Anticipated joint venture between Pura Foods Limited and Princes Limited

The OFT's decision on reference under section 33 given on 10 June 2005. Full text of decision published 28 June 2005.

Please note square brackets indicate information excised or replaced by a range at the request of the parties for reasons of commercial confidentiality

PARTIES

1. **Archer Daniels Midland Company (ADM)** is a publicly listed US company. One of ADM's main business activities in Europe is the processing and trading of oil seeds (primarily soya and rapeseed, and to a lesser extent sunflower) and the edible oils derived from them.

2. ADM owns **Pura Foods Limited (ADM Pura)**, which is active in the acquisition of crude and/or refined seed oil as its raw material, primarily in the UK. In May 2003, ADM Pura purchased the bulk refined seed oil business of Unilever Bestfoods UK Limited (UBUK).[1] ADM Pura also entered into a number of ancillary agreements with UBUK including a [ ] year seed oil supply and refining agreement, and an agreement to bottle certain branded refined seed oil products for UBUK (namely Olivio, Flora and Crisp'n'Dry).

3. **Princes Limited (Princes)** is ultimately owned by the Mitsubishi Corporation. Princes supplies grocery products, including edible oil, to the UK retail sector. Princes operates an olive oil bottling business at Belvedere. Princes also has a wholly owned subsidiary, **Edible Oils Limited (EOL)**, which in February 2005 acquired UBUK's branded bottled seed oil businesses (namely its Olivio, Flora, Crisp'n'Dry, and Mazola businesses) and the business of supplying Cookeen and Spry Crisp'n'Dry vegetable fats.

TRANSACTION

4. ADM Pura and Princes propose to form a 50/50 joint venture which will be known as Edible Oils Limited (referred to as 'the joint venture' in the rest of this decision). ADM Pura will sell its edible oils bottling business to the joint venture (the primary asset being ADM Pura's bottling plant at Erith). Princes will sell its edible oils business to the joint venture (primarily consisting of its bottling plant at Belvedere)

[1] Including a seed oil refinery and facilities for blending bulk oils. [More than 75] percent of this business consisted of supplies to members of the Unilever group, that had previously been 'captive'.

5. ADM Pura also intends to sell its retail white fats business to the joint venture, but this is not yet the subject of a binding agreement.

6. Princes has entered into agreements to provide certain administrative and ancillary services to the joint venture, and to act as the exclusive distributor of all products sold through the joint venture. ADM Pura will enter into a service supply agreement with the joint venture, agreeing to provide certain logistical services to the Erith site, as well as access to ADM Pura's Quality and Development Centre at Belvedere.

7. The parties notified the transaction on 13 April 2005 and the administrative deadline is 10 June 2005.

JURISDICTION

8. As a result of this transaction, ADM Pura's edible oils bottling and white fats businesses, and Princes' edible oils and white fats businesses will cease to be distinct. The parties overlap in the supply of seed oil and white fats, and the share of supply test in section 23 of the Enterprise Act 2002 (the Act) is met. The OFT therefore believes that it is or may be the case that arrangements are in progress or in contemplation which, if carried into effect, will result in the creation of a relevant merger situation.

9. The parties submit that the EC Merger Regulation (ECMR) does not apply because the formation of the joint venture does not constitute a 'concentration' as defined by the ECMR. The European Commission (the Commission) has confirmed this view in a 'comfort letter' to the parties on 5 April 2005.

BACKGROUND

10. Both ADM Pura and EOL supply seed oil and fats to the retail channel in the UK. More specifically, the parties supply: bulk refined seed oils (BRSO); packed refined seed oils (PRSO); and fats to the retail channel. We have examined seed oils and fats separately.

A. BULK AND PACKED REFINED SEED OILS

11. Seed oils are one of the two types of vegetable oils. The other type is olive oils, but since ADM Pura does not supply these products in the EU, they have not been considered further in this investigation.

12. Edible seed oils are manufactured by processing oilseeds. Oilseeds are crushed to produce crude seed oils, which are then refined and may then be supplied in bulk (i.e. BRSO). BRSO may be packed into bottles or cans for onward sale to end users (i.e. PRSO).

RELEVANT MARKET

Bulk refined seed oils

13. Neither Princes nor EOL is active in the supply of BRSO, thus there is no horizontal overlap. However, EOL requires BRSO and is supplied by ADM Pura

pursuant to the EOL Oil Supply Agreement which will continue to apply. Therefore, the BRSO segment has been examined as an upstream market.

Product market

14. The parties submit that the supply of BRSO constitutes a separate product market, which is consistent with the view reached in a number of EC decisions.[2]

15. The main types of BRSO are soya, sunflower and rapeseed. The parties submit that the BRSO segment should not be further sub-divided by individual seed oil type. On the demand side, the parties submit that different seed oil types may be equally suited to a given range of end-use applications. This has been confirmed by third parties. On the supply side, the parties submit that there are close substitution possibilities between the refining of different seed oil types at BRSO level. If refining margins on the production of one seed oil type were to increase unilaterally, refiners could and would be expected to switch their refining activity towards this seed oil type.

16. For the purposes of this analysis, we have taken the supply of BRSO as the relevant frame of reference.

Geographic market

17. The parties submit, and third parties concur, that the relevant geographic market for BRSO is at least EEA-wide. Previous EC decisions support this on the basis that BRSO are traded internationally, prices are the same throughout the EEA and bulk purchasers seek price quotes for refined seed oils based on the commodity market price for crude seed oils plus a premium. The parties submit that purchasers are sensitive to price differences and imports of BRSO accounted for [5-15] per cent of UK sales in 2003, with [0-10] per cent of UK production being export. Finally, transport costs for bulk deliveries are generally well below [5-15] per cent of the final selling prices.

Packed refined seed oils

Product market

18. Previous EC decisions have identified separate markets for PRSO supplied to the retail sector (e.g. supermarkets) and PRSO supplied to the foodservice sector (e.g. restaurants) since there are differences in terms of the level of service typically expected, and the type and size of pack supplied. The parties overlap in the supply of PRSO to the foodservice sector but given the minimal increment ([less than one] per cent), this sector has not been considered further. The rest of our analysis has focussed on the supply of PRSO to the retail sector.

19. The parties submit that the PRSO segment should not be sub-divided by individual seed oil type (soya, sunflower, rapeseed). On the demand side, different seed oil types may be equally suited to a given range of end-use applications. On the

[2] See, for example, Case M.1126 *Cargill/Vandemoortele* [1998], paras.18-19; and Case M.1125 *Cereol/Sofiproteol-Saipol* [1998], para. 20.

supply side, the bottling and packaging assets used by companies operating in the sector can be (and are) used to package multiple oil types.

20. The Commission has, in the past, defined separate markets for private label and branded PRSO. On the demand side, suppliers of branded PRSO do not tend to bid for private label contracts and vice versa. Very few customers responded to our enquiries, but those that did respond do not view branded and private label oils as substitutes. On the supply side, all products are generally identical in terms of composition, packaging, production methods and costs. However, in the parties' experience, there is a substantial difference between the commercial skills required and the costs of supply of branded and private label products. The supply of branded PRSO requires investment in marketing support and sales force effort. This difference in cost is reflected in the substantial price premiums that branded products enjoy over other PRSO.

21. The impact of the joint venture on both the total supply of PRSO and the supply of branded PRSO and private retail label PRSO separately is analysed below.

Geographic market

22. Previous Commission cases have defined a regional market for PRSO relating to the distance of suppliers from customers (up to 300km). The distance at which delivery becomes unviable is likely to vary considerably from case to case. In the UK, supplies to supermarkets and large buying groups that are cross-border involve distances well in excess of 300km. It is worth noting that a 300km radius from East London would capture PRSO competitors based in Northern France and Belgium.

23. The parties submit that PRSO suppliers in other Member States regularly and often successfully bid for UK contracts. The parties provided examples of competitors located in France, the Netherlands and Belgium (abbreviated together with the UK as 'North West Europe') who are currently supplying PRSO into the UK. Some of these suppliers have won business from ADM Pura over the last year. Moreover, in 2003, imports into the UK represented [30-40] per cent of all PRSO sales.

24. The above factors, in particular the substantial volume of imports, support the proposition that UK customers do source from abroad and would therefore be willing to switch to continental suppliers if the price of UK-sourced private label oils increased. Although one customer commented that it is not easy to import branded oils, we received no substantiated evidence to suggest that UK suppliers are not constrained by imported volumes from the above-mentioned Member States (indeed, third parties were generally unconcerned by the transaction).

25. In addition, one third party submitted that prices for PRSO do follow similar trends across Europe and that the geographic scope is European wide, although local packers and processors tend to be more significant players in their own countries.

26. The weight of evidence available to the OFT suggests that competition from the continent constrains UK suppliers and it appears reasonable to consider a frame of reference that is wider than the UK; in this case, the OFT was provided with share data on a North West Europe basis.

HORIZONTAL ISSUES

Shares of supply

Bulk refined seed oils

27. ADM Pura has a [15-25] per cent share of supply of all BRSO seed oil in the EEA. Princes does not supply BRSO and therefore there is no increment resulting from the transaction.

Packed refined seed oils

28. The parties provided estimated shares of supply of PRSO in North West Europe, and these are set out in the table below:

Supplier	Share of sales in North West Europe (per cent)
ADM Pura	[5-15]
EOL	[5-15]
Combined	***[15-25]***
Lesieur	[20-30]
Cargill-Associated Oil Packers (AOP)	[20-30]
Antwerp Oil Refiners (AOR)	[15-25]
KTC (Edibles) Limited	[0-10]
Frylite	[0-10]
Other	[0-10]
Total (MT'000)	[350-450]
HHI post-transaction	2324
HHI increment	[150-250]

Source: ADM estimates

29. Although the Herfindahl-Hirschman Index (HHI) indicates a highly concentrated industry in North West Europe with a significant HHI increment resulting from the transaction, the parties' combined share of supply is relatively low, there will be four apparently significant suppliers post-merger, and third parties were generally unconcerned by the transaction.

30. For completeness, the parties also provided estimated shares of supply of PRSO in the UK. These figures showed that the joint venture would have a combined share of around [55-65] per cent. While maintaining that the relevant geographic scope is at least North West Europe, the parties submit that their large combined share of supply of PRSO in the UK will not raise competition concerns for the following reasons additional to those identified above:

- ADM Pura only supplies private label PRSO while EOL only supplies branded PRSO.[3]
- The bidding process used by the major UK supermarkets to award contracts leads to significant changes in shares of supply over time. This is largely borne out by the data provided, although EOL's UK share has remained fairly stable

[3] ADM Pura supplies [50-60] per cent of private label PRSO in the UK while EOL supplies [85-95] per cent of branded PRSO in the UK.

over time and the relative position of each of the players has remained the same over the last five years.

- ADM Pura's margins have been falling over time as a result of increasing competitive pressure exerted by suppliers in North West Europe. Recent attempts by ADM Pura to raise its prices [ ]
- Over the past 12 months, ADM Pura has not lost any UK PSRO supply contracts to Princes, suggesting that there is little actual competition between the parties at present. This might also suggest that any competition between the parties has not been a factor preventing ADM Pura from raising prices.

31. Although the weight of evidence provides little basis for competition concerns, the OFT did inquire of statements in Princes' internal documents, [ ] On balance, the OFT does not believe that the joint venture would be able to [ ], when the evidence indicates that ADM Pura has not been able to achieve this in the past and there appears to be little actual competition between the parties.

Barriers to entry and expansion

32. Consistent with the above findings on the constraint of imports and the geographic frame of reference, the parties submit that it would be relatively easy for suppliers from other Member States to achieve at least a five per cent share of supply in the UK by winning a PRSO contract for one of the top five national supermarkets. Figures provided by the parties also indicate that many continental PRSO suppliers have spare capacity, implying that it would be relatively easy for these firms to expand their supply.

33. The parties do note, however, that it is unlikely that entirely new entrants in the UK would enter the PRSO segment for retail supply, given the prevailing excess capacity and low margins.

Buyer power

34. The parties submit that the national supermarkets in the UK exercise strong countervailing buyer power. They argue that a supplier such as ADM Pura stands to lose significant volumes if it does not offer a competitive price, particularly given the existence of overcapacity in bottling plants across North West Europe. The parties have provided evidence demonstrating that customers frequently switch supplier and this can result in the loss of large volumes.

35. Furthermore, the parties argue that retailers can exploit portfolios of products offered by a supplier, asking for one product to be reduced in price, or sold on better terms, while threatening to de-list or reduce support for another, more vulnerable product. The joint venture's products are only likely to constitute [10-20] per cent of Princes' sales to UK retailers following the transactions. A retailer would be able to force price reductions in the joint venture's products in return for supporting other products supplied by Princes.

36. Very few customers responded to our enquiries. Those that did respond indicated that they have a degree of buyer power and this will not be lost through the transaction.

NON-HORIZONTAL ISSUES

37. ADM Pura is active in the supply of refined seed oils both upstream (BRSO) and downstream (PRSO). There is no increment to the upstream sector as Princes does not supply BRSO. ADM Pura has agreed to supply all of the joint venture's oil needs. This implies that some of ADM Pura's oil capacity that was available to other PRSO competitors will no longer be available.

38. Two other BRSO suppliers (Cereol/Bunge and Cargill – AOP) are also vertically integrated and between them, the three vertically integrated companies supply [50-60] per cent of BRSO in the EEA. In 2003/4, ADM Pura accounted for [20-30] per cent of ADM's BRSO sales implying that the joint venture will still account for less than half of ADM's BRSO sales. In addition, there are a number of smaller non-vertically integrated competitors in the BRSO segment. Moreover, no third party raised this as a potential issue. It therefore appears unlikely that the transaction would have a material impact on downstream competitors.

39. Princes' internal documents also suggest that one strategic benefit of the joint venture is 'a consolidated supplier position with the full range of bottled products including both branded and retailer branded supplies in both olive and seed oils. [ ] While a greater portfolio may be beneficial to customers as it reduces their transaction costs, this might imply that Princes hopes to raise prices through leverage gained by having a greater portfolio of oils.

40. Princes argues that there is no connection between the way that retailers buy branded and private label products. Moreover, it submits that rather than being able to benefit from portfolio power, the wide portfolio of products could constitute a weakness in its relationship with retailers (e.g. by threats to de-list or reduce support for a more vulnerable product). Third parties did not believe that the joint venture will create any portfolio power that the parties would be able to utilise to their advantage.

B. RETAIL FATS

RELEVANT MARKET

Product market

41. The parties overlap in the supply of fats to the retail sector. Retail fats include yellow and white fats. The latter are predominantly used for cooking, baking, pastry making and shallow frying, while yellow fats are mostly used as spreads. Retail fats can also be categorised according to the underlying fat source, into animal and vegetable fats.

42. The parties submit that these different types of fat constitute a single market to the retail channel. From a demand side perspective, there is a spectrum of white and yellow fats ranging from lard to soft margarine. While it is clear that a product from one end of the spectrum cannot generally be substituted for one at the other end, the parties argue that each type of fat has a range of uses and will tend to overlap with a number of other fat types. This is supported to some extent by market research obtained by the OFT.

43. However, the parties have provided data which shows significant price differences between the different types of fats, and indicates that they do not all follow similar price trends. Third parties generally do not believe that there is substitutability between yellow and white fats, and between animal and vegetable fats, from a demand side perspective.

44. On the supply side, the parties argue that each type of white and yellow fat shares its packing process with certain other types, and not others. They also submit that although UK retailers tend to insist on absolute segregation of animal and vegetable fat production lines, there is no reason why a line could not be switched from one to the other with sufficient interim cleaning. Third parties had mixed views on the ease of switching between animal and vegetable fats.

45. Given the lack of evidence provided by the parties and the fact that third parties do not agree that different types of fat are substitutable, we have analysed the impact of the merger on four separate (but overlapping) segments: yellow fats; white fats; animal fats; and vegetable fats.

Geographic market

46. The parties submit that the relevant geographic market for the supply of fats to the retail channel is at least EEA-wide. In the ADM/Pura case,[4] the Commission found that the supply of white and yellow fats *could* be wider than national and may be EEA-wide since many producers have global brand positioning in Europe and cross-border sourcing is common.

47. The parties submit that fats are typically sold as standardised commodities and are commonly traded on a cost-competitive basis across European borders. There are no barriers to the supply of products between Member States and imports of retail fats from other Member States account for approximately [5-15] per cent of UK sales. Some third parties have commented that they would source from abroad if prices were to increase

48. In the absence of significant third party comment, the weight of evidence tends to suggest an EEA-wide or in any event wider than UK frame of reference, but it is unnecessary to conclude on this issue as no competition concerns arise even on a UK basis.

HORIZONTAL ISSUES

Shares of supply

49. The parties overlap in the supply of white fats only. Estimated shares of supply of the various types of fats are set out in the table below.

[4] Case Comp/M.3044, 3 April 2003. The precise geographic market definition was left open.

Supplier	EEA - Retail Fats	UK - Retail Fats	UK - Animal Fats	UK - Vegetable Fats	UK - White Fats	UK - Yellow Fats
Pura	[0-10]	[0-10]	[5-15]	[0-10]	[10-20]	[0-10]
EOL	[0-10]	[0-10]	[0-10]	[0-10]	[10-20]	[0-10]
Combined	[0-10]	[0-10]	[5-15]	[0-10]	[30-40]	[0-10]
UBUK	-	[40-50]	[0-10]	[40-50]	[0-10]	[40-50]
Unilever	[40-50]	-	-	-	-	-
Dairy Crest	[0-10]	[20-30]	[0-10]	[20-30]	[0-10]	[20-30]
Matthews	[0-10]	[5-15]	[70-80]	[5-15]	[40-50]	[5-15]
Kerry	[0-10]	[5-15]	[0-10]	[5-15]	[0-10]	[5-15]
Fischermanns	[0-10]	[0-10]	[0-10]	[0-10]	[0-10]	[0-10]
Other	[30-40]	[0-10]	[0-10]	[0-10]	[0-10]	[0-10]
Total (MT'000)	[1450-1550]	[250-350]	[5-15]	[250-350]	[15-25]	[250-350]

Source: Pura's estimates of annual capacity
Notes: The Cookeen and Spry Crisp'n'Dry branded white fats businesses that have been acquired by Princes from UBUK are reflected in the shares of supply above. UBUK's shares exclude sales of the white fats businesses sold to Princes. Those sales have been attributed to EOL.

50. The parties' combined share of supply of total retail fats in the EEA and the UK is very small. However, they have a [30-40] per cent share of UK retail sales of white fats and this is likely to increase in the future for two reasons: (i) [ ][5] and (ii) [ ]

51. The parties consider that the relevant geographic market is at least EEA-wide but submit that even on a UK geographic market, their combined share of supply of white fats will not lead to a substantial lessening of competition for the following reasons:

- A number of actual and potential competitors will continue to be present following the transaction.
- The retail white fats segment is in sharp decline in the UK, mainly due to a decline in more traditional baking and for health reasons. The decline in volumes has led the national supermarkets to reduce the shelf space available to white fats in favour of higher volume, more profitable alternatives.
- Following ADM Pura's closure of its white fats production operations and UBUK's decision to exit white fats production in the UK, Nortech's facilities remain as the [main][6] packing facility for white fats in the UK. Both ADM Pura and EOL are in discussions with Nortech to have their white fats packed by Nortech. Absent the transaction, competition would take place between the parties only at the distribution level.
- Given the decline in white fats sales, it is likely that either ADM Pura or EOL would exit the supply of white fats to the retail channel in any event in the next two years if the transaction does not take place.

[5] Princes' wholly owned subsidiary, EOL, acquired UBUK's branded bottled seed oil businesses (Crisp'n'Dry, Olivio, Flora and Mazola) and the business of supplying Cookeen and Spry Crisp'n'Dry vegetable fats. [ ]
[6] Correction to the parties' original submission.

52. In the absence of third party concerns or comment that otherwise contradicts the above propositions, the OFT has no reason to believe that competition concerns arise in relation to retail fats.

Barriers to entry

53. Given the very small shares of supply involved (other than in UK white fats), it is not necessary to conclude on barriers to entry. However, it is notable that since white fats is a declining sector, it would appear unlikely that anyone would seek to enter.

Buyer power

54. The parties' arguments on buyer power in relation to PRSO are also relevant in the context of retail fats. Again, very few retail fats customers responded to our enquiries. Those that did respond indicated that they have a degree of buyer power and this will not be lost through the transaction.

VERTICAL ISSUES

55. This transaction does not raise any vertical issues in relation to the supply of retail fats.

THIRD PARTY VIEWS

56. Third parties were generally unconcerned about the transaction. A low proportion of third parties actually responded (despite extensive efforts by the OFT to contact them) which might be an indication that those in the industry are not concerned. Customers that responded were unconcerned mainly because ADM Pura and Princes do not compete to any significant degree given that one produces branded oils and fats and the other produces private label. Only one retail fats competitor commented that the joint venture could be very strong but did not comment on whether or not it was concerned.

ASSESSMENT

57. The parties overlap in the supply of PRSO and retail white fats.

58. On the evidence available, the relevant geographic frame of reference for the supply of PRSO is wider than the UK. On a North West Europe scope, the parties' combined share of supply is below 25 per cent and there are a number of other significant suppliers. Recent attempts by ADM Pura to increase PRSO prices have been unsuccessful due to customers switching to other European suppliers. Moreover, it appears that the parties are not currently close competitors: no third party has ever played off ADM Pura, which supplies private label oils, and Princes, which supplies branded oils, against the other. Third parties were generally unconcerned. The OFT considers that the loss of this potential rivalry will therefore not lead to a substantial lessening of competition in the supply of PRSO.

59. At a European and UK level, the parties have very small shares of supply of total retail fats, and no third parties raised material concerns about the parties' position

in retail white fats in the UK, the only sector in which the share data suggest a potential issue.

60. 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

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