



Anticipated acquisition by Koch Industries, Inc of J & H Bunn Limited

ME/4849/11

The OFT's decision on reference under section 33(1) given on 24 February 2011. Full text of decision published 3 March 2011.

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.

PARTIES

1. **Koch Fertiliser Limited ('KFL')** is an indirect wholly-owned subsidiary of Koch Industries, Inc ('Koch') and is active in the sale of fertilisers in the UK. Koch is a privately-owned company headquartered in Wichita, Kansas, USA. It is the ultimate parent company of the Koch Group. The Koch Group is an international group of companies with operations in refining, wood and paper products, polymers and fibres, fertilisers, commodity trading and chemical engineering. Koch's UK turnover in 2009 was £[]billion of which £[] million was derived from fertiliser sales.
2. **J&H Bunn Limited ('Bunn')** is a privately owned company headquartered in Great Yarmouth, Norfolk, UK. Bunn blends and sells fertilisers to farmers and agricultural merchants. Its UK turnover in the year ended 31 March 2010 was £141.5 million.

TRANSACTION

3. KFL intends to acquire majority control (up to 100 per cent) of Bunn. The transaction is conditional on OFT clearance.

4. The OFT received a satisfactory submission on 17 January 2011. The administrative deadline is 14 March 2011.

JURISDICTION

5. As a result of this transaction KFL and Bunn will cease to be distinct. The UK turnover of Bunn exceeds £70 million, therefore 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 will be created.

RATIONALE

6. KFL entered the UK fertiliser market relatively recently in 2008 and [].
7. The parties state that Bunn represents a particularly good fit with Koch's existing global business. KFL has particular expertise with regard to nitrogen fertilisers, and Bunn's strength and reputation lies in blended complex fertilisers.

MARKET DEFINITION

8. The parties overlap in respect of the supply of fertilisers in the UK. In particular, both Bunn and Koch's UK fertiliser business, operated by KFL, supply wholesalers distributors/retailers and end users with straight nitrogen, straight potassium, straight phosphorous and complex (blended and compound) fertilisers.
9. Fertilisers consist of one or more main nutrients required by plants, in particular, 'primary nutrients', which are nitrogen 'N', potassium 'K' and phosphorous 'P'. All plants need a balance of these primary nutrients, although the proportion of each nutrient that a plant needs will vary from crop to crop. These primary nutrients are applied to the land either separately, in the form of a 'straight' fertiliser (consisting of a fertiliser containing just one primary nutrient) or combined, in the form of a

'complex' fertiliser (whereby the fertiliser contains more than one primary nutrient). Both parties supply straights and complex fertilisers.

10. Complex fertilisers, also known as 'NPK fertilisers' or 'multi-nutrient fertilisers', come in two forms:

- Blended fertilisers: these are obtained by dry mixing several materials in a blending machine. Each fertiliser granule contains one type of primary nutrient but in aggregate, the whole blend of raw materials contains the mix of N, P and K that the farmer has requested.
- Compound fertilisers: these are obtained by combining primary nutrients by way of a chemical reaction, such that each individual granule contains the required mix of primary nutrients as requested by the farmer.

Supply chain

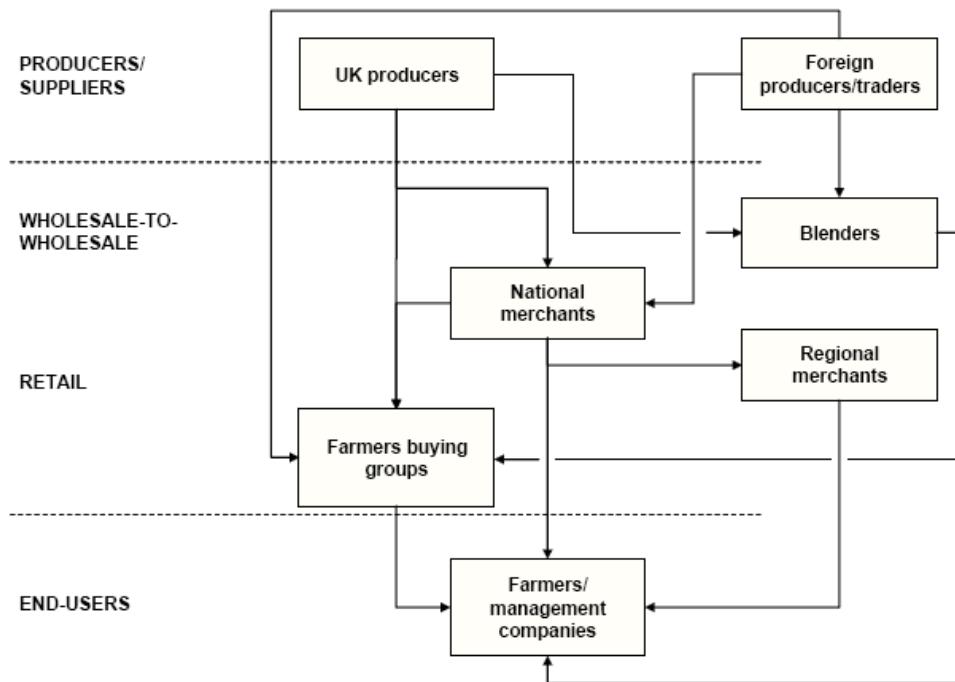
11. In Yara/Kemira¹ three different levels of the supply chain were distinguished by the European Commission; supply to wholesalers; supply to distributors/retailers; and supply to end users.

12. In Kemira/Terra² the Competition Commission (CC) in the UK found that the distribution of fertiliser was more complicated than a supplier-wholesaler-retailer relationship. In particular, suppliers could use a range of distribution channels for their fertilisers. Figure 1 reproduces a graphical representation of the supply chain of fertilisers used in Kemira/Terra:

¹ COMP/M.4730, *Yara/Kemira GrowHow* (21 September 2007).

² CC report *Kemira GrowHow Oyj and Terra Industries Inc merger inquiry: A report on the anticipated joint venture between Kemira GrowHow Oyj and Terra Industries Inc* (11 July 2007).

Figure 1: the fertiliser supply chain



Source: CC, based on Terra and Kemira.

13. The parties' positions in the supply chain seem to be broadly consistent with that of 'blenders' for Bunn and of 'national merchant' for KFL given that they both sell to end users and buying groups. Although, a distinction was drawn in Kemira/Terra on sale to wholesale and retail customers, it was noted in Origins/Masstock³ that the distinction is blurred in relation to the supply of fertiliser. The OFT agrees with this assessment. It has not therefore been necessary to conclude in definitively categorising the parties although the OFT is of the view that they broadly operate at the same level of the supply chain.⁴

14. The large majority of KFL's sales are made at the wholesale level of trade (approximately [] per cent). Bunn makes approximately [] per cent of its sales to the wholesale level and [] per cent to end users.

³ Completed acquisition by Origin Enterprises plc of Masstock Group Holdings Limited, decision of 22 May 2008.

⁴ In any case, the parties submitted that although they were unable to estimate the total size of the market split between wholesale and retail customers, they estimated that their market shares would not differ materially to if both of these segments were taken together. No third party respondents disagreed with this assessment.

15. Bunn blends fertilisers for KFL as well as blending its own fertilisers which it sells on. KFL does not manufacture any fertiliser products within the UK, and all its sales are the result of reselling imported products, either directly to farmers or to agricultural merchants. Most of KFL's UK fertiliser sales consist of straight nitrogen products, but a small amount (less than [] per cent) represents sales of blended fertiliser products. Of KFL's blended fertiliser products, the majority (about [] per cent) are blended by Bunn, under an OEM toll manufacturing or packing arrangement. The remaining [] per cent of KFL's blended fertilisers consist of products blended by KFL at its Avonmouth site. This vertical relationship between the parties is considered further under Vertical Issues.

Product market

16. The OFT considered whether straight and complex fertilisers were part of the same product market. On the supply side, it seems that large suppliers of complex fertilisers could switch to supplying straight fertilisers directly if the price of straight fertilisers was to increase. While ultimately leaving the market definition undecided, the European Commission (Commission) also suggested in Yara/Kemira⁵ that end-users could mix nutrients together themselves. In Kemira/Terra the CC considered straight N fertilisers separately from complex fertilisers, although was not required to come to a conclusion on this issue for the purposes of its analysis. The views of third parties on substitution between straight and complex fertilisers were inconclusive, so the OFT has taken a cautious approach and considered straight and complex fertilisers separately.
17. There are multiple types of straight N, P and K fertilisers. In relation to N fertilisers, for example, these include urea, calcium and ammonium nitrate, amongst others. These varieties can require different production facilities and some are more appropriate for certain crops than others. However, previous cases have found that for N, P and K fertilisers there are separate product markets which include all varieties within these markets, and the OFT did not obtain evidence to suggest that it should change this approach.

⁵ COMP/M.4730, *Yara/Kemira GrowHow* (21 September 2007).

18. Finally, the OFT considered whether there was a distinction between 'compound' and 'blended' complex fertilisers. Compound fertilisers are produced by combining the nutrients N, P and K in a single granule by means of a chemical reaction. Blended fertilisers mechanically mix different granules containing either N, P or K to form a desired composite of N, P and K. In Kemira/Terra the CC found that, although farmers had preferences for either blended or compound fertilisers, they were substitutes and formed part of one 'complex' fertilisers market. The OFT did not obtain any evidence during its investigation to suggest that it should change this approach.

19. In summary, the following distinctions can be drawn from the OFT's analysis of the various product markets:

- N, P and K fertilisers are considered distinct markets
- straight/complex fertilisers are considered separately
- no single combination of compound or blended fertilisers is considered distinct, and complex fertilisers, that is compound and blended complex fertilisers are considered in the same market.

20. Despite these distinctive product markets, the issues arising in the competitive assessment are relatively similar in relation to each product.

Geographic market

21. In previous OFT, CC and Commission investigations, the various markets for fertiliser have tended to be at least UK wide. In Kemira/Terra the market for N fertilisers was considered to be at least EEA wide, and the market for complex fertilisers considered to be UK wide. In Yara/Kemira a distinction was made at various levels of the supply chain; wholesalers were found to source fertiliser on at least an EEA wide basis whereas the supply to retailers and end customers was found to have a national dimension. On a cautious basis, in Origin/Masstock, the OFT considered the transaction on a regional basis as well as on a national one.

22. The parties submitted that the market is national at its narrowest. They noted that retailers such as agricultural merchants import fertilisers from overseas but that the supply to retailers and end users tends to occur on

a national basis. Bunn supplies fertilisers across the UK through twelve terminals, while KFL has only one terminal at Avonmouth⁶. The parties submitted that they both supply across the UK, however in response to further questions they stated that approximately [] per cent of KFL's customers are located within 120 miles of Avonmouth.

23. On a cautious basis, the OFT considered whether the market could be divided along regional lines based on the location of the majority of each of the parties' customers.
24. On the demand side the parties submitted that over [] per cent of KFL's customers are at the wholesale level such as national merchants and farmers buying groups. In response to third party enquiries wholesalers and farmers buying groups broadly agreed that they did not require a regional presence from suppliers and deal directly with suppliers from across the UK. Those end user customers contacted also stated they used national as well as regional suppliers.
25. Further evidence for a national market was given from the supply side by the relatively small percentage of total production costs associated with transport. The parties estimated that transport costs account for [] per cent of total production costs which third parties broadly agreed with and one competitor (Growhow) stated that they have a national pricing policy irrespective of transport costs.
26. While KFL operate primarily from a single depot in the south-west the majority of their customers are at the wholesaler/buying group level where the most appropriate geographic frame of reference appear to be at the UK level. Bunn, as a blender with nationwide depots, also fits within a UK frame of reference.
27. Ultimately, it was not necessary for the OFT to reach a conclusion on whether the relevant market was narrower than the UK since the merger does not give rise to competition concerns on either a regional, national or European wide market definition. Customers of the parties who responded to the OFT confirmed that they typically purchase on the basis of a single nationwide contract with one or more suppliers. Competitors confirmed that they either already supplied on a national basis or if they did not do

⁶ It also subcontracts packaging and blending services from Bunn at Great Yarmouth.

so already, that they were willing and able to do so should a contract require it. On this basis, the OFT has assessed this merger on the basis of a UK wide geographic market.

HORIZONTAL ISSUES

Market shares

28. The parties provided estimates of market shares for the supply of each of the three straight fertilisers (N, P, and K) and for complex fertilisers. They informed the OFT that they did not believe there was any significant difference to market shares if each of these markets was split according to whether customers were wholesale or end-users. The market share estimates were broadly supported by third party respondents.

Straight N fertilisers

29. The parties have an estimated combined share of supply of [0-10] per cent in straight N fertilisers in the UK with an increment of [0-10] per cent from KFL. There are strong competitors present in the market such as GrowHow UK with around [40-50] per cent, and Yara with around [20-30] per cent share of the market. In addition there are many other smaller players. The OFT did not receive any complaints about any adverse competition effects in relation to the supply of straight N fertiliser.

Straight P Fertiliser

30. The parties have an estimated combined share of supply of [40 -50] per cent in straight P fertilisers in the UK with an increment of [0-10] per cent from KFL. Although, the parties will have a significant market share the increment is small and is unlikely to change market conditions. There are several other significant providers in the market including Origin with around [20 – 30] per cent share and Carrs with an estimated [10 – 20] per cent market share. The OFT did not receive any complaints about any adverse competition effects in relation to the supply of straight P fertiliser.

Straight K Fertiliser

31. The parties have an estimated [40 -50] per cent share of supply in straight K fertilisers in the UK with an increment of [0 – 10] per cent from KFL. Given that the increment is so small the merger is not believed to have a significant effect on the supply of this product. In addition, there will remain other significant suppliers with the ability to constrain the parties such as Origin with an estimated [20-30] per cent of the market and Carrs with [10 – 20] per cent. The OFT did not receive any complaints about any adverse competition effects in relation to the supply of straight K fertiliser.

Complex fertilisers

32. The parties have an estimated combined share of supply of complex fertilisers of [30 – 40] per cent with an increment of [0-10] per cent from KFL. The increment is modest and the parties will continue to face competition from Origin with an estimated [20-30] per cent share of supply, GrowHow UK with an estimated [20-30] per cent share of supply, Carrs with an estimated [10-20] per cent share of supply and Yara with an estimated [0-10] per cent share of supply. In addition, the OFT did not receive any complaints about any adverse competition effects in relation to the supply of complex fertilisers.

Closeness of competition

33. The parties submitted that they do not compete closely because, as noted above at paragraph 7, KFL specialises in nitrogen fertilisers such as urea and urea ammonium nitrate, and Bunn focuses on blended complex fertilisers. In addition, KFL has a substantially smaller presence in each of the overlap markets, as evidenced by its market shares, to be considered to provide anything nearing a competitive constraint on Bunn.

34. The information obtained from third parties confirms that the parties do not compete closely. One competitor commented that, Koch is mainly focused on UREA and UAN (straight fertilisers) while Bunn is focussed on blended fertilisers. This is supported by the fact that KFL has a considerably lower market share in each of the fertiliser markets identified than Bunn. Third parties indicated that post-merger they would continue to have several alternative suppliers from whom to obtain fertilisers.

35. This is further evidenced by over [] per cent of Koch's overall supply of fertilisers being in the market for straight N fertilisers compared to less than [] per cent of Bunn's overall supply. In addition over [] per cent of Bunn's overall supply of fertilisers is in the market for complex fertilisers compared to less than [] per cent of Koch's overall supply.
36. In summary, the evidence suggests that, the parties are not close competitors. KFL's presence in the supply of all fertilisers is sufficiently small and the number of alternative competitors sufficiently great, such that even if they were direct competitors the transaction would not raise competition concerns. The OFT does not therefore consider that the merger will result in competition concerns on a horizontal basis in any of the relevant product markets.

VERTICAL ISSUES

37. No vertical concerns were raised by third parties. However, given the vertical relationship between the parties (see paragraph 15 above), the OFT considered whether the parties would have the ability and incentive to foreclose supply to downstream market participants, or foreclose a route to market for upstream market participants.
38. There are two aspects to the vertical relationship between the parties:
- (i) KFL supplies straight N fertiliser to Bunn amounting to around [] per cent of Bunn's total purchase of straight N fertiliser.
 - (ii) KFL has limited blending capabilities itself, and is primarily involved in the purchase and sale of fertiliser to end users and wholesalers. As explained above, Bunn blends [] per cent (some [] tonnes) of KFL's complex fertilisers, using raw ingredients supplied by KFL.
39. Given the small amounts involved in each of these arrangements, the OFT does not consider that there is a realistic prospect of the merger leading either to foreclosure of supply of N fertilisers or to foreclosure of blending facilities.

THIRD PARTY VIEWS

40. The OFT consulted a range of third parties at all levels of the supply chain. None had any merger specific concerns. Several indicated that they felt that this was a market which was experiencing consolidation in recent years although they did not have any specific concerns arising from this particular merger.

ASSESSMENT

41. Both KFL and Bunn are involved in the supply of fertiliser in the UK.

42. Both parties operate at the wholesale level of the supply chain.

43. The starting point for the OFT's assessment of the relevant markets were the previous CC and Commission decisions in the fertiliser industry. Third parties consulted by the OFT supported the product markets identified in these cases, including separate markets for straight and complex fertilisers, separate markets for N, P and K fertilisers, and no clear distinction between compound and blended fertilisers.

44. In relation to the geographic market, third parties agreed that competition occurred on a national basis consistent with conclusions in previous CC and Commission decisions. Overall however, similar issues arose in the competitive assessment irrespective of the various product and geographic markets identified.

45. Unilateral concerns do not arise as a result of the proposed transaction. In all the markets identified the increments are small (below [] per cent) and there are several other competitors to rival the parties. Most competitors were unconcerned by the merger. The majority of the parties' customers, informed the OFT that they believed they would retain a sufficient degree of choice post-merger. No vertical concerns were raised by this merger.

46. Consequently, the OFT does not believe that it is or may be the case that the merger has resulted or may be expected to result in a substantial lessening of competition within a market or markets in the United Kingdom.

DECISION

47. This merger will therefore not be referred to the Competition Commission under section 33(1) of the Act.