

Anticipated acquisition by AB Agri Limited of the business and assets of the Uffculme Feed Mill

ME/5095/11

The OFT's decision on reference under section 33(1) given on 1 September 2011. Full text of decision published 15 September 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. **AB Agri Limited** (AB Agri) is a wholly owned subsidiary of Associated British Foods plc (ABF). AB Agri manufactures and distributes agricultural products, animal feed and related products. AB Agri's turnover for the year ended 18 September 2010 was £954 million. It is a national UK animal feed supplier, which produces compound feed for monogastric animals through its ABN division and markets blended feed and co-products for ruminants through its alternative feeds division, KW Trident. AB Agri has nine compound feed mills manufacturing monogastric feed in Great Britain,¹ the closest of which to Uffculme Mill is Cullompton Mill in Devon.
2. **The Uffculme Mill** (Uffculme Mill) produces monogastric animal feed solely for Hook2Sisters and is a single feed mill in Devon. It is held as follows:
 - i. Uffculme Feed Mill Limited owns the feed production business and rights associated with the Uffculme Mill and manages the feed production business and

¹ In addition to its own manufacturing facilities, AB Agri currently has [] agreements with independent companies in relation to monogastric compound feed under which those companies manufacture additional products for distribution and sale by AB Agri. This is known as contract or toll manufacturing and involves the manufacture of feed by a third party to AB Agri's formulation (in respect of which AB Agri owns the IP rights).

- ii. ASG Properties (Jersey) Limited owns the freehold interest and assets in the Uffculme Mill.²

Both these companies (together 'the sellers') are registered in Jersey and are ultimately held by [], the beneficiary of which is the Boparan family.

3. The acquisition relates to Uffculme Mill and its associated assets. The UK turnover of the Uffculme Mill in 2010 was approximately £[] million.

TRANSACTION

4. The sellers have agreed to sell the Uffculme Mill and business to AB Agri. The transaction will include the purchase of the following assets:
 - the freehold interest in Uffculme Mill
 - the assets and rights used in connection with the operation of Uffculme Mill and
 - the plant, machinery and equipment at Uffculme Mill.
5. As part of the transaction AG Agri will enter into a feed supply agreement with Hook2Sisters which currently purchases all of the output of Uffculme Mill. Under these supply arrangements, Hook2Sisters will continue to purchase a minimum of [] tonnes of feed and treated wheat per annum for a period of [zero-five] years following completion of the transaction.
6. In line with its previous decisions, for example, in the Cineworld case,³ the fact that different components are being acquired from different parties (the sellers) does not negate the conclusion that an enterprise is being transferred. As a result, the OFT believes that it is or may be the case that the Uffculme Mill is an enterprise for the purposes of consideration under the Act. As a result of this transaction AB Agri and Uffculme Mill will therefore cease to be distinct.

² ASG Properties (Jersey) Limited acquired the land and assets from the 2 Sisters Food Group. The 2 Sisters Food Group has a 50:50 joint venture with PD Hook Limited ('PD Hook') called Hook2Sisters Limited, which rears broiler chickens. PD Hook is a chicken producer involved in hatching, breeding and rearing and is ultimately owned by James Hook and Fiona Hook.

³ Anticipated acquisition by Cineworld Group plc, through its subsidiary Cine-UK Limited, of the cinema business operating at the Hollywood Green Leisure Park, Wood Green, decision of 17 March 2008.

7. AB Agri notified the transaction to the OFT on 7 July 2011. The OFT's administrative deadline is 2 September 2011.

JURISDICTION

8. AB Agri and Uffculme Mill overlap in the supply of compound monogastric feed. On the basis of the Uffculme Mill's turnover for 2010, the turnover test in section 23 of the Act is not met. However, together, AB Agri estimates that they account for approximately [30-40] per cent of the supply of UK retail compound poultry feed in the UK. Consequently, the share of supply test in section 23 of the Act is met.
9. The OFT therefore believes that it is or may be the case that a relevant merger situation has been created.

RATIONALE

10. AB Agri informed the OFT that the merger would enable it to [].

MARKET DEFINITION

Background

11. AB Agri and the Uffculme Mill are both compound feed manufacturers and supply compound monogastric animal feed for poultry.
12. However, the parties argue that there is no genuine overlap between AB Agri and the Uffculme Mill because the existing feed requirements served by the Uffculme Mill have not been available in the open market since 2008 and have only been supplied to Hook2Sisters. In considering whether such captive production should be included in the open (or 'merchant') market, the OFT asks whether it would be profitable for the supplier (here Uffculme Mill) to forego its captive use and sell into the merchant market in response to a SSNIP.⁴
13. In this regard, the OFT notes that:

⁴ Merger Assessment Guidelines, paragraph 5.2.20, fourth bullet.

- although Uffculme Mill has not supplied feed to any other customer, the agreement to supply Hook2Sisters has not been on an exclusive basis
 - customers and competitors foresaw Uffculme Mill as potentially competing with AB Agri and Uffculme Mill has previously supplied into the merchant market and
 - it received no evidence that the profit margins on Uffculme Mill's sales of animal feed are materially different to those of AB Agri.
14. On a cautious basis, therefore, the OFT has treated AB Agri and Uffculme Mill as overlapping.
15. Livestock may be fed a number of different products, including compound feed, straight feeds (often referred to as 'straights'), home mixed feeds and home grown feeds.
16. Compound feeds are combinations of various ingredients (including cereal grains, oilseed products, pulses, human food industry by-products such as wheat feed, vitamins and minerals and permitted feed additives) which are blended together in different proportions according to the feed's intended purpose. Compound feed can be sold in meal or pellet form, and can be complete or complementary.⁵ Straight feeds are raw materials such as wheat, soya and barley which are mixed with supplements and/or home grown products to create home mixed feeds (home mixing).⁶ AB Agri estimates that straights and home mixing account for around 49 per cent of the total UK animal feed market, with compound feeds accounting for the remaining 51 per cent.
17. Compound feed manufacturers can specialise in producing feed for ruminants (including cattle and sheep) and/or monogastric animals (including poultry and pigs).

⁵ Complete compound feed is a compound mixture of feed materials supplying the total daily dietary needs of an animal. Complementary compound feed is a compound mixture of feed materials with a high concentration of certain nutrients which is sufficient to provide the total daily dietary needs of an animal when fed in combination with other feedstuffs.

⁶ Home mixing involves livestock producers either mixing the straights and supplements on-site using their own equipment, or through the services of a mobile mill and mixer.

Product Market

18. AB Agri submitted that the relevant product market should include all types of animal feed (including compounds and straights) for both monogastric and ruminant animals.
19. However, in *Thompson/AB Agri*,⁷ and *AB Agri/Porter*⁸ the OFT considered that ruminant and monogastric feeds should be considered as separate product markets. In considering whether monogastric feeds should be further delineated between pig and poultry feed, the OFT considered there to be no demand-side substitution. Although the OFT found few barriers to supply-side substitution, it took a cautious approach and considered pig and poultry feed separately. The OFT also took a cautious approach and considered compounds, straights and blends separately.
20. Market definition begins with the narrowest plausible candidate market in which the parties overlap.⁹ In the present case, that is compound poultry feed, as Uffculme Mill only produces this. In considering whether to widen the relevant product market, the OFT has considered:
 - whether straight poultry feed is in the same market as compound poultry feed
 - whether compound/straight feed for pigs and poultry (both monogastric animals) are in the same market and
 - whether feed for ruminants (cattle and sheep) is in the same market as feed for monogastric animals.
21. These distinctions are considered below.

Compounds and straights

22. AB Agri submitted that compounds and straights¹⁰ form part of the same product market on the basis of demand-side substitution. It considered that livestock producers can either purchase compound feed or they can

⁷ Anticipated Acquisition by John Thompson Limited of the Northern Ireland Compound Feed Business and Assets of AB Agri Limited (July 2008).

⁸ Anticipated acquisition by AB Agri Ltd of certain of the business and assets of JE Porter Ltd from the Porters Group (17 April 2009).

⁹ Merger Assessment Guidelines, paragraph 5.2.11.

¹⁰ In addition to any additives and supplements required.

purchase straights, vitamins, minerals and other supplements, which they can then use for home mixing.

23. AB Agri has submitted that although home mixing is less widespread in poultry farming, it has been common place in the past and would be expected to be more widespread were compound prices to increase.
24. None of the customers that provided information to the OFT considered that switching to home mixing was a viable option in response to a small price increase in compound feeds. Potential reasons for this include the geographical distribution of customers' farms, the quantities purchased by those customers and the necessary capital expenditure required to build or purchase the necessary capacity to undertake home mixing.
25. In terms of supply-side substitution, compound producers can switch to supplying straights easily and quickly, as they already purchase them for use in the manufacture of compounds. However, one competitor submitted to the OFT that this is unlikely to be a commercially attractive option to a compound feeds supplier, given the high fixed costs associated with a compound feed mill.
26. Given the mixed information received from third parties, the OFT has taken a cautious approach and considered compound feeds separately to straights in this case.

Pig and poultry feeds

27. On the demand side-side, poultry feed cannot be fed to pigs and vice versa. On the supply side, AB Agri considers that switching production between producing pig and poultry feed can be done easily, in a short time period and at limited cost. AB Agri submitted that it switches between pig and poultry feed production on a daily basis; all apart from one of its mills manufacture both types of feed¹¹ and the cost of switching production is so limited that it is not even recorded.

¹¹ AB Agri submitted that its mills generally have one or two mixers through which all products are mixed. Cross-contamination is controlled through scheduling or the use of a 'flush' batch. Flush batches are mainly used to ensure that batches are not contaminated with traces of medication.

28. Consistent with this, in *AB Agri/Porter*, the OFT found that supply-side substitution between poultry and pig feed was possible. Given that no significant technical or regulatory changes have taken place since that decision, the OFT sees no reason to depart from this assessment in this case.

Monogastric and ruminant feeds

29. On the demand side, different animals require different feeds. For example, a ruminant animal feed cannot be fed to monogastric animals (and vice versa). This is supported by the submissions of AB Agri, third parties and by analysis in previous cases (*Duffield/Bury Nutrition*,¹² *ABF/Primary Diets*,¹³ and by the OFT more recently in *Thompson/AB Agri* and *AB Agri/Porter*¹⁴). Therefore, the OFT considers that there is unlikely to be demand-side substitution between animal feed for different animals.
30. In relation to supply-side substitution, AB Agri has submitted that feed manufacturers can, and do move relatively easily between the manufacture of feeds for different species (between both ruminant and monogastric animals and between different types of monogastric animals), within short periods of time and at low cost. They submitted that this is made easy given that most compound feeds have a high degree of common ingredients.
31. Third party competitors did not support the parties' assertion on the ease of supply-side substitution. Competitors suggested that monogastric and ruminant feeds are commonly produced at separate plants, or on separate production lines, and that switching would not occur following a 10 per cent price rise, both due to the cost of switching and differences in margin structure.
32. Given the lack of substitution on the demand-side and the mixed evidence on supply-side substitution the OFT has taken a cautious approach and has not considered ruminant feed to be in the same product market as monogastric feed.

¹² Acquisition by W L Duffield & Sons Limited of the ruminant feed business of Bury Nutrition, part of ABNA Limited (December 2002).

¹³ Case ME/2522-06: Completed Acquisition by ABF Holdings Limited of Primary Diets Limited (September 2006).

¹⁴ See footnotes 7 and 8.

Conclusion on product market definition

33. In the light of the above and on a cautious basis, the OFT has analysed this merger by reference to: (i) compound feed supplied for monogastric animals and (ii) compound feed supplied for poultry.

Geographic market

34. AB Agri has submitted that the geographic scope of the market should be the UK. While it noted that customers tend to be more concentrated the closer they are to mills, it argued that it is not essential for mills to be located close to the end customer.
35. AB Agri provided margin data which indicated that margins were significantly less for supplies beyond [] miles from its Cullompton Mill and that the majority of customers were located within a 100 mile catchment of the Cullompton Mill.
36. A third party competitor indicated that customers are located across the country and average delivery distance would be less than 50 miles with a competitive maximum of 120 miles depending on area.
37. Based on this and the OFT caution in previous animal feed cases,¹⁵ the OFT does not consider that there is sufficient evidence to support AB Agri's view that the relevant geographic market is national.
38. In any event, the OFT did not find it necessary to conclude on the geographic market as it does not affect the outcome of the competitive assessment in this case.

HORIZONTAL ISSUES

Unilateral effects

39. AB Agri provided estimates of shares of supply of compound poultry feed and of compound monogastric feed of the parties within the 100 mile

¹⁵ In *AB Agri/Porter* (see footnote 8) the OFT took as its starting point a 100 mile catchment area centred around the target, and in *Duffield/Bury Nutrition* (see footnote 12) the OFT considered that animal feed was typically delivered over a 50 to 60 mile distance from the target mill but could be delivered up to 200 miles from it.

radius of Uffculme Mill. Following the merger, AB Agri estimated that it would have

(a) a combined share of supply of [10-20] per cent (with an increment of [zero - five] per cent from AB Agri) of the supply of compound poultry feed within 100 miles radius of the Uffculme Mill and

(b) a combined share of supply of [20-30] per cent (with an increment of [10-15] per cent from Uffculme Mill) of the supply of compound feed for monogastric animals within a 100 mile radius of the Uffculme Mill.

40. The parties indicated that the estimates above are cautious and assume that the volumes produced by Uffculme Mill are available on the open market rather than solely to Hook2Sisters.
41. Even ignoring the position of Uffculme Mill pre-merger as a supplier to just one customer, these shares are not high enough to give the OFT cause for concern over unilateral effects, given it has drawn the market narrowly (albeit not necessarily to be the narrowest satisfying the hypothetical monopolist test).
42. Consistent with this, customers have raised no concerns regarding any loss of competition as a result of the merger and none of the competitors located within 100 miles of Uffculme Mill contacted by the OFT listed Uffculme Mill as one of their top five competitors.
43. The closest geographic rivals identified by third parties as potential competitors to AB Agri were BOCM Exeter, Crediton Milling and Lloyd's Animal Feeds (Southern) Limited but not Uffculme Mill.¹⁶
44. Further, AB Agri submitted that the high levels of spare capacity in the sector make switching easier¹⁷ and several customers commented that they would switch to alternative suppliers if faced with a small but significant and non-transitory price increase and did not view this as being difficult given the large number of alternative suppliers both within the 100 mile radius of AB Agri and beyond.

¹⁶Which are located 10, 16 and 28 miles respectively from the Uffculme Mill.

¹⁷ AB Agri estimated that there remain three million tonnes of spare capacity in the UK and that only 20 per cent of mills do not have spare capacity.

45. For these reasons, the OFT does not consider that the merger gives rise to a realistic prospect of a substantial lessening of competition on the basis of unilateral effects.

ANCILLARY RESTRICTION

46. As part of the transaction, AB Agri and Hook2Sisters will enter into a [zero-five] year feed supply agreement. The parties submit that this agreement will provide for the same fixed quantities as supplied to Hook2Sisters pre-merger from the Uffculme Mill and that there will therefore be no change to the supply chain. The supply agreement will not confer preferred or exclusive supplier or purchaser status on AB Agri or Uffculme Mill and any surplus product would be available to third parties for purchase. The parties therefore submitted that they consider that the agreement is an ancillary restriction which is directly related and necessary to the implementation of the merger.
47. Under the European Commission Notice on restrictions directly related and necessary to concentrations¹⁸ supply agreements may be considered ancillary for a transitional period to ensure continuity of supply but should be limited to a period necessary for the replacement of the replacement of dependency by autonomy in the market. Supply obligations aimed at guaranteeing the quantities previously supplied may be justified for up to five years.¹⁹
48. The feed supply agreement provides for fixed quantities previously supplied to Hook2Sisters by Uffculme Mill. Any further volumes produced by Uffculme Mill can be acquired by or sold to third parties on the market. On this basis the OFT shares the parties view that the feed supply agreement may be justified as an ancillary restraint.
49. The OFT notes that the merger does not alter the agreement which was in place prior to the transaction taking place. Furthermore, given the discussion in the unilateral effects section and the lack of concern therein, the OFT concludes that the merger does not raise a realistic prospect of an SLC through the parties' supply relationship with Hook2Sisters.

¹⁸ European Commission Notice on restrictions directly related and necessary to concentrations (2005/C56/03), see also Paragraph 4.80 of OFT's Jurisdictional and Procedural Guidance.

¹⁹ Paragraph 33 of the Commission Notice.

THIRD PARTY VIEWS

50. During the course of its investigation the OFT solicited views from competing suppliers and also customers of AB Agri. None of the third parties that responded to the OFT indicated that the merger raised competition concerns. Specific comments of third parties relevant to the OFT's assessment in this case are summarised above as appropriate.

ASSESSMENT

51. AB Agri and the Uffculme Mill are both compound feed manufacturers and overlap in the supply of compound monogastric animal feed.
52. On a cautious basis, the OFT has examined the merger both on the basis of the supply of compound feed for monogastric animals and on the basis of compound feed for poultry. The OFT has not found it necessary to conclude on the geographic scope of the market as no competition concerns arise on the narrowest geographic market definition of a 100 mile radius.
53. Within 100 miles of Uffculme Mill, there are several monogastric feed mills. AB Agri's post merger share of supply of compound feed for monogastric animals would be [20-30] per cent (with an increment of [10-15] per cent). Customers raised no concerns, naming a range of alternative suppliers.
54. Uffculme Mill appears not to have been competing with AB Agri nor any other feed producers as it only had one customer Hook2Sisters which accounted for all its output. As part of the transaction AB Agri and Hook2Sisters will enter into a [zero-five] year non exclusive supply agreement for the supply of monogastric animal feed. The feed supply agreement provides for fixed quantities previously supplied to Hook2Sisters by Uffculme Mill. Any further volumes produced by Uffculme Mill can be acquired or sold by third parties on the market. On this basis the OFT shares the parties' view that the feed supply agreement may be justified as an ancillary restraint.
55. On the basis of the range of alternative suppliers, the existence of spare capacity, the possibility of constraints from outside the 100 mile

catchment and the lack of third party concerns, the OFT considers it unlikely that the merger will give rise to competition concerns.

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

DECISION

57. This acquisition will therefore **not be referred** to the Competition Commission under section 33(1) of the Act.

END NOTE

In relation to paragraph 19, the OFT clarifies that, while in its *Thompson/AB Agri* decision it assessed pig and poultry feed separately, in its subsequent *AB Agri/Porter* decision it did not consider this necessary given the ease of supply-side substitution.