COMPETITION TRIBUNAL
REPUBLIC OF SOUTH AFRICA

Case no.: 57/LM/Oct03

In the large merger between:

Sasol Oil (Pty) Ltd

and

Exel Petroleum (Pty) Ltd

Reasons

Introduction

The Tribunal approved the proposed transaction between Sasol Oil (Pty) Ltd and Exel Petroleum (Pty) Ltd on 10 December 2003. The reasons for this decision follow.

The transaction

Sasol Oil (Pty) Ltd ("Sasol Oil"), which is primarily a producer of petroleum products, acquired the former Powerlib Group's 36% shareholding in Exel Petroleum (Pty) Ltd ("Exel"), a retailer of petroleum products. Sasol, through its wholly owned subsidiary Naledi Industry Company (Pty) Ltd, already holds a 22,5% interest in Exel's holding company Naledi Petroleum Holdings (Pty) Ltd ("NPH").

Sasol Oil was also granted a call option on the shares sold by the Sizanani Trust, consisting of:

?? 8% NPH shares from Autoworkers Pension Fund;
?? 5% NPH shares from Autoworkers Provident Fund;
?? 3,5% NPH shares from South African Black Women's Investment Holdings (Pty) Ltd;
?? 9,5% NPH shares from Nozweni (Pty) Ltd

Sinzanani Trust agreed to transfer its NPH shares to Sasol Oil after the termination of the main supply agreements. This is subject to a restriction whereby Sasol Oil must use any dividends received in respect of the shares for the furtherance of historically disadvantaged businesses.

On completion of the transaction NPH will become a wholly owned subsidiary of Sasol Oil.

Parties

Sasol Oil is a wholly owned subsidiary of Sasol Limited, the ultimate holding company of the Sasol Group, which is listed on the JSE Securities Exchange. Sasol Oil is responsible for Sasol's crude refining activities and for the marketing of all liquid and gaseous fuels (excluding pipeline gas) together with lubricants manufactured by Sasol.

Exel is the wholly owned subsidiary of NPH, which has no other business interests. Exel is a fuel marketing company, which was established by historically disadvantaged South African investors with the assistance of Sasol in 1997 to foster the empowerment of historically disadvantaged persons in the petroleum industry.

Rationale for the transaction

The oil companies, BP, Shell, Caltex, Engen, Total, Exel, Tepco and Afric Oil are currently parties to Main Supply Agreements ("MSA's") and Blue Pump Agreements ("BPA's").

The salient features of the MSA are that the oil companies would purchase Sasol's production of petroleum products up to certain maximum volumes from defined permitted sources of supply and Sasol may not market petroleum products except for certain exceptions set out in the preamble of the MSA.

The BPA's are directly linked to the MSA'S. In terms of these agreements between Sasol and the oil companies, Sasol may market petrol only through roster sites (i.e. service stations untied to any oil company in terms of the so-called Government sponsored "rationalisation plan") and through Sasol Blue Pump sales at service stations of the other oil companies in the Blue Pump Area.

These agreements will terminate on 31 December 2003. This means that the commercial restriction on Sasol marketing its own petroleum products will fall away. Sasol as producer of liquid fuels needs to integrate downstream into the retail market to compete with its main vertically integrated rivals. From Exel's perspective it needs to vertically integrate upstream to gain access to the upstream petroleum market in order to compete effectively with its rivals.

Sasol is also a signatory to the Charter for the Empowerment of historically disadvantaged businesses in the liquid petroleum industry, which requires that at least 25% of ownership and control of all facets of the industry must be owned by historically disadvantaged South Africans. In order for Sasol to comply with the Charter requirements it is necessary to integrate Exel into the larger Sasol Oil thereby fulfilling its commitments.

According to Exel this transaction would contribute to a more significant and sustainable growth in black economic empowerment. However, should Sasol enter the retail market as a competitor of Exel it would have a negative impact on Exel's sustainability in the market.

The fuel industry in South Africa

The liquid fuel industry is highly regulated with price control and import control being the cornerstones of the regulatory dispensation. The petrol price is regulated whilst a maximum wholesale price is set for diesel and a maximum retail price is set for unpackaged illuminating paraffin. This does not seem likely to change in the near future.[1]

Competition Analysis

The petroleum supply chain can be divided into upstream and downstream activities. The upstream activities consist of oil exploration, extraction and transportation. The downstream activities consist of refining, marketing and distribution.

This is a horizontal as well as vertical merger. Sasol is involved in the refining of petroleum products in the upstream market as well as in the marketing and distribution of liquid fuels while Exel is active in the downstream market, in the marketing and distribution of the petroleum products and does not have any refining capacity.

<u>The upstream market</u>

Sasol is involved in the production and refining of petroleum products such as diesel, petrol, base oils, fuel oil, bitumen, liquid petroleum gas ("LPG"), aviation gasoline and kerosene.

In South Africa there are four crude oil refineries, Calref owned by Caltex, Enref owned by Engen, Sapref a joint venture between Shell and BP and PetroSA owned by Government, and two synthetic fuel refineries, Synfuels owned by Sasol and Natref a joint venture between Sasol and Total.

[1] In fact, during the hearing the parties pointed out that the industry was being re-regulated rather than de-regulated.

Of these only Synfuels and Natref are located inland. Calref and PetroSA are located in Cape Town, supplying the Western and Eastern Cape, while Enref and Sapref are located in Durban, supplying the Kwa-Zulu Natal regions. According to the parties this situation allows for logistical optimization between the refineries, as the base products are "swopped" between companies in order to provide product to customers in each surrounding area.[2] The respective oil companies then add their own additives at a later stage in the supply chain.

Table 1 shows the percentage market shares per petroleum product (refinery production volumes) of each of the oil companies:

Product	Calref %	Enref %	PetroSA %	Natref[3] %	Sapref[4] %	Synfuels %	Natref & Sasol combined[5] %
Petrol	12.5	14	8.4	13.30	18.30	33.40	**41.86**
Diesel	14.58	18.60	5.52	16.30	28.90	16.10	26.53
Kerosene	15.63	17.33	4.27	27.94	22.72	12.18	**30.05**
LPG	11.75	10.65	15.04	4.72	23.71	34.14	**37.00**
Fuel Oils	18.70	34.10	0.90	2.60	40.40	3.30	5.00
Aviation Fuels	0	26.70	0	0	73.30	0	0
Base Oils	0	46.90	0	0	53.10	0	0
Bitumen	3.8	31.80	0	13.40	14.30	36.70	45.31

From the above table it is clear that Sasol is dominant in the markets for the production of petrol, kerosene, bitumen and LPG, a position, which also raised competition concerns from its competitors. These mainly concerned foreclosure by raising rival's costs.

Sasol is the major inland supplier of refined fuel to most of its rivals via the MSA. When the agreement is terminated in January 2004 Sasol, the dominant manufacturer of refined petroleum inland, would also become a downstream competitor. It will then become vertically integrated. Sasol's competitors, who are also vertically integrated, are however dependent on Sasol to furnish them with some product inland because they are not able to meet their own needs fully via the pipeline from their coastal refineries. In light of this they are concerned that Sasol, being in a dominant position inland, would post the merger raise their input costs by raising its prices.

[2] These agreements are known as product exchange agreements.
[3] This market share should be distributed between Total and Sasol and is not the exclusive market share attributable to Sasol Oil.
[4] The Sapref refinery is split between Shell and BP on a 50:50 basis.
[5] These combined values are the combined production volumes of the Natref refinery and Sasol's Synfuels refinery.

The merging parties did not agree with the concerns raised, claiming that it would not be in Sasol's interest to "self-deal"[6] or to raise input costs because of the presence of its vertically integrated rivals, which could reciprocate at any time by withholding hospitality and exchange facilities. They explained that since "swopping" arrangements existed between the refineries, it would not be in Sasol's favour to foreclose product inland to its competitors because they could retaliate by refusing Sasol product in the coastal areas where it does not have refineries. Moreover, Exel is a very small player in the downstream retail product markets as can be seen from the analysis of the downstream market. In fact, its market shares are below 10% in all the markets while Sasol's downstream market shares are 4.5% in petrol, 0.8% in diesel. The merged entity would, according to Sasol, only take up 14-15% of Sasol's total production the rest would be sold inland to its rivals.

It is thus highly unlikely that Sasol, who intends growing its downstream coastal market share, would compromise its vulnerable coastal position in any way.

We therefore find that competition will not be substantially lessened or prevented in the upstream market for the refining of petroleum products.

Downstream market

The downstream market entails the marketing and distribution of liquid fuels to the commercial and wholesale segment and the retail segment of the market. The geographic market for the retail segment is regional while for the commercial and wholesale segment it is national.

Both merging parties sell petrol, diesel and fuel oils to the commercial segments, which include customers such as parastatals, commercial/passenger transport, agriculture, manufacturing, construction, mining, local communities and resellers. Both parties also sell petrol and diesel to the retail segment.

Commercial segment

Table 2 shows the merged entity's three largest competitors in each province, expressed as a percentage market share, in the commercial petrol market:

	Afric Oil	**BP**	**Caltex**	**Engen**	**Shell**	**TSA**	**Merged Entity**
Western Cape		17.3		23.7	15.4	23.2	14.9
Eastern Cape				20.5	18.6	34.6	7.1
Northern		36.6			19.5	21.6	4.5

[6] Confining its purchases of upstream product to its downstream division only.

	Afric Oil	BP	Caltex	Engen	Shell	TSA	Merged Entity
Cape							
Free State				38.6	19.1	28.0	6.9
KZN		15.0		31.8		32.7	3.3
North West Province		22.7		28.5		19.6	7.9
Gauteng		20.4		22.4		23.7	15.9
Mpumalanga				18.9	18.5	36.0	7.2
Limpopo		14.5			14.4	44.3	10.2

In none of the provinces will the merged entity be the largest player. The market shares indicate that Engen, Total and BP are the largest players in most of the provinces.

Table 3 shows the percentage market share of the three largest competitors of the merged entity in each province in the commercial diesel market:

	Afric Oil	BP	Caltex	Engen	Shell	TSA	Merged Entity
Western Cape			25.2	19.4	19.0		5.5
Eastern Cape				28.7	21.0	16.7	7.2
Northern Cape			21.1		16.5	26.8	5.6
Free State			27.1	32.0	18.1		3.8
KZN				29.4	22.3	17.4	2.2
North West Province		15.3	15.1	27.8			16.5
Gauteng		13.8		22.4	22.2		8.1
Mpumalanga			14.4	28.2	24.8		12.0
Limpopo		19.5	20.6		23.3		7.5

In only one of the provinces, North West Province, will the merged entity be one of the top four competitors. The merged entity will be the second largest player with a market share of 16.5% and the largest player, Engen, will hold a market share of 27.8% and the third largest player, BP, 15.3%. The change in the HHI post the merger will only result in an increase of 3.28 points, thus far below the 50 points said to have an adverse competitive effect in a concentrated market. It is thus clear that the merger would not result in a significant change in concentration in this market.

In the commercial market for fuel oils the parties have submitted that their combined market share is 54%. However, this constitutes only inland market sales and does not reflect coastal or include bunker fuel oil sales that are made to ships in coastal regions. The market shares may therefore be diluted further since Engen, Shell and BP have huge production volumes in this market.

Retail segment

The merged parties sell petrol and diesel to the retail market segment. The market shares for the retail market segment at the national market level are provided in table 4:

Products	**Afric Oil**	**BP**	**Caltex**	**Engen**	**Shell**	**TSA**	**Merged entity**
Petrol	-	16.2	17.8	27.6	18.3	12.9	7.2
Diesel	-	17.4	14.8	27.8	20.8	15.0	4.2

The merged entity would have an insignificant market share at the national level. In the narrower geographic markets, i.e. magisterial districts, the Commission found that Exel had a stronger presence in certain local markets but that the merger would not result in a significant change in concentration levels. The reason for this is that Sasol Oil's presence in the retail markets is limited to its blue pump agreements and a few service stations around the country.

We therefore agree with the Commission that the merger would not prevent or lessen competition substantially in any of the relevant markets.

Public interest issues

The parties envisage that the merger will lead to a few adjustments in respect of senior managers. However, they foresee no retrenchments arising from the integration process itself.

____________ 3 February 2004

D Lewis **Date**

Concurring: N Manoim, P Maponya