

## Completed acquisition by British Salt Limited of New Cheshire Salt Works Limited

The OFT's decision on reference under section 22(1) given on 26 May 2005.  
Full text of decision published 24 June 2005.

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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. **British Salt Limited (British Salt)** is a wholly-owned subsidiary of British Salt Holdings LLC. British Salt is based in Middlewich, Cheshire and is active in the production and sale of vacuum salt products.
2. **New Cheshire Salt Works Limited (NCSW)** is a family-owned business based in Northwich, Cheshire. NCSW is also active in the production and sale of vacuum salt products. In 2004, NCSW's UK turnover was [ ].

### TRANSACTION

3. On 24 February 2005, British Salt acquired the entire issued share capital of NCSW. The administrative deadline in this case expires on 27 May 2005.
4. On 30 March 2005, the OFT accepted initial undertakings from British Salt and British Salt Holdings LLC pursuant to section 71 of the Enterprise Act 2002 (the Act).

### JURISDICTION

5. As a result of this transaction British Salt and NCSW have ceased to be distinct. The parties' combined UK shares of supply of each of Pure Dried Vacuum (PDV) salt and compacted salt exceed 25 per cent and the share of supply test in section 23 of the Act is therefore met. The OFT therefore believes that it is or may be the case that a relevant merger situation has been created.

## RELEVANT MARKET

6. The parties overlap in the manufacture and supply of vacuum salt products in the UK. In particular both parties manufacture and supply PDV salt and both produce compacted salt. British Salt is also active in the manufacture and supply of Undried Vacuum (UV) salt, while NCSW also produces and supplies pharmaceutical salt.

### Product market

7. Depending on the raw material and method of production, three types of salt can be identified: rock salt, solar salt and vacuum salt. Most salt produced in the UK is vacuum salt and this is the type of salt that is produced by the parties.
8. There is mixed evidence on the substitutability of the three types of salt identified above. According to the parties, rock salt accounts for around 3 per cent of all salt sales in the UK; most of this is imported into the UK by ESCO; small quantities of rock salt are also produced domestically. Statistics of European salt consumption by end-use application indicate that salt used for road maintenance (de-icing) is predominantly rock salt (70 per cent) and that it has more limited use in other applications. For example, rock salt may be substitutable for PDV salt in the leather tanning industry.
9. According to the consumption statistics, the greatest level of substitution is likely to be between solar salt (also known as sea salt) and vacuum salt for use in the food sector and as table salt.<sup>1</sup> However, the parties noted that solar salt, which is less pure than PDV salt, has only a small place in the food sector and has a bigger role in non-food applications. According to the parties, solar salt accounts for approximately 0.7 per cent of all salt sales in the UK; most of it is imported from Israel, although very small quantities are produced domestically.
10. Rock salt and solar salt were excluded from the scope of reference of the 1986 investigation of the white salt market by the Monopolies and Mergers Commission.<sup>2</sup>
11. Although the European Commission has previously held that the three types of salt are substitutable to a large extent, in this case we have focused the competitive analysis on vacuum salt. This appears to be justified in view of the conflicting evidence on substitutability, the prominent role of vacuum salt in the

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<sup>1</sup> Approximately 30 per cent of all salt used in the UK is used in food applications.

<sup>2</sup> A Report on the supply of White Salt in the United Kingdom by producers of such salt, June 1986, Cmnd 9978. For the purpose of the reference, white salt was defined as solid salt obtained by the evaporation of water from brine.

UK salt sector (it accounts for 96 per cent of total UK salt sales) and the fact that this is the area of product overlap.

12. Depending on the degree of processing, vacuum salt can be divided into the following product categories:
  - (i) UV salt – this contains up to 4 per cent moisture and has the consistency of wet sand. It is commonly used as a source of brine in the chemical industry, e.g. as a raw material for the production of chlorine and caustic soda.
  - (ii) Standard PDV salt – this is produced by further drying of UV salt and has a moisture content of between 0.05 per cent and 0.2 per cent and is free-running. PDV salt is used, inter alia, as table salt and in the food sector; it is also sold for industrial uses. Further sieving and scalping of standard PDV salt produces finer grades of salt known as Fine 50 PDV and Fine 60 PDV. Finer grades of PDV salt are used in the food ingredients business. PDV salt is sold both in bulk and in bags.
  - (iii) Compacted salt – this is produced by compacting standard PDV salt. It comes in the form of granules, tablets or briquettes and is mainly used for water softening applications; it is sold both as a branded and unbranded product.
  - (iv) Pharmaceutical salt – this is produced by further processing and purification of PDV salt; it is used for medical applications.
13. As noted above, the parties overlap in the manufacture and supply of PDV salt and compacted salt respectively; these products are the focus of our competition analysis.
14. According to the parties, British Salt accounts for [55-65] per cent of UV salt sales in the UK. The remainder of sales is attributable to Salt Union; there are no imports of UV salt. This situation is unaffected by the merger because NCSW uses all of the UV salt it produces as feedstock for the production of PDV salt and pharmaceutical salt. UV salt accounts for around [20-25] per cent of the total volume of vacuum salt supplied in the UK. There is no overlap in the production and supply of pharmaceutical salt because only NCSW is active in this segment in the UK. Pharmaceutical salt accounts for [ $<0.5$ ] per cent of the total volume of vacuum salt supplied in the UK. Since the activities of the parties do not overlap in these segments, they will not be considered further.

## Geographic market

15. Salt is a bulky, low value commodity and transport costs are high relative to selling prices. The parties estimate that the cost of transporting a tonne of bagged PDV or compacted salt over a distance of 100 miles is around £14.00 and the cost of transporting bulk PDV salt is around £16.50 (compared to average realised prices per tonne in the region of [ ] for bagged PDV salt, [ ] for compacted salt and [ ] for bulk PDV salt).
16. The three British salt producers, British Salt, Salt Union and NCSW are located in Cheshire. Customer data submitted by the parties indicate that both British Salt and NCSW supply PDV salt and compacted salt products throughout Great Britain. British Salt also supplies salt in Northern Ireland.
17. There is conflicting evidence on the precise level of imports but it is reasonable to assume that imports of salt account for around 10 per cent of total UK salt consumption by volume (i.e. 3 per cent rock salt, 0.7 per cent solar salt and 6 per cent vacuum salt). According to the parties, in 2004 imports of PDV salt accounted for around 6 per cent of total UK PDV salt sales and imports of compacted salt accounted for around 15 per cent of total UK compacted salt sales by volume.<sup>3</sup>
18. The parties' estimates indicate that the average delivered price per tonne of PDV salt and compacted salt is lower on the Continent than in the UK. Third parties agreed that imported product is sometimes competitive in the UK, but competitiveness is also influenced by factors such as exchange rate fluctuations, transport costs (some third parties noted that road haulage may be less expensive than sea freight) and delivery times/frequency.
19. In these circumstances, it is appropriate to take the UK as a starting point for the geographic frame of reference, but to investigate separately the effect of imports by customers and/or via independent UK distributors.

## HORIZONTAL ISSUES

### Unilateral effects

#### Compacted salt

20. In the supply of compacted salt, the merged entity accounted for approximately [25-30] per cent (increment: [5-10] per cent) of UK sales in 2004 and Salt Union

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<sup>3</sup> Import data received from third parties indicates that the total level of imports of compacted salt was around 12 per cent (by volume) in 2004.

accounted for [50-60] per cent. The remainder was made up of imports from ESCO ([5-10] per cent), Akzo ([5-10] per cent) and Salins du Midi ([0-2] per cent).<sup>4</sup>

21. Salt Union purchases some compacted salt from both British Salt and NCSW; this indicates that Salt Union is operating at close to capacity in compacted salt. Therefore, it may not be an effective constraint on the merged entity in this segment, in particular in view of the fact that this is commonly thought to be a growth segment. The parties have stated that an additional compacting unit would require a capital investment of around [ ]; however some third parties were of the opinion that this would not cover the full cost of an additional compacting unit and associated packaging line.
22. NCSW has a significant number of customers (small, medium and large)<sup>5</sup> in this segment and evidence submitted by the parties shows that NCSW's average ex works prices for medium size customers are competitive as compared to those of British Salt. Evidence also indicates that the ex works prices charged by the parties are highly divergent [ ].
23. The merger reduces the number of domestic producers of compacted salt from three to two. Moreover, the leading producer, Salt Union, appears to face capacity constraints in this segment. In these circumstances, unilateral price increases by British Salt post-merger may be profitable since Salt Union would be unable to expand production to absorb customers switching away from British Salt. The majority of third parties contacted by us in this inquiry expressed concerns that compacted salt prices would increase as a result of the merger.
24. If imports are an effective constraint, that is more likely to be in relation to compacted salt than PDV salt because the level of imports is more significant in this segment than in PDV, it is a higher value product and demand for compacted salt is increasing. The role of imports is discussed below.

#### PDV salt

In the supply of PDV salt, the estimated combined UK share of supply (2004) resulting from the merger is [60-65] per cent (increment: [5-10] per cent). Salt Union supplies [30-35] per cent and imports account for the remaining [5-10] per cent (Akzo: [ $<5$ ] per cent, ESCO, [ $<5$ ] per cent).<sup>6</sup>

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<sup>4</sup> Source: the parties' best estimates; see also footnote 3.

<sup>5</sup> Small customers are those who purchased less than 10 tonnes of product annually; medium size customers purchased between 10 and 100 tonnes; large customers are those who purchased more than 100 tonnes.

<sup>6</sup> Source: the parties' best estimates. It is our understanding that Salins du Midi is absent from this segment, although it does import industrial and food grade sea salt.

25. The concentrated nature of the sector may lead to price increases and reduced service levels for customers of PDV salt. This was the expectation expressed by the majority of third parties who responded to our inquiries.
26. British Salt argued that it did not compete for the same customers as NCSW. However, evidence submitted by the parties shows that NCSW's average ex works prices for small and medium size customers are competitive as compared to those of British Salt, and that NCSW has a substantial number of customers who purchase up to 50 tonnes of compacted salt per annum (81, as compared to 135 for British Salt). NCSW does appear to have been less successful in winning business from larger customers. Any loss of competition following the merger may therefore be felt particularly by small and medium size customers.
27. Following the merger, British Salt expects to retain [the majority] of NCSW's customers. These are predominantly small and medium size customers and there is some support in the parties' internal documents for the assumption that, upon contract renewal, customers might be charged higher prices by British Salt. Price variation is prevalent in this segment, [ ].

#### Vacuum salt

28. In respect of sales of all vacuum salt products (i.e. UV salt, PDV salt, compacted salt and pharmaceutical salt), the parties have estimated shares of supply (by volume) as follows: British Salt: [45-55] per cent, NCSW: [5-10] per cent, Salt Union: [35-45] per cent. The remaining [5-10] per cent was made up of imports.

#### **Coordinated effects**

29. Coordinated effects could take the form of tacit (or express) collusion on pricing, tendering, customer allocation and/or geographic or product market sharing.
30. Tacit collusion may arise in circumstances where market participants have the incentive and ability to align their behaviour in the market. In this instance, the homogenous nature of the products, the existence of supply links between the British salt manufacturers and the relative stability and symmetry of cost and shares of supply may facilitate tacit collusion. The merger enhances symmetry of shares of supply, although British Salt was (and remains) strong in PDV salt, while Salt Union is strong in compacted salt. The merger also enhances symmetry of cost and product homogeneity by removing from the market a competitor whose production costs are stated by the parties to have been higher and whose strategic focus has been the manufacture of higher value products.

31. For tacit collusion to be successful, firms must have the ability to sustain the coordinated behaviour over time. In the vacuum salt sector, the limited role of imports and the high barriers to entry (see below) indicate that this could be the case. The merger removes from the market a player whose independent presence might reduce the risk of tacit coordination.
32. While imports could affect the sustainability of coordinated behaviour by British salt producers, this would not be the case if importers were concerned about the risk of retaliatory action by the domestic salt producers.
33. Finally, a successful tacit collusion strategy depends on the ability of firms to detect and punish any deviation. In this sector, supply arrangements are fluid and switching is easy, therefore price cuts could act as a punishment mechanism. The possibility of detecting deviation may be enhanced by the merger, since the acquisition results in the reduction in the number of market participants and leads to increased product homogeneity and greater cost symmetry. Evidence submitted by the parties indicates that there is a wide divergence in ex works prices for the types of salt produced by the parties. This lends support to the theory that prices in this market are opaque, thereby significantly reducing the possibility of coordinated effects. However, there is some evidence that suggests that producers are aware of prices charged by their competitors, so pricing may be more transparent than it first appears, and this could increase the likelihood of collusion and detection of cheating.

#### **Barriers to entry and role of imports**

34. Given the fact that post merger, the two remaining British salt producers will both have significant spare capacity in PDV salt, salt prices have fallen, overall UK demand for salt is declining and natural resources are limited, new entry to UK salt production seems unlikely.
35. However, the threat of geographic expansion and/or increased levels of imports from Continental European producers such as Akzo, ESCO and Salins du Midi could constrain the behaviour of the British salt manufacturers post merger, both by rendering unilateral price increases unprofitable and by making coordinated effects unsustainable. The parties note that these overseas producers have significant spare capacity.
36. We noted above that imports account for around 10 per cent of all salt consumption in the UK; imports account for [5-10] per cent of PDV salt and [10-15] per cent of compacted salt. The parties have argued that imports have increased by 44 per cent (relative to total volume) over the past five years. There is some conflicting evidence on this point and if British salt producers were

constrained merely by the threat of imports the precise level of imports would be immaterial. Moreover, the parties state that prices in the UK have fallen, and in these circumstances, all else being equal, one would not expect to see an increase in imports.

37. Evidence from third parties suggests that larger customers, in particular those who have access to imports due to their location, do obtain price quotes and bids from overseas suppliers such as Akzo, ESCO and Salins du Midi and, in the event of an increase in UK prices, would be able to divert some of their custom to these suppliers. The level of price increase that would trigger this diversion depends on factors such as freight costs (which are currently understood to be high) and the sterling/euro exchange rate. For certain customers, considerations relating to the quality of the imported product may also play a role. However, it should be noted that there is a perception, and some evidence, that strategic local pricing by British producers makes the UK unattractive for overseas suppliers.
38. The parties have stated that customers for whom direct imports are not an option have the possibility of sourcing supplies from independent distributors such as Basic Chemicals, Biachem, Brøste, Ice-Thaw, Peacock Salt, Premier Salt, Salinity, Salt Express and Walkers. However, a number of these companies do not currently import vacuum salt in any significant quantity; some of those that do import vacuum salt have a customer base that is predominantly made up of private individuals who use salt for domestic water softeners (i.e. they do not supply the types of customer that source supplies from NCSW and British Salt). Nevertheless, it seems feasible for these companies to increase their level of imports to some degree should it be profitable to do so, and barriers to entry in distribution are likely to be low. In addition, some of the distributors supply a portfolio of products, which has the effect of reducing the transport cost of salt when it is delivered as part of a mixed load.
39. Responses from some competitors and distributors suggest that the low level of imports is due to the competitiveness of the UK salt sector as a whole. However, other competitors and distributors have indicated that transport costs are a major factor: some noted that maritime freight rates are at a record high and others said that inbound freight is more expensive than outbound freight. It is suggested that this has an overall insulating effect on the UK market. Some respondents also noted that there is a proliferation of longer term contracts which raises barriers to entry and excludes 'spot' competition.
40. In light of the above, there is insufficient evidence to be confident that imports (either direct imports or imports via distributors) would effectively constrain the behaviour of British salt producers to the extent that this would counteract a loss of competition resulting from the acquisition by British Salt of NCSW.

## **Buyer power**

41. Countervailing buyer power appears unlikely itself effectively to constrain the behaviour of the parties post merger. Third party responses indicate that some larger customers are of the opinion that they can exercise some buyer power, and there is evidence that larger customers who have access to imports are able to negotiate lower prices. However, the exercise of buyer power depends on the presence of a number of credible alternative suppliers, which is reduced by this merger. Smaller customers are unlikely to be able to exercise any significant degree of buyer power.

## **THE COUNTERFACTUAL**

42. We considered a number of arguments put forward by the parties related to the counterfactual (i.e. the position of NCSW absent the merger), namely environmental benefits, brine supply issues and viability of the NCSW business. However, our analysis and responses from third parties indicate that, absent the merger, NCSW would be able to operate viably in the medium term; this has therefore been taken as the appropriate counterfactual.

## **THIRD PARTY VIEWS**

43. The majority of customers who responded expressed the view that prices would rise as a result of the merger. Some distributors and competitors were of the view that the UK salt sector is competitive and that the merger does not affect this. However, others were of the opinion that the UK salt sector is insulated from competition by European suppliers and that a reduction in the number of British salt producers would be detrimental to competition.
44. As regards competition in respect of the UK supply of salt for use in the food sector, DEFRA was unconcerned, provided we were satisfied that imports would be a sufficient constraint on British salt producers post merger.

## **ASSESSMENT**

45. The acquisition by British Salt of NCSW reduces from three to two the number of British producers of vacuum salt. The merger combines the first largest and third largest suppliers of PDV salt and the second and third suppliers of compacted salt.
46. In view principally of the increased level of concentration and the homogenous nature of the products, the merger might lead to unilateral and/or coordinated effects, resulting in price increases for customers of PDV salt and compacted salt.

Such price increases may however be unprofitable and/or unsustainable due to the threat of increased levels of imports from Continental Europe, but we have not been provided with sufficient evidence to demonstrate this proposition and the views of third parties in this respect are mixed.

47. If imports, or the threat of imports, are a sufficient constraint, this is most likely to be in relation to larger customers who are located close to ports. Smaller customers, and those who are not located close to import facilities, are more likely to be affected by price increases resulting from the merger. These include the customers mostly likely to have been capable of being supplied by NCSW before the merger and to have been the subject of competition between NCSW and other potential suppliers. It is not clear that distributors would have the incentive and ability to provide these customers with sufficient volumes of imported salt products to counteract the effect of the reduction in the number of national salt producers.
48. Consequently, the OFT believes that it is or may be the case that the merger has resulted or may be expected to result in a substantial lessening of competition within a market or markets in the United Kingdom

#### **UNDERTAKINGS IN LIEU**

49. [ ]

#### **DECISION**

50. This merger will therefore be **referred** to the Competition Commission under section 22(1) of the Act.