
Anticipated acquisition by J.M. Huber Corporation of CP Kelco APS

The OFT's decision on reference under section 96 given on 22 September 2004

PARTIES

1. **J.M. Huber Corporation** (Huber) is a diversified US corporation active in a broad range of commercial activity including specialty chemicals, forestry and energy. **CP Kelco APS** (Kelco) is a Danish company specialising in the manufacture of additives used in the food, industrial, personal care and pharmaceutical sectors.

TRANSACTION

2. Huber already owns 28.6 per cent of the voting shares and 22.9 per cent of the non-voting shares in Kelco. Agreement was reached in July 2004 for Huber to acquire the remainder of the share capital in Kelco. Completion is subject to regulatory approval from the UK, US and German competition authorities. The target date is 30 September 2004.
3. Huber notified its proposed acquisition of Kelco by means of a Merger Notice under Section 96 of the Enterprise Act 2002 (the Act). The statutory deadline is 22 September 2004.

JURISDICTION

4. As a result of this transaction, Huber and Kelco will cease to be distinct. The parties overlap in the supply of hydrocolloids (see paragraph 5) 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 arrangements are in progress or in contemplation which, if carried into effect, will result in the creation of a relevant merger situation.

RELEVANT MARKET

Product market

5. Hydrocolloids (also known as 'water soluble polymers') are substances that dissolve, disperse or swell in water. Hydrocolloids react with the water to form gels, pastes and emulsions. They also act as stabilisers, flocculents, coagulants, film formers, humectants, binders and lubricants. They are used in a wide range of applications, including paper production, mineral processing, detergents, textiles, foods, personal care products, pharmaceuticals, drilling fluids (for oilfields etc) and surface coatings.
6. Huber submits that there are approximately 25 different types of hydrocolloid and that these different types fall into three principal categories: natural, semi-synthetic and synthetic.
7. Huber manufactures only one specific hydrocolloid, carboxymethylcellulose (CMC), a substance which is also known as 'cellulose gum'. CMC is classified as a semi-synthetic hydrocolloid.
8. Kelco manufactures three types of hydrocolloid: biogums (primarily xanthan gum), pectin and carrageenan – all of which are classified as natural hydrocolloids.
9. Huber submits that each of CMC, xanthan gum, pectin and carrageenan vary in terms of their function and properties – although different types of hydrocolloid can be used in combination for certain applications. Third parties have confirmed the distinct characteristics of each of the four polymers, the limited scope for substituting between them and the fact that they are more frequently complements than they are competing substitutes for most purposes.
10. According to Huber, the manufacturing processes for (1) CMC, (2) biogums, (3) pectin and (4) carrageenan also differ significantly. Production equipment designed to produce one of the four polymers cannot be readily converted in order to produce any of the other polymers. It therefore seems reasonable to assume that specialist plant is required in the production of the different types of hydrocolloid and that the scope for supply-side substitution is limited.
11. There are three main sectors in which the specific hydrocolloid produced by Huber is or can be used in conjunction with one or more of the specific hydrocolloids produced by Kelco. These sectoral areas are (1) oil field drilling, (2) food and (3) personal & dental care.

12. Huber submits (and third parties have confirmed) that in each of these applications, the different properties of the hydrocolloids manufactured by the parties make them suited for different functions within the overall application. Two respondents in the food sector pointed to possibilities for substitution between CMC and pectin in the production of certain beverages, for the purposes such as enhanced viscosity and cloud stabilisation. However, these same two respondents also stated that they had no concerns regarding the merger.

Geographic market

13. Huber proposes that the geographic scope for the supply of hydrocolloids is global and that purchasers source these polymers from around the world.
14. It also submits that hydrocolloid manufacturers typically have large plants in a few countries from which they supply a range of polymers to customers throughout the world. Huber itself supplies all of its customers (both its own and Kelco's customer lists indicate that business is conducted on a worldwide basis) from its three plants in Finland, Sweden and the Netherlands.
15. Comments from third parties support the view the geographic frame of reference is wide, possibly global.
16. The responses received from third parties indicated a lack of horizontal overlap between the merging parties in respect of the hydrocolloids they produce. The view taken by all the respondents in each of the three sectors discussed in paragraph 11 is that the parties' respective products are primarily complementary rather than substitutable.
17. Taking due account of the absence of horizontal overlap, no increment in the share of supply of the CMC produced by Huber on the one hand, and the supply of biogums, pectins and carrageenan produced by Kelco on the other hand, is attributable to the proposed merger. It is therefore unnecessary to reach any firm conclusion on how the market should be delimited in terms of the product or the geographic frame of reference.

COMPETITION ANALYSIS

Conglomerate Issues

18. Third parties were consulted in each of the three sectoral areas where Huber's CMC and Kelco's biogums, pectin and carrageenan can be used as hydrocolloids in combination (see paragraph 11). One respondent, a customer who buys hydrocolloids for use in personal care/dental applications, expressed concerns over

the merged entity's range of complementary products. No concerns of this or of any other kind were expressed by any of the other respondents.

19. Huber's estimates of the parties' combined share of supply of hydrocolloids which can be used in a complementary mix in the relevant three sectors are set out in Table 1.

Table 1 – Merging parties' combined shares of supply of the four types of hydrocolloid according to category of end use (percentages)

	Oil field drilling			Food			Personal care/dental		
	UK	EU	World	UK	EU	World	UK	EU	World
Huber	1-5	15-25	5-15	1-5	1-5	1-5	5-15	5-15	5-15
Kelco	15-25	5-15	15-25	1-5	1-5	1-5	20-30	5-15	5-15
Combined	20-25	25-35	25-35	1-5	5-10	5-10	25-35	15-25	15-25

Source: Huber - Data has been ranged. Huber submits that the estimates of market share are maxima and that its own market share is either below or at the levels indicated.

20. Some consideration is clearly warranted as to the possibility for potential conglomerate effects. However, there would appear to be no obvious concerns in view of the wide extent of the geographic frame of reference and taking due account of the fact that the figures are meaningful only as collated totals of the shares of supply of four distinct hydrocolloids. Post merger, buyers in all three sectors will continue to be able to make choices on competitive terms between each of the four hydrocolloids produced by the merged entity and equivalent products manufactured by its competitors in order to obtain the required complementary mix of polymers for any particular application.

Barriers to entry and expansion

21. The parties estimate that new plant would cost in the order of £15-25m. There is evidence of new entry into the supply of hydrocolloids in recent years. Deoson, for example, has built a factory producing xanthan gum in China, from which it supplies oilfield drilling companies worldwide. Citrico has built a pectin production facility in Germany from which it supplies, amongst others, customers in the UK. Moreover, Huber has made no commercial plans in recent years to produce hydrocolloids of the type manufactured by Kelco (or vice versa). Consequently the proposed merger does not amount to a loss of potential competition.

Buyer power

22. Buyers of hydrocolloids are principally large or multi-national purchasers who appear able to switch suppliers and to exert countervailing buyer power.

VERTICAL ISSUES

23. There are no vertical issues. Neither Huber nor Kelco are vertically integrated with any supplier or purchaser of hydrocolloids. The average length of contract for the supply of hydrocolloids is estimated at around twelve months.

THIRD PARTY VIEWS

24. Only one expression of concern was received – although the company concerned (based outside the UK) indicated that switching between hydrocolloids occurred 'mostly due to special application profiles'. All third parties agreed with Huber's submission that the hydrocolloids in question were complementary products.

ASSESSMENT

25. This pre-notified merger combines the parties' production and supply of hydrocolloids: specifically Huber's supply of CMC and Kelco's supply of biogums, pectin and carrageenan. Responses from third parties have confirmed that these products are not readily substitutable except for a few marginal applications. In effect, the merger does not give rise to horizontal overlap. Rather the merging parties' respective hydrocolloid products are widely held to be complementary.
26. 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

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