

AKZO NOBEL NV/METLAC HOLDING SRL MERGER INQUIRY

Summary of hearing with Diostyl held on 13 June 2012

Background

1. Diostyl is a Netherlands-based company, founded in 2008 by a small group of people previously employed at international can-coating and can-making companies. It was set up to serve some of the smaller, niche product segments. It does little or no business in the UK at present.

Market

2. Diostyl told us it had been encouraged into the market following the consolidation of the coatings market over the last 20 to 30 years and also concerns from the can manufacturers regarding their dependency on a few large coatings suppliers. Can makers were concerned both about the availability of niche products, given the moves by the large suppliers towards rationalizing their portfolios, and about the prices they were being offered which had risen following the consolidation of the market.
3. From a practical point of view, the can coatings market could be divided between beverage and non-beverage (ie the food and general line markets). The non-beverage market comprised a vast array of different products, including three-piece cans, two-piece cans, can ends, aerosols and monoblocs, all in different sizes and of different metal types. The beverage market, however, was much more streamlined. The beverage market was probably more than half the total market of can coatings. Diostyl, however, did not currently operate in the beverage market, only the food and general line markets.
4. Diostyl did not manufacture its coatings itself but used a Belgian toll manufacturer to fulfil its orders. It had taken around six months between setting up the business and delivering its first order to a customer. It emphasized that this was possible because it had previous knowledge of the industry structures, and because it chose to enter the general line market first where the time taken to qualify a product was shorter than for food contact coatings. In addition, it had received support from customers to enter the market with a new product offering. If it had chosen to build its own plant, however, the process would have taken considerably longer.
5. Diostyl was a small player in the market and did not believe it was important enough to concern the major suppliers. It considered the whole of the can coating market as its competitors and so its strategy was to find gaps in the market where can manufacturers had a need for a product that the larger operators were not supplying. It indicated that several of the smaller operators functioned on this basis, with product rationalization by the larger manufacturers creating these gaps in the food and general line markets.

Switching

6. There were two categories of materials: straightforward mix products and epoxy technologies. The first category was a straightforward process that any reasonably

equipped chemical factory was able to perform by mixing the chemicals required to manufacture a product and only required a reasonable amount of testing. However, the other category (epoxy technologies (which was required for internal sprays)) was more difficult to toll manufacture as most plants did not have the reactors needed to produce the resin. Companies could switch supply of products from one factory to another relatively easily in the case of the first category but for epoxy technologies, the right equipment was needed and this was expensive and not always available.

7. Capacity in the beverage internal spray market was currently somewhat constrained, which limited the extent to which any individual operator could increase output in the short-term and thus limited the opportunity of switching to customers.
8. A coatings product was only used by a customer once it had been qualified and approved. As such, switching did not occur in the same way as it did in the retail market where customers could select products and discard them if they did not meet the customer's requirements. Instead, once a customer had 'bought-in' to a product, the process was initiated and could take up to four years to complete. Therefore, customers were reluctant to switch products due to the uncertainty of whether new formulations would meet their requirements in all circumstances.

Purchasing process

9. The beverage market was very concentrated with five or six different customers present. Each had a number of factories spread across a number of regions and each factory had several production lines. Customers tended to award contracts according to commercial principles.
10. Transport costs were typically up to 5 per cent of the cost of the product. Coatings were principally transported by road but on occasions by ship and so the cost of transport varied significantly depending on energy costs and on supply and demand.
11. The bidding process for large beverage customers was a formal, very well-structured process and usually occurred on an annual basis where all suppliers were invited to bid. Volumes were agreed with margins of error and pricing was either fixed or subject to agreed alterations during the course of the contract. The bidding process for large non-beverage customers was less rigorous and typically negotiated on a regional basis. For these customers, overall volumes were often negotiated but exactly how that volume would be put together, which products were included and which factories would be supplied could be left flexible. The non-beverage market was also subject to some seasonality.
12. The smaller and medium-sized customers tended to negotiate with Diostyl and its competitors, during which the provision of incentives would be discussed. Price stability for longer than three to six months was unusual due to the volatility of raw material costs.

BPA-NI technology

13. Bisphenol-A non-intent (BPA-NI) products were made from epoxy-free resins. Epoxy resins were used in about 70 per cent of internal food and beverage contact materials and had been used for over 40 years, and so had a proven track record. The technological challenge for paint and can makers and for food and beverage companies was that BPA-NI was a 'step into the unknown'. BPA-NI technology also removed the need for the expensive manufacturing equipment that was currently required to make epoxy resins. There was therefore the possibility that some

companies would be left with a very expensive piece of manufacturing equipment whilst other companies, with cheaper equipment, would now be able to compete if they were able to develop the right technologies.

14. The development of BPA-NI technology would open the market to companies other than those that were currently there at the moment due to the lower level of manufacturing requirement. For example, Diostyl could not economically make 2,000 tonnes of epoxy spray. However, if Diostyl were asked to supply a BPA-NI product, it would potentially have the capability to produce it. Companies would need the required know-how but this was one barrier to entry that would be significantly lower.

Barriers to entry

15. The various regulations that govern the metal coatings industry, particularly in relation to food-contact coatings, required significant resource to manage. A number of firms in the broader paint industry had failed to enter the market, despite potentially attractive margins, as a direct result of regulation.

Parties to the merger

16. AkzoNobel acquired '[probably] the gold standard of packaging coatings in Europe' when it purchased ICI Packaging Coatings (ICI) a few years ago. However, because ICI had been subject to competitive price pressures and forced to downsize, customers whilst still believing it to be a very good company, possibly felt it was not going to deliver to the same level as it had before. Diostyl, and other companies, had probably won business from AkzoNobel as a result of this process.
17. The Metlac business was somewhat regionally skewed and so Diostyl did not encounter it that often when competing for contracts. However, when the two companies did compete, Metlac usually always provided pretty low-priced products.
18. Metlac had a high market-share in the Italian coatings market, supplying out of its factory in Italy and offered excellent technical service support to customers.
19. To its knowledge, apart from the beverage spray market, Metlac was probably not a very significant competitor in the UK and therefore it would struggle to see why there would be any significant area of competition within the UK should AkzoNobel acquire Metlac.