

MITTAL INVESTMENTS SARL

Competition Commission inquiry into aggregates, cement and ready-mix concrete

Response to Provisional Remedies Decision

1. Introduction

- 1.1 This document sets out the response of Mittal Investments S.à.r.l. (Mittal) to the Provisional Decision on Remedies (PDR) published by the Competition Commission (CC) on 8 October 2013.
- 1.2 Mittal's response addresses the CC's provisional decision to bar Mittal from acquiring the cement and GBS/GGBS assets to be divested by Lafarge/Tarmac and Hanson, respectively (the Divestiture Assets), as a remedy for the adverse effects on competition (AEC) identified by the CC in the GB bulk and bagged cement markets.¹
- 1.3 This response is supported by an expert report prepared by AlixPartners on the economic merits of the CC's provisional decision to exclude Mittal (the Alix Report). This is attached as Appendix 1.

2. Summary:

- 2.1 Mittal believes that it should not be prevented by the CC's final remedies decision from bidding for any and all of the Divestiture Assets and that the appropriate time for the CC to assess Mittal's suitability as a purchaser of these assets is during the divestiture process, in the CC's purchaser suitability assessment. This is the same position that the CC intends to take as regards all

¹ Provisional Decision on Remedies, s 4(a)(ii) and 4(d)(iii)

other prospective purchasers, including Aggregate Industries². Mittal's reasons are as follows.

2.2 None of the PDR, the Provisional Findings (PFs), or the Addendum to the Provisional Findings (Addendum) adequately explains the CC's justification for excluding Mittal and for requiring a fifth competitor in the GB bulk and bagged cement markets. In particular:

- a) The CC has accepted that Mittal's acquisition of the Divestiture Assets would lead to an “*important structural change*” and would increase the market share of non-coordinating firms relative to the coordinating group, even if, in the CC's view (which Mittal disputes), Mittal's acquisition would not be as effective as an acquisition by a non-GB cement producer³.
- b) The CC's analysis as to why Mittal should be excluded is limited to a single of text⁴, with no reference to any of its provisional findings, and without regard to the overall effects of the package of remedies.
- c) The CC has not examined Mittal's strength as an existing fourth, non-coordinating competitor. There is no proper consideration of whether and how the expansion of Mittal's capacity through its acquisition of Divestiture Assets could remedy the AEC identified by the CC. Nor has the CC considered how prohibiting Mittal's acquisition would assist in remedying the AEC.
- d) There is no comparative analysis of the relative benefits of a fifth player as against Mittal as an enhanced fourth player, particularly since any other new owner would at best be a single plant operator.
- e) No consideration is given to the combined effect of the other remedies proposed by the CC and a purchase by Mittal of the Divestiture Assets.

² Provisional Decision on Remedies, s 3.165(c)(i)

³ Provisional Decision on Remedies, s 3.24 and 3.28

⁴ Provisional Decision on Remedies, 3.28

- f) The CC has not specifically considered Mittal's suitability as a purchaser of the Divestiture Assets under any of the usual suitability criteria, nor under the criteria set out in 3.165 of the PDR, which remain subject to consultation.

2.3 The CC relies on an assertion that the relevant markets would be less transparent with a new fifth player in the relevant markets⁵. However, as set out in more detail in the Alix Report, simply counting the number of competitors is not economically meaningful⁶:

- a) Increasing the number of independent competitors does not of itself remedy any of the features enabling the co-ordinating group to identify and monitor a co-ordinated outcome amongst themselves⁷.
- b) Nor does it impact on any of the features contributing to the internal stability of a co-ordinated outcome⁸.
- c) As regards the external stability of a co-ordinated outcome⁹:
 - i. The CC's own merger guidelines suggest that four competitors might be sufficient.
 - ii. The CC does not consider the possibility that small competitors may be less effective rivals, notwithstanding its own guidance that *"counting firms or fascias does not take into account differences in market shares or the size difference of firms"* and that *"External sustainability will typically be easier where the competitive fringe does not impose a strong competitive constraint and is unlikely to be able to expand."*¹⁰
 - iii. Any fifth competitor would be small and so may be less effective – the CC has made exactly the same comments about the lack of

⁵ Provisional Decision on Remedies, 3.28

⁶ Alix Report, s 1.13 and 1.14 and Section 4

⁷ Alix Report, s 4.8-12

⁸ Alix Report, s 4.13-14

⁹ Alix Report, s 4.15-25

¹⁰ *"Merger Assessment Guidelines"*, at s 5.3.4 and 5.5.18 respectively.

external competitive constraint provided by Tarmac (pre-2013) and Mittal (post-2012), focusing on the fact that both have only a single plant. Given the CC's view that Mittal's ability to compete is compromised by the fact that it has a single plant, why will a similarly compromised fifth competitor provide greater competitive constraint than a strengthened fourth competitor?

- iv. A stronger fourth competitor could engender greater competition.

These issues, and the interaction of the other remedies in the CC's proposed package with the divestiture remedies, are also not addressed by the CC in its PFs, PDR or Addendum. In particular, the CC has not addressed why there is an appreciably greater likelihood of coordination if Mittal, rather than another prospective purchaser, acquires further assets given that

- i. the remedies package reduces market transparency and thus the ability of the co-ordinating firms to reach and monitor any co-ordination;
- ii. Lafarge's incentives to adhere to the coordinated terms will be reduced as it will lose its position of market leadership due to any divestment; and
- iii. external competition will increase due to the growth of competition in the GGBS supply chain and from other cement suppliers.

2.4 Mittal, consequently, has not had the opportunity to express its views about a decision which directly and adversely affects Mittal's interests, nor to advise the CC of the implications of that decision for Mittal's Hope Construction Materials business.

2.5 Mittal believes that its acquisition of the Divestiture Assets would be pro-competitive. It would gain sufficient flexibility and economies of scale to compete aggressively with Lafarge/Tarmac, Cemex and Hanson. [§]. There can be no assurance that if Mittal is barred from bidding for the Divestiture Assets a viable fifth competitor will emerge or that any potential fifth

competitor will satisfy the CC's suitability requirements. Mittal's acquisition of some or all of the Divestiture Assets may prove to be the most pro-competitive alternative.

- 2.6 CC's decision to bar Mittal from bidding for the Divestiture Assets is premature and unnecessary for the realization of the structural changes in the GB cement market the CC seeks to achieve. The suitability of any proposed purchaser of the Divestiture Assets does not have to be determined until after the CC has taken a final remedies decision and after any proposed purchaser has had the opportunity to assess and bid for the Divestiture Assets and to explain to the CC how it proposes to employ those assets to compete.
- 2.7 Mittal has been supplying bulk cement in GB for only ten months. At the time CC assesses proposed purchasers, Mittal will have at least a full year's results and track record and a revised business plan. CC's decision as to whether Mittal should be allowed to acquire the Divestiture Assets should be made then, based on the latest available information, not now.
- 2.8 Finally, Mittal considers that its exclusion from acquiring any of the Divestiture Assets would be disproportionate and reduce the purchase price which will be achieved.
- 2.9 Mittal's reasons are set out in more detail below.

3. Background

- 3.1 Mittal has been supplying bulk cement in GB through two subsidiaries trading as Hope Construction Materials (HCM), for under ten months. HCM's business comprises the production and supply of cement, concrete, aggregates and asphalt in the UK. It started operating in January 2013, more than a year after the end of the period (2007-11) over which the CC has assessed competition in the GB bulk and bagged cement markets.
- 3.2 Mittal's aim is for HCM to develop as a strong independent competitor in the GB bulk and bagged cement markets, [REDACTED]
- 3.3 HCM operates one cement plant, at Hope in Derbyshire. The Hope cement plant has [REDACTED] to increase production when the construction industry emerges from recession. Lafarge/Tarmac, Cemex and Hanson, on the other hand, all have significant latent capacity, as demonstrated in Table 4 on p14 of the GGBS and GBS Addendum. This table shows that in 2011 Hope had a 15% share of the cementitious market. If the market were to be restored to 2007, pre-recession, levels, Hope would have only a 10% share.
- 3.4 In establishing itself in the relevant markets, HCM has taken account of the concerns expressed by the CC in relation to co-ordination. In particular, it has not adopted the other producers' practices of issuing price increase letters. It has joined the MPA to benefit from the MPA's lobbying activities, but on a temporary basis, for an initial six months, pending the outcome of the CC's inquiry.
- 3.5 The CC has expressly recognized HCM's independence by referring to it in the PDR as a non-co-ordinating producer.
- 3.6 Mittal's intention has always been to expand its presence in the GB cement markets, as the CC is aware from Mittal's submissions to it.
- 3.7 The CC's decision, if implemented, will deny Mittal an opportunity to acquire any of the Divestiture Assets and thereby heighten the intensity with which

HCM competes with the co-ordinating producers in the relevant markets. The expanded capacity would give HCM [✂]

4. No adequate explanation of the CC's justification for preventing Mittal from acquiring the Divestiture Assets

A The CC has accepted that an acquisition by Mittal would be effective

4.1 The PDR does not explain the CC's rationale for barring Mittal from acquiring any Divestiture Assets. s 4(a)(ii) and 4(d)(iii), under the rubric *Suitable purchaser*, state that a purchaser of Caudon or Tunstead cement works and of any GGBS plant or GBS plant cannot be one of the existing GB cement producers and that this will facilitate the entry of a fifth and independent GB cement producer. No distinction is made between Lafarge/Tarmac, Cemex and Hanson, as co-ordinating producers, and HCM, as a non-co-ordinating producer that has not contributed to the AEC.

4.2 The CC's rationale for its decision not to permit Mittal to acquire a divested cement plant, as stated in 3.24, is that the divestiture of a cement plant would be "*substantially enhanced*" if it were to increase the number of GB cement producers. The CC states that it did not consider that a divestiture to HCM would be "*as effective a remedy as HCM already owns a cement plant*". The CC goes on to say in 3.28 that a remedy that increases the number of GB cement producers "*would be more effective at reducing market transparency and disrupting the strategic interdependence of the co-ordinating firms than a remedy that resulted in the expansion of HCM*".

4.3 The CC has clearly not ruled out the possibility that Mittal's acquisition of the Divestiture Assets could be effective in reducing market transparency and in disrupting the interdependencies of the co-ordinating firms. The CC states in 3.24 that the divestiture would result in a limited but important structural change in the GB cement market that would "*increase the share of the GB cement markets held by a non-co-ordinating producer or producers, relative to the co-ordinating group*." That change could be achieved by a divestiture to Mittal as well as to a new market entrant. 3.164, despite referring to the exclusion of Mittal, concludes by referring to "*potential purchasers interested*

in the opportunity to enter, or expand their presence in the GB cement markets (emphasis added)".

- 4.4 In light of the fact that the CC considers a divestment to Mittal to be effective, albeit in the CC's view not as effective as a divestment to a purchaser other than a GB cement producer (which Mittal disputes), it is not clear why the CC has chosen to rule Mittal out.

B The CC's assertions

- 4.5 The CC's decision to prohibit Mittal from acquiring any of the Divestiture Assets appears to rest on the fact that HCM already owns a cement plant and that a fifth player would be more effective¹¹.

C The absence of any justification for the CC's assertions

- 4.6 The CC does not, however, consider the merits of an acquisition by Mittal in either absolute or comparative terms. It moves from stating in 3.24 of the PDR that an acquisition by Mittal would not be "*as effective*" as an acquisition by a fifth player, to stating in 3.164 that it had "*earlier ruled out existing GB cement producers including MI (HCM) as suitable purchasers*" without in the interim providing any proper analysis of an acquisition by Mittal, nor any indication of the point at which what it appears to present in 3.164 as a final decision to rule Mittal out was made.

- 4.7 The PDR does not contain any analysis of whether and how the expansion of HCM's capacity through its acquisition of Divestiture Assets could remedy the AECs the CC has identified in the relevant markets. The PDR also provides no analysis why an acquisition by Mittal would not remedy these AECs. The PDR offers no assessment of the ability of an expanded HCM to reduce cement market transparency – particularly in light of the other remedies the CC is proposing, including restrictions on the disclosure of GB cement data and a prohibition on generic cement price announcements – or to disrupt the strategic interdependence of Lafarge/Tarmac, Cemex and Hanson. Without

¹¹ Provisional Decision on Remedies, 3.24

that analysis, precluding HCM's acquisition of Divestiture Assets is at best premature.

4.8 Mittal also expected to see in the PDR a detailed comparison of the merits of an acquisition by Mittal on the one hand and an acquisition by a fifth player on the other. There is no such analysis. Without it, the CC's decision to bar Mittal from acquiring Divestiture Assets, on the basis their acquisition by a fifth market entrant would be more effective, is unreasonable.

5. **The CC's rationale for requiring divestiture to a fifth competitor**

5.1 The Alix Report in Appendix 1 addresses the absence of any economic justification for the CC's prohibition on an acquisition by Mittal and requirement that the Divestiture Assets be sold to a fifth player.

5.2 Mittal notes that Lafarge operated the Hope Cement facility at maximum capacity prior to its sale to HCM to enhance the attractiveness of that divestment to the CC and Mittal. If Hope expands its capacity to beyond historic maximums, Hope might be able to produce [REDACTED]. Extrapolating from Table 4 on page 14 of the GGBS and GBS Addendum, Mittal estimates that, [REDACTED], the fourth and fifth cement producers will have likely market penetration of [REDACTED]% and [REDACTED]%, respectively, with the co-ordinating producers sharing [REDACTED]% of the market less any imports. Imports in [REDACTED] were approximately [REDACTED] and, therefore, the big three would have a market penetration of circa [REDACTED]% [REDACTED]. Mittal does not find the argument compelling, in these circumstances, that a fifth market entrant would materially decrease the adverse economic effect of co-ordination by the co-ordinating producers. In any event, HCM with [REDACTED]% market share [REDACTED] as HCM with [REDACTED]% and a fifth competitor with [REDACTED]%.

6. **No prior discussion and no consultation with Mittal**

6.1 The CC has not engaged in any substantive discussion directly with Mittal in relation to the exclusion of Mittal as a purchaser of any of the Divestiture

Assets. It is not clear to Mittal whether the CC has already decided this, as 3.164 of the PDR suggests¹², or whether it is still provisional.

6.2 A decision by the CC to exclude Mittal directly and adversely affects Mittal's interests. Mittal has not had the opportunity to express its views about such a decision, nor to advise the CC of the implications of that decision for HCM.

7. The decision to bar Mittal from acquiring the Divestiture Assets is premature

7.1 Mittal is not asking the CC to promote it as a suitable purchaser, but is asking the CC to afford Mittal the chance to show that it would be a suitable purchaser should it wish to bid for the Divestiture Assets.

7.2 The CC is not obliged by statute to make a decision now. It is also not necessary or desirable for the CC to rule Mittal out of bidding for the Divestiture Assets at this stage. Assuming the CC decides after consultation that divestiture is an appropriate remedy, the divestiture process that takes place after its final decision will provide the CC with ample opportunity to consider Mittal's suitability as a purchaser. That assessment would be based on information up to the date of the final decision, when the Divestiture Assets have been finally identified, the identity of potential purchasers is known and their business plans and capabilities have been prepared.

7.3 Under a typical divestiture process, no decision would be made as to the suitability of any potential purchaser of the assets to be divested until:

- a) the scope of the divestiture package had been fully settled;
- b) the prospective purchaser had had a chance to carry out due diligence and had made an offer; and
- c) the purchaser had had a chance to make submissions in response to the CC's purchaser suitability criteria and demonstrate how it would use the divested assets to compete in the relevant markets.

¹² Provisional Decision on Remedies, 3.164: "... we earlier ruled out existing GB cement producers including MI (HCM) as suitable purchasers..."

7.4 In excluding Mittal from the range of potential purchasers now, the CC has made a decision against Mittal without going through the CC's normal process. This:

- a) denies Mittal the opportunity to be assessed fairly as a suitable purchaser based on Mittal's particular characteristics and proposals, which the CC has not taken into account in making the decision to bar Mittal from acquiring the Divestiture Assets; and
- b) precludes the CC from assessing Mittal's suitability in the ordinary course after potential buyers bid for the Divestiture Assets, when Mittal's position as a non-co-ordinating producer will be considerably clearer and there will be a greater volume of information available to enable the CC to assess Mittal's candidacy.

8. **Mittal would be a suitable purchaser**

8.1 If the CC excludes Mittal now, it may be precluding the most competitive solution to the structural issues in the GB cement industry.

8.2 Mittal believes that an acquisition by HCM has greater potential to address the AEC identified by the CC than an acquisition by a fifth competitor.

- a) HCM has already introduced a new competitive dimension into the GB cement markets, on price and quality of service, as can be seen from the comments made by its competitors and customers to the CC.¹³

[✂]

- b) It is independent in its approach, as supported by the content of a) above.

Mittal is committed to the GB cement markets, having made a substantial investment in then earlier this year. Mittal has the expertise and resources, and access to further expertise and resources, to compete aggressively in these markets. [✂]

¹³ Provisional Decision on Remedies, s 3.11, 3.13, 3.14 and 3.20

- c) An acquisition by Mittal would not give rise to regulatory concerns.
- d) HCM would be a more efficient producer of cement if its capacity increases. A second plant would provide it with scheduling flexibility and economies of scale that would afford significant cost savings.
 - i. [✂]
 - ii. The fact that it would have a larger footprint would allow it greater purchasing and other economies of scale which would enhance its competitiveness.
 - iii. [✂]

8.3 An acquisition by Mittal could also provide swift resolution of the AEC identified by the CC:

- a) Mittal is likely to be able to do a deal more quickly, based on its recent experience of acquiring assets divested by Tarmac and Lafarge and its familiarity with the market. [✂]
- b) This will result in the competitive benefits for the market being realised sooner.
- c) [✂]
- d) The major risk identified by the CC is that, without the incentive of clearing their JV, Lafarge/Tarmac will not be motivated sellers, resulting in a protracted deal in which the invested assets will be minimally maintained. Lafarge/Tarmac predicts a 2016 completion. Adding Mittal as another potential bidder to the auction, and one that can move quickly, would mean that the price paid for the Divested Assets is likely to be higher, thereby making Lafarge/Tarmac a more cooperative seller.

9. Conclusion

9.1 In conclusion, Mittal requests the CC to afford it the opportunity to bid for the Divestiture Assets and to defer any decision about Mittal's suitability as a purchaser of any of the Divestiture Assets until after it has made a final decision on remedies and the divestiture process starts.

Mayer Brown International LLP

29 October 2013

APPENDIX 1

ALIX REPORT

Mittal Investments SARL

Competition Commission investigation into the supply or acquisition of aggregates, cement and ready-mix concrete (RMX)

**REVIEW OF THE COMPETITION COMMISSION'S PROPOSED DIVESTMENT REMEDY
AND SPECIFICALLY THE PROVISIONAL DECISION TO EXCLUDE HOPE
CONSTRUCTION MATERIALS AS A SUITABLE PURCHASER**

29 October 2013

AlixPartners UK LLP
When it really matters.

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1 EXECUTIVE SUMMARY

1.1 AlixPartners UK LLP (“AlixPartners”) has been instructed by Mayer Brown International LLP (“Mayer Brown”), solicitors acting on behalf of Mittal Investment SARL (“Mittal”), to consider the economic merits of the Competition Commission’s (“CC”) proposed decision to bar Mittal’s business Hope Construction Materials (“HCM”) from acquiring any cement plant which the CC has proposed should be divested in order to remedy the adverse effect on competition (“AEC”) which the CC has identified in the cement industry.

1.2 In order to assess the merits of the CC’s provisional decision to exclude HCM from being a suitable purchaser of one of Lafarge Tarmac’s (“Lafarge”) designated cement plants, it is appropriate to consider first the AEC which this divestment is intended to address in the context of the CC’s proposed package of remedies.

The CC’s Provisional Findings Report and Provisional Decision on Remedies

1.3 In its Provisional Findings Report (“PFR”), published on May 21 2013, the CC found that a combination of structural and conduct features gave rise to an AEC in GB cement markets through coordination.¹ These included high market concentration, barriers to entry, and evidence of coordinated behaviour.

1.4 Furthermore, the CC noted that:

“...the conditions for coordination to be sustained were met in the GB cement markets (with shares of sales as the focal point) in relation to the ability to reach and monitor coordination, the existence of a mechanism for internal sustainability and the external sustainability of coordination.”²

1.5 The CC’s analysis is succinctly summarised in the PFR:

“We found that it was likely to be in the interests of Lafarge, Cemex and Hanson to adhere to the mechanism for coordination we described, whereas Tarmac was likely to be a fringe player. Furthermore, Lafarge’s position as the largest cement producer, as well as the least vertically-integrated producer, was likely in our view to give it strong incentives to take a leadership role in the coordination—and in particular to take on more of the costs of coordination (including the costs of accommodating the growth in share of sales of fringe cement suppliers, ie Tarmac and cement importers). The different incentives of the GB

¹ Provisional Findings Report, paragraph 4.

² Provisional Findings Report, paragraph 40.

producers (arising, for example, from differences in their size and in the extent to which they made external sales of cement) explained the different roles they adopted in the market, which in turn explained why shares of sales had not been perfectly stable despite the coordination which had been occurring in the market. Their different incentives also explained why asymmetries in their shares of sales, capacity and degree of vertical integration did not prevent—and might even facilitate—coordination.”³

1.6 The CC found that historically the fourth smallest GB cement producer, Tarmac, whilst being “*outside of the coordinating group*”, was a “*fringe player*” which did not destabilise coordination between the three market leaders. The CC also concluded that the new fourth competitor, HCM, would be insufficient to destabilise coordination:

“...we considered that the replacement of Tarmac (a single plant producer which we had found to be outside the coordinating group of firms without coordination breaking down as a result) by HCM (which is also a single-plant producer—albeit with some additional capacity compared with Tarmac) as the smallest GB cement producer was likely to be insufficiently market disrupting on its own materially to reduce our concerns about coordination in the GB cement markets.”⁴

1.7 The CC set out its proposed remedies in its Provisional Decision on Remedies (“PDR”), published on October 8th 2013.⁵ These included:

- (a) the divestiture by Lafarge Tarmac (the largest operator) of either its Cauldon or Tunstead cement plant, with associated supporting measures to ensure an effective implementation of the divestiture remedy;
- (b) two measures aimed at reducing transparency, namely:
 - restrictions on the publication of GB cement market data, ensuring a lag of no less than three months from the time to which the data refers, before the data can be made public; and
 - the prohibition of the practice of issuing generic price announcement letters; and
- (c) measures to increase competition in the supply chain for ground granulated blast furnace slag (“GGBS”).

³ Provisional Findings Report, paragraph 42.

⁴ Provisional Findings Report, paragraph 43.

⁵ Provisional Decision on Remedies, paragraph 4.

The exclusion of HCM as a suitable purchaser of a cement plant

1.8 In our view, there is a logical structure to this overall package of remedies, having regard to the criteria which may affect the risks of anti-competitive coordination⁶ and the CC's specific findings. In particular:

- (a) the coordinated firms need to be able to reach and monitor the terms of coordination. The measures to reduce transparency should make it harder to reach and monitor the terms of coordination, with reducing the information available on market shares potentially being the most important factor given the CC's finding that coordination was occurring at this level. On the other hand, the proposed divestment of capacity makes market shares more symmetrical, with such symmetry tending to mean in some circumstances that firms' incentives are more aligned thereby making it easier to reach and sustain the terms of coordination.⁷ However, as noted above, such concerns do not apply in the present case given the CC's specific findings as to how Lafarge's role as market leader has facilitated coordination;
- (b) coordination needs to be internally sustainable amongst the coordinating group, i.e. firms find it in their individual interest to adhere to the coordinated outcome. The divestment by Lafarge of capacity will reduce its position of market leadership, thereby making coordination less internally stable, with the CC emphasising that this leadership role is important "*in particular to take on more of the costs of coordination (including the costs of accommodating the growth in share of sales of fringe cement suppliers, ie Tarmac and cement importers)*"; and
- (c) coordination needs to be externally sustainable, in the sense that there is little likelihood of coordination being undermined by competition from outside the coordinating group. Reducing the market share of the coordinating group should increase the external competition that the coordinating group face (including competition from HCM and importers), thereby destabilising coordination. In addition, greater competition in GGBS should also increase the external competition which cement producers face.

⁶ These criteria are succinctly summarised in the CC's and OFT's "*Merger Assessment Guidelines*" at paragraph 5.5.9.

⁷ See, for example, the concerns expressed about symmetry between firms facilitating coordination in the CC's and OFT's "*Merger Assessment Guidelines*" at paragraph 5.5.16 and 5.5.19.

- 1.9 However, the CC's analysis as to why HCM is not a suitable purchaser is apparently based solely on the basis of assertion that the market would be less transparent in the presence of a new entrant, and without regard to its findings as to competitive effects or its overall package of remedies:

“We considered that the greater the number of GB cement producers, in particular the number of non-coordinating producers, the greater the potential reduction in market transparency as the scope for, and relative significance of, independent rather than coordinated action increases. Therefore, we considered that a remedy that increased the number of GB cement producers would be more effective at reducing market transparency and disrupting the strategic interdependence of the coordinating firms than a remedy that resulted in the expansion of HCM (the only non-coordinating GB cement producer at present).”⁸

- 1.10 There does not appear to be any analysis whatsoever in the CC's PFR or PDR to justify the CC's assertion. We are puzzled by this, particularly since the exclusion of HCM raises serious issues as to the efficacy and proportionality of the CC's divestment remedy.

- 1.11 As regards to the CC's brief arguments as to transparency in the PDR (no reasons are given in the PFR), the CC fails to explain why the ability of the coordinating group to reach the terms of coordination will be appreciably affected in any way by whether there are more non-coordinating competitors per se (i.e. simply counting the number of the non-coordinating competitors). By definition, the coordinating players need to coordinate with one another, and this is why the CC is proposing remedies aimed at reducing market transparency.

- 1.12 The CC also dismisses any divestment to HCM without any comparison of the competitive effects of a sale to HCM versus a sale to any other category of prospective purchaser. The CC's competitive effects assessment seems – in the absence of any further analysis being set out in its reports – to be based on simply counting the number of competitors, five being “better” than four. However, in isolation, this statement is not economically meaningful for a number of reasons:

- (a) it is a “benchmark-free” observation. Six independent firms, or for that matter 13⁹, would obviously be a larger number than five. (In this regard, one could

⁸ Provisional Decision on Remedies, paragraph 3.28.

⁹ There are 13 cement plants in Great Britain (see Figure 2.2 of the Provisional Findings Report).

point to the CC's and OFT's "*Merger Assessment Guidelines*" which suggest that four effective competitors might be sufficient:

"In relation to the number of firms, previous OFT decisions in mergers involving retailers suggest that the OFT has not usually been concerned about mergers that reduce the number of firms in the market from five to four (or above)".¹⁰

(b) the CC does not consider the possibility that small competitors may be less effective. As observed in the CC's and OFT's "*Merger Assessment Guidelines*" "*counting firms or fascias does not take into account differences in market shares and the size distribution of firms*".¹¹

1.13 In particular, in the present case, the CC is clear that Tarmac, as the fourth smallest player, was an ineffective competitive constraint - in fact, Tarmac was referred to as a "*fringe player*"¹². As noted above, the CC is equally clear in its expectation that this will also be the case as regards HCM, particularly given that it is a single plant operator, whereas even post divestment Lafarge will have five cement plants in GB, and Cemex and Hanson will have three¹³. Accordingly, we are puzzled why the CC does not consider in some detail why the sale of a single plant to a cement importer (or an undertaking not currently active in supplying cement) will engender greater competition, than the sale of this plant to HCM and the creation of a stronger fourth competitive force. This is particularly the case as the CC has found that at present HCM as the fourth competitor is an insufficient competitive constraint.

1.14 *Prima facie*, it seems to us that external competitive constraints will be greater if a major fourth external competitor is created which is more able to compete, than the addition of another single-plant competitor. Indeed, the CC's and OFT's "*Merger Assessment Guidelines*" emphasise that:

*"External sustainability will typically be easier where the competitive fringe does not impose a strong competitive constraint and is unlikely to be able to expand."*¹⁴

1.15 Finally, the CC does not consider how the divestment of a cement plant to HCM would not comprehensively address the AEC given the broader effects of the package of remedies, including the facts that:

¹⁰ The CC's and OFT's "*Merger Assessment Guidelines*", paragraph 5.3.5. We are not citing these guidelines in any way to seek to fetter the CC's discretion to judge the matter based on the facts, but simply to highlight relevant facts which may be worthy of consideration.

¹¹ The CC's and OFT's "*Merger Assessment Guidelines*", 5.3.4.

¹² Provisional Findings Report, paragraph 42.

¹³ Provisional Findings Report, Figure 22 on page 2-18.

¹⁴ "*Merger Assessment Guidelines*", at paragraph 5.5.18.

- (a) the market will be rendered less transparent (rendering it harder to reach and monitor coordination);
- (b) Lafarge would no longer have a position of market leadership following a divestment (reducing the internal sustainability of coordination); and
- (c) external competition from a larger HCM and GGBS would increase (reducing the external sustainability of coordination).

The importance of considering all three conditions is emphasised by the CC's and OFT's "*Merger Assessment Guidelines*" which are explicit that: "*All three of the [conditions for coordination] must be satisfied for coordination to be possible*".¹⁵

1.16 Accordingly, we consider that there are no grounds to conclude that HCM's purchase of a cement plant would render the remedies appreciably less effective. The exclusion of HCM would also seem disproportionate as publically excluding a credible potential purchaser – and the main one which would be able to achieve appreciable operational synergies as it is the only cement producer in the UK¹⁶ outside of the members of the 'coordinating group' – is likely to depress the sale price achieved by Lafarge from the divestment of its cement plant.

Conclusion

1.17 In light of the above, it seems inappropriate, disproportionate and premature to preclude HCM from acquiring a cement plant from Lafarge. Any proposed acquisition by HCM could still be assessed by the CC by reference to its suitable purchaser criteria.

¹⁵ "*Merger Assessment Guidelines*", at paragraph 5.5.9.

¹⁶ At least, the only producer of cement outside of the coordinating group of firms who we consider would be likely to fall outside of the suitable purchaser requirements.

2 INTRODUCTION

AlixPartners' instructions

- 2.1 The CC has provisionally decided that a package of remedies should be imposed, which include Lafarge being required to divest either its Caudon or Tunstead cement plant.
- 2.2 AlixPartners has been instructed by Mayer Brown, solicitors acting on behalf of Mittal, to consider the economic merits of the CC's proposed decision to prohibit Mittal's business HCM from acquiring any cement plant which the CC has proposed should be divested in order to remedy the identified AEC in the cement industry.
- 2.3 At the request of Mayer Brown, this Report has been prepared by AlixPartners in accordance with the standards required of an independent expert witness providing evidence for UK court proceedings under Part 35 of the Civil Procedure Rules. All opinions stated in this report are our own. We have reviewed the PFR, the PDR, and the CC's "*Addendum to the provisional findings: further analysis on GGBS and GBS and provisional findings*", and we have also discussed various matters with Mittal and HCM.
- 2.4 This report has been written by Mat Hughes, Partner and Derek Holt, Director at AlixPartners:
- (a) Mat Hughes is a partner in AlixPartners' European Economics Consulting practice. He has more than 20 years' experience in advising businesses across a number of sectors in relation to merger, market/sector investigations and anti-trust cases. Mat Hughes was formerly Chief Economist at Ashurst LLP; and
 - (b) Derek Holt is a director in AlixPartners' European Economics Consulting practice. He has more than 18 years' experience in advising a wide range of clients across many sectors in relation to regulatory, finance/profitability, merger, market/sector investigations and anti-trust cases. He was previously an economist at Oxera Consulting Ltd.

Structure of the report

- 2.5 This report is structured as follows:
- section 3 provides a summary of the AEC the CC has identified and the provisional remedies which it proposes to implement, with a focus on those issues

of greatest relevance to the CC's decision in relation to HCM's suitability to acquire the divested cement plant;

- section 4 provides our assessment of the CC's application of the suitable purchaser condition in the context of its proposed divestment remedy for a cement plant by one of the three main operators in GB; and
- section 5 sets out our conclusions.

3 SUMMARY OF THE CC'S PROVISIONAL FINDINGS AND CEMENT MARKET REMEDIES

3.1 This section provides a brief summary of the CC's provisional findings and provisional remedies to provide context for the assessment of its suitable purchaser condition in relation to the cement plant divestment remedy (addressed in section 3).

CC's identification of an AEC in the cement market

3.2 The CC found that there was a combination of structural and conduct features that gave rise to an AEC in the GB bulk and bagged cement markets. In relation to structural features, the CC found there to be:¹⁷

- high market concentration;
- transparency of sales and production shares, wins and losses and customer-supplier relationships;
- high barriers to entry (including limits to the constraint imposed by imported cement);
- homogeneity of product;
- customer characteristics and behaviour (in particular, regularity of purchases, purchases at fixed locations, concentration of customer base and single sourcing of a particular job site); and
- vertical integration from cement into downstream operations.

3.3 The conduct features noted by the CC included:¹⁸

- a strategic focus on maintaining market share stability between the members of the coordinating group, frequently manifested in a focus on maintaining existing (or returning to pre-existing) relative shares of sales;
- price announcement behaviour (contributing to price leadership and price following, and softening of customer resistance to price increases);
- “tit-for-tat” share behaviour used to balance shares and for retaliation;

¹⁷ Provisional Findings Report, paragraph 45.

¹⁸ Provisional Findings Report, paragraph 46.

- use of cross-sales as a mechanism for transparency, signalling and, on occasion, share balancing and retaliation; and
- attempts to target importers beyond normal competition on price and service.

3.4 The CC found that the structural and conduct features combine together to give rise to an overarching feature in the GB cement markets, namely coordination among Cemex, Hanson and Lafarge.¹⁹ In particular it found that the three conditions necessary for coordination to be sustained are met in the GB markets (though the extent to which each condition was satisfied may have varied over time).²⁰ It found that:²¹

- firms are able to reach an understanding and monitor the terms of the coordination;
- coordination is internally sustainable (i.e. it is in the individual interest of each coordinating firm to adhere to the coordinated outcome); and
- coordination needs to be externally sustainable (i.e. coordination is unlikely to be undermined by competition from firms outside the coordinating group).

Ability to reach and monitor a coordinated outcome

3.5 The CC found that the first condition is satisfied “*given the high degree of market transparency of shares of sales, customer wins and losses and customer-supplier relationships, and (to an extent) pricing behaviour at a general level, with evidence that the Top 3 cement producers closely monitor these parameters.*” It also noted that coordination was facilitated by high concentration in the industry.²²

Internal stability of the coordinated outcome

3.6 The CC found that the second condition is satisfied given the “*low gains from deviation, the existence of effective deterrent mechanisms, and the low risk of incorrect or accidental punishment.*” It found that “*differences between the Top 3 cement producers, in terms of their cement production capacities and the extent of their vertical integration into downstream operations, gave rise to different incentives that manifest themselves in*

¹⁹ Provisional Findings Report, paragraph 47.

²⁰ Provisional Findings Report, paragraph 8.278.

²¹ Provisional Decision on Remedies, paragraphs 2.7-2.8.

²² Provisional Decision on Remedies, paragraph 2.8, first bullet.

the different roles adopted by each member of the coordination group, but do not prevent coordination taking place.”²³

3.7 Furthermore, the CC found that asymmetry in the share of sales of firms in the coordinating group, in particular the position of Lafarge as the largest cement producer, did not prevent and may have facilitated coordination:

“Lafarge’s position as the largest cement producer, as well as the least vertically-integrated producer, was likely in our view to give it strong incentives to take a leadership role in the coordination—and in particular to take on more of the costs of coordination (including the costs of accommodating the growth in share of sales of fringe cement suppliers, ie Tarmac and cement importers). The different incentives of the GB producers (arising, for example, from differences in their size and in the extent to which they made external sales of cement) explained the different roles they adopted in the market, which in turn explained why shares of sales had not been perfectly stable despite the coordination which had been occurring in the market. Their different incentives also explained why asymmetries in their shares of sales, capacity and degree of vertical integration did not prevent—and might even facilitate—coordination.”²⁴

External stability of the coordinated outcome

3.8 The CC found that the third condition is satisfied given the “*high barriers to entry into GB cement production; the limited (although variable over time) constraint from imported cement and non-coordinating firms more generally; and the limited impact of countervailing buyer power.*”²⁵

3.9 In relation to the role of Tarmac as the fourth GB supplier in the cement sector (pre-2013), the CC noted that:

- Tarmac is in a very different position from that of the Top 3, having the lowest market share and production capacity;
- unlike the Top 3, Tarmac was (for much of the period 2007 to 2011) a net buyer of cement, rather than a net seller (i.e., it was vertically integrated to a higher degree than the Top 3); and

²³ Provisional Decision on Remedies, paragraph 2.8, second bullet.

²⁴ Provisional Findings Report, paragraph 42.

²⁵ Provisional Decision on Remedies, paragraph 2.8, third bullet.

- it sold cement externally only on an opportunistic basis, and due to its low external sales and high capacity utilisation it would be difficult to punish though would be unlikely to have an incentive to undermine coordination.²⁶

3.10 In relation to the potential for HCM to act as a constraint on the ability of the Top 3 to achieve a coordinated outcome, the CC found that:

"...the replacement of Tarmac (a single plant producer which we had found to be outside the coordinating group of firms without coordination breaking down as a result) by HCM (which is also a single-plant producer-albeit with some additional capacity compared with Tarmac) as the smallest GB cement producer was likely to be insufficiently market disrupting on its own materially to reduce our concerns about coordination in the GB cement markets."²⁷

3.11 In relation to the role of importers, the CC noted that:

"We found that for the cement importers we analysed, unit total costs were generally higher than the average ex-works price of domestically-produced cement. Therefore, even before taking into account a cement importer's own required margin, the cement importer had a cost disadvantage in competing against the price of domestically-produced cement."²⁸

3.12 The cost disadvantage suffered by importers relative to GB producers was cited as a factor leading to the limitation in their ability to exert a competitive constraint.²⁹

Summary of provisional remedies

3.13 The CC set out its proposed remedies in its Provisional Remedies Notice, published on October 8th 2013. These include:

- cement plant divestiture: Lafarge should be required to choose between divesting either its Caudon or Tunstead cement plant (with associated supporting measures relating to access to a minimum level of capacity of ready-mix concrete plants, the application of suitable purchaser criteria and the implementation of the divestiture remedy)³⁰. The production capacity of the divested plant would be around 1MT per annum, representing approximately 10% of the market;³¹

²⁶ Provisional Findings Report, paragraphs 8.252-5.

²⁷ Provisional Findings Report, paragraph 43.

²⁸ Provisional Findings Report, paragraph 7.89.

²⁹ Provisional Findings Report, paragraph 38.

³⁰ Provisional Decision on Remedies, Figure 3.1.

³¹ Provisional Decision on Remedies, paragraph 3.142.

- restrictions on publication of GB cement market data: All data currently provided by the GB cement producers to the Mineral Products Association (“MPA”) and published by the MPA and the Department of Business, Innovation and Skills (“BIS”) should be subject to a time lag of no less than three months from the time to which the data refers, before the data can be made public;³²
- prohibition of the practice of issuing generic price announcement letters: GB suppliers should only be permitted to send customer-specific price announcement letters that state clearly, as a minimum, both the current actual unit price and the proposed revised unit price;³³ and
- measures to increase competition in the GGBS supply chain: The measures would include divestments of by each of Hanson and Lafarge and as well as associated requirements for divestments to be acquired by a suitable purchaser and various implementation requirements to ensure the effectiveness of the divestments.³⁴

Impact of the CC's remedies

3.14 The CC considers that its cement plant divestiture remedy would have the following effects on the ability of the GB suppliers to coordinate outcomes:

- it would reduce the market share of the coordinating group (from 70% to around 55-65%³⁵), leading to a reduction in market transparency and an increased requirement for firms within the coordinating group to take into account in their decisions the independent competitive actions of any new entrant or expanding non-coordinating producer;³⁶
- the resulting reduction in market transparency and increase in strategic uncertainty could have a significant impact on the ability of the Top 3 cement producers to monitor the terms of coordination;³⁷
- it would reduce the market share of the leader (assuming the divestiture would be of one of Lafarge Tarmac's plants), leading to a reduction in the ability and incentive to maintain a coordinated outcome including bearing the costs of coordination;³⁸ and

³² Provisional Decision on Remedies, Figure 3.2.

³³ Provisional Decision on Remedies, Figure 3.3.

³⁴ Provisional Decision on Remedies, Figure 3.4.

³⁵ Provisional Decision on Remedies, paragraph 3.142.

³⁶ Provisional Decision on Remedies, paragraph 3.28.

³⁷ Provisional Decision on Remedies, paragraph 3.29.

- the creation of a new entrant would lead to an enlarged group of non-coordinating producers and could undermine any coordination among the Top 3 suppliers.³⁹

3.15 In our view, there is a logical structure to this overall package of remedies, having regard to the criteria which may affect the risks of anti-competitive coordination and the CC's specific findings. In particular:

- the coordinated firms need to be able to reach and monitor the terms of coordination. The measures to reduce transparency should make it harder to reach the terms of coordination, with reducing the information available on market shares potentially being most important factor given the CC's finding that coordination was occurring at this level. The proposed divestment of capacity, however, makes market shares more symmetrical, with such symmetry tending to mean in some circumstances that firms' incentives are more aligned thereby making it easier to reach and sustain the terms of coordination.⁴⁰ However, as noted above, such concerns do not apply in the present case given the CC's specific findings as to how Lafarge's role as market leader has facilitated coordination;
- coordination needs to be internally sustainable amongst the coordinating group, i.e. firms find it in their individual interest to adhere to the coordinated outcome. The divestment by Lafarge of capacity will reduce its position of market leadership, thereby making coordination less internally stable, with the CC emphasising that this leadership role is important "*in particular to take on more of the costs of coordination (including the costs of accommodating the growth in share of sales of fringe cement suppliers, ie Tarmac and cement importers)*"; and
- coordination needs to be externally sustainable, in the sense that there is little likelihood of coordination being undermined by competition from outside the coordinating group. Reducing the market share of the coordinating group should increase the external competition that the coordinating group face (including competition from HCM and importers), thereby destabilising coordination. In addition, greater competition in GGBS should also increase the external competition which cement producers face.

³⁸ Provisional Decision on Remedies, paragraph 3.31(b).

³⁹ Provisional Decision on Remedies, paragraph 3.32.

⁴⁰ See, for example, the concerns expressed about symmetry between firms facilitating coordination in the CC's and OFT's "*Merger Assessment Guidelines*" at paragraph 5.5.16 and 5.5.19.

3.16 However, the CC's analysis as to why HCM is not a suitable purchaser is apparently based solely on the basis of assertion that the market would be less transparent in the presence of a new entrant, and without regard to its findings as to competitive effects or its overall package of remedies. We assess the CC's basis for this conclusion in the next section.

4 ASSESSMENT OF THE CC'S EXCLUSION OF HCM

4.1 As noted in section 3, the CC has provisionally concluded that HCM should be excluded from acquiring the cement plant to be divested.

4.2 The main justification for this decision is set out below:

*"We considered that the greater the number of GB cement producers, in particular the number of non-coordinating producers, the greater the potential reduction in market transparency as the scope for, and relative significance of, independent rather than coordinated action increases. Therefore, we considered that a remedy that increased the number of GB cement producers would be more effective at reducing market transparency and disrupting the strategic interdependence of the coordinating firms than a remedy that resulted in the expansion of HCM (the only non-coordinating GB cement producer at present)."*⁴¹

4.3 The CC furthermore considers that an enlarged group of non-coordinating producers in the GB cement markets than can successfully undermine any coordination, could also reinforce the impact of the remedy on the other two conditions necessary for coordination to be sustained, namely the ability to reach an understanding and monitor the terms of coordination; and the ability and incentives of the coordinating group to maintain a coordinated outcome.⁴²

4.4 Put simply, the CC considers that having five producers in the GB market will be "better" than having four.

4.5 Our views on the CC's decision to restrict the cement plant purchaser to be a non-GB producer rather than, say, a firm outside of the coordinating group of firms, and the reasoning which the CC advances in support of this decision, are set out below.

The CC has failed to adequately justify its decision

4.6 The CC has stated that it considers a greater number of non-coordinating producers would lead to a more effective competitive constraint than would arise in the case of an expansion of an existing non-coordinating group producer. There does not appear to be any analysis whatsoever in the CC's PFR or PDR to justify the CC's assertion. Neither has it sought to carry out any detailed assessment of how the two alternative post-divestment market structures (i.e., one scenario in which a fifth producer enters the market and another where the existing fourth producer increases in size) would affect the

⁴¹ Provisional Decision on Remedies, paragraph 3.32.

⁴² Provisional Decision on Remedies, paragraph 3.33.

ability of the 'non-coordinating' group to exert competitive constraints on the coordinating group.

- 4.7 We are puzzled by this lack of evidence or detailed reasoning, particularly since the exclusion of HCM raises serious issues as to the efficacy and proportionality of the CC's divestment remedy. Any such analysis should examine in detail the effects of such a restriction on the three conditions for a coordinated outcome emerging in the market. Relevant issues for the CC to consider are set out below.

Impact of suitable purchaser on ability to identify and monitor a coordinated outcome

- 4.8 The CC highlights that a number of features have led to a situation in which the coordinating group has had the capacity to identify⁴³ a coordinated outcome. These are:

- high concentration;
- interactions between firms continue for many years;
- homogeneity of the product;
- interaction between firms through JVs and cross-sales leading to increased transparency;
- high degree of market share transparency; and
- a degree of price transparency.

- 4.9 As regards the CC's brief arguments as to transparency, the CC fails to explain why the ability of the coordinating group to reach the terms of coordination will be appreciably affected in any way by whether there are more non-coordinating competitors per se (i.e. simply counting the number of the non-coordinating competitors). By definition, the coordinating players need to coordinate with one another, and this is why the CC is proposing remedies aimed at reducing market transparency.

- 4.10 From the above list of features which may have enabled the coordinating group to reach a coordinated outcome, it is difficult to see what incremental benefit would arise from the restriction imposed by the CC's suitable purchaser condition. The only one which could reasonably be argued to be improved at all by the restriction of the acquisition to a non-GB producer could be the degree of concentration in the sector. It is clear that if the

⁴³ Provisional Findings Report, paragraph 8.162.

divested cement plant is acquired by a new entrant, concentration as measured by the market share of the top four firms (or C4), or the Hirschman-Herfindahl Index (“HHI”), would be reduced somewhat. However, this would be a matter of degree and it could also be argued that the C3 concentration ratio would fall to the same level irrespective of whether the CC applies a non-GB constraint to the suitable purchaser condition.⁴⁴ This measure of concentration may be particularly relevant given that it is the top three firms which have been identified as forming the coordinating group.

4.11 In relation to the ability of the coordinating group to monitor the terms of coordination, the CC identified the following features:⁴⁵

- transparency of production capacity as well as customer wins and losses;
- awareness of downstream conditions through the ready-mix concrete business;
- purchasing behaviour of customers;
- high concentration of sales across a relatively small number of customers; and
- ability to identify the producer to which a customer has switched.

4.12 There is no evidence to suggest that any of the above features which would enable monitoring of a coordinated outcome would be affected by the nature of the purchaser of the divested cement plant. Furthermore, it is clear that remedies already proposed in relation to price and market share transparency would significantly reduce the ability of the coordinating group to monitor a coordinated outcome.

Impact of suitable purchaser on internal stability of a coordinated outcome

4.13 The CC identifies the following features of the market which have enhanced the internal stability of any coordinated outcome:⁴⁶

- geographical considerations leading to limitations in the ability to capture all of the demand of a multi-site operator, suggesting that deviations are likely to occur at a relatively small-scale level;
- the ability of coordinating firms to adopt a ‘tit-for-tat’ strategy, given the fact that deviations are likely to occur at a relatively small-scale level;

⁴⁴ This assumes that if the CC were to amend the suitable purchaser condition it would continue to bar any firms within the coordinating group from acquiring the divested plant.

⁴⁵ Provisional Findings Report, paragraph 8.166 – 8.168.

⁴⁶ Provisional Findings Report, paragraph 8.180 – 8.207.

- the presence of significant cross-sales which can be used as an effective retaliation mechanism;
- the multi-market contact of members of the coordinating group leading to additional opportunities to punish deviators; and
- the significant degree of market information leading to a low risk of accidental punishment.

4.14 Given that all of the features above relate either to specific characteristics of the nature of interaction within the coordinating group and the fact that these characteristics would be independent of the purchaser of the divested plant, there is no evidence to suggest that any of the features above would be affected by the CC's suitable purchaser condition.

Impact of suitable purchaser on external stability of a coordinated outcome

4.15 The CC also dismisses any divestment to HCM without any comparison of the competitive effects of a sale to HCM versus a sale to any other category of prospective purchaser. The CC's competitive effects assessment seems – in the absence of any further analysis being set out in its reports – to be based on simply counting the number of competitors, five being “better” than four. However, in isolation, this statement is not economically meaningful for a number of reasons:

- it is a “benchmark-free” observation. Six independent firms, or for that matter 13⁴⁷, would obviously be a larger number than five. (In this regard, one could point to the CC's and OFT's “*Merger Assessment Guidelines*” which suggest that four effective competitors might be sufficient:

*“In relation to the number of firms, previous OFT decisions in mergers involving retailers suggest that the OFT has not usually been concerned about mergers that reduce the number of firms in the market from five to four (or above)”.*⁴⁸)

- the CC does not consider the possibility that small competitors may be less effective. As observed in the CC's and OFT's “*Merger Assessment Guidelines*”

⁴⁷ There are 13 cement plants in Great Britain (see Figure 2.2 of the Provisional Findings Report).

⁴⁸ The CC's and OFT's “*Merger Assessment Guidelines*”, 5.3.5.

*“counting firms or fascias does not take into account differences in market shares and the size distribution of firms”.*⁴⁹

4.16 *Prima facie*, it seems to us that external competitive constraints will be greater if a major fourth external competitor is created which is more able to compete, than the addition of another single plant competitor. Indeed, the CC’s and OFT’s *“Merger Assessment Guidelines”* emphasise that:

*“External sustainability will typically be easier where the competitive fringe does not impose a strong competitive constraint and is unlikely to be able to expand.”*⁵⁰

4.17 The lack of evidence in relation to the justification for the bar to HCM’s acquisition of the divested plant can be considered by reference to the features of the market which the CC considers have enhanced the external stability of any coordinated outcome. These include:⁵¹

- the presence of significant barriers to entry;
- limited incentive and ability of the competitive fringe (in particular Tarmac during the period 2007-2011) to exert competitive constraints owing to its lower market share and production capacity, high degree of vertical integration and high utilisation;⁵²
- limited competitive threat from imports due to their significant cost disadvantage as well as steps taken by GB cement producers to undermine the viability of imported cement;⁵³ and
- the presence of price discrimination which implies that even if some buyers can exert a degree of buyer power this is unlikely to undermine the ability of GB cement producers as a whole to coordinate on sales of cement to other buyers.⁵⁴

4.18 The two potential features above which could potentially be affected by the CC’s formulation of the suitable purchaser condition are the effectiveness of competition from the competitive fringe and the effectiveness of competition from imports. However, there is no evidence to suggest that either of these sources of competitive constraint would be

⁴⁹ The CC and OFT’s *“Merger Assessment Guidelines”*, 5.3.4. (We are not citing these guidelines in any way to seek to fetter the CC’s discretion to judge matter based on the facts, but simply to highlight relevant facts which may be worthy of consideration).

⁵⁰ *“Merger Assessment Guidelines”*, at paragraph 5.5.18

⁵¹ Provisional Findings Report, paragraphs 8.208 – 8.216.

⁵² Provisional Findings Report, paragraphs 8.252-8.254.

⁵³ Provisional Findings Report, paragraph 8.211.

⁵⁴ Provisional Findings Report, paragraphs 8.214-8.215.

enhanced by the exclusion of HCM. Furthermore there are reasons to suppose that the effectiveness of the external competitive constraint may be weakened as a result of the exclusion of HCM.

- 4.19 In relation to the ability of the competitive fringe (defined here as the group of non-coordinating firms) to undermine a coordinated outcome, the following factors would suggest that a stronger fourth player could exert a greater competitive threat compared with a greater number (i.e., two instead of one) of firms, each of which is only about half the size of the hypothetical larger fourth producer.
- 4.20 In particular, it is important to consider the trade-off between the risk of a larger fourth producer contributing to the coordinated outcome versus the ability of the fourth producer to effectively challenge the top three producers. In our view, this trade-off is clear cut: the CC found that Tarmac was only a “fringe” competitor and it expects that HCM will not be an effective competitive constraint as a single-plant operator. The creation of a fourth viable competitor would *prima facie* appear to be a superior competitive outcome to the addition of another single-plant operator.
- 4.21 In this regard, it would also seem relevant to have regard to the CC’s analysis of the *Safeway/Morrisons* merger in 2003. Clearly, each case turns on its facts, and the groceries market is not the same as the cement market. However, this report does illustrate the importance of having close regard not only to the number of competitors but also their ability to compete, and that four credible rivals may well be a superior competitive outcome:

“At the national level, we do not expect the acquisition of Safeway by Morrisons to reduce the number of national players or to exacerbate the conditions in which coordinated effects are likely to occur. Thus, we do not expect that, following the merger, effective price and non-price competition would be reduced in the UK one-stop grocery market. First, we take the view that, in so far as a Morrisons/Safeway entity would result in four substantial multiple grocery retailers of broadly similar scale, with a significant presence in every region of the UK, this may not be expected to reduce the sorts of competitive rivalry that have been a feature of the market in the past decade. Established as a fourth national player, our expectation is that Morrisons would seek to challenge its three main rivals on price and non-price aspects of competition. Second, with four national players, there is far less likelihood of coordination since the greater the number of parties involved, the more difficult

coordination becomes in this context. Four national players may be expected to pose considerably less of a threat of coordinated behaviour than three.”⁵⁵

4.22 The CC considers that single-plant operators such as Tarmac (pre-2013) and HCM (from 2013) have been unable to exert a sufficient competitive constraint to undermine the coordinated effects of the top 3 producers. If it were to acquire the divested plant, HCM would become an operator of two plants. This would lead to a number of pro-competitive effects stemming from the enhanced economies of scale that a two-plant producer could be expected to achieve:

- improvements in production scheduling; and
- average cost reductions arising from spreading of fixed central costs across greater volumes.⁵⁶

4.23 In contrast, non-GB producers, should they acquire the plant, would remain single-plant producers in GB, leading to an absence of the scale economies noted above. Furthermore, as the CC has highlighted, the ability of alternative operators to compete may be affected by the relatively high cost of imports - i.e. cost disadvantages matter.

4.24 There is a reasonable probability that, were an importer to acquire the divested plant, the plant's output would substitute for the imported volumes, leading to a risk that total volumes available to GB consumers would decline initially. While these volumes may be replaced by alternative imports, this may take time and the alternative import source may be more costly.

4.25 HCM, if it were to acquire the divested plant, would also have strong incentives to compete strongly in the market owing to the significant amount of its up-front investment (necessitating a high degree of utilisation to ensure the cost of financing the investment is recovered), and the need to find external purchasers for its output.

Impact of CC's other proposed remedies on ability to identify or sustain a coordinated outcome

4.26 The CC does not consider how the divestment of a cement plant to HCM would not comprehensively address the AEC given the broader effects of the package of remedies, including the fact that the market will be rendered less transparent, Lafarge would no

⁵⁵ Competition Commission (2003), Safeway plc and Asda Group Limited (owned by Wal-Mart Stores Inc); Wm Morrison Supermarkets PLC; J Sainsbury plc; and Tesco plc. A report on the mergers in contemplation.

⁵⁶ Logistics cost savings are likely to be modest due to the proximity of HCM's plant with both of the designated divestment plants, albeit this increases the scope for maximising production coordination-based efficiencies.

longer have a position of market leadership, and external competition from GGBS and suppliers outside the coordinating group will increase.

4.27 For example, the price publication and market information remedies will make it more difficult to reach and sustain a consensus price or market share. These remedies would also lessen the risk that a fourth operator would join the coordinating group. In addition, the loss of its position of market leadership will reduce Lafarge's incentives to coordinate. Furthermore, the GGBS remedy and the growth of suppliers outside the coordinating group will serve to enhance external competition in the cement market, irrespective of whether HCM were to acquire the divested cement plant.

4.28 The importance of considering all three conditions is emphasised in the CC's and OFT's "*Merger Assessment Guidelines*" which are explicit that: "*All three of the [conditions for coordination] must be satisfied for coordination to be possible*".⁵⁷

Conclusions

4.29 Accordingly, we consider that there are no grounds to conclude that HCM's purchase of a cement plant would render the overall package of remedies proposed by the CC appreciably less effective.

4.30 The exclusion of HCM would also seem disproportionate as publically excluding a credible potential purchaser – and the main one which would be able to achieve appreciable operational synergies as it is the only cement producer in the UK⁵⁸ outside of the members of the 'coordinating group' – is likely to depress the sale price achieved by Lafarge from the divestment of its cement plant.

⁵⁷ "*Merger Assessment Guidelines*", at paragraph 5.5.9.

⁵⁸ At least, the only producer of cement outside of the coordinating group of firms who we consider would be likely to fall outside of the suitable purchaser requirements.

5 CONCLUSIONS

5.1 In our view, it seems inappropriate, disproportionate and premature to preclude HCM from acquiring a cement plant from Lafarge. This conclusion is based on the following key points:

- the absence of any detailed assessment by the CC of the competitive effects of its proposal to preclude HCM from acquiring the divested plant. As regards to the CC's brief arguments as to transparency, the CC fails to explain why the ability of the coordinating group to reach the terms of coordination will be appreciably affected in any way by whether there are more non-coordinating competitors per se (i.e. simply counting the number of the non-coordinating competitors). By definition, the coordinating players need to coordinate with one another, and this is why the CC is proposing remedies aimed at reducing market transparency;
- the absence of any evidence that the preclusion of HCM from acquiring the divested plant would assist in undermining the external stability of any coordinated outcome. The assumption that more operators would lead to greater competition is not economically meaningful in the absence of any assessment of the ability of individual producers to impose a competitive constraint;
- neither Tarmac (pre-2013) nor HCM (from 2013) have been considered by the CC to be capable, as the fourth producers in the market operating only a single cement plant, to exert a sufficient competitive constraint on the coordinating firms. This clearly suggests that there could be scope to enhance the degree of competition in the cement market by enabling a fourth operator to become a more effective competitor;
- the CC has not taken into account the wider package of remedies which it has proposed, including the measures it has taken to reduce the leadership of Lafarge, steps to reduce market and price transparency, and steps to increase the competitiveness of the GGBS market, when considering the case for precluding HCM from acquiring the divested plant. Each of the remedies above would reduce the ability of the coordinating firms to reach and maintain a coordinated outcome, irrespective of whether the divested plant was acquired by HCM; and
- the fact that the CC would still have the opportunity to assess any proposed acquisition by HCM by reference to its suitable purchaser criteria.