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## Completed acquisition by Lenzing AG of Tencel Holding Ltd

The OFT's decision on reference under section 22 given on 6 September 2004

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

### PARTIES

1. **Lenzing AG (Lenzing)** is headquartered in Lenzing, Austria and is one of the world's leading producers of man-made fibres. Lenzing is active in the manufacture and supply of, among other things, lyocell fibres, which are made from wood pulp and characterized by high wearing comfort and moisture management. Its production capacity accounts for about 40,000 tonnes of lyocell from its plant located in Austria (actual production in 2003 was about 13,500 tonnes). Lenzing claims that its lyocell business has never been profitable. Lenzing imported just 8 tons of lyocell into the UK in 2003 which amounted to less than £10,000 sales value.
2. **Tencel Holding Limited (Tencel)** was part of the international financial group CVC. Its production capacity for lyocell amounts to [70,000-90,000] tonnes and it has production sites in Alabama, USA (actual production for 2003 of [15,000-25,000] tonnes), and Grimsby, UK, (actual production [20,000-30,000] tonnes in 2003). Its total UK turnover is less than £ 70 million.

### TRANSACTION

3. On 4 May 2004, Lenzing took over the entire Tencel group of companies including Tencel. The transaction was notified to the OFT on 9 July 2004 and the administrative timetable expires 6 September 2004. The extended statutory deadline is 1 October 2004. The merger was found to qualify for review in Austria and has been notified to the competent authorities.
4. The parties signed initial undertakings not to integrate further their businesses pursuant to section 71 of the Enterprise Act 2002 (the Act) on 28 July 2004.

## **BACKGROUND**

5. In 2001, the EC Commission (the Commission) prohibited the proposed acquisition by CVC (who owned Acordis, of which Tencel was then a part) of Lenzing AG (Comp/M.2187). The Commission concluded that the relevant product markets at that time were: commodity viscose staple fibres (VSF); spun-dyed viscose staple fibres; viscose staple fibres for tampons; lyocell; and lyocell production and processing technology. It held that the transaction would have strengthened a dominant position in relation to the supply of VSF for tampons and would have created a dominant position in all the remaining relevant product markets. It concluded, *inter alia*, that the merger would create the world's leading supplier of lyocell, with Lenzing accounting for about 25 per cent and Tencel for 75 per cent of total worldwide sales at that time.

## **JURISDICTION**

6. As a result of this transaction Lenzing and Tencel have ceased to be distinct. The parties overlap in the supply of lyocell and the share of supply test in section 23 of the Act is met. The OFT therefore believes that it is or may be the case that a relevant merger situation has been created.

## **RELEVANT MARKET**

7. Lyocell is the generic term for a man-made cellulose fibre produced from wood pulp made by a solvent spinning process in which the fibre is formed by directly dissolving the wood pulp into organic solvents. The parties are both active in the supply of lyocell production and processing technology. Lyocell is characterised by its high wearing comfort and moisture management properties. In the 1980s, Lenzing and Courtaulds plc (subsequently the Tencel business) each obtained a license from Akzo to further develop this technology, which the parties are also licensing to potential lyocell producers.
8. Currently some 65 per cent of lyocell is used in textile applications such as clothing, home textiles (e.g. bed linen) and technical textiles such as tyre cord; while 35 per cent of lyocell is used in non-woven applications for example wipes, medical gauze and liquid filters including tea bags. The production of woven and non-woven products is slightly different and switching between the two requires some plant down-time.
9. Lenzing markets its lyocell fibres under the brand name 'Lyocell by Lenzing' and 'Tencel' is the brand name for the lyocell fibres produced by Tencel.

## Product market

10. The Commission in its correlation analysis in the market investigation in CVC/Lenzing found that other fibres such as VSF, cotton and polyester were not substitutable for lyocell. It found in particular that lyocell had specific product characteristics, such as its high tenacity in both wet and dry states and low shrinkage in water which were particularly favoured by certain customers. However, the parties have argued that, in the time since the Commission's investigation, for the majority of lyocell applications, fibres such as cotton, viscose, polypropylene or micro polyester could be and have been used as alternatives, which is supported by some third party evidence received by the OFT. The parties pointed out that whereas lyocell was originally developed as a 'premium-fibre' in textiles, it has from 2000 onwards increasingly been used for non-woven applications such as duvet-fillings, wipes and tea bags. Lyocell used in non-wovens as opposed to textiles is sometimes of a different quality. There appears to be a wider choice of fibres in non-wovens which could explain the lower lyocell prices for non-wovens as compared to textiles.
11. There does not appear to be any supply-side substitutability between lyocell and other fibres given the different production process involved and the capital investment which would be required to acquire the necessary technology.
12. The parties argued that they are unaware of any use for which lyocell is essential and for which no reasonable substitute exists. For both textiles and non-wovens, manufacturers have, they contend, a wide choice of natural, synthetic and cellulosic fibres. As such, customers will only use lyocell if the price is competitive and would switch to other fibres in response to short term relative price changes. To support their case the parties have also pointed out that since the Commission's decision the makers of luxury jeans – which were found to be one of the most prominent applications for lyocell at the time (paragraph 56 of Commission's decision) – have all switched to other substitute products and no longer use lyocell.
13. The majority of third party respondents supported this view. In any event, for the reasons explained below, since this merger is not considered to result in a lessening of competition that is substantial within any market or markets in the UK for goods or services, it is not necessary for the OFT to conclude on exact delineation of the relevant product market. Neither is it necessary for the OFT to determine whether there continues to be a distinct market for the supply of lyocell production and processing technology as indicated in the Commission's decision. The parties have pointed out that while prepared to licence their technology they have never received a request to do so. Moreover, Hanil, a

Korean fibre manufacturer, has begun lyocell production without any need for the parties' technology. No third parties raised this as an issue and it will therefore not be considered any further.

### **Geographic market**

14. The Commission in CVC/Lenzing left open the question of geographic scope for the manufacture and supply of lyocell (whether EEA or Worldwide) as this did not make a material difference to the assessment. However, as with the product market, defining the geographic market is not crucial to the competition assessment.

## **HORIZONTAL ISSUES**

### **Market shares**

15. The data available to the OFT indicates that in 2003 at a European level Tencel had a share of around [65-75 per cent] of the supply of lyocell and Lenzing [25-35 per cent] (shares are similar for volume and value). Worldwide, Tencel had a [70-80 per cent] share of supply, Lenzing [15-25 per cent] and the Korean producer Hanil [5-10 per cent] (based on volume and value). Comparing these figures with production capacity indicates utilisation rates of [55-65 per cent] for Tencel and [30-40 per cent] for Lenzing.
16. However, the parties have submitted that pre-merger they did not directly compete for customers in the UK. The available evidence confirms that the parties did not compete substantially in the UK. In 2003 Lenzing has imported fewer than 10 tonnes of lyocell into the UK (representing about 1 per cent of UK supply), which was also cut differently from Tencel lyocell and could therefore not be used for many of the same applications. In the four years 1999-2003, Lenzing sold fewer than 45 tonnes of lyocell in total into the UK and the majority of this was sub-standard lyocell sold into the UK on a 'spot' basis as filling for duvets/pillows.

### **Barriers to entry and expansion**

17. The merged entity holds most of the patents for lyocell but the parties submit that these patents will expire in 2006. The available evidence indicates that a high level of capital investment would be necessary successfully to enter the lyocell business. That said, the Korean lyocell producer Hanil has recently entered the market and currently holds a market share of [5-10 per cent] worldwide. There is also some evidence for potential entry by Indian and Chinese lyocell producers who already operate pilot plants.

## **Buyer power**

18. The existence of negotiating strength on the part of buyers would depend on the availability of alternative fibres, which may vary according to the end use of lyocell. In certain applications such as non-wovens there may be a range of alternative fibres but evidence suggests that there may be fewer for certain textile fibres. This would tend to be consistent with the pricing information which shows that lyocell for non-woven applications is priced below that supplied for textile use (assuming no difference in quality). We have received some evidence that customers have negotiation strength but this appears to come more from the threat to switch to other fibres rather than any ability to switch between the parties.

## **THIRD PARTY VIEWS**

19. Numerous third parties were contacted by the OFT but not many responded. The majority of those that did respond were not concerned about the merger due to the availability of substitute fibres for lyocell. Although some third parties did view the properties of lyocell as unique, a majority did not expect this transaction to affect competition adversely within the UK. However, one UK customer did assert that the merger would lead to a reduction in its choice of lyocell supplier. But the OFT's investigation suggests that this customer has a particular requirement that can not be met by Lenzing. This is because while the lyocell supplied by Tencel and Lenzing is chemically the same, it is cut and produced in different ways. Furthermore Lenzing submitted evidence to the OFT suggesting that the capital investment required to enable it to supply this customer would be considerable and could not be justified given the unpredictability of this demand.

## **ASSESSMENT**

20. The merged entity would be the major supplier of lyocell and lyocell processing and production technology worldwide. However, the question at hand is whether the merger has resulted, or may be expected to result, in a lessening of competition that is substantial within any market or markets in the UK. Lenzing has not been a substantial supplier to, or competitor in, the UK; nor are there grounds to believe that it would become one. In addition the third party investigation carried out by the OFT revealed that for the majority of customers within the UK a range of fibres (depending on the application) appear to be available and lyocell is only used as long as it is competitively priced.

21. 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**

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