ease with which customers can and do switch suppliers; and the extent of excess capacity.

1.8 The CC's price concentration analysis and the CC's entry and exit analysis show that the presence of an additional supplier in a local aggregates market has little effect on prices and the Updated Issues Statement hypothesises that this finding could be consistent with co-ordination. AI considers that such a view would be a serious misinterpretation of the data. In fact this outcome reflects the dramatic fall in demand for aggregates over the last few years. Suppliers have spare capacity and can flex output quickly, and at little additional cost, in order to meet changes in demand. It is therefore no surprise that the presence or lack of an additional supplier makes little difference to prices in an already very competitive market.

1.9 With regard to cement, as the CC has recognised, AI does not produce cement in the UK. [REDACTED].

1.10 The CC has raised the possibility that vertical integration may support co-ordinated conduct in aggregates, lead to independent rmx producers being foreclosed from access to aggregates and/or raise barriers to entry in the rmx market. However, as no company has been identified as having market power in either the aggregates or rmx markets, and no evidence has been advanced of co-ordination in either market, it is difficult to understand how vertical integration could have such effects in theory; in practice the share of independent rmx producers is increasing, as the CC recognises.

1.11 In summary, the Updated Issues Statement identifies no feature, or combination of features, of the aggregates or rmx markets that prevents, restricts or distorts competition in the supply or acquisition of aggregates and rmx in the UK.

1.12 The rest of this response addresses the following points in more detail with regard to the aggregates and rmx markets in the UK:

- (a) the current economic outlook;
- (b) AI's profitability;
- (c) market definition;
- (d) the first theory of harm set out in the Updated Issues Statement, namely that high levels of concentration and barriers to entry mean that the suppliers can exercise unilateral market power;
- (e) the second theory of harm set out in the Updated Issues Statement, namely that coordination between producers reduces or prevents competition;
- (f) the third theory of harm set out in the Updated Issues Statement, namely vertical integration and exclusionary behaviour; and

- (g) the fourth theory of harm set out in the Updated Issues Statement, namely that aspects of policy and regulation may reduce or prevent competition.

2. ECONOMIC OUTLOOK

2.1 A sharp downturn in demand since 2008 has resulted in an unprecedented contraction in house building and infrastructure spend:

- (a) according to the Construction Products Association (*CPA*), construction output is at its lowest level for more than 10 years, private housing output in the third quarter was 10.6% lower than one year ago and infrastructure output was 11.3% lower⁷;
- (b) according to the Office for National Statistics, comparing the results for June to August this year as against the same period last year:
- (i) construction output has decreased by 11.9%;
 - (ii) new public housing has decreased by 20.7%;
 - (iii) new private housing has decreased by 12.1%; and
 - (iv) new infrastructure spending has decreased by 18.4%⁸.

2.2 The fall in construction output has had a severe effect on the demand for aggregates and rmx:

- (a) in the last five years, demand for aggregates has fallen by over 25% and demand for rmx has fallen by approximately 35%⁹; and
- (b) in the third quarter of this year alone, sales of crushed rock were down 4%, sand and gravel 11% and rmx 9%, against the same period last year¹⁰.

2.3 [✂] Unfortunately, as the statistics in paragraph 2.1(a) show, both public and private sector spending have dramatically declined.

2.4 Furthermore, there is no sign that the downturn is due to end any time soon:

- (a) the number of major road projects (costing more than around £1 billion) in the UK has declined from three, between 2001 and 2006, to none since 2007. Repair and maintenance budgets are also under pressure with most highways authorities top dressing and repairing rather than rebuilding roads;
- (b) the Chancellor, in his Autumn Statement 2012, announced an additional £1 billion to be spent on roads, additional spending on 100 new schools and funding to assist the building of up to 120,000 new homes. However, this will

⁷ CPA press release (November 2012)

⁸ Office of National Statistics, Output in the Construction Industry, August 2012

⁹ Based on MPA statistics

¹⁰ MPA press release (October 2012)

take time to get underway and the public procurement function remains frustratingly inefficient;

- (c) negotiations on the second high speed rail link do not seem to be close to resolution. In the last decade, expenditure on major rail projects (costing more than around £100 million) has decreased from around £10 billion between 2000 and 2005 to just £2.5 billion between 2006 and 2011;
- (d) no new airport runways are planned and political debate on whether, and if so where, to site additional runways is far from exhausted; and
- (e) in London, no new project is in the pipeline to replace the Olympics and many London authorities will have used their budgets for the replacement and repair of infrastructure for the foreseeable future.

2.5 In AI's view, the current market situation represents a permanent step change in market conditions. There is no realistic prospect of demand returning to levels seen pre-2008. Moreover, the long-run drivers of demand have changed:

- (a) steel, glass and timber, for example, are increasingly used as a replacement for rmx;
- (b) improvements in the design of buildings and houses, as well as better concrete specification, have also significantly reduced the demand for aggregates and concrete; and
- (c) demand for secondary and recycled aggregates and sustainable products has increased.

2.6 [✂]

3. PROFITABILITY

3.1 Customers for aggregates and rmx are companies active in the construction and infrastructure industries which have been hard hit by the recession. These companies have therefore been looking, more than ever, to squeeze the best possible terms from their suppliers. Combined with excess capacity resulting from the fall in demand, this has had a significant adverse effect on the returns earned by aggregates and rmx suppliers.

3.2 [✂]

3.3 [✂]

3.4 AI is therefore not surprised that:

- (a) The CC's "*preliminary profitability analysis of the Majors' aggregates operations across GB suggests that returns on capital employed have been low to modest across these businesses over the last five years...*". [✂]
- (b) The CC's "*preliminary profitability analysis of the Major's RMX operations suggests that the generally large returns on capital employed in 2007 have*

deteriorated a great deal since that time.” AI would go further to say, in its experience, returns on rmx operations are exceptionally low. [✂]

3.5 These findings are consistent with other evidence presented by the CC regarding the strength of competition in these markets. In particular:

- (a) analysis that shows aggregates and rmx customers have plenty of choice;
- (b) case studies that have revealed evidence of strong competition, even in apparently highly concentrated areas;
- (c) the lack of any finding of local market power in the price-concentration analysis¹¹; and
- (d) evidence of extensive excess capacity throughout the market, including the number of mothballed quarries and plants.

4. MARKET DEFINITION

Aggregates

Product Market Definition

4.1 AI agrees with the preliminary finding of the Updated Issues Statement that there is a single product market for all construction aggregates, including recycled and secondary aggregates.

4.2 There are, however, a few points of detail in the Updated Issues Statement with which AI disagrees.

- (a) The CC notes that sand and gravel may only be a partial substitute for crushed rock in general construction applications. Given the volume of sand and gravel produced in the UK, AI considers that a significant volume must be used for general construction purposes and that its use for these purposes has therefore been underestimated.
- (b) The CC notes that sand and gravel does not appear to be suitable for asphalt production. The use of sand and gravel in asphalt may be more or less prevalent by geographic region, but it is not accurate to suggest that sand and gravel are not good substitutes for crushed rock in asphalt applications. Natural sands are in fact a very good substitute for crushed rock fines in asphalt. Specifications are increasingly performance driven, rather than ingredient driven, thereby allowing for a high degree of substitutability of aggregates. [✂]
- (c) The CC notes that for the production of asphalt, there appears to be a substantial degree of substitutability between primary, recycled and secondary aggregates, although the figures may be inflated by the inclusion of asphalt planings¹². It is not clear to AI why the CC should exclude asphalt planings as

¹¹ CC aggregates PCA and EEA slides, slide 11

¹² CC working paper on market definition for aggregates, cement and RMX, paragraph 27c

these are not recycled just for the bitumen content but also for the aggregates. In fact asphalt plantings were first re-used in areas where aggregate was unavailable. Asphalt plantings can comprise up to 50% of new asphalt sub-base mixes and 20% of surface layers.

- (d) The CC notes that for rmx and concrete block production there seems to be little scope for substitution between primary, recycled and secondary aggregates. [§]. AI therefore considers that there is greater substitution between these product types than the Updated Issues Statement suggests¹³.
- (e) More generally the Updated Issues Statement underplays the competitive impact of secondary and recycled aggregates. According to the MPA, recycled and secondary aggregates have grown from 9% in 1989 to 28% in 2010. This growth has been aided by a number of schemes designed to encourage the use of recycled and secondary aggregates and standards that mandate the use of recycled and secondary materials.
 - (i) In 2002, for example, the Waste & Resources Action Programme (**WRAP**), funded by DEFRA, was launched to minimise demand for primary aggregates through the promotion of recycled and secondary sources. To ensure that demolition waste could be processed into aggregates of an appropriate quality that conformed with appropriate European standards, WRAP worked with the industry to formulate a quality protocol, the latest version of which was published in 2008 and an update is being consulted upon at the moment.
 - (ii) Similarly BREEAM (an environmental assessment method and rating system for buildings) has a stated aim to “*recognise and encourage the use of recycled and secondary aggregates, thereby reducing demand for virgin material and optimising material efficiency in construction.*” Credits are given for buildings that use more than 25% of certain recycled and secondary materials. This has had a major impact on demand for these materials.

Nor is it correct to state that recycled and secondary aggregates have hit a ceiling in terms of availability. There is a substantial volume of slate in north Wales, for example, which is used as a secondary aggregate. Furthermore, as noted above, specifications for projects increasingly require use of recycled and secondary materials. Given the lack of aggregates levy on recycled and secondary aggregates these products can also be transported further cost effectively.

¹³ AI notes that a third party has submitted that “*recycled aggregates were not suitable for use in the production of higher-strength concrete when quality assurance was an important consideration*”¹³. AI disagrees. Crushed glass sand (a recycled aggregate) and china clay waste (a secondary aggregate) were used by AI in higher strength mixes for the Olympics site. Furthermore, technological advances, in processing the material and in the end use for the material, is allowing recycled and secondary aggregates to achieve higher end- use specification and acceptance.

Geographic market definition

4.3 With regard to the size of the geographic market, the CC concludes that an appropriate definition for construction aggregates may be a radius of approximately 30 miles from the point at which the construction aggregates are produced (or from rail or water linked depots where they are stored).¹⁴ The CC uses a more conservative 20 mile radii in urban areas and 28 mile radii in non urban areas for its price-concentration and entry and exit analysis by road¹⁵ but, even on this basis, concentration is low (see paragraph 5.3 below).

4.4 Moreover, the use of rail increases the distance over which a quarry can cost effectively supply customers and increases choice for customers in the areas around the depots. [✂]

RMX

Product market definition

4.5 AI agrees with the preliminary finding of the Updated Issues Statement that there is a single product market for rmx that includes site plants and volumetric trucks.

4.6 The CC notes its initial view that volumetric trucks will be more competitive for smaller projects and site plants for larger projects. AI has, however, noticed volumetric trucks are increasingly used on large projects such as motorways and housing developments. Often the trucks will be used for certain aspects of large projects, particularly those that require potentially long waiting times on site. For example: JC Balls used volumetric trucks on the M1 widening contract and Amey switched from AI to Accumix, who used volumetric trucks, on the M5 corridor repairs.

4.7 Similarly, AI has noticed contractors on small projects increasingly purchasing cement and aggregates and mixing the ingredients themselves on site to produce rmx¹⁶.

4.8 The CC notes that it has “*some concerns about whether the competitive conditions may be different for customers requiring very large quantities of rmx, for example there may be fewer suppliers with the necessary capability (such as having several rmx plants in close proximity to the project) to supply such customers.*” AI does not believe any concern is warranted. These are a very small minority of contracts awarded following highly sophisticated procurement techniques by expert customers who are well able to safeguard their commercial interests.

4.9 Moreover, to the best of AI’s knowledge, independents operate approximately the same proportion of small plants as large plants. Independents operate

¹⁴ Updated Issues Statement, Paragraph 15.

¹⁵ CC aggregates PCA and EEA slides, slide 11

¹⁶ Roseville, for example, mix rmx on-site.

approximately 30% of plants with production below 40,000m³ and approximately 34% of plants with production of more than 40,000m³.

4.10 For a few very large projects, such as the Shard, the Olympics and Hinkley Point, security of supply is an issue for customers. Suppliers with an integrated supply chain and back up sources of supply will tend to have an advantage. [✂]

Geographic market definition

4.11 With regard to the size of the geographic market, AI agrees with the CC finding that the majority of customers are typically within 8 to 10 miles of an rmx plant.

5. THEORY OF HARM 1: HIGH LEVELS OF CONCENTRATION AND BARRIERS TO ENTRY MEAN THAT THE SUPPLIERS CAN EXERCISE UNILATERAL MARKET POWER

5.1 AI agrees with the broad conclusion of the Updated Issues Statement that the overwhelming majority of purchasers of aggregates and rmx have access to a large number of competing suppliers. Furthermore, most suppliers have excess capacity that can readily be flexed to meet changes in demand. Returns, as highlighted in section 3, are low. The aggregates and rmx markets do not therefore give rise to concerns of unilateral market power.

Aggregates

Customers have significant choice

5.2 The use of the term “major” when it comes to aggregates in the context of local markets is potentially misleading. Within a local area there will be a number of quarries of differing sizes and it is not the case a supplier with a national presence will always own the largest quarry.

5.3 The CC’s findings demonstrate that customers in almost all areas enjoy a wide choice of supplier. Using conservative 20 and 28 mile catchment areas (for urban and non-urban areas respectively), the CC finds that:

- (a) over 90% of job sites had a choice of more than 5 suppliers in 2011¹⁷;
- (b) only 8% of job sites were located in catchment areas in which the largest company had more than a 50% market share; and
- (c) only 18% of job sites were located in catchment areas in which the four largest companies collectively had a market share of more than 90%.

5.4 Of itself, this level of choice indicates that the features of the aggregates markets will not prevent, restrict or distort competition.

¹⁷ It is unclear whether these figures include all recycled and secondary sources which the CC finds are in the same market. If it does not then these figures under-represent the choice available to customers.

5.5 It is difficult for AI to comment further on the few areas of alleged high concentration without the CC identifying the areas in relation to which it has come to this finding. However, AI's own analysis shows that areas with fewer suppliers are invariably local markets with low demand or in some cases a lack of suitable available primary aggregates due to local geology. As set out in AI's response to the Issues Statement, the few areas with less than three alternative suppliers present (the Scottish Highlands and Snowdonia) are also sparsely populated areas with few customers. [✂]

5.6 Furthermore customers face minimal costs in switching supplier. There are no technical barriers that prevent customers switching supplier and generally contracts are not long term:

(a) supply in these markets tends not to be made under long term exclusive supply contracts. [✂]

(b) [✂]

5.7 The working paper, reporting the results of the CC's case studies, finds "*that the Majors are in fact competing as they focus on gaining market share or pursuing the competitors' customers to switch to their services.*"

5.8 [✂]

Barriers to expansion are minimal

5.9 In the last five years demand for aggregates has fallen by over 25%¹⁸ and [✂].

5.10 As noted earlier in this response, there are no indications that demand will recover to 2007 levels nor that the substantial spare capacity across the industry will be utilised any time soon. In that context barriers to entry are not of great relevance.

5.11 The key question is whether there are any barriers to expanding output. This is not the case. In the event that it is necessary to bring spare capacity back into use, production can be increased in several ways:

(a) first, by increasing production at a plant which is already open, but is not operating at its full capacity, [✂]. Furthermore, even if a quarry is operating at maximum permitted operating hours, production can still be increased by increasing the number of staff or installing additional equipment.

Production in this case can be increased almost immediately. The costs incurred are for additional labour and any additional equipment required.

A reduction in production is equally straightforward. There may be minor additional delay and cost due to redundancy processes.

¹⁸ Based on MPA statistics

- (b) Second, by reopening a mothballed plant. This would require:
- (i) checks on the site to ensure that all machinery and equipment is at an operational standard;
 - (ii) procurement of any machinery and equipment that is in need of replacement; and
 - (iii) re-employment of staff or reallocation from other sites.

Production in this scenario could be increased in 1 to 3 months. The costs incurred are for additional labour and any additional equipment required.

[✂]

A reduction in production is equally straightforward. There may be minor additional delays and costs due to redundancy processes.

- (c) Third, by expanding an operational plant. This involves design, procurement, planning and commissioning, and can take between 6 months and 2 years, depending on the complexity of the planned expansion. If planning permission is required, the timeframe could be longer. The cost of a major expansion would be between £300,000 and £3 million.

5.12 Given the downturn there is spare capacity throughout the industry that can be readily flexed to meet additional demand.

Barriers to entry are not an issue

5.13 As noted above, local markets are not highly concentrated and in markets with excess capacity where supply can readily be scaled to meet demand at little cost, barriers to new entry are not particularly relevant.

5.14 Nevertheless, AI agrees with the CC when it finds that the availability of primary aggregates resources is not a barrier to entry, that the cost of developing a new site is not prohibitive, and that government policy regarding aggregates landbanks is unlikely to be distorting competition in local aggregates markets. Moreover, as the CC notes, the new planning guidance issued by the Department for Communities and Local Government states that adequate landbanks should not be used as a reason for declining a planning application.

5.15 Furthermore, the planning process for a new quarry applies equally for all applicants. In fact MPA figures on planning applications for all new quarries show that small companies may be more successful in obtaining planning permissions than large companies. According to the MPA there were 51 planning applications in England, Scotland and Wales between 2000 and 2008, of which 41 (78%) were successful. The MPA reports that for large companies (companies with more than 1,000 employees) the success rate was 77% and for small companies (less than 1,000 employees) the success rate was 100%.

Price concentration analysis and entry-and-exit analysis

5.16 In such circumstances it is not surprising that the presence of an additional major, independent, secondary or recycled aggregates supplier has little effect upon prices. As most suppliers have spare capacity and output adapts quickly to match changes in the level of demand, there is no scope for suppliers to increase prices without this leading to a response by rivals with nearby spare capacity.

Conclusion

5.17 In summary, the CC has not identified unilateral market power as a feature of the aggregates markets in the UK. Local markets are competitive as a large number of different suppliers, independents as well as larger companies, with excess capacity chase falling demand. Even in areas that the CC considers potentially highly concentrated it found in its case studies that “*both Major and non-Major aggregates suppliers are competing with each other in these areas to gain market share and/or persuade competitors’ customers to switch suppliers.*” Ultimately the low returns earned by aggregates suppliers on capital employed provides strong evidence that suppliers cannot exercise unilateral market power.

Rmx

Concentration is low

5.18 The CC notes that the highest market share held by any major rmx producer in a county is 56% but that not all major rmx producers are present in all counties and in some counties independent rmx producers have significant market shares.

5.19 [✂]

5.20 Furthermore customers face minimal costs in switching supplier. Supply in these markets tends not to be made under long term agreements. [✂]

Barriers to entry are minimal

5.21 AI agrees with the view that there are no significant barriers to entering rmx markets. Even in a market characterised by falling demand and overcapacity, there has been entry reflecting the low capital expenditure requirements and know how required to supply rmx:

- (a) the Office of Fair Trading found that the number of independent suppliers has grown steadily since 2000 with 23 new suppliers entering between 2005 and 2009; and
- (b) as the CC notes, the market share of the independent rmx producers has grown between 2008 and 2011.

5.22 Furthermore, as the CC states, there are few barriers to expanding the output of a rmx plant within its existing capacity, not least as most rmx plants are currently operating well below their maximum productive output.

Conclusion

5.23 In summary, customers have access to a number of alternative sources of supply for rmx and barriers to entry in the rmx markets are low. Areas in which customers enjoy less choice are remote, so there is insufficient demand to support more suppliers. AI therefore agrees with the conclusion of the CC that unilateral market power is not a feature of the rmx markets in the UK. With the downturn there is currently significant excess capacity which has driven down returns on capital employed. [✂]

6. THEORY OF HARM 2: COORDINATION BETWEEN PRODUCERS REDUCES OR PREVENTS COMPETITION

6.1 The CC quotes, from its draft Market Investigation Guidelines, that “*a market must exhibit certain characteristics for coordination to be possible*”, namely:

- (a) “*Firms need to be able to agree and monitor the terms of coordination...*”;
- (b) “*Coordination needs to be internally sustainable among the coordinating group—ie firms have to find it in their individual interests to adhere to the coordinated outcome*”; and
- (c) “*Coordination needs to be externally sustainable, in that coordination is unlikely to be undermined by competition from outside the coordinating group or from the reactions of customers.*”

6.2 In addition to exhibiting the relevant characteristics, however, under the statutory test the CC also needs to satisfy itself that co-ordination in fact occurring. AI does not consider that the features of the aggregates and rmx markets support co-ordination nor that there is any evidence of co-ordination occurring.

Aggregates

6.3 The CC finds, and AI agrees, that the following features of the aggregates markets would make it difficult to agree and sustain co-ordination among suppliers.

- (a) “*Aggregates markets are, however, local (see paragraph 15), which means that there is geographical differentiation between aggregates produced at different locations.*”
- (b) “*Competitive conditions (eg the number and nature of competitors) may vary from one local area to another.*”
- (c) “*There are also a large number of non-Major aggregates suppliers across GB, supplying a fragmented customer base (ie there are a large number of different suppliers and customers).*”
- (d) “*Customers tend to purchase aggregates on a project-by-project basis and prices are negotiated bi-laterally.*”

6.4 The CC notes that the following structural features may be conducive to coordination. AI does not agree.

- (a) *“concentration in the supply of aggregates at a national level.”* However, the national market share figures show no symmetry between the top five suppliers that would result in an alignment of incentives. Tarmac, the largest supplier of aggregates, had a share of 20.8% of primary production in 2010 whereas Lafarge, the smallest of the top five suppliers, had a share of only 7.8%¹⁹. The difference in share between Tarmac and Lafarge (13%) is much larger than the difference in share between Lafarge and the largest independent Breedon (5.3%). Furthermore, the national market share figures produced by the CC do not appear to take account of the presence of recycled and secondary producers. In any event, these are local markets that are not concentrated.
- (b) *“a high share of the market held by the five GB Majors in some local aggregates markets”.* As noted above the CC finds that over 90% of job sites had a choice of more than 5 suppliers in 2011. Suppliers currently have excess capacity and the ability to quickly and cost effectively increase output should customers wish to switch. There are no barriers to customers switching as aggregates tend to be purchased on a project by project basis. There is no indication that a high local share of volume translates into any market power or market stability. In any event, market conditions in those somewhat more concentrated areas, are typically explained by objective reasons to do with geological features and population density, rather than strategic behaviour.²⁰
- (c) *“structural links between the Major aggregates suppliers, including joint ventures and membership of a common trade association”.* [§]. Membership of trade associations is common among many industries so AI assumes that the CC is not suggesting that membership of the MPA is a concern *per se*. The CC will no doubt satisfy itself as to the MPA’s compliance procedures.
- (d) *“barriers to entry into aggregates supply (see paragraphs 27 and 28) may be sufficiently high that entry would be unlikely to undermine any coordination”.* As noted above barriers to expansion are low and in any event there is currently excess capacity, held by a wide range of different suppliers, which could quickly and cost effectively be used to increase output in response to a customer looking to switch. Furthermore, the CC has found that the availability of primary aggregates resources is not a barrier to entry, that the cost of developing a new site is not prohibitive, and that the policy regarding aggregates landbanks is unlikely to distort competition in local aggregates markets.
- (e) *“although there are many different sub-types of aggregates, within each sub-type the aggregates produced by different suppliers are largely homogenous”.* [§]. Furthermore, suppliers are all looking to distinguish their offer with the

¹⁹ BDS Market Research 2010.

²⁰ AI notes that, if nearly all markets have a large number of different suppliers and in some markets the largest supplier has a large share, market shares at the local level are unlikely to be symmetric.

services that they provide in these difficult trading conditions. Other matters that affect the nature of supply include haulage, timing, volume, frequency, duration of contract, creditworthiness, day or night delivery, up front or delayed payment, waiting time, testing fees, small load fees, etc. Co-ordination would therefore be practically much more difficult than the Updated Issues Statement suggests.

6.5 The CC has analysed whether aggregates price announcement letters sent out by the major aggregates suppliers may play a part in sustaining co-ordination. However, the CC finds “*no single overall pattern to the Majors’ announcements*”. Furthermore the CC finds that “*In almost all the cases that we analysed, the majors were able to increase the average price of aggregates following a price increase announcement, although the actual increase was usually lower than that announced*”.

6.6 Not only was the actual price increase achieved lower than that announced but there is no obvious relationship between the size of the increase requested and the size of the increase achieved. Furthermore, different customers will end up paying different increases depending upon their specific circumstances and outcome of bilateral, individualised negotiations. Moreover, any achieved price increases likely reflect increases in input costs, given that the CC has observed that margins have remained broadly constant over the period. The inherent variation and lack of transparency of prices achieved would make it highly unlikely that any coordination could be sustained.

6.7 [✂]

6.8 Finally the CC notes that lack of correlation between prices and the number of major aggregates suppliers or independents in a local area is “*consistent with coordination in at least some local aggregates markets (although other explanations are also possible)*.” As noted above, AI disagrees with this interpretation of the CC’s results, which is at odds with a range of evidence identified by the CC concerning the competitiveness of these markets, including significant excess capacity and low returns on capital employed. The CC’s case studies have shown that, even in areas of allegedly high concentration, competition between aggregates suppliers is intense.

6.9 In summary, it would be highly complex to organise and difficult to sustain tacit co-ordination across multiple local aggregates markets, with:

- (a) differing competitive conditions;
- (b) with a highly fragmented customer base;
- (c) bi-laterally agreed prices on a project by project basis;
- (d) an extensive choice of suppliers;
- (e) the ease with which customers can switch;
- (f) a lack of structural links between AI and other Major aggregates producers;
and
- (g) excess capacity that can be easily flexed to meet changes in demand

6.10 If the CC has particular concerns about co-ordination occurring in a specific local market, AI would be happy to respond to them. Without that clarification and opportunity for further comments the CC cannot sustain this theory of harm.

Rmx

6.11 The CC in the Updated Issues Statement finds that *“The supply of RMX in GB appears to have fewer structural features than in the case of aggregates or cement that might give rise to concerns about coordination.”* The CC does not specify any market features that may give rise to concerns about coordination.

6.12 The CC notes that there is some evidence that the major rmx suppliers may collectively hold a high share in some local rmx markets. The CC, however, has not, as far as AI understands, undertaken a local market analysis. Furthermore, as stated above, AI does not consider, in markets in which there is significant excess capacity to meet customer switching, that shares of local volume indicate market power. The CC itself notes that *“the lack of barriers to entry into RMX supply (see paragraphs 58 to 61) coupled with the complexity of maintaining coordination in multiple local RMX markets reduces our concerns about the possibility of coordination in RMX markets in isolation.”*

6.13 The CC finds no evidence of co-ordination in fact occurring. The CC finds that returns on capital employed in rmx are negative. There is therefore no evidence to substantiate a finding that tacit co-ordination is a feature of the rmx markets that prevents, restricts or distorts competition.

7. THEORY OF HARM 3: VERTICAL INTEGRATION AND EXCLUSIONARY BEHAVIOUR

7.1 The CC states that its *“concerns about vertical integration currently include the possibility of unilateral foreclosure, coordinated foreclosure, increased barriers to entry and the facilitation of coordination in the cement market.”*

7.2 With regard to the concerns about unilateral and coordinated foreclosure of aggregates to rmx producers, the CC has found no unilateral market power or co-ordinated conduct in the supply of aggregates, while the share of independents is increasing. It is therefore difficult to understand how there could be a foreclosure concern and AI agrees with the intention of the CC not to pursue these lines of inquiry further.

7.3 With regard to increased barriers to entry, the CC appears to have two possible concerns:

- (a) first, insecurity might be created for a new entrant regarding its supplies of aggregates from a supplier which is also a competitor in rmx. However, as noted above suppliers of aggregates do not hold unilateral market power and purchasers of aggregates have a significant choice of supplier. This foreclosure concern therefore seems unmerited in theory and unevidenced in practice; and

- (b) second, vertical integration into aggregates might result in significant efficiencies in rmx production making it more difficult for non-integrated rmx producers to compete. AI believes that increased vertical integration has brought benefits to customers and has helped AI develop and bring value added products to customers with the confidence that it has a supply chain capable of delivering the necessary inputs. However, it has not prevented competition from independent rmx producers. As the CC notes, the market share of the independent rmx producers has grown between 2008 and 2011. Therefore this theory is not borne out by the available evidence.

7.4 The CC has found that [REDACTED].

7.5 With regard to the concern that vertical integration may facilitate upstream co-ordination in aggregates, as noted above the features of the aggregates markets do not support co-ordination nor is there any evidence of co-ordination occurring. The idea that supplies of aggregates between majors across multiple local aggregates markets for use in multiple different rmx markets; in which the competitive conditions differ market to market and; where prices are agreed in bilateral negotiations on a project by project basis, increases transparency and the opportunity to punish deviations from a common understanding, has little credibility. No evidence has been advanced to support this proposition in any event. Furthermore, independent rmx producers have access to a number of competing suppliers, all with excess capacity and earning low to negative returns on capital, making it highly unlikely that such co-ordination would be sustainable.

8. POLICY AND REGULATION

8.1 The Updated Issues Statement notes that the Carbon Reduction Commitments (**CRC**) (together with Climate Change Agreements and the Climate Change Levy) “*could have different impacts on different types of producers of the reference products, causing some differences in their cost bases and possibly some distortion in competition.*”

8.2 The CRC does indeed have a distortive effect on competition. As the CC notes, installations covered by the EU Emissions Trading Scheme (**ETS**) are exempted from the CRC. Large cement producers in the UK are therefore exempted from the CRC. Furthermore, small aggregates producers below the electricity consumption threshold of 6,000 MWh are also not subject to the CRC. As a result, only medium to large size aggregates producers, with no cement production activities, such as AI, are subject to the CRC.

8.3 This distortion has been further exacerbated by Government’s response to the recent consultation on simplifying the CRC energy efficiency scheme, under which Government will now disapply the CRC rules on the supply of energy to facilities covered by the EU ETS (such as cement plants).²¹

²¹ Her Majesty’s Government, *Consultation on simplifying the CRC Energy Efficiency Scheme: Government response* (December 2012), paragraph 95.

9. CONCLUSION

9.1 As set out in this response, the CC has not established that there are any features of the aggregates or rmx markets that result in an adverse effect upon competition. There is no evidence of higher prices, lower quality, less choice or less innovation. The low returns on capital at a time of exceptionally low demand show that suppliers are not benefiting from any prevention, restriction or distortion of competition.

9.2 AI therefore urges the CC to consider whether there is sufficient compelling evidence that, on the balance of probabilities, supports a finding that there is a feature, or combination of features, of the aggregates and rmx markets, that prevents, restricts or distorts competition in connection with the supply or acquisition of aggregates or rmx in the UK. To the contrary, the evidence would support provisional findings in these markets that no such features exist.
