Completed acquisition by Lion Capital LLP of the business and certain assets of Cumbrian Holdings Limited

ME/5321/12

The OFT's decision on reference under section 22(1) given on 27 March 2012. Full text of decision published 21 May 2012.

Please note that the square brackets indicate figures or text which have been deleted or replaced in ranges at the request of the parties or third parties for reasons of commercial confidentiality.

THE PARTIES

1. **Lion Capital** ('Lion') is a private equity investment firm, based in London. Lion Capital controls the Findus Group ('Findus'), a UK-based company that is active across Europe in the supply of frozen and chilled food, including frozen and chilled branded and private-label seafood products. Findus is active in the UK through its subsidiary, Young's Seafood Limited ('Young's'), which supplies frozen and chilled fish and seafood products.

2. **Cumbrian Seafoods Limited and Border Laird Limited** are wholly owned subsidiaries of Cumbrian Holdings Limited (together 'Cumbrian'). Cumbrian was active in the processing, packing and supply of chilled fish and seafood products to retailers in the UK.[1] Most of Cumbrian's products are essentially bulk products which Cumbrian purchases as fillets from its suppliers and re-packs and re-labels for use in retailers' fish counters. The company also produces some value-added products (namely, coated and smoked fish). The vast majority of its business (around [ ] per cent) is comprised of private label products supplied to the major grocery retailers.[2] The remainder is comprised of minor brands (Perfect Catch, Ocean Pure, and For the Love of Fish) that are used for retailer promotions.

[1] Cumbrian operated three sites at Seaham, West Lakes and Border Laird.
[2] Cumbrian's main customers were [].

TRANSACTION

3. Lion acquired the business and certain assets of the Cumbrian business on 5 December 2011, for a consideration of £[ ].[3]

4. The administrative deadline, extended with agreement of the parties, for the OFT to make a decision in this case is 27 March 2012. The statutory deadline is 14 April 2012.

JURISDICTION

5. As a result of the transaction Lion and Cumbrian have ceased to be distinct. The UK turnover of the target businesses exceeds £70 million, so the turnover test in section 23(1)(b) of the Enterprise Act 2002 (the Act) is satisfied. The OFT therefore believes that it is or may be the case that a relevant merger situation has been created.

RATIONALE FOR THE MERGER

6. Lion submit that it acquired Cumbrian in a 'rescue-and-salvage' effort after the Cumbrian business had failed and was facing imminent liquidation by its administrators. The acquisition followed a six-week effort by KPMG to find other buyers. Cumbrian's liquidity issues and growing difficulties with its suppliers, along with pressure from its main lender, Barclays, imposed a very short time frame in which the transaction had to be completed.

7. [ ].

COUNTERFACTUAL

8. The parties submit that the relevant counterfactual against which to assess the merger is a situation in which Cumbrian would have exited the market, having failed and been unable to find an alternative purchaser. The parties also considered that under this scenario, a major portion of Cumbrian's business would have switched to Young's over the near term. On this basis, the parties argued that, to the extent there were any loss of competition in the market, this was caused by the exit of the Cumbrian business as a competitor to Young's, and was not causally attributable to the merger.

[3] Lion Capital paid £[ ].

9. The OFT will, as a general policy, adopt the prevailing conditions of competition as the counterfactual against which to assess the impact of a merger.[4] Due to the circumstances of this transaction, however, the OFT considered whether the exiting firm scenario was applicable in this case. In forming its view, the OFT considered:

   a. whether the firm would have exited through failure and, if so,

   b. whether there would have been an alternative purchaser for the firm or its assets to the acquirer under consideration, and

   c. what would have happened to the sales of the firm in the event of its exit.

a. Whether the firm would have exited through failure

10. The OFT notes that in October 2011 KPMG was tasked with selling the Cumbrian business as a going concern. Although the Cumbrian business had been profitable until the summer of 2011, a quality issue[5] led to the loss of business. This, combined with an increase in costs, resulted in a reduction in working capital and the firm reported losses. The Cumbrian business's bank, Barclays, was unwilling to increase its lending and asked PWC to review the business's cash needs.

11. The OFT understands that KPMG approached 35 parties (both trade and financial) but received a limited number of offers, two of which were below the solvent sale value and the third offer was withdrawn. With no alternative solvent buyers, the Cumbrian business issued a notice to appoint administrators on 1 December 2011.

12. PWC took over the Cumbrian business on 5 December having previously contacted 11 of the 35 parties approached by KPMG. The Administrators decided that in the best interests of the creditors, it would not trade the business as it did not have sufficient working capital to do so.

13. On the basis of the evidence available, the OFT considers that limb 1 of the failing firm scenario is met, that the Cumbrian business would not have continued to operate independently.

[4] OFT/CC joint *Merger Assessment Guidelines*, September 2010, paragraph 4.3.5.
[5] [].

b. Whether there would have been an alternative purchaser for the firm or its assets to the acquirer under consideration

14. The OFT understands that the offer from Lion Capital was the only formal bid made to PWC to acquire the Cumbrian business. At £[ ]. The parties submit that, as no real estate was acquired, the only Cumbrian assets that might have been acquired piecemeal were production equipment and that this equipment is not highly specialised. Further, the parties submit that the equipment is readily available from a variety of manufacturers and dealers, both new and used, at moderate cost.

15. The parties also submitted that due to significant excess capacity in the industry, any piecemeal acquisition of Cumbrian's assets by competitors would not change the competitive outcome. Further, the parties submit that Cumbrian's sites were configured in such a way that made piecemeal disposal difficult, in that Cumbrian configured its three plants so that they operated inter-dependently, with Seaham relying on Border Laird and Whitehaven for semi-processed inputs.

16. The OFT notes the parties' submissions. However, the OFT understands that there was tentative interest from other parties in the market with regard to acquiring some of the assets of the business including acquiring and operating individual sites and this has been confirmed by the OFT's third party enquiries. Although no bidder (other than Lion) appears to have been willing to acquire the whole firm without partners, the OFT was informed by several third parties that they would have been potentially interested in part of the business, but were not given sufficient opportunity to arrange and make a formal bid. Some of these potential purchasers are already active in the industry and hence would not need a site to operate fully independently and therefore may have considered purchasing some of the assets including real estate leases. The OFT understands that, between them, the third parties contacted by the OFT expressed interest in buying and operating all of the three sites used by Cumbrian.

17. the OFT is also mindful that it was not able to contact the 11 parties that PWC, as administrator had contacted: PWC considered that with respect to confidentiality it was unable to provide any details on the potential purchasers that it had spoken to. The lack of transparency over potential bidders contributed to the OFT being unable to conclude that there was not an alternative purchaser for the Cumbrian business or its assets.

18. Based on the evidence above, the OFT is therefore not able to be confident that in terms of limb 2, that there was no prospect of an alternative purchaser for the firm or its assets, although it appears likely that there was no firm willing to buy the entire business.

c. What would have happened to the sales of the firm in the event of its exit.

19. The parties submit[6] that [ ]. Nevertheless, the OFT considers that [], the commercial reality is that Young's is in an enhanced position to capture a proportion of the sales of the target business. Further, the OFT notes in the parties' internal documents[7] [ ].

20. The OFT understands that if no buyer had been found for the Cumbrian business, it would have ceased trading and its customers would have sought supply from others in the market. It is not unreasonable to assume that these contracts may have been split across a number of suppliers. The OFT notes that Cumbrian's sales had fallen [30-40 per cent] prior to the merger and, whilst some had switched to Young's, other suppliers had also benefited. The OFT is therefore not convinced that substantially all of these contracts would have been won by Young's in an open tender bid. It therefore cannot exclude that the exit of the Cumbrian business and its assets may have resulted in a different outcome for competition than the merger.

Conclusion on counterfactual

21. On the evidence currently available, the OFT is not confident that limbs 2 and 3 of the exiting/failing firm scenario are satisfied. On that basis, the OFT has proceeded to examine the merger on a counterfactual of the status quo where the Cumbrian business (albeit under different ownership) continued to operate in competition with Young's. Although the OFT has assessed the merger on this basis, it is mindful that a key factor in the demise of Cumbrian had been the quality issues regarding the supply of seafood to its customers and the resulting reputational impact this had on its ongoing commercial relationships. The OFT therefore considers that the Cumbrian business operating under different ownership would have had to rebuild, to a certain extent, its reputational standing with its customers and

[6] Parties letter dated 20 February 2012.
[7] Parties' submission Annex 3(b) 'Investment Committee Memorandum' page 5.

this would have taken a period of time to achieve. During this time, it is likely that Cumbrian would have been a less strong competitive constraint on Young's than prior to June 2011.

RELEVANT PRODUCT AND GEOGRAPHIC SCOPE

INTRODUCTION

22. The purpose of market definition is to provide a framework for the OFT's analysis of the competitive effects of the merger. The OFT's approach is to consider if narrow candidate product frames can be widened through substitution on the demand-side in each of the product categories in the first instance, and then, if appropriate, to consider if substitution on the supply-side allows the frame to be widened or aggregated.[8]

23. The parties overlap in the supply to retailers[9] of chilled ready-to-eat (RTE) seafood,[10] chilled ready-to-cook (RTC) seafood[11] and raw fish. The parties submit that around [ ] per cent of sales from the Cumbrian business were of private label chilled seafood products supplied to the major grocery retailers. The vast majority of Young's products are also own-label. In previous cases,[12] the OFT has considered that, on the demand side, branded goods constrain own label but not necessarily vice versa. On a cautious basis, therefore, the OFT has assessed the merger on the supply of own-label chilled fish and frozen seafood.

PRODUCT SCOPE

24. The parties submit that the appropriate frames of reference are chilled RTE products and chilled RTC products.[13] The parties submit that chilled RTE seafood products are distinguished from both raw fish and chilled RTC

[8] This approach is in line with the UK Authorities' joint *Merger Assessment Guidelines*, September 2010, paras.5.2.6 to 5.2.19.
[9] Cumbrian did not supply chilled seafood to food service operators.
[10] RTE seafood products include smoked salmon/mackerel, prawns, surimi and miscellaneous speciality products (for example, shellfish and terrines).
[11] RTC seafood products include coated fish and ready meals (for example, fish packaged with sauces or carbohydrates).
[12] See ME/4960/11 '*Anticipated acquisition by Princes Limited of the canning business of Premier Foods Group Limited'* 22 June 2011 and ME/4033/09 *'Completed acquisition by Dr. Oetker (UK) Limited of the business and assets of Schwan's consumer brands UK Limited*.' 5 May 2009
[13] Similar arguments were put forward in the 'Anticipated acquisition by Young's Bluecrest Seafood Limited of Macrae Food Group Limited and Pan European Seafoods UK Limited. 27 September 2004.

seafood, which require some preparation by the consumer. Further, the parties submit that the market should be widened to include all chilled RTE products including meat, cheese and vegetable products as all these products serve a common function, as snacks for entertaining, sandwich fillers and the like. Similarly, the parties submit that chilled RTC seafood products are distinguished by the ease of consumption from both raw fish (which requires greater and more skilled preparation by the consumer) and chilled RTC seafood (which requires essentially no preparation by the consumer) and these seafood products are sold in a market for all chilled RTC products.

25. The parties also submit that RTE and RTC seafood products are distinguished from frozen seafood products on the basis of a different customer demographic.

26. The parties also submitted supply side arguments in support of their view that the relevant product market is chilled RTE products and chilled RTC products. The parties submit that companies engaged in the processing/production of many RTE seafood products can switch relatively quickly and at low cost between different types of seafood. The parties also submit that producers of non-seafood RTE products can often switch easily into the production of seafood products and explain that surimi[14] is made with essentially the same process as is used to make pulverized meat products. In terms of chilled RTC seafood products, the parties submit that RTC seafood and poultry products require similar production lines and know-how, including coating, frying, filling and packaging. Further, the parties submit that many suppliers of RTC seafood and non-seafood products already supply a range of different products, and can therefore respond easily to changes in demand or competitive conditions.

27. The OFT's investigation did not support the parties' submission. Specifically, the majority of both customers and competitors consider that competition in chilled seafood operates on a product by product basis. Some third parties did view the market as broader than particular products, but this did not necessarily mean that they considered the whole of RTC or chilled seafood as one market.

[14] Surimi is a kind of pulverised fish paste used to make fish balls and imitation seafood products.

28. The OFT also notes that the internal documents of the Findus group marketing plan clearly considers the competitive conditions for each product type separately and several competitors are specialised to a single process or type of fish. Although the merging parties overlap in many different product areas, there are few other competitors that have such a broad base. As a result, the OFT considers that competitive conditions may differ in each product area reflecting the differences in, and the numbers of, competitors supplying that product. The OFT considers in detail below the supply-side arguments presented by the parties to widen the market.

29. In terms of the parties' supply-side arguments, the OFT generally refers to demand-side substitution alone when defining the relevant product market, but there are specific circumstances where it may aggregate several narrow markets into one broader one:

    a. production assets can be used by firms to supply a range of products which are not demand-side substitutes, and the firms must have the ability and incentive to quickly shift capacity between these products depending on demand, and

    b. the same firms compete to supply these different products and the conditions of competition between the firms are the same for each product.[15]

30. Given that evidence on the demand-side points to individual product areas, such as coated fish and cold water prawns, the OFT has considered whether these should be aggregated on the basis of supply side substitution, before considering the parties' arguments in relation to the wider aggregation of all RTE and RTC products.

31. As regards condition a., the OFT understands that the degree to which production assets are required in the supply of chilled seafood will differ between product areas. As a result, there may be constraints on a supplier of prawns, for example, shifting capacity to the supply of hot smoked salmon because of the need to acquire smoking equipment and associated technical expertise, together with the relevant supply and customer contracts and the associated food safety certification. Whilst there may be greater scope for a supplier of white fish to move into the supply of smoked fish, the OFT considers that the additional resources needed will

[15] CC/OFT *Merger Assessment Guidelines*, September 2010, paragraph 5.2.17

limit the ability of suppliers to quickly switch capacity between these products in response to changes in demand. The OFT has not seen convincing evidence on the relative margins of different products and the ease of switching to show that all or most seafood suppliers can easily enter other product areas.

32. As regards condition b., the OFT notes that with the exception of the merging parties, suppliers of chilled seafood tend to focus their supply in a limited number of product areas, for example Lyon in the supply of prawns, Thistle in the supply of coated fish, Morpol in the supply of salmon. Therefore it does not appear that the same firms compete to supply all the product areas of chilled seafood and hence the conditions of competition may be different in each product area.

33. Therefore the OFT considers that there is insufficient evidence to broaden the market to chilled RTE seafood or chilled RTC seafood, or wider (as proposed by the parties) to chilled RTE products and chilled RTC products on the basis of supply side substitution.

34. Market definition begins from the narrowest plausible market in which the parties overlap and therefore on a cautious basis, the OFT has considered the impact of the merger on each of the separate product areas.

Conclusion on Product Scope

35. The OFT considers it appropriate to assess the competitive effects of the merger in relation to the narrowest market satisfying the hypothetical monopolist test, that is, the separate product areas of:

- RTC Seafood – natural fish
- RTC Seafood – coated fish
- RTC Seafood – salmon
- RTE Seafood – smoked salmon
- RTE Seafood – hot smoked salmon
- RTE Seafood – hot smoked mackerel
- RTE Seafood – prawn cocktail

- RTE Seafood – prawns
- RTE Seafood – surimi
- RTE Seafood - shellfish

36. However, in the absence of competition concerns, the OFT does not consider it necessary to conclude on the precise product scope.

GEOGRAPHIC SCOPE

37. The parties submit that the transaction should be assessed on the basis of a UK-wide frame of reference. This is because the major suppliers are active UK-wide and supply customers on a national basis.

38. All customers and competitors contacted during the investigation agreed that the parties competed in the supply of chilled seafood to the major grocery retailers, who purchase on a UK-wide basis. The OFT has therefore examined the transaction at a UK level.

COMPETITIVE ASSESSMENT – UNILATERAL EFFECTS

39. The OFT has examined the possibility that the merged entity could unilaterally impose prices above the pre-merger level or deteriorate its competitive offering and has considered the evidence of the parties' shares of supply and closeness of competition.

Shares of supply

40. The merging parties are number one and number three in the supply of own-label chilled seafood (RTC and RTE), including white and coated fish to the major grocery retailers in the UK.

41. The share of supply estimates provided by the parties[16] show a combined share of the chilled seafood market of [30-40] per cent (with an increment [five-15] per cent). The OFT notes that the Findus group business plan, which shows shares of supply for 2010 by product segment, gives the parties a higher combined share of supply of [40-50] per cent (with an increment of [10-20] per cent) in the supply of chilled seafood with higher shares of supply in a number of individual product areas.

[16] Parties submission Annex 4.

42. The estimated shares of supply for each product area (by value) provided by the parties are set out in the table below. These shares of supply represent the average sales of the parties during the 12 months prior to the acquisition. However, with reference to the counterfactual, it has been possible to observe the changes in the parties' shares of supply leading up to the transaction.

43. The parties submit that they face significant competition from a large number of chilled seafood suppliers and name 16 competitors including Icelandic, Alfesca, Thistle Seafoods, Smales, Essco, Joseph Robertson, Morpol.

Product area	Value (£m)	Young's Per cent	Cumbrian Per cent	Combined Per cent
RTC Seafood – natural fish	323	[ ]	[ ]	[25-35]
RTC Seafood – coated fish	185	[ ]	[ ]	[35-45]
RTC Seafood – salmon	[ ]	[ ]	[ ]	[ ]
RTE Seafood – smoked salmon	[ ]	[ ]	[ ]	[ ]
RTE Seafood – hot smoked salmon	[ ]	[ ]	[ ]	[ ]
RTE Seafood – hot smoked mackerel	[ ]	[ ]	[ ]	[ ]
RTE Seafood – prawn cocktail	23	[ ]	[ ]	[45-55]
RTE Seafood – prawns	115	[ ]	[ ]	[40-50]
RTE Seafood – surimi	19	[ ]	[ ]	[80-90]
RTE Seafood – other shellfish[17]	38	[ ]	[ ]	[30-40]

Source: The Parties using Kantar data

[17] 'Other shellfish' includes a range of RTE varieties like crab, crayfish, langoustines, lobster, mussels, scallops, and mixed assortments of the forgoing.

44. The OFT notes there is no overlap in 'RTC Seafood – salmon' and 'RTE Seafood – hot smoked mackerel' and therefore these product areas are not considered further in the competitive assessment. The OFT also notes the minimal increment in 'RTE Seafood – hot smoked salmon' and in the absence of third party concerns, does not consider that the merger raises competition concerns over unilateral effects in this product area and therefore has not been considered further.

45. In relation to smoked salmon, Cumbrian had acted as a distributor of smoked salmon on behalf of Grants, which had the supply relationship with customers.[18] As there is no overlap in the supply of smoked salmon resulting from the merger, this product area has not been considered further.

46. In relation to the remaining product areas, the OFT considers that the shares of supply may be sufficiently high to raise prima facie concerns over unilateral effects and warrant further consideration.

47. The OFT also noted that the parties' Internal plans prepared for the merger[19] [ ].[20] Further, the Findus business plan names Cumbrian [ ].[21] In light of this evidence, the OFT asked the parties to provide details of their gross margins for each of the product areas identified in order to help it assess the competitive effects of the merger.

RTC Seafood – natural Fish

48. The parties have an estimated combined share of supply of [25-35] per cent with an increment of [10-20] per cent in the supply of natural fish. Icelandic is the closest competitor to the merged entity with an estimated share of supply of [10-20] per cent. Other competitors include SeaLord,[22] Smales, and Dawnfresh.

49. A number of customers initially raised concerns in relation to whether they would be able to find alternative supplies of white or counter fish in the short term. However, on further investigation they clarified these concerns

[18] Cumbrian sold Grant's Smoked Foods in August 2009 and thereafter acted as Grant's agent and distributor.
[19] Lion Capital 'Investment Committee Memorandum' 4 December 2011.
[20] Parties' submission Annex 3(b) 'Investment Committee Memorandum' page 5.
[21] Parties' submission Annex 8 'Findus Group: AOP Presentation' December 2010.
[22] SeaLord is a dedicated supplier to Waitrose.

related to the question of short term supply and switching costs and most customers agreed there were several supply options even in the short-term. A number of competitors that the OFT contacted during the investigation confirmed that they would consider entering or expanding in this market. It was noted, however, by one third party that the breadth of operations of the merging parties allows for greater integration of processes, for example using offcuts of fish from fillet products to produce fishcakes, which may put them at a competitive disadvantage. Furthermore, one competitor considered that it could take up to two years to secure new lines of supply to be able to assure supermarkets of the reliability required.

50. The OFT also spoke to one competitor that suggested that entry or expansion was difficult because retailers had longer term agreements with the parties that restricted retailers' ability to switch supply in the short term, however OFT enquiries did not suggest that there were fewer opportunities for gaining business in 2012 post merger than was likely pre-merger. In particular, retailers confirmed that the merger has given them more reason to review the supply options available in this market in order to limit the extent of short-term dependence on one supplier.

51. In order to assess the closeness of competition between the parties, the OFT requested information on the value of contracts that customers have switched from Cumbrian to an alternative supplier.[23] During the second half of 2011 prior to the merger, Cumbrian lost some £[ ] of natural fish business supplying the major grocery retailers, of which over £[ ] was won by competitors to Young's. Based on changes in recent supply contracts, the OFT has calculated a diversion between the parties in relation to natural fish of [ ] per cent. Further, based on the information provided by the parties, the OFT considers their gross margins in this product area relatively low for a production business at between [ ] and [ ] per cent,

52. The OFT's investigation identified a number of suppliers that have existing spare capacity to be able to supply the major supermarkets with natural fish. In addition, the OFT notes that some suppliers have invested in new capacity and this is due to become available in the coming months. This is discussed further in the entry and expansion section below and counteracts the concern expressed regarding securing new lines of supply.

[23] [ ].

53. Although the shares of supply in this product area are not low, set against this is the evidence that the margins are low and the majority of Cumbrian's contracts have been won by competitors to Young's, resulting in a relatively low diversion ratio between the parties. The OFT considers that on the balance of evidence, the merger does not raise unilateral competition concerns in the supply of natural fish.

RTC Seafood – coated fish

54. The parties have an estimated combined share of supply of [35-45] per cent with an increment of [five-15] per cent in the supply of coated fish. Icelandic is the closest competitor to the merged entity with an estimated share of supply of [10-20] per cent. Thistle Seafoods and Northern Seafoods each have an estimated [10-20] per cent share of supply of coated fish.

55. The OFT received one concern in relation to the supply of coated fish. The OFT notes that the parties' margins are higher for coated fish at [ ] per cent than for other product areas. However, with reference to Cumbrian's contracts that were lost in 2011, of the £[ ] lost business, none went to Young's. As a result, the parties estimate that their current share of supply of coated fish has fallen to [five-15] per cent. Further, a number of the suppliers that OFT spoke to during the investigation confirmed that they did have spare capacity and could expand production to meet new orders from the main grocery retailers.

56. On the basis that customers have switched supply to alternative suppliers and there is evidence of spare capacity remaining, the OFT does not consider that the merger raises unilateral competition concerns in the supply of coated fish.

RTE Seafood – prawn cocktail

57. The parties have an estimated combined share of supply of [45-55] per cent with an increment of [0-10] per cent. Icelandic is the closest competitor to the merged entity with an estimated share of supply of [20-30] per cent, followed by Alfesca at [10-20] per cent.

58. The parties are considered to be low cost producers in this product area and have estimated margins of approximately [ ] per cent. Some concerns were raised by a third party in that the merger has resulted in the loss of specialised equipment used to produce prawn cocktail; this third party indicated that to compete at high volume, higher throughput equipment costing £1-2 million may be required. However, the parties disputed that the equipment is specialised. Young's confirmed that [ ]. Further, the parties submit that production lines used to produce prawn products cost approximately £500,000 to £1 million and are widely available. Other than this one third party, no other respondent suggested prawn cocktail should be considered separately to cold water prawns.

59. The OFT notes that Cumbrian has lost business including a contract to one of the retailers worth nearly £[ ] in the second half of 2011. As a result, the parties' current combined share of supply is estimated to be [30-40] per cent. The OFT considers that there are a number of strong existing competitors and recent entrants in this product area that should place sufficient constraint on the merged entity post merger.

RTE Seafood – prawns

60. The parties have an estimated combined share of supply of [40-50] per cent with an increment of [15-25] per cent in the supply of prawns. Alfesca is the closest competitor to the merged entity with an estimated share of supply of [40-50] per cent and Blue Earth has a share of [0-10] per cent.

61. The parties submit that each sources prawns from independent suppliers and their operations consist of repacking bulk supplies into smaller consumer-sized trays. Accordingly, the parties' estimated margins are relatively low at [ ] per cent.

62. One third party commented that there were few remaining sources of production available for cold water prawns. However, in terms of processing, the OFT notes that in addition to Alfesca, a number of smaller suppliers have recently won contracts to supply the major retailers resulting in a decline in the parties' estimated combined share of supply to [15-25] per cent. Further, the OFT notes that some suppliers have invested in new capacity and this is due to become available in the coming months. Customers confirmed that there were suitable suppliers with spare capacity

in these products. This is discussed further in the entry and expansion section below. The OFT therefore considers that there are a number of strong existing competitors and recent entrants in this product area that should place sufficient constraint on the merged entity post merger.

RTE Seafood surimi

63. The parties have an estimated combined share of supply of [80-90] per cent with an increment of [20-30] per cent in the supply of surimi. Other small suppliers account for the remaining [10-20] per cent share of supply of surimi.

64. The partiers submit that surimi is traded internationally (both parties obtain their current supplies from independent manufacturers in East Asia) and the surimi processing industry has significant excess capacity.

65. The OFT notes that [ ]. Despite the high shares of supply, no third party concerns have been raised in relation to this product even from customers that have considered the issues in surimi and raised initial concerns in other areas. Customers considered that this was a very simple production process in the UK that could easily be done by other suppliers. Given that the parties both had to source their supplies from East Asia, they would have no competitive advantage in purchasing surimi compared with a new entrant.

66. The OFT also notes that, whilst the parties have estimated margins of between [ ] and [ ] per cent, recent press reports state that retailers are refusing to pass on any cost increases to consumers despite increases in raw material costs and are also looking to overseas suppliers.[24] On the evidence available, the OFT does not consider that the merger raises unilateral competition concerns in the supply of surimi.

RTE Seafood other shellfish

67. The parties have an estimated combined share of supply of [30-40] per cent with an increment of [five-15] per cent in the supply of other shellfish. Alfesca is the closest competitor to the merged entity with an estimated share of supply of [10-20] per cent and Icelandic has a share of [0-10] per cent. There is a long tail of other smaller suppliers.

[24] 'Surimi processors: Retailers won't pass on price increases' Intrafish.com, 5 March 2012.

68. The OFT has not received concerns regarding this product area and notes that there are a range of suppliers who already supply the retailers with other products, including Blue Earth and the Big Prawn Company. Therefore, on the evidence available, the OFT does not expect the merger to raise unilateral competition concerns in the supply of other shellfish.

Conclusion on Unilateral Effects

69. The parties will, as a result of the merger, have a combined share of supply of chilled seafood by value of [30-40] per cent. Overall, on the basis of the available information, the parties are not considered to be sufficiently close competitors in any of the product areas reviewed, with the exception of the supply of surimi (where customers considered that it was straightforward to source alternative suppliers such that the large share of supply did not reflect market power on the part of the merged entity). The OFT is persuaded by the evidence provided by the parties in relation to the loss of Cumbrian's sales since mid 2011 that indicates reasonably low diversion ratios between the parties. This, together with the relatively low margins experienced by the parties, indicates that the merger is not considered to raise competition concerns over unilateral effects.

70. The OFT considers there is sufficient evidence of existing spare capacity in these markets and during its investigation, it received further evidence of expansion and entry. Added to this, the OFT received few complaints regarding the merger, but customer reaction merely reflected initial uncertainty and short-term switching costs or market adjustment. The OFT therefore does not consider there to be a realistic prospect of an SLC in the supply of chilled fish or seafood to the large grocery retailers in the UK or in any of the individual product categories within chilled fish or seafood.

SUPPLY-SIDE RESPONSES

71. The OFT has considered the potential for new entry and expansion and the extent that buyer power exists in the supply of individual product areas of chilled seafood to the major grocery retailers.

Prospect of entry and expansion

72. When assessing possible supply-side responses, including entry, expansion and repositioning, the OFT will consider whether the response would be (i) timely, (ii) likely, and (iii) sufficient.[25] In terms of timeliness, the guidance suggests that the OFT will look for entry to occur within two years.

73. The parties submit that there are low barriers to entry and expansion into the supply of chilled seafood. The parties submit that the basic raw materials – fish, other ingredients and packaging – can be readily obtained from numerous suppliers. Further, that the supply of seafood does not require highly specialised factory space, equipment or personnel. The parties submitted that Cumbrian's equipment primarily relates to final-stage processing and packaging from bulk to consumer-sized packages and is generic to the food processing industry. The parties submit that this equipment is freely available from both new and second hand sources.

74. The parties submit that the existence of a large number of small or specialised suppliers demonstrates that a new entrant need not offer a wide range of products. This is made easier, according to the parties, by the fact that major retailers multi-source their supply, thereby providing frequent opportunities for new suppliers to obtain new business.

75. The parties also submit that suppliers of frozen fish and ready meals may be well placed to expand into the supply of chilled seafood and identify Alfesca, Boparan/Northern Foods and Smales as examples. The parties also submit that potential supplies such as Bakkavor Group, Greencore Group and Kerry Foods/Headland Foods have the recognised brands, financial resources and relationships with retailers to enter the market.

76. The OFT's investigation confirmed that some competitors have spare capacity in existing factories and others are expanding. One competitor confirmed that they are building a new site that will be operational in 6 weeks which has the capacity to service contracts, valued at £50 million. Although some retailers have dedicated suppliers or facilities, there was evidence that the majority of suppliers serve a range of customers.

77. Whilst the OFT received some concerns from third parties regarding the availability of equipment, the OFT considers, based on the information

[25] CC/OFT '*Merger Assessment Guidelines'*, September 2010 paragraph 5.8.3.

available, that the equivalent equipment to that used by Cumbrian is available on the new or second hand market and therefore should not represent a barrier to entry or expansion in the supply of chilled seafood.

78. Further, during the investigation, Morrisons, the grocery retailer announced that it had acquired a fish processing plant in Grimsby and plans to produce 10,000 tonnes of seafood a year.[26] In respect of this entry, the OFT is aware that this capacity is intended to be used for self-supply rather than supply to third party purchasers. However, Morrisons' entry is still relevant both in so far as it demonstrates an alternative supply route available to the large grocery retailers (see the buyer power section, below) and in so far as the capacity that would otherwise have been used to supply Morrisons will going forward be available for third party supply.

79. Two third parties raised concerns about obtaining upstream sources of supply when entering or expanding a new product market in chilled seafood. However, these concerns were not shared by the majority of suppliers.

Conclusion

80. The OFT considers that there is evidence of entry and expansion in this market which is timely, likely and sufficient to allow suppliers to compete effectively with the merged entity and therefore act as an effective competitive constraint on the merged parties.

Buyer Power

81. The parties submit that they face significant buyer power from their customers, the major grocery retailers, due to the significant volumes purchased by them and hence, suppliers are dependent on them as a route to market. Further, that the major grocery retailers can switch suppliers at short notice, particularly for private label products where the supplier can not claim any consumer brand loyalty.

82. The parties submit that switching is facilitated by the fact that supply contracts generally contain a standard 12-week notice provision and that the grocery retailers typically multi source from a large number of chilled seafood suppliers. The parties provided examples of where the major

[26] Retail Week 'Morrisons buys fish factory in acquisition drive' 5 March 2012.

retailers have switched suppliers over the past year. The parties submit that some retailers are now [ ], thereby shifting the risks of raw material cost increases to suppliers.

83. The OFT notes that the major grocery retailers have switched their contracts to alternative suppliers with a limited notice period of between two and 12 weeks. While switching supplier may create some disruption to retailers, evidence indicates that they can and do engage in regular tenders.

84. The OFT is also mindful of the fact that there is evidence that the major grocery retailers can adopt different strategies to reduce any dependence on seafood suppliers, specifically:

- Morrisons has vertically integrated by investing in its own fish processing factory, and
- certain other grocers, [ ] and [ ], purchase certain fish products directly from original suppliers, without relying on purchases through Young's or other competitors.

85. The OFT considers, therefore, that there is evidence in this case that the grocery retailers may enjoy some degree of buyer power in relation to their purchases of fish. However, given its view on the competitive assessment described above, it has not been necessary for the OFT to conclude on the issue of buyer power in any further detail.

THIRD PARTY VIEWS

86. The OFT received comments from major customers and competitors of the parties. The OFT has included specific reference to third party views in the above detailed assessment but for the sake of completeness, notes the following.

87. The OFT received the following concerns from customers. Some of those customers that Cumbrian had hitherto supplied considered that the merger would result in a reduction in the choice of suppliers. However, this was subsequently clarified as it became apparent that there was sufficient spare capacity in the industry to meet customer requirements and related more to concerns over potential costs involved in switching suppliers. Ultimately, only one customer considered that the merger may raise concerns of limited supply options in the short term. The OFT observed that in addition

to the spare capacity available in each of the product areas, there was also evidence of new entry and expansion by a number of suppliers. This includes the recent announcement by Morrisons, as outlined above, to enter the market themselves.

88. The comments received from competitors were more mixed, with one supplier raising a concern with regard to potential difficulties in obtaining sources of supply. However, this concern was not shared by other suppliers and, overall, it was considered that whilst the merger has led to greater consolidation, there remains spare capacity in the industry resulting in a very competitive market.

ASSESSMENT

89. The parties overlap in the supply of own-label chilled fish and seafood to the major grocery retailers in the UK. The parties were two of the four largest suppliers and have an estimated combined share of supply of [30-40] per cent in the supply of chilled seafood (with an increment of [five-15] per cent).

90. Cumbrian entered administration on 5 December 2011 and was sold to Lion Capital the same day. The OFT considered whether the criteria of the failing/exiting firm scenario were established, but could not be satisfied, in relation to limb 2, that there was no alternative purchaser for the firm or its assets, particularly when the prospect of different purchasers acquiring different parts of the Cumbrian business is taken into account. Nor was it clear to the OFT that limb 3 of the failing/exiting firm scenario is satisfied. The OFT therefore examined this merger with a counterfactual of the status quo where the Cumbrian business (albeit under different ownership) would have continued to operate in competition with Young's.

91. The OFT has assessed the merger on the basis of individual product areas including natural fish, coated fish, prawns and prawn cocktail, surimi, and other shellfish. Whilst the parties' internal documents indicate that they are close competitors, it became apparent during the investigation that there are a number of alternative suppliers in each of the product areas (including surimi, in which the parties would enjoy high market shares). Specifically, the OFT was able to observe the diversion between the merging parties as a significant proportion of Cumbrian's customers switched their contracts to alternative suppliers in the period leading up to the merger. In the six

months prior to the transaction, the sales of Cumbrian fell [30—40 per cent]. Of this lost volume, approximately [ ] per cent transferred to Young's [ ].

92. Most of the product overlaps of the parties did not give rise to concerns in the market. Limited concerns were raised with regard to the supply of white fish and coldwater prawns, where the parties have an estimated share of supply of approximately [30-40] per cent. However, in both these product areas, margins are relatively low and there is evidence of significant entry and expansion, including entry by the grocery retailer, Morrisons, which has acquired its own fish processing plant. The OFT therefore considers that existing and timely new capacity would be sufficient to replace that lost by the merger.

93. In relation to surimi, where the parties' market share is very significant, customers were clear that the merger did not give rise to concerns given the ease of obtaining alternative suppliers and the fact that entrants into this market would be able to compete effectively with the merging parties given that the parties themselves were required to source this product from East Asia.

94. The OFT also found some evidence that the grocery supermarkets were in a position to exercise a degree of buyer power in relation to these markets, both through regular tendering processes, vertical integration or the prospect of direct supply.

95. On the balance of evidence and given the size and speed of entry into these markets that has actually taken place, or is in the process of taking place, since the merger, the OFT does not consider that this merger results in a realistic prospect of a substantial lessening of competition in the supply of chilled fish or seafood in the UK or any of the specific product categories in which the parties overlap.

DECISION

96. This merger will therefore not be referred to the Competition Commission under section 22(1) of the Act.

ENDNOTES

1. With reference to paragraph 44, the parties clarified that there is no overlap in 'RTE Seafood – hot smoked salmon' because Cumbrian acted only as a distributor on behalf of Grant's. This clarification does not impact on the OFT's conclusions in this case.