

Completed acquisitions by Celsa Steel Service (UK) Limited of the manufacturing and reinforcement divisions of:

BRC Limited
Express Reinforcements Limited, and
The ROM Group

ME/3982/08, ME/3963-08 and ME/3964-08

The OFT's decisions on reference under section 22(1) given on 29 January 2009. Full text of decision published on 20 February 2009.

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

PARTIES

1. **Celsa Steel Service (UK) Limited (Celsa)**, is a wholly-owned subsidiary of Celsa (UK) Holdings Limited. The ultimate parent company of Celsa (UK) Holdings Limited is Catalunya Steel SL, a Spanish company, which is one of a number of companies managed under the 'Grupo Celsa' brand. Celsa is mainly active in the manufacture of reinforcing bars (rebars), reinforcing bars in coil shape or 'reinforcing coils' (coils); and mesh wire rod (MWR). These are specialized reinforcement steel products that are used (typically after further processing) in construction applications to reinforce concrete.
2. **The manufacturing and reinforcement divisions of BRC Limited (BRC), Express Reinforcements Limited (Express) and The ROM Group (ROM)** (the target companies) are each involved in the processing and distribution of reinforcement steel products. They purchase reinforcing steel in the form of rebars and coils from steel manufacturers (such as Celsa) and process it into reinforcement steel products for concrete which is then sold to construction companies and builders' merchants. BRC and ROM also manufacture steel mesh from MWR, which they acquire from companies such as Celsa.

3. In 2007, BRC had a turnover in the UK of approximately £130 million, Express had a turnover in the UK of approximately £68 million and ROM had a UK turnover of approximately £113 million.

TRANSACTION

4. On 1 September 2008, Celsa acquired BRC from Acertec plc. The statutory deadline, as extended, for the OFT's consideration of this case expired on 29 January 2009.
5. On 18 November 2008, Celsa, Compania Espanola de Laminacion SL and Global Steel Wire SA (all companies within the Grupo Celsa Group) acquired the entire issued share capital of Express from Ash & Lacy Services Limited, a subsidiary of Hill & Smith Holdings plc.
6. On 9 January 2009, Celsa, Compania Espanola de Laminacion SL and Global Steel Wire SA completed its acquisition of ROM.¹
7. Celsa notified the OFT by way of informal merger submission of all three acquisitions on 12 December 2008.

JURISDICTION

8. As a result of these transactions Celsa has ceased to be distinct from each of BRC, Express and ROM. The UK turnover of each of BRC and ROM exceeds £70 million, so the turnover test in section 23(1)(b) of the Enterprise Act 2002 (the Act) is satisfied in relation to these acquisitions.² In relation to Express, the combined share of supply of Celsa post-mergers exceeds 25 per cent of all processed reinforcing steel products supplied in the UK, so the share of supply test in section 23(3) of the Act is satisfied in relation to this acquisition.³ The OFT therefore believes that it is or may be the case that a relevant merger situation has been created in each case.

MARKET DEFINITION

9. Celsa and the target companies are active in relation to the supply of reinforcement steel products in the UK. Celsa has submitted that the supply chain can be sub-divided into three levels: upstream, intermediate and downstream.
 - At the upstream level, which is where Celsa operates, rebars, coils and MWR are manufactured.

¹ When Celsa notified the OFT of this transaction it was still an anticipated transaction.

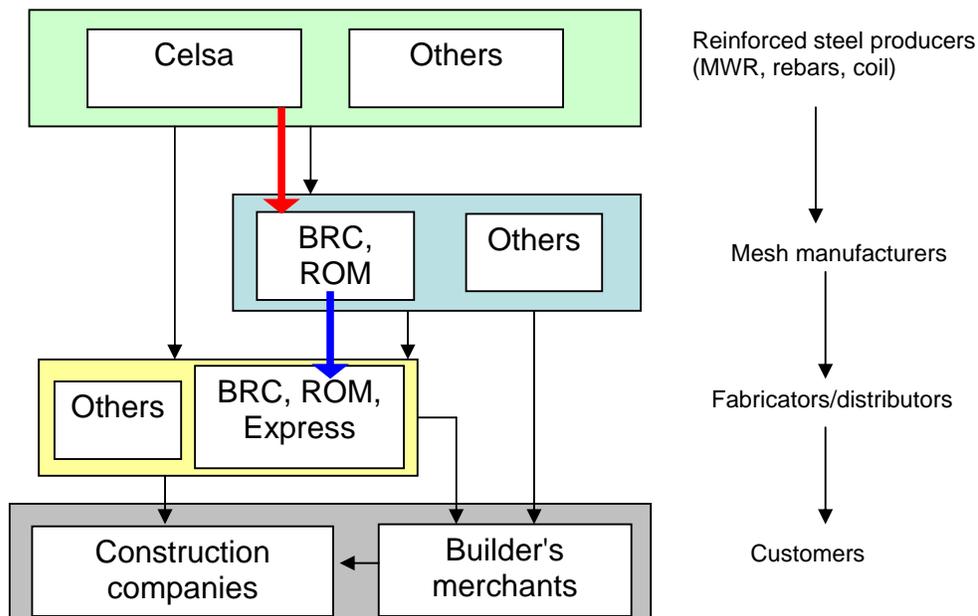
² The share of supply test is also met in relation to BRC and ROM for the same reasons that it is met for Express.

³ See discussion under 'The Counterfactual' at paragraphs 40 to 45 for an explanation of why the OFT has summed the share of supply for all target companies for the purpose of the share of supply test under section 23(3) of the Act.

- At the intermediate level, where BRC and ROM (but not Express) operate, mesh is manufactured from MWR.
- At the downstream level, where BRC, Express and ROM all operate (but not Celsa), rebars and mesh are sold on; rebars and coils are customized into 'cut and bent' products; and rebars, coils and mesh are customized into prefabricated products.

10. This market structure is illustrated in Figure 1, below.

Figure 1: Market structure



Upstream level – manufacture of rebar, coil and MWR

Product scope

11. Celsa argued that the relevant upstream market, and the market in which it operates, should be defined as the manufacture of rebar, coil and MWR.
12. On the demand-side, Celsa argued that rebars and coils are substitutable because they are the same product stored in a different shape, and it is straightforward to convert coils into rebars where both are available in the same diameter. While market enquiries supported this contention, a number of market participants did not consider the two always to be exact substitutes. The majority of market participants advised that coil is only available up to a maximum diameter of 20mm, whereas rebar is available in diameters up to 50mm. As such, from the user's perspective, coil is not a substitute for rebar where a diameter of greater than 20mm is required. Nevertheless, Celsa advised that rebar and coil of 12mm and 16mm diameter comprise half of the sales of rebar and coil made by Celsa.

13. On the supply-side, Celsa argued that rebar, coil and MWR are substitutable because manufacturers can easily switch between the three in response to prevailing price and demand conditions. Celsa advised that it could alter its production profile to this effect inside 24 hours, and pointed to the fact that most upstream manufacturers tend to produce all three products as further support for this proposition. The OFT's market enquiries supported Celsa's arguments on the technical ability to switch between the manufacture of these products. The OFT then went on to consider whether it would be profitable to switch production in the event of a small but significant and non-transitory increase in price (SSNIP). In this regard, Celsa provided information showing that the profit margins of rebar, coil and mesh are highly correlated (having a monthly correlation in 2007 and 2008 of over 0.9, which is high). Such a high and positive correlation suggests margins of rebar, coil and mesh move closely together over time, consistent with manufacturers switching production between them to arbitrage any differences in relative prices (that is, consistent with supply-side substitution).
14. While the evidence on the demand-side suggested that, at best, coil, rebar and MWR are imperfect substitutes, the OFT considered that upstream producers could easily and profitably switch between production of all three products in the event of a SSNIP. The OFT therefore concluded that the relevant upstream product market incorporated rebar, coil and MWR.

Geographic scope

15. Celsa submitted that the relevant geographic scope at the upstream level is at least EU wide and also includes Turkey. It cited the EC decision in *Celsa/Fundia*⁴ (which did not conclude on geographic market definition but considered that it could be EU wide) as support for this proposition. Celsa also adduced a range of data and information to support its view, including data sourced from the Iron and Steel Statistics Bureau (ISSB). In particular, this data showed that imports of rebar and coil made up between 30 and 55 per cent of UK demand between January and October 2008 and imports of MWR made up between 25 and 45 per cent.^{5,6}
16. Based on ISSB estimates, Turkey was the largest single independent source of imports between 2006 and 2008 (approximately 25 per cent), as shown in Table 1.

⁴ COMP/M.4225

⁵ It should be noted that fewer than three per cent of imports in the past three years were made up by Celsa importing rebar from its own overseas operations. Celsa advised that it has not imported any coil or MWR in the last three years.

⁶ Imports of rebar and coil, by country of origin, were comprised of: Spain (25.5 per cent), Turkey (25 per cent), Latvia (14 per cent), Germany (9.5 per cent), Luxembourg (8 per cent), Portugal (11 per cent) and 7 per cent from other sources.

Table 1: Share of supply attributable to imports (2006-08), per cent

Import shares	2006	2007	2008 (Jan-Oct)
Import Share of UK Demand	40.0	45.2	42.6
Turkish Imports (as a Share of Total Imports)	28.9	56.8	24.8

Source: Merging parties, citing ISSB

17. Finally, Celsa provided evidence showing a high correlation between European and Turkish prices for rebar (0.85 controlling for movements in common costs) in support of its argument that the relevant geographic scope of the upstream market includes the EU and Turkey.
18. Market enquiries were mixed on the level of competitive constraint that imports currently impose on upstream UK manufacturers. It was generally suggested that, in the past, significant volumes of rebar, coil and MWR had been imported into the UK. For example, one market participant stated that, on its figures, imports made up 47 per cent of the upstream market as at October 2008. Despite this, doubt was raised by a significant number of market participants regarding the share of imports of reinforcement steel products currently (that is, since November 2008) coming into the UK. According to a number of sources, there has been a decline in the level of imports due to the increased price of steel in the Middle East, relative to the price in the UK, attracting increased volumes to the Middle East from many Turkish mills, which, as seen in Table 1 comprise a substantial proportion of imports into the UK. This, it was suggested, may have led to an increase in Celsa's prices at the end of 2008.⁷
19. The OFT does not have reliable information on the extent to which there has been a decline in imports since October 2008. Although the level of imports may have fallen in the last two months, the OFT understands that such a decline has coincided with a reduction in demand in the UK. When demand picks up again, the level of imports would be expected to rise, consistent with historical trends of import levels rising and falling, particularly from Turkey (see Table 1, above). Indeed, a steel industry newsletter reported in January 2009 that Turkish suppliers were actively searching for orders from UK customers.⁸ Finally, the OFT notes that if overseas mills are shifting production in response to relative price changes between the UK and elsewhere, this may actually be evidence suggesting the adoption of a broader geographic market definition. For example, another steel industry newsletter reported in January 2009 that at the end of December and beginning of January 2009, a major importer brought in 10,000 tonnes of rebar from Turkey, which resulted in Thames Steel and

⁷ Celsa argued that its price increase was driven by an increase in the price of scrap.

⁸ *Metal Bulletin*, 'Desperate Turkish rebar producers seek orders in the UK', 9 January 2009.

Celsa reducing their prices.⁹

20. Nonetheless the OFT received concerns that imports do not effectively constrain domestic products. For example, a number of third parties advised that they could not source all of their requirements from overseas companies as some of these companies' products are not CARES approved.¹⁰ However, as explained later at paragraph , below, the OFT did not consider this to be a barrier to overseas companies competing.
21. Some third parties also suggested that importing may lead to certain additional costs, such as longer lead times, increased exchange rate risk¹¹ and higher storage costs,¹² which mean that imports are not commercially viable substitutes for domestically produced products. Despite these concerns, however, the OFT found numerous examples of both small and large operators sourcing inputs from overseas suppliers in addition to many operators which stated that, while they currently do not import, or only import to a limited extent, such a strategy would be a commercially viable option in the future. For example, the OFT is aware of at least one fabricator that maintains an inventory of products in a warehouse, including significant volumes of imports that it orders ahead of demand and utilises as and when required.
22. On balance, market enquiries revealed that imports have historically been a significant feature in the manufacture and supply of reinforcement steel products, and likely comprised over 40 per cent of UK consumption as recently as October 2008. On this basis, where imports and domestically-produced products are almost seamlessly interchangeable, then the boundaries of the geographic market could be wider than the UK. Nevertheless, concerns raised by third parties—such as additional costs, longer lead times and currency and price fluctuations—do raise questions about the level of competitive constraint currently being provided by imported products. On this basis, the OFT has taken a cautious approach and assessed the mergers on the basis of a UK market, albeit with imports playing a strong competitive role within that UK market.
23. Consequently, taking a cautious approach, the OFT has assessed the

⁹ *Steel Business Briefing* 'Scrap & imports push UK rebar prices in different directions', 19 January 2009.

¹⁰ CARES is an independent accreditation body for construction steels that provides a regime of regulation, testing and inspection. The OFT understands that there is a strong preference among end users that steel used in construction projects be CARES approved.

¹¹ Some market participants advised that recent fluctuations in the price of steel mean that importing steel involves some risk in that decreases in the domestic price can render imported steel uncompetitive due to the longer lead times associated with securing imports. See fn 13 for further information on lead times.

¹² The OFT understands that steel sourced from overseas needs to be ordered at least one month in advance, although it was made aware of specialist importers that import large quantities of steel and then sell to fabricators and builders' merchants as and when they require it.

mergers on the basis of a UK market for the manufacture and supply of reinforcement steel products, and has given appropriate consideration and weight to the constraint from imports in the competition assessment below.

Intermediate level – wholesale supply of mesh

Product scope

24. Celsa submitted that neither it nor Express is active at the intermediate level in the UK, whereas BRC and ROM are. Celsa is, however, active at this level in Scandinavia and Spain.
25. Celsa contended that there is a market for the wholesale supply of mesh into the UK. It argued that there is a series of mesh wholesaling specialists that supply both fabricators and stockists. According to Celsa, the absence of specialists performing this function for cut and bent products (that is, products made from coil and rebar) means that wholesale mesh comprises a market of its own.
26. Several mesh wholesaling specialists, as well as a number of specialist mesh importers, were identified during market enquiries, supporting Celsa's view in this regard. Nevertheless, market enquiries also revealed that most, if not all, companies that operate at this level of the supply chain are vertically integrated with either an upstream manufacturer or a downstream fabricator. Further, many market participants tended to describe the industry as comprising an upstream and downstream segment, with mesh wholesaling comprising part of one or the other. The fact that ROM and BRC used around [65-75] per cent and [75-85] per cent respectively, of the mesh they produced 'in-house' in 2007 would tend to support this proposition.
27. On the basis of the evidence before it, the OFT considered it plausible that there could be a distinct market for the wholesaling of mesh. Given that it does not materially affect the outcome of the OFT's substantive assessment, however, the OFT did not consider it necessary to conclude on this point and will treat mesh as part of the 'upstream' market in its competitive assessment.

Geographic scope

28. Celsa submitted that the market is at least as wide as Western Europe. It argued that transport costs are not prohibitive (typically £20 per tonne) and contended that, in 2007, imports made up 10 to 15 per cent of this market. In support of this point, it noted that transport costs comprised less than three per cent of the total cost of an order of mesh at £700 per tonne in September 2007. Celsa further argued that, although the price of steel has fallen since September 2007, which could translate into transport costs comprising a higher percentage of overall costs, transport costs have

themselves also fallen, meaning that transport costs still account for a very small percentage of overall costs. Thus, it argued that a UK-wide SSNIP would be defeated by imports.

29. Market enquiries were mixed as to whether mesh imports have followed the same recent trends as other steel reinforcement products, with some identifying companies from The Netherlands and Germany as prominent importers, while others considered they were not. Nevertheless, in general, market enquiries indicated that there are many active foreign companies in this market supplying UK customers. For example, the OFT understands that at least one fabricator has received active support from overseas providers in the past. The OFT also received evidence of BRC purchasing mesh from an overseas source in 2007.
30. In light of the evidence before it, the OFT considered it plausible that any wholesale mesh geographic market would be at least EU-wide. As discussed earlier, however, the OFT did not consider it necessary to conclude on the exact scope of the market for wholesale mesh.

Downstream level – processing and distribution of fabricated steel reinforcement products

Product scope

31. All three target companies operate at this level of the supply chain; Celsa does not.
32. Celsa contended that there is no basis for distinguishing between different reinforcement products in this market and that the market includes the fabrication and distribution of mesh, cut and bent and prefabricated products. In support of this proposition, Celsa argued that fabricators tend to deal with the same customers regardless of which type of reinforcement product they are supplying. Similarly, fabricators will tend to deal with the same suppliers of rebar, coil and mesh. Finally, Celsa submitted that fabricators will make final products themselves from all three raw materials (mesh, bar and coil) and will 'invariably provide a portfolio of cut and bent, mesh and prefabricated products' which will meet the needs of the specific job at hand. Subsequently, Celsa argued that demand- and supply-side switching would result following a price rise by a hypothetical monopolist on any individual product.
33. On the demand-side, although customers may use the same fabricator (and a fabricator may use the same supplier) for each type of reinforcement product, this need not necessarily mean that the market should include all such products. (By analogy, for example, supermarkets sell thousands of grocery products but this need not mean that all grocery products are in the same product market.) However, on the supply-side, market enquiries tended to support Celsa's arguments on the ability of suppliers to switch production quickly and at little or no cost following a price rise. Some

suggestions were made that there may be a distinction between servicing large contracts (over 10,000 tonnes) and servicing smaller ones. Further, some market participants argued that ROM manufactures proprietary products, which may limit the ability of others to compete. Nevertheless, the OFT considered that these issues go to the relative strength of competitors in the market, and (as discussed in the Unilateral Effects section below), do not warrant any narrowing of the market based on customer size or intellectual property.

34. Overall, the OFT did not consider it necessary to conclude on whether mesh, cut and bent and fabricated products should constitute separate markets as the parties' shares of supply do not vary significantly across these products. For the purposes of its assessment in this case, the relevant downstream product market therefore comprises the processing and distribution of prefabricated steel reinforcement products.

Geographic scope

35. Celsa contended that it is appropriate to consider the scope of the relevant downstream geographic market as being at least a 150 mile radius around a fabricator's depot. In support of its argument, Celsa presented statistics for the target companies suggesting that each of them supplies a substantial volume (30 to 50 per cent) of both cut and bent products to customers over 100 miles from a depot (although it noted that there is conflicting evidence in the case of mesh¹³).
36. Market enquiries were generally consistent with Celsa's contention that the geographic scope of the market was no smaller than 150 miles. In fact, a significant number of market participants quoted 150 miles as the range within which fabricators tend to supply customers. Further, most respondents stated that it is viable for fabricators to supply further afield than 150 miles, with some suggesting that the relevant geographic market is national. For example, many market participants noted that the price paid by customers in England and Wales was unlikely to vary according to the location of the particular job tendered.¹⁴ Most market participants considered that, while some regional variations may exist in terms of the number and identity of suppliers, a strong national element to competition exists with respect to price and non-price factors at the fabrication level. Finally, market enquiries suggested that most significant competitors supply customers nationally.
37. Market participants in England and Wales did however indicate that

¹³ Figures for BRC and ROM indicated that these companies supply higher volumes of mesh than rebar and cut and bent products to customers more than 150 miles away. Express, on the other hand, tended to supply more mesh than rebar and cut and bent products within a 150 mile radius of its depots. All target companies supply rebar, mesh and cut and bent products to customers both less than 100 miles away and greater than 150 miles away.

¹⁴ Although fabricators generally prefer supplying as close to their depots as possible.

additional transport costs are involved in supplying customers in Scotland and Northern Ireland. Nevertheless, the OFT understands that there are companies in Ireland who supply Northern Ireland and vice versa. The OFT is also aware of at least one company in Northern Ireland that supplies Scotland.

38. The OFT considers there are arguments for defining markets of 150 miles radii around fabrication plants, but also some arguments for adopting a UK-wide frame of reference. Therefore, the OFT has chosen to consider whether there is a realistic prospect of a substantial lessening of competition on the basis of (a) national markets and (b) sub-national markets using a 150 mile radius as the maximum supply distance from any depot.
39. Given the large scale of such sub-national markets relative to the UK, the OFT focussed its review on two regions where concerns were raised by third parties: Scotland and South West England/Wales.¹⁵

THE COUNTERFACTUAL

40. Paragraph 3.24 of the OFT's Substantive Assessment Guidance¹⁶ states:

In most cases, the best guide to the appropriate counterfactual will be prevailing conditions of competition. However, the OFT may need to take into account likely and imminent changes in the structure of competition in order to reflect as accurately as possible the nature of rivalry without the merger.

41. For each of the three transactions at hand, given the fact that the OFT assesses facts at the time of its decision on reference, the prevailing conditions of competition are that Celsa is a vertically integrated steel manufacturer/mesh wholesaler/fabricator and distributor. This is by virtue of the fact that Celsa has completed the acquisition of three steel fabricators and distributors, two of which also supply mesh on a wholesale basis in the UK.
42. Although it is the case that each transaction is subject to its own merger review, and thus the possibility that it could eventually be unwound, these outcomes are, at this stage, uncertain and it is entirely realistic that the two other transactions remain completed. Given this uncertainty, the OFT considers it plausible that, for each merger, the counterfactual may involve none, one or both of the other two mergers that form part of the counterfactual being unwound.
43. The OFT's task in assessing each merger is to determine whether there is a

¹⁵ See paragraphs 75 et seq. The OFT did not receive any evidence suggesting that concerns of a sub-national basis arose in any other parts of the UK.

¹⁶ Mergers Substantive Assessment Guidance (OFT 506).

realistic prospect that that particular merger will substantially lessen competition. Given that all three of the alternative counterfactuals described above for each merger are realistic at this stage, the OFT assessed each merger by reference to the most conservative but realistic counterfactual; namely that, for each transaction, the other two transactions will not be unwound (which equates to the prevailing conditions of competition for each merger). The OFT considered that, if a given merger can be cleared on this conservative counterfactual, then it would not be necessary to test it against the alternatives (that is, that one or both of the other transactions have been unwound).

44. As such, for each transaction, the OFT tested the merger by reference to the below counterfactuals:¹⁷
 - a. for the acquisition of BRC—Celsa owning both Express and ROM
 - b. for the acquisition of Express—Celsa owning both BRC and ROM, and
 - c. for the acquisition of ROM—Celsa owning both BRC and Express.
45. In each case, the relevant question for the OFT was whether the addition of the relevant target business itself created a realistic prospect of a substantial lessening of competition. In determining the answer to this question for each relevant merger situation, the OFT assessed the competitive constraints that the merged entity would be likely to face following the mergers (as it would do in assessing an individual merger).

UNILATERAL EFFECTS

Fabrication and distribution of steel reinforcement products

46. The OFT received several concerns from market participants claiming that the mergers would be likely to raise competition issues due to the target companies' share of spare capacity in the fabrication/distribution market, giving it the potential to withhold supply; the potential for price leadership; and the inability of other players to constrain the merged entity.

Share of capacity and potential supply withholding

47. The mergers will result in the three largest fabricator/distributors of reinforcement steel products in the UK coming under the control of Celsa. As a result, the mergers will result in Celsa having a market share according to the parties, by total capacity, of between 45 and 55 per cent. Table 2, below, sets out the market shares of the target companies, by installed capacity, as well as the other major players in this market based

¹⁷ Celsa accepted that this approach to the counterfactual was appropriate in the context of a first phase investigation.

on installed capacity.¹⁸

Table 2: Percentage shares of installed capacity of cut and bent, mesh and combined cut and bent/mesh in the UK (2007)

Fabricator	Cut and bent	Mesh	Total
BRC	[15-25]	[15-25]	[15-25]
ROM	[5-15]	[15-25]	[15-25]
Express	[5-15]	[5-15]	[5-15]
Combined	[45-55]	[45-55]	[45-55]
Kierbeck	[5-15]	[5-15]	[5-15]
Roe	[5-15]	[0-10]	[5-15]
Hy-ten	[5-15]	[0-10]	[5-15]
Others	[25-35]	[35-45]	[25-35]

Source: Celsa estimates

48. Some third parties estimated that the parties' share of actual sales would be higher than their share of installed capacity and would be in the range of 60 to 70 per cent. Although the OFT was unable to accurately verify this claim, this does not affect the substantive analysis of these mergers, because the OFT considered shares of installed capacity to be a more appropriate measure of market power where products are relatively undifferentiated and productive capacity is important, for two reasons: first, other competitors have substantial amounts of spare capacity; and second, the incremental costs of utilising this capacity are low. Both are discussed in detail below.
49. The OFT also considered the extent to which there is spare capacity in the market, and Celsa's share of any such capacity post-mergers. If its share was such that it became the marginal source of supply in the market, the OFT's concern was that this would give Celsa the ability and incentive to withhold supply to the market with the effect of increasing prices because competitors would not have sufficient spare capacity to increase output to defeat such a price rise. Indeed, a number of market participants suggested that the share of spare capacity held by the merged entity would place it in a favourable position to stabilize over-capacity in the market, which the OFT understands has, until now, been a factor in driving down prices in the UK.
50. Celsa advised that, in 2008, each of the target companies operated with a significant amount of spare capacity: BRC had [30-40] per cent; Express had [40-50] per cent; and ROM had [30-40] per cent. The total spare capacity of the three target companies was approximately [200,000 – 300,000] tonnes, representing approximately [10-20] per cent of total installed capacity in the UK.

¹⁸ Installed capacity refers to the total capacity of the market if every fabrication plant was operating at its maximum legal capacity. It takes into account the fact that some fabrication plants are unable to operate 24 hours per day due to, for example, noise restrictions.

51. Celsa submitted, however, that post-mergers there would be ample independent spare capacity left in the market (it estimated competitors' spare capacity in the market at 44 per cent) such that fabricators would be able to increase production to make up for the loss of any supply that Celsa withheld from the market. In this regard, Celsa provided estimates of fabricators' installed capacities, which, when totalled, summed to a capacity of approximately 1.5 million tonnes per annum, giving some 660,000 tonnes of spare capacity, compared to less than [200,000 – 300,000] tonnes for BRC, ROM and Express. Consistent with this, if the parties' combined share of sales was higher than their combined share of capacity—consistent with the third party estimates in paragraph —then Celsa's share of spare capacity would indeed be lower than its competitors.
52. Market enquiries confirmed that this estimate of market capacity of 1.5 million tonnes was a good one. While one sizeable player indicated that it was operating near capacity, most fabricators (including a number of other substantially-sized fabricators) indicated that they had substantial amounts of spare capacity. As such, Celsa estimated it would need to withhold supply corresponding to approximately [75-85] per cent of its capacity in order to exhaust the total spare capacity of rival fabricators.
53. The OFT considered whether it would be commercially viable for competitors to mobilise their spare capacity in response to a supply withholding strategy by Celsa. That is, whether competitors' spare capacity is effective spare capacity — that could profitably be used to defeat a supply-withholding strategy — or is merely notional spare capacity that could not. Market enquiries indicated that the costs associated with expanding plant production to exploit spare capacity are low, with fabricators advising that production can easily be expanded by putting on additional shifts, usually at night.¹⁹
54. Market participants indicated that the major cost associated with expanding supply was the incremental cost of hiring additional unskilled labour, which can easily be sourced from employment agencies. Several third parties indicated that supply increases on the order of 50 per cent would be achievable at relatively limited additional cost and within a short time period. In light of the low costs associated with expansion, market participants indicated that it would be profitable to expand production by putting on an additional shift in response to a five to ten per cent price rise. Market participants did not suggest that such capacity would be less efficient than currently utilised capacity.
55. In light of the above, the OFT considered that the 'effective' spare capacity figures quoted for competitors by Celsa are realistic. This confirms Celsa's

¹⁹ Although the OFT understands that some plants are barred from putting on additional shifts at night because, for example, they are located in a residential area, many fabricators questioned indicated that most, if not all, of their plants did not face this restriction.

argument that it would have to withhold approximately [75-85] per cent of its capacity in order to push competitors to full capacity and increase the market price.²⁰ The OFT considers that such a strategy would be highly unlikely to be profitable given the small remaining sales base over which the parties would be able to recoup lost profit via potentially increased prices.

56. The OFT was also made aware of numerous examples where third parties had materially increased potential capacity over the last two to three years. In total, the OFT understands that more than 200,000 tonnes of capacity has been added to the market since 2004 (equating to approximately 25 per cent of estimated 2009 demand), 95 per cent of which was added in the last three years.
57. On the demand-side, market enquiries revealed that customers have a good knowledge of prices in the market and a feel for whether a particular fabricator's prices are in line with current trends. Switching costs also appear to be low, with the majority of those surveyed indicating that they have the ability easily to switch between fabricators, and either have done so in the past in response to a price rise, or have extracted better terms from their existing supplier in response to a threat to switch.
58. On the basis of the above, the OFT did not consider that the mergers would give Celsa the ability or incentive to engage in a strategy of withholding supply from the market in order to increase prices. In response to such a strategy, rival fabricators are likely to easily and profitably bring more capacity on-line and low switching costs means customers are likely to divert business away from the merged entity.

Inability of other competitors to constrain the merged entity

59. Post-mergers, a number of potentially significant competitors will remain in the market. However, Celsa will be considerably larger than each of these firms, and over five times larger in some cases. A number of concerns were raised in the market regarding the ability of the remaining competitors to constrain the merged entity.

Scale and scope advantages

60. A significant number of end users argued that the remaining competitors would not have sufficient scale to constrain the merged entity, with some customers also raising concerns that Celsa would have a much wider product range than its competitors, adversely affecting rivals' ability to compete. Some customers also advised that, for certain products, there will be no viable alternatives to the merged entity because its products are

²⁰ This calculation assumes, consistent with the evidence presented at paragraphs 53-54, that industry wide marginal costs do not vary significantly with output.

patent protected.²¹

61. Celsa argued that scale economies are not fundamentally important to being a viable competitor in this market. In support of this, it noted that each of the target companies' operations are comprised of multiple depots including a number of small depots (as small as 5,000 tonnes per annum) as well as large ones. If scale economies were important, Celsa argued, one would expect to observe large companies servicing the UK from just two or three large depots. Further, even if the largest depots are examined, Celsa argued that 11 out of the 24 largest are owned by Celsa's competitors.²² In the absence of scale economies, Celsa argued that the fact that it will be the largest fabricator in the UK (in terms of capacity) did not give it substantial market power and therefore would not raise competition concerns.
62. During the course of its investigations, the OFT did not receive any quantifiable evidence that scale economies were important in this market. Indeed, the substantial volume of supply (approximately 53 per cent) in the UK market that is represented by firms with a capacity of 10,000 tonnes per annum or less would tend to support a finding that scale economies are not materially important.
63. In terms of product range, Celsa argued that the target companies did not have a wider range of products than those available elsewhere in the market, arguing that alternatives were available for all the products it sells. While this issue was raised by some customers, the majority of these stated that only a small number of products would be affected and many supported Celsa's contention that alternative products were available (although these may be imperfectly substitutable). Further, these products did not tend to be 'core' products and were in some cases even discretionary. Aside from the proprietary products (access to which the mergers do not affect), the OFT did not receive any evidence to suggest that competitors could not begin manufacturing the affected products should the need arise.
64. As such, the OFT did not consider that the mergers would allow the merged entity to realise any scale or scope advantages that would be likely to give rise to competition issues.

Large customer contracts

65. Market participants also raised concerns regarding the ability of remaining competitors to bid effectively for very large customers' contracts (typically 10,000 tonnes and above). For example, a number of third parties advised that the target companies are frequently 'played off' against each other

²¹ For example, the OFT understands that ROM has a product under patent which is a market-leading prefabricated steel cage used in concrete piling.

²² Celsa accounts for [50-60] per cent of the capacity of the 20 largest depots.

(including being subjected to threats of switching) in order to achieve lower prices for these contracts. Additionally, while some customers noted that they spread their large-contract needs across different companies, in many cases this spread appeared predominantly to be across BRC, Express and ROM. In some cases, the target companies accounted for over 80 per cent of a customer's steel supply. As such, many customers felt that their negotiating strength with fabricators would be reduced due to increased concentration in the market and the fact that fewer sizeable competitors for their business would remain.

66. Some fabricators contacted by the OFT advised that the target companies are the market leaders for supplying large customers. However, this was on the basis of reputation rather than any physical advantage. Some fabricators also cited the existence of preferred supplier arrangements and less formal long term relationships, sometimes personal in nature, between large customers and large fabricators. Nonetheless, most indicated that there were no material barriers to winning large contracts except having sufficient capacity to undertake the work.
67. Celsa submitted a number of reasons why the merged entity would continue to face competitive constraints for the supply of large contracts following the mergers. First, Celsa argued that customers at this end of the market are generally large, well-resourced companies with some degree of buyer power. A number of large customers, however, indicated that they felt that what buyer power they currently have will be decreased by the merger with the loss of competitive tension between the merger parties. Nevertheless, the majority of these customers named at least two other fabricators which they believed could service their needs.
68. Second, Celsa also argued that large construction companies are adept at structuring contracts to maximise the competitive dynamics of tenders, including splitting contracts into a number of smaller 'lots': Celsa provided a list of contracts it claimed had been structured in this way. Market enquiries confirmed that large contracts can be, and are, split into smaller lots on a relatively regular basis. The OFT understands that this practice has become more common recently as a result of the fluctuating price of steel. Nevertheless, some market participants indicated that having multiple suppliers can raise issues of its own. For example, having multiple suppliers increases the risk of delay via plant breakdown or late deliveries. Where the product being delivered is of a 'just in time' nature (for example, a reinforcing cage for concrete, which must be used before the concrete sets) such delays can incur significant costs. The OFT acknowledges that splitting contracts can create additional issues of this nature, but notes that it remains a common practice before the merger and that there is no reason why it should not continue to be used post-mergers.
69. Another way in which large customers can exert some degree of buyer power is to vertically integrate backwards into fabrication. They can do this

on a permanent or temporary basis either via joint ventures or by setting up their own operations. The OFT was made aware of a number of examples of this occurring for very large scale contracts, such as the construction of the Glendoe hydro-electric dam and the establishment of Thames Reinforcement as the steel reinforcing arm of reinforced framework contractor J. Reddingtonne Ltd.²³ Nevertheless, this practice does not appear to be widespread in the industry, given the relative rarity of such large scale projects, and the OFT was unable to verify as to whether self-supply would be a viable alternative more generally to purchasing from third parties.

70. Celsa submitted evidence of the size of contracts serviced by the target companies in 2007 and 2008. Of these projects, Celsa argued that a very small percentage (under five per cent by number, representing under ten per cent by volume of total UK demand) of these would have been 'incontestable' as a practical matter for a fabricator with an annual capacity of 10,000 tonnes. In addition, Celsa argued that the vast majority of projects are less than 2,000 tonnes (just [0-10] per cent were in excess of 2,000 tonnes in 2007-08). Therefore, even if the conclusion were reached that small fabricators were excluded from competing for large contracts, Celsa noted that the merged entity will still face competition from at least eight other fabricators in the UK with capacities greater than 25,000 tonnes per annum, and around 27 competitors with a capacity of greater than 10,000 tonnes.
71. On the basis of the above, the OFT did not consider there to be a realistic prospect that competition issues would be likely to arise in relation to large customers. The existence of viable alternatives to the merged entity, combined with strategies such as splitting contracts and, in limited cases, self-supplying, means that Celsa is likely to be constrained in any attempt to exercise market power in respect of large customers following the mergers.

Price leadership

72. Some market participants raised concerns that the mergers would be likely to create a 'price leader' in the fabrication/distribution market, raising the prospect that rivals could price-up to the level set by the merged entity. With a market share of approximately [45-55] per cent, it was put to the OFT that Celsa would have sufficient market power to set a focal point for pricing, in effect dictating the market price set by other, much smaller, competitors.
73. Even where other fabricators are in a position to defeat a price rise (by expanding production, as described earlier), they may have an incentive not to if they believe that the market leader can credibly commit to a strategy

²³ Thames Reinforcements services not only the needs of its parent company, but also supplies third parties.

resulting in increased prices market-wide. Indeed, one fabricator explicitly stated that it probably would not try to undercut a price rise by Celsa but instead seek to increase its profit margins. In addition to these factors the OFT considered whether Celsa's significant upstream position (see the Vertical Effects section, below) would provide it with the opportunity to increase transparency over the downstream input so as to stabilise costs across the market, thereby enhancing its ability to dictate prices in the market.

74. On the basis of the information before it, however, the OFT could not find an empirical basis for these claims. As discussed earlier, the market appears to be characterised by a significant amount of spare capacity spread among a substantial number of competitors. In these circumstances, it is unlikely that Celsa would be in a position to commit to a price leading strategy by withholding supply, as it does not have a large enough share of spare capacity to make this commitment credible. Nor does Celsa appear to have any other sort of cost advantage that could make its commitment to withhold supply credible. Subsequently, smaller competitors are likely to find it profitable to undercut Celsa (or equivalently, expand supply) in order to win business from it. Further, although upstream pricing appears to be relatively transparent, tender prices are not (and the very large majority of projects are tendered). In the absence of collusion or coordination (which is dismissed as a concern below), it would therefore be difficult for competitors to determine Celsa's downstream prices accurately enough in order to 'follow' them.

Sub-national issues

75. As noted at paragraph , above, evidence presented to the OFT suggested that some degree of competitive variation exists at the regional/local level, despite the fact that depots consistently service customers further away than 150 miles and that many customers considered the market to be largely national. On a conservative basis, the OFT therefore considered whether, in addition to the issues considered above at a national level, any unilateral concerns could arise in any market with a geographic scope narrower than the UK. In practice, given the strength of evidence supporting markets wider than 150 miles the OFT has focussed its analysis on regions of the UK that may be serviced by somewhat fewer fabricators; namely, (i) Scotland and (ii) Wales and the south west of England.
76. In its assessment the OFT was mindful that arguments presented at the national level will, in large part, be relevant to the local or regional level. In particular the OFT notes that evidence of expansion (see paragraphs to , above) suggests that competitors within any local market can expand operations at minimal cost. Moreover, the OFT is aware that within any location in the UK, a substantial number of suppliers (more than three) will continue to operate at a sufficient scale to service large contracts (see paragraphs to , above). Additionally, the OFT notes that the large majority

of concerns were focussed on competition issues at the national level: namely those relating to vertical effects, Celsa's share of supply at the fabrication level and the ability of others fabricators to service large contracts.

77. With respect to regional concerns, two complaints were made to the OFT focussing on the target companies' shares of supply in Scotland. One complainant estimated that, post-mergers, Celsa would account for approximately 70 per cent of the market. However, while Celsa's share may be somewhat greater in Scotland than in the UK overall, the OFT's market enquiries revealed that at least three other suppliers will remain in Scotland post-mergers, and that a further two will continue to supply into Scotland from England.
78. The OFT was not made aware by any other customers that the number of alternative suppliers available to them would be materially affected in this area, and many highlighted the fact that numerous suppliers operate on a national basis.
79. Finally, consistent with its findings at the national level, the OFT considers that any attempt to withhold supply is likely to be unprofitable due to substantial levels of spare capacity that competitors are able to profitably mobilise to defeat such a strategy. In particular, at least one rival fabricator in Scotland indicated that supply could be increased by 50 per cent with little difficulty.
80. With respect to Wales and the south west of England, one concerned third party indicated that Celsa would have a share of supply of around 70 per cent in this region. The OFT notes that BRC's depots in Wales represent its two largest in the UK ([70,000-90,000] tonnes and [40,000-60,000] tonnes), while Express' Welsh depot is also its largest in the UK ([80,000-100,000] tonnes).
81. However, the OFT notes that, post-mergers, at least six other competitors will have depots within this region, ranging from 7,000 to 25,000 tonnes. Moreover, the majority of Celsa's facilities situated in Wales will face potential competition from the numerous suppliers situated in Birmingham and the Midlands. Again, the OFT was not made aware by any customers that the number of alternative suppliers available to them would be materially affected in this area.
82. Overall, the OFT considered that the mergers would not give Celsa the ability or incentive to withhold capacity from the market in order to engineer a price rise within any sub-national geographic area.

Intermediate level – wholesale supply of mesh

83. The OFT received one complaint specifically in relation to the wholesaling of mesh, however this was vertical in nature and its assessment forms part

of the Vertical Effects section, below. Other concerns relating to this level of the supply chain formed part of broader concerns raised in relation to either the relevant upstream or downstream markets and are accordingly covered with elsewhere in the decision (in the Horizontal Effects section, above, and the Vertical Effects section, below).

Conclusion on unilateral effects

84. In light of the significant volumes of spare capacity in the market, the presence of a number of significant competitors and the low incremental costs (in terms of time and money) involved in increasing supply, the OFT considered that the mergers would not give Celsa the ability or incentive to withhold supply from the market (whether as a 'price leader' or not) in order to engineer a price rise at either the national level or in any sub-national area. The OFT also did not consider the mergers would give rise to scale or scope economies that would raise competition concerns, nor impact significantly on competition for large contracts.

COORDINATED EFFECTS

85. No third parties raised concerns of a purely coordinated nature in the upstream, intermediate or downstream markets. This lack of concern is consistent with the fact that, in the downstream and intermediate markets, the transaction increases supplier asymmetries with respect to market shares in a market characterised by a large number of small suppliers, each with spare capacity. Generally, the OFT considers that these factors lessen the likelihood of pure coordinated outcomes, as Celsa's and its competitors' incentives are not well aligned, making a coordinated outcome unlikely.
86. With respect to the upstream market, the OFT notes that the lack of an increment resulting from the transaction makes it unlikely that coordinated effects concerns would arise as a result of the mergers.
87. As such, the OFT considers that coordinated effects are unlikely to arise in any relevant market post-mergers.

VERTICAL ISSUES

88. Vertical mergers are generally efficiency-enhancing, and as such are viewed by the OFT as presumptively competitively benign, unless there is a realistic prospect of vertical effects, incorporating a coherent story of harm. For example, vertical mergers can lead to the 'internalisation of double mark-ups' which may result in lower prices downstream as the downstream mark-up on a product is internalised by the merged entity. Indeed, one fabricator indicated that this may already be happening, advising that the target companies are quoting prices of '£20 to £30 lower' than what his company has been quoting.

89. Nevertheless, a substantial number of third parties were concerned that the vertical integration between Celsa and the target companies resulting from the mergers would adversely affect Celsa's competitors both in the upstream manufacture of rebar, coil and MWR and the downstream distribution of rebar, coil and mesh.
90. As noted, following the mergers, Celsa will become a vertically integrated manufacturer/fabricator with a market share of approximately [45-55] per cent in the UK fabrication/distribution market. During the course of its investigation, the OFT received a number of concerns from market participants that Celsa's significant upstream position, combined with its [45-55] per cent downstream market share, would give rise to Celsa foreclosing rival downstream fabricators or upstream manufacturers.
91. Where a merger gives rise to such potential vertical competition concerns, the OFT will assess whether the transaction confers (i) the ability and (ii) the incentive on the merged entity to foreclose. If so, it will then (iii) assess whether rivals would be foreclosed to an extent that compromises their ability to compete such that there is a realistic prospect that a substantial lessening of competition will occur.
92. This foreclosure may take the form of Celsa 'upstream' increasing the price of an input (that is, rebar, coil and MWR) to its 'downstream' rivals (known as partial input foreclosure); or refusing to supply that input (known as total input foreclosure). It may also take the form of Celsa 'downstream' increasing the price of a route to market (that is, refusing to fabricate/distribute their products) to its 'upstream' rivals (known as partial customer foreclosure); or refusing them access to the downstream market (known as total customer foreclosure).

Input foreclosure

93. Celsa argued that it would not have the ability or incentive to foreclose its rivals at the intermediate wholesale mesh level or the downstream fabrication/distribution level by increasing the price to them of rebar, coil and MWR (partial input foreclosure) or by refusing to supply them (total input foreclosure).
94. Celsa said that it would not have the ability for two reasons. Firstly, it argued that it will not have sufficient market power at the manufacturing level to make such a strategy possible or profitable and, second, it posited that it will be constrained by the other UK supplier, Thames Steel, and by the prevalence of imports. As such, it contended that, were it to attempt to either deny its rivals access to key inputs, or refuse to supply them altogether, its rivals could viably switch to other sources of rebar, coil and MWR.
95. In addition, Celsa claimed that, even if had the ability to engage in such a

foreclosure strategy, it would lack the incentive to do so. Both of these points are examined below.

Ability to engage in input foreclosure

96. As discussed at paragraphs to , above, Celsa will continue to face competition from another UK producer, Thames Steel, and the supply of imports from the EU and Turkey.²⁴ Given the fluctuating level of imports coming into the UK, UK market shares at this level of production have historically also tended to be unstable. It was generally accepted, however, that Thames Steel's market share has remained fairly consistent at between five and ten per cent. Thus, at October 2008, if imports comprised 47 per cent of the market, Celsa's market share could have been as high as 48 per cent.
97. A number of market participants cast doubt on the ability of Thames Steel to constrain the merged entity. For example, some in the market stated that Thames' product range was not as broad as Celsa's. However, despite Thames' historically low UK market share, the majority of fabricators surveyed indicated that Thames was a viable alternative to Celsa and that they would switch to either Thames, overseas manufacturers or both were Celsa to attempt to increase prices.
98. The OFT therefore considers that, were Celsa to seek partially to foreclose access to its product range, it would be viable for fabricators to switch either to Thames Steel or overseas companies to service their needs. As such, the OFT did not consider that Celsa would have the ability partially to foreclose downstream fabricators.
99. With respect to **total** input foreclosure, and as noted earlier, some market participants advised that the product ranges of Thames Steel and companies located outside the UK are not as wide as Celsa's. This, it was argued, meant that there are some products that only Celsa will be able to supply following the mergers. Nevertheless, few respondents suggested that such factors would fundamentally undermine their competitive position. While fabricators conceded it would cause them some inconvenience, most were relatively confident that they would be able to secure products from alternative providers such as Thames Steel or overseas suppliers. As such, the OFT did not consider that Celsa would have the ability to engage in total input foreclosure.

Incentive to engage in input foreclosure

100. In the light of the presumptively benign nature of such vertical mergers and in the absence of an ability to engage in partial or total input foreclosure,

²⁴ The OFT also understands that another company, Mirinvest UK (known as Mir Steel UK), owns manufacturing facilities in the UK that could be used to compete against Celsa but that these facilities are not currently in operation.

the OFT's overall concern regarding input foreclosure cannot arise. Therefore, the OFT has not needed to consider whether Celsa would have the incentive to engage in such conduct.

101. Nevertheless, the OFT is considers there to be a number of factors that may work against there being such incentives in this case.
102. Specifically, in respect of the relative margins at the manufacturing and fabrication/distribution levels, Celsa provided evidence suggesting that upstream variable gross margins across bar, coil and MWR average around [.] per cent, some two to three times greater than its estimated downstream margins (based on information provided by the target companies), which are of the order of [.] to [.] per cent.
103. Such evidence is consistent with the fact that upstream steel manufacture is a high fixed cost enterprise where contributory (or variable) margins would be expected to be high. All else being equal, lower relative margins at the downstream level make it less likely that Celsa could successfully recoup profits foregone from a restriction of supply at the upstream level by increasing sales at the downstream level.
104. Additionally, although Celsa's share of supply upstream is likely to be in excess of 40 per cent, downstream operators have the ability to source from importers. The OFT therefore considers that, following an attempt by Celsa to totally or partially foreclose downstream rivals, a significant volume of sales would switch to these alternative sources of supply resulting in a significant loss of upstream profits. All else being equal, this is likely to lessen the profitability of such a strategy.
105. On the basis of above, the OFT does not consider that such a strategy would be obviously profitable in the short to medium term. Moreover, the OFT understands that 'mothballing' of downstream capacity is relatively costless.²⁵ Therefore, and without reaching a final view on the matter, the OFT does not consider that the parties would necessarily be in a position to derive a long term benefit from engaging in either partial or total input foreclosure by forcing its competitors to exit the market.

Conclusion on input foreclosure

106. On the balance of the evidence presented, the OFT does not consider there to be a realistic prospect that Celsa would have the ability to foreclose rivals via total or partial input foreclosure, given the ability of customers to source the relevant products from alternative suppliers. Given this lack of availability, it was not necessary for the OFT to conclude on incentive, but

²⁵ The OFT understands that the useful life of machinery used by fabricators is measured in hours of operation, rather than by how old it is. Thus, *ceteris paribus*, two machines that have operated for the same amount of hours would be equally valuable, even if one is five years older than the other. See paragraph 122 for further detail.

it is not at all obvious that foreclosure would be profitable given (a) the existence of alternative sources of inputs; (b) the relative lack of incentive created by high upstream margins; and (c) the difficulty in forcing rivals to exit the market given the ability to mothball machinery costlessly.

Customer foreclosure

107. A small number of concerns were raised during the OFT's investigation relating to Celsa's ability and incentive to totally foreclose access to downstream customers.
108. In assessing whether any such customer foreclosure is likely to raise competition issues, a merger must give the acquirer the ability and incentive to foreclose upstream rivals, as well as have the effect of substantially lessening competition. Part of the rationale for the transactions was for Celsa to obtain a secure route to the downstream fabrication and intermediate mesh markets via the ownership of companies at these levels of production. Evidence received during market enquiries indicated that all three target companies now source the vast majority, if not all, of their reinforcement steel needs from Celsa. Given Celsa has already internalised these volumes, it is unnecessary to consider whether it would have the incentive and ability to do so (because it has already done it). Therefore, the below analysis focuses on the effect of this strategy.
109. Specifically, the OFT considered whether the mergers would result in Celsa having sufficient downstream customer volumes to foreclose Thames Steel and importers, thereby undermining their ability to compete against Celsa such that there is a realistic prospect that a substantial lessening of competition will occur.²⁶
110. As noted, following the mergers, Celsa will have a share of approximately [45 to 55] per cent of the downstream fabrication market (by installed capacity). For the purposes of its assessment²⁷, the OFT took a cautious approach and assumed that, on the basis of Celsa self-supply, this share of the market will be unavailable to third parties. However, some third parties argued that the volume of business that could be foreclosed following the mergers may actually be as high as 75 to 80 per cent due to rumoured further vertical integration in the market and effective 'tied' sales.
111. At least one market participant (an importer) indicated that these factors together with the mergers are likely to undermine its ability to profitably supply downstream fabricators as a result of reduced volumes leading to a loss of scale economies; indeed, it indicated that it has already ceased supplying the UK for this reason.

²⁶ Given the OFT's decision on market definition in the upstream market (that is, UK wide), any customer foreclosure concern relates primarily to Thames Steel.

²⁷ Notwithstanding the example of a vertically integrated Celsa subsidiary supplying downstream rivals in Scandinavia.

112. On the issue of tied sales, Celsa submitted that no exclusivity contracts with any of its customers presently exist and customers are in a position to switch to alternative suppliers. This was confirmed by fabricators surveyed, with none indicating they were contractually or otherwise bound to purchase exclusively from Celsa, and many providing examples of recent purchases from other upstream suppliers.
113. With respect to the prospects for further vertical integration in the market foreclosing further companies, the OFT noted that Thames Steel has recently taken a shareholding in the downstream fabricator, Kierbeck (with a share of installed capacity of [5-15] per cent – see Table 2 above).²⁸ At the time of the decision the OFT was not aware of the precise nature or size of this shareholding.
114. Taking a cautious approach, the OFT considered whether customer foreclosure effects would occur if Thames Steel were to internalise all of Kierbeck's demand.²⁹ For the reasons set out below, the OFT considered that no such concerns would be likely to arise.
115. The EC's Non-Horizontal Merger Guidelines³⁰ states that non-horizontal mergers are unlikely to pose competitive threats where the merged entity does not have a significant degree of market power in at least one market:
- Because of this downstream presence, the merged entity may foreclose access to a sufficient customer base to its actual or potential rivals in the upstream market (the input market) and reduce their ability or incentive to compete. In turn, this may raise downstream rivals' costs by making it harder for them to obtain supplies of the input under similar prices and conditions as absent the merger. This may allow the merged entity profitably to establish higher prices on the downstream market.
116. However, as discussed in paragraphs 46 to 84, above, the OFT did not consider the mergers would be likely to give Celsa substantial market power in the downstream fabrication or intermediate mesh markets, in particular as a result of the significant amount of spare capacity in the market.³¹ Further, at paragraphs to , above, the OFT found that it was unlikely that Celsa could deny rival fabricators access to upstream inputs due to the presence of Thames Steel and importers as viable alternatives to Celsa. In the absence of any market power at the downstream level, the OFT considered that any decision by Celsa to self-supply would not be capable of raising any competition concerns on the basis that a sufficient

²⁸ Thames Steel informed the OFT on 27 January 2009 that it had taken an ownership stake in fabrication company, Kierbeck.

²⁹ In these circumstances, 43 per cent of the market would remain contestable.

³⁰ 'Guidelines on the assessment of non-horizontal mergers under the Council Regulation on the control of concentrations between undertakings' at 23.

³¹ In other words, the market shares for installed capacity (see above) were not an accurate reflection of competition in the relevant markets.

portion of the downstream market would remain contestable for upstream rivals.

117. Finally, as noted at paragraph 113, above, the other active UK manufacturer, Thames Steel, now owns a share in a downstream fabricator: Kierbeck. Although at the time of writing the OFT was not aware of the exact level of shareholding, this affiliation is likely to ensure Thames Steel has an avenue to market and is therefore likely to continue to provide a competitive constraint on the merged entity.

118. The OFT is therefore not persuaded that any attempt by Celsa to foreclose upstream competitors (including importers) through total customer foreclosure in the UK would give rise to a realistic prospect of a substantial lessening of competition.

Conclusion – customer foreclosure

119. On the basis of all the evidence presented, the OFT did not consider there to be a realistic prospect of a substantial lessening of competition arising via customer foreclosure. At least [45 to 55] per cent of the fabrication market will remain contestable immediately following the mergers.

Conclusion – vertical effects

120. On the basis of the evidence before it, the OFT was satisfied that the mergers would not give Celsa the ability to engage in either partial or total input foreclosure. It was also not obvious that it would be profitable to do so. The OFT was also satisfied that any customer foreclosure strategy that Celsa attempted to engage in would not be likely to raise competition concerns. Indeed, the OFT notes that the merger may actually be efficiency-enhancing given the evidence of lower prices being quoted by the target companies since the acquisitions completed.

BARRIERS TO ENTRY

Upstream manufacturing market

121. For the purposes of the Vertical Effects assessment the OFT considered whether barriers to entry or expansion exist in the upstream manufacturing market.

122. On this issue, Celsa submitted that Mir Steel UK has a mothballed plant (the former assets of Alpha Steel), which could be brought into operation at relatively low cost and in a timely fashion, meaning the barriers to re-entry to the UK are relatively low in that particular case. The OFT was, however, unable to confirm what costs, if any, would be involved in bringing this facility back on-line, or whether the current owners would consider re-entry into the market as a possible strategy going forward were prices to rise.

123. In terms of de novo entry, third parties consistently commented that barriers are relatively sizeable. One respondent suggested that it would cost a new entrant in the region of £60-70 million to replicate Celsa's operations in the UK, with a timescale of 16 to 18 months following planning approval. On this basis, the OFT considers it unlikely that de novo entry could occur in a timely manner, particularly given the current unstable nature of the market.
124. The OFT was also made aware that UK fabricators (and end customers) have a strong preference for products that are CARES approved.³² However, obtaining CARES certification does not appear to be an overly time-consuming or costly task, with many overseas producers being CARES approved for a wide variety of products. Given the CARES classification system relates to the UK and Ireland only, this would suggest that this is not an insurmountable barrier for overseas producers.
125. With respect to the likelihood of an expansion in the level of imports, the OFT notes that many downstream fabricators view imports as a viable source of supply, and would actively seek to increase levels of imports following any increase in price. With respect to importers themselves, while the OFT was unable to confirm with importers whether current market conditions are conducive to expansion of supply following any increase in price in the UK market, the OFT notes that imports have formed a substantial part of the market for at least the past three years, and is aware of independent reports stating that Turkish rebar exporters have recently increased their focus on the UK market as conditions in other markets have changed.³³
126. Overall, the OFT did not need to conclude on the level of competitive constraint that de novo entry or expansion are likely to impose on Celsa following the mergers because it considered the potential for expansion by existing sources of imports meant competition concerns were unlikely to result from the mergers.

Mesh wholesaling

127. Market enquiries indicated that mesh wholesaling, in its most rudimentary form, requires (a) access to a reliable and economic source of MWR; (b) the ability to transform MWR into mesh (which requires specialised machinery) and (c) access to a customer base.
128. With regards to (a), and as discussed in the Vertical Effects section, the OFT did not conclude that Celsa would have the ability or incentive to foreclose access to input products, including MWR.
129. In terms of the machinery required, the OFT did not receive any specific

³² See fn 8.

³³ *Metal Bulletin*, 'Desperate Turkish rebar producers seek orders in the UK', 9 January 2009.

concerns from the market that this is especially difficult to obtain, and evidence was received regarding the operation of a second hand market.

130. Finally, with respect to (c), as discussed at above, the merger is unlikely to result in the creation of market power at the downstream level³⁴, or in an unduly large proportion of the market being foreclosed to competition.³⁵
131. As noted earlier, market enquiries indicated that many mesh wholesalers are vertically integrated either upstream or downstream and that many fabricators self-supply by manufacturing mesh themselves. This would tend to indicate that barriers to entry for current upstream and downstream companies are low.
132. Overall, the OFT did not find it necessary to conclude on whether barriers to entry were significant in the mesh wholesaling as it was satisfied that existing competitors in the market, as well as imports, were likely to constrain Celsa following the mergers.

Fabrication and distribution of rebar, mesh and coil

133. Celsa contended that barriers to entry in the downstream fabrication market are low due to relatively low sunk costs being required to produce cut and bent products (five per cent or less of turnover), making both small and large scale entry viable, as well as making integration by large buyers a credible threat. Moreover, Celsa pointed towards several instances of new entry since 2007, including Thames Reinforcements (which has a production capacity of 40,000 tonnes per annum), Frank Brazil (25,000 tonnes) and Midland steel (36,000 tonnes) as evidence that the cost of entry is, in general, low for de novo entrants.
134. However, the results of the OFT's investigations cast doubts on Celsa's arguments in this regard. Specifically, many third parties suggested that the sunk costs of de novo entry are high relative to the volume of sales that could be achieved by a new entrant. Third parties suggested that this was particularly relevant in the current economic climate due to the substantial over capacity that exists in the market as a result of falling demand. No third parties indicated that entry was likely in the short to medium term given current market conditions.
135. In terms of backwards integration by large customers, Celsa argued that this would be a viable counter-strategy for construction companies facing a rise in the cost of steel reinforcement products and cited a number of examples to support its case. The OFT's investigations tended to confirm that such backwards integration was only viable for the largest jobs, such as Heathrow terminal 5, and in general would not be considered as a viable alternative in most circumstances.

³⁴ At paragraphs 46 to 82.

³⁵ At paragraphs 107 to 121.

136. Overall, while the OFT had reasons to believe that timely entry was relatively unlikely, it did not find it necessary to conclude on whether any such entry was sufficient to constrain Celsa in light of the continued competitive constraint it is likely to face from existing competitors in the market.

THIRD PARTY VIEWS

137. The OFT received a significant number of concerns relating to the mergers. At the downstream level, a number of end customers raised concerns that the merger of the three largest fabricator/distributors would reduce customer choice and buyer power. Concerns were also raised regarding the ability of the remaining competitors in the market to offer services of a sufficient scale and scope to constrain the merged entity.

138. Specifically, a number of fabricators raised concerns regarding their ability to source steel from upstream suppliers post-mergers. Many argued that Celsa has a very large upstream market share and would seek to favour its downstream operations at the expense of rival fabricators. Thames Steel was not viewed as an equally good alternative by certain customers, and concerns were also raised about the ability of imports to compete with Celsa. One fabricator also noted that Celsa has already begun to favour the target companies in terms of charging them lower prices, such that the target companies are now quoting prices '£20 to £30 per tonne' lower than the rest of the market.

139. Finally, a small number of market participants raised concerns that the merger would result in the number of contestable fabricator customers decreasing to a point where it will not be viable to continue supplying them.

140. All of these issues are referred to above where appropriate.

ASSESSMENT

141. The OFT considered whether competition issues would arise from Celsa's acquisition of approximately [45 to 55] per cent of the downstream fabrication/distribution market. It further considered whether concerns would arise from the combination of this downstream market share with its substantial upstream market share. A concern regarding the ability of the remaining competitors in the market to service large contracts was also considered.

Unilateral effects

142. At the downstream level, the OFT considered whether the acquisitions would lead to increased prices through either Celsa withholding fabrication supply from the market and/or acting as a price leader.
143. In terms of withholding supply, the evidence before the OFT suggested that there is a substantial amount of spare capacity in the fabrication market spread among many competitors, including a number of relatively large and well-resourced ones. Further, market enquiries suggested that there are no material costs associated with fabricators increasing output, leading the OFT to conclude that any supply withdrawn from the market could be easily replaced by a competitor. Celsa would therefore have to forego a high volume of sales before it would become the marginal supplier, which, based on the evidence before it, the OFT considered would be unlikely to be profitable. The OFT also considered that inter alia the existence of spare capacity would undermine Celsa's ability to credibly commit to any strategy of price leadership.
144. Finally, the OFT considered whether competition issues could arise with respect to large construction contracts, but ultimately dismissed such concerns. Post-mergers, Celsa will be constrained by a number of well resourced companies that can (and do) tender for large contracts. While market enquiries did reveal some concerns that the merger would decrease choice for customers, many market participants commented that their needs could be serviced by companies other than the target companies. Further, the OFT noted that contracts can be (and indeed are currently) split between a number of fabricators, or into multiple lots as the contract progresses, such that smaller companies are able to tender for parts of larger contracts. Very large contracts allow for the possibility of backwards integration into fabrication by the end customer.

Vertical effects

145. In terms of input foreclosure, the OFT was not persuaded that the mergers would give Celsa the ability to engage in either partial or total input foreclosure.
146. Given that the OFT views vertical mergers as presumptively benign, in order for an input foreclosure strategy to be anticompetitive, Celsa would need to have substantial market power upstream. While there was some tension between the information provided by Celsa (based on independent evidence) and some market participants as to the competitive constraint provided by Thames Steel, on balance the OFT believes that the existence of Thames Steel will have a constraining effect on Celsa. Further, a number of market participants advised that they either actively import materials from overseas or could do so in the event that Celsa attempted fully or

partially to foreclose them. The OFT was also made aware of specific examples of fabricators ordering volumes ahead of demand to overcome the longer lead times involved with imports. As such the OFT did not believe that Celsa would have the ability to forelose downstream rivals.

147. Given this lack of availability, it was not necessary for the OFT to conclude on incentive for input foreclosure. Nevertheless, there appear to be a number of factors that may work against there being such incentives on this occasion, in particular the existence of alternative sources of inputs, the relative lack of incentives created by high upstream margins, and the difficulty in forcing rivals to exit the market given the ability to utilise mothballed machinery virtually costlessly.

148. In terms of customer foreclosure, given the OFT has found that the mergers are unlikely to give Celsa substantial market power at either the intermediate or downstream levels of production, the OFT considered that any strategy of this nature was unlikely to raise competition concerns. In particular, the ability of rival fabricators to both expand production and switch to rival upstream sources of supply (both in the UK and overseas) meant that the OFT was comfortable that Celsa internalising the total demand of the target companies would not create a realistic prospect of a substantial lessening of competition.

CONCLUSION

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

DECISION

150. None of these three mergers will therefore be referred to the Competition Commission under section 22(1) of the Act.