
Completed acquisition by SIG plc of Orion Trent Holdings Ltd

The OFT's decision on reference under section 22 given on 11 November 2004

Please note square brackets indicate figures replaced by a range at the request of the parties

PARTIES

1. **SIG Group** (SIG) is a European specialist distributor of construction materials such as insulation, dry lining, fire protection, roofing and ceiling products as well as petrochemicals and offshore manufacturing industries.
2. **Orion Trent Holdings Ltd** (Orion) is a specialist distributor of insulation, fire protection and dry lining materials and a wide range of ancillary and related products. Its UK turnover for the year ending 12 December 2003 was £28.3 million.

TRANSACTION

3. On 4 September 2004 SIG acquired the entire issued share capital of Orion. The transaction was made public on 8 September 2004 and the statutory deadline therefore expires on 7 January 2005. The administrative deadline expires 11 November 2004.

JURISDICTION

4. As a result of this transaction SIG and Orion have ceased to be distinct. The parties overlap in the distribution of construction materials and the share of supply test in section 23 of the Enterprise Act 2002 (the Act) is met in respect of the distribution of structural insulation products in the United Kingdom (the UK). The OFT therefore believes that it is or may be the case that a relevant merger situation has been created.

RELEVANT MARKET

Product market

5. The parties overlap in the distribution of:

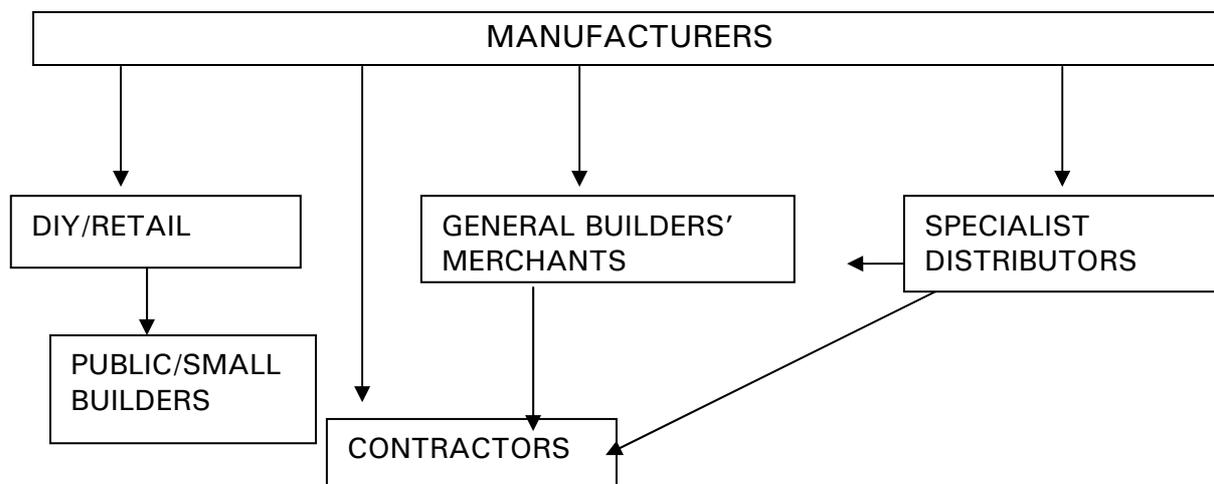
- structural insulation products (which are used in lofts, walls, floors and roofing to insulate sound and heat (excluding industrial applications as Orion is not active in this sector))¹;
- structural fire protection products (which are designed to resist and prevent fire damage);
- dry lining materials (which are used for wall and ceiling construction); and
- ancillary and related products (such as tools, wooden battens and tape for fixing insulation).

Distribution

6. Manufacturers sell these products through four major supply chains: DIY stores, general builders' merchants (GBMs), specialist distributors and direct to contractors. Whilst DIY stores will sell to the public and, in some cases, small jobbing builders, GBMs and specialist distributors sell to the larger building contractors alone. In addition to purchasing from manufacturers GBM's will also source product through specialist distributors, for instance in the event that they are unable to obtain a particular product from the manufacturer in either the quantity or within the timescale they require. The structure of the industry is outlined below.

¹ Industrial applications include usage in heating and ventilation systems and various other industrial process uses generally operating over a wider temperature range than structural applications.

Supply of structural insulation, fire protection and dry lining - industry structure



7. The proportion of the overlap products sourced through each channel of supply differs depending on the product under consideration. Due to the generic nature of dry lining, for example, the expertise of specialist distributors is not required, leading to a higher proportion being sourced by contractors from GBMs. The introduction of unitisation within the product range and the ability to store some products outside, has made it easier for small contractors to trade directly with the manufacturer, according to one third party manufacturer. As specialist distributors, the parties both supply to contractors and GBMs. Pre-merger SIG was already the biggest specialist distributor for the supply of structural insulation products to contractors and GBMs.

Structural insulation products

8. As noted above, the main area of overlap between the parties is in the distribution of structural insulation products where they are engaged in supply to both contractors and GBMs.

- Distribution of insulation products to contractors

9. The parties submit and third parties confirm that specialist distributors compete with GBMs for sales to contractors. Specialist distributors have the advantage of technical knowledge and a wider range of stock and will also split packs and deliver direct to site on a just-in-time basis. However, builders merchants can offer a wider branch network from which product can be collected as required.
10. Manufacturers typically supply contractors direct when the contractor has the ability to store the product, such as in a major housing development or

construction project. Four of the five manufacturers contacted sell only 5-6 per cent of products direct to customers whereas the remaining manufacturer had direct sales accounting for more than 25 per cent of sales. As the evidence on the extent to which manufacturers are able to exert a competitive constraint on distributors is not conclusive, the OFT has focused its analysis on the supply to contractors from specialist distributors and GBMs, whilst noting the potential constraint from manufacturers.

- *Distribution of insulation products to GBMs*

11. Information presented to the OFT suggests that, on average, GBMs appear to purchase about 80 per cent of their insulation products from manufacturers and 20 per cent from specialist distributors. The proportion of manufacturers' sales sold to GBMs direct varies from between 6-50 per cent. GBMs generally have good storage facilities and will take larger deliveries than most contractors, particularly of fast moving products. This would tend to suggest that in supplying to GBMs, manufacturers would be an effective alternative to specialist distributors.

Structural fire protection products

12. As noted above, structural fire protection products include special building materials designed to resist and prevent fire damages, as opposed to active fire protection products, such as sprinklers. The parties submit that plasterboard is the most commonly used product for general fire protection and is stocked by all GBMs. More specialist products may be stocked by some builders' merchants, but are more likely to be stocked by specialist distributors, due to the technical advice required and the infrequency of demand.

Dry lining

13. The parties suggest that dry lining is part of the wider segment of plasterboard, plaster and other related generic materials used for wall and ceiling construction. All these products are stocked by national and independent GBMs. Plasterboard, the largest single product by sales value, is sold by manufacturers to GBMs, specialist distributors and direct to larger contractors.

Ancillary products

14. The vast majority of the ancillary products sold by the parties are sold by other suppliers in the construction sector and have a wide range of uses outside of insulation. The parties share of supply is modest and these products are, therefore, not considered further in this assessment.

Conclusion on product market

15. Noting the comments made above, the appropriate product frame of reference for the assessment of the competitive effects of this merger is taken to be the supply of structural insulation products, fire protection products and dry lining materials by manufacturers, GBMs and specialist distributors. Taking a cautious view, the supply of structural insulation is further segmented into the supply to contractors (by GBMs and specialist distributors) and supply to GBMs (by specialist distributors and manufacturers). Given the lack of concern expressed by third parties, it has not been necessary to consider segmenting the supply of structural fire protection products and dry lining products in any way.

Geographic market

16. The parties submit that for structural fire protection, dry lining and insulation products, the geographic market at the distribution level is the UK. Evidence has been submitted indicating that prices for insulation are similar across the UK, with the largest price variation across the UK standing at 2.4 per cent. The focus of the OFT's analysis is therefore UK wide, although note is taken of potential local issues.

Competition assessment

Structural Insulation

17. Estimates of the overall value of the UK structural insulation market and the relative size of participants vary (due to factors such as the difficulty of splitting structural and industrial applications and obtaining accurate competitor sales data). Given these factors, the parties had some difficulty estimating shares of supply in the sector and third party views on the parties shares of supply differ (with third parties who express a view often quoting a higher combined share of supply for the parties). The table below should be viewed with these caveats in mind.

Table one: shares of supply – distribution of structural insulation

	Total structural insulation distribution %	Supply to contractors/% (by GBMs + Specialist Distributors), excluding direct supplies from manufacturers)	Specialist Dist. only/% (to contractors and GBMs)
SIG	[15-25]	[20-30]	[35-45]
Orion	[less than 5]	[less than 5]	[less than 10]
<i>combined</i>	<i>[20-30]</i>	<i>[25-35]</i>	<i>[40-50]</i>

Source: SIG (and OFT estimates using data supplied by SIG).

18. On the basis of the parties estimates, Encon is SIG's largest competitor followed by CCF / Keyline and the FGF Organisation (FGF). The Encon share of supply (at [10-20] per cent in the total structural insulation sector, [15-25] per cent for supply to contractors and [20-30] per cent for specialist distributors only) is approximately double that of CCF / Keyline. Ten further distributors follow with shares of supply in the various sectors estimated as ranging between 1 per cent and 10 per cent.

19. In terms of the distribution of insulation products to contractors, third party enquiries show that contractors believe that the possibility of switching to alternative sources of supply (to distributors, GBMs and manufacturers) exists and they are generally unconcerned about the transaction. The evidence presented above shows that even ignoring the potential constraint from manufacturers, post merger, a number of other specialist distributors of a reasonable scale (such as Encon and CCF) remain, along with a tail of smaller distributors.

20. In terms of the supply of insulation products to contractors and GBMs, several specialist distributors remain post-merger. In addition, direct supply by the manufacturer, as noted above, is estimated to make up some 80 per cent of the supply of structural insulation products to GBMs. Direct supply by manufacturers to contractors is estimated to make up some 5-10 per cent of supply.

21. A number of third parties commented that SIG is considered to be one of only two national suppliers (Orion itself did not supply nationally). However, the parties note that in their own experience, contracts for national supply are

extremely uncommon and the proportion of sales made in relation to national contracts is [negligible] for both parties.

- Local Issues

22. Orion and SIG both had branches in Bristol, Manchester and Sheffield. The parties submit that the increment in their share of supply in these areas will only be a few per cent higher than the national shares. Local third party customers in the overlap areas suggest that switching suppliers post-merger is still possible, although the loss of Orion was regretted in some cases. In general, third parties in these areas are not concerned.

Fire Protection

23. The parties submit that of the UK supply of structural fire protection products (through GBMs, specialist distributors and manufacturers), the combined entity will have a share of [15-25] per cent (increment: [less than 5] per cent). SIG considers itself the largest distributor in this sector, followed by FGF and Encon. No third parties have raised concerns regarding this sector and one third party suggested that a vast number of sources of fire protection products exist, so switching was not considered a problem. Other third party comments confirm that builders' merchants and specialist distributors compete for fire protection sales to contractors.

Dry Lining

24. Looking at the supply of dry lining (through GBMs, specialist distributors and manufacturers) the combined entity has a UK share of supply of [15-25] per cent, according to the parties (an increment of [less than 5] per cent). SIG considers CCF the largest distributor of dry lining, followed by itself, with Encon in third place. Third party comment suggests that customers have a vast number of sources of dry lining supply and specialist distributors and builders' merchants compete in this sector and no third party concerns have been raised.

Barriers to entry and expansion

25. The parties submit that there are no technical barriers to entering the insulation sector as a distributor. Products can be sourced as needed from manufacturers and at its most basic level only a delivery van and garage are required to set up a distribution business. Examples of new entry over the last few years include Atkins, Keyline, CCF, C P Insulation and FGF.

26. The homogeneous nature of insulation, fire protection and dry lining products leads distributors to compete on quality of service rather than branding of goods. Price and stock availability are also important factors. The parties submit that lack of reputation does not act as a barrier to entry and no loyalty to a particular distributor exists.
27. Third parties have confirmed that barriers to entry are low; that recent entry had occurred; and that in theory a regional distributor could expand to a national level. Building regulations have led to a steady expansion in the structural insulation market, which is forecast to continue.
28. The estimated cost of entry varies across parties, from £100,000-£300,000. Third parties are, however, consistent in noting that only space and money are needed for new entry. Only if a large warehouse was required would extensive planning permission be needed – a process that could be completed within six months. To become fully established, one third party suggests that 12-18 months would be needed. One third party suggests that to begin trading as an independent distributor would be difficult as manufacturers have distribution networks in place and look for a newcomer to have a track record. Another third party, however, suggests that obtaining supplies is easy. For some third parties, the possibility of new entry leads to the transaction raising no competition concerns.
29. A significant proportion of new entry has been by distributors set up by builders' merchants (such as Minster by Jewsons). Alternatively, a builders' merchant can buy a distributor. Third parties have noted that the business principles are the same and the clients, warehouse, transport and staff would be in place.

Buyer power

30. There is little evidence of large customers having buyer power. The Independent Insulation Distributors Association (IIDA) allows small, independent distributors to obtain a more competitive price from the manufacturer. SIG also submitted that it would expect the buyer power of builders' merchants to increase through market consolidation.
31. Some concerns have been raised as to the merged entity's increased buyer power with regard to manufacturers (particularly given the current shortage of insulation products following increased demand due to new building regulations), however, the OFT believes that given the small increment, the impact on SIG's buyer power would be minimal. In the current shortage situation, an allocation process has been put in place by many manufacturers, based upon an average of

previous sales volumes with the manufacturer and this is unlikely to change in the short term.

THIRD PARTY VIEWS

32. Third party views were mixed with the majority believing that adequate competition would remain. However some concern was voiced at the loss of a competitor in the sector and the increased buyer power of SIG. These and further issues raised by third parties are addressed above. Some concern was expressed regarding this being a further example of a 'creeping acquisition' by SIG in the sector.

ASSESSMENT

33. The parties overlap in the distribution of structural insulation products (both to contractors and GBMs), fire protection products and dry lining materials.

34. Post-merger the parties account for [15-25] per cent (increment [less than 5] per cent) in fire protection and for [15-25] per cent (increment [less than 5] per cent) in dry lining. The parties submitted and third parties confirmed that a number of alternative competitors exist and no concerns were raised in relation to these products.

35. In the supply of structural insulation products to contractors, the OFT's investigation shows purchasers generally unconcerned and believing that viable alternative sources of supply remain. In the supply of structural insulation products to GBMs, manufacturers' direct supply is a significant constraint on the parties, moreover, in both sectors of supply (to contractors and GBMs) the merged entity will continue to face significant competition from other specialist insulation distributors, and barriers to entry are low.

36. On the basis of the above, the OFT therefore believes that post merger sufficient competitive constraints will remain on the parties to prevent price increases and/or a reduction in service or quality in the supply of structural insulation products, fire protection products and dry lining materials. Regarding the creeping acquisition comment made by some third parties, the OFT notes that further acquisitions in the sector would need to be carefully considered to ensure a similar level of constraint remains.

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

DECISION

38. This merger will therefore **not be referred** to the Competition Commission under section 22(1) of the Act.