

In The Large Merger Between:

Rainbow Farms (Pty) Ltd

And

Vector Logistics (Pty) Ltd

Reasons for Decision

Approval

1. On 27 October 2004 the Competition Tribunal issued a Merger Clearance Certificate approving the transaction between Rainbow Farms (Pty) Ltd and Vector Logistics (Pty) Ltd. The reasons for this decision follow.

The Parties

2. The primary acquiring firm is Rainbow Farms (Pty) Ltd ("Rainbow Farms"), a wholly owned subsidiary of Rainbow Chicken Limited, a public company listed on the JSE Securities Exchange South Africa. Industrial Partnership Investments Limited ("IPIL") currently holds 64,6% of the issued share capital in Rainbow Chicken Ltd while the remaining 35,4% is held by members of the public and Rainbow Chicken employees. IPIL is in turn a wholly owned subsidiary of Remgro Limited ("Remgro"), which ultimately controls Rainbow Chicken Ltd and Rainbow Farms. Remgro is a public company listed on the JSE Securities Exchange South Africa. No one shareholder either directly or indirectly controls Remgro and its largest shareholders,¹ holding in excess of 5% of the issued share capital are: Public Investment Commissioners 12,97%), Old Mutual Life Assurance Company (8,78%) and Sanlam (5,66%).
3. The primary target firm is Vector Logistics (Pty) Ltd ("Vector"). Vector is controlled by AVI Limited ("AVI") (90%). Dyambu Investment Nominees (Pty) Ltd ("Dyambu") and Ntshonalanga Consortium Investment Nominees (Pty) Ltd ("Ntshonalanga") hold the remaining 10% of shares in equal parts. AVI is a public company listed on the JSE Securities Exchange South Africa. No one shareholder controls AVI.
4. Vector controls Vector Logistics Limited as well holds a 49% stake in IsoVec (Pty) Ltd ("Isovec") an empowerment joint venture between Vector and Isolami Investments Holdings.

¹ As at 31 March 2004

The transaction

5. The transaction involves the acquisition by Rainbow Farms of 100% of the issued share capital in Vector from AVI and Dyambu and Ntshonalanga. On completion of the sale of shares transaction, Rainbow will control 100% of the issued share capital of Vector. According to the parties, the acquisition of Vector will allow Rainbow to gain control of the route to market and customer centered initiatives, thereby ensuring Rainbow's long-term survival.

The Parties' Activities

6. Rainbow Farm is a fully integrated broiler producer that breeds and rears its own poultry, processes the chicken, and markets fresh, frozen, value added and further processed chicken nationally and internationally. Rainbow sells these products under brands such as Farmer Brown, Rainbow and Bonny to local retailers and wholesalers of food services and through export channels. Rainbow Farm also produces animal food under the Epol brand.
7. Remgro is an investment holding company mainly involved in the management of investments in sectors such as tobacco products, banking and financial services, life insurance, medical services, mining, engineering and motor components, petroleum products, food, wine and spirit.
8. Vector provides specialist logistic services to the food and food-related industries across the retail, wholesale and food service sectors. Vector also provides services such as warehousing, selling, order processing, delivery, merchandising and field marketing, credit management and administration.
9. Iovec focuses on sales, marketing and distribution within the food industry servicing institutional outlets and the mining industry.
10. While there is not horizontal overlap in the activities of the parties, Rainbow and Vector are in a vertical relationship with each other as Vector provides logistics and distribution services to Rainbow.

The relevant markets

11. As stated above, Rainbow is a fully integrated broiler producer and breeds and rears poultry, processes chicken, and markets fresh, frozen, value added and further processed chicken. Rainbow therefore competes with other producers of fresh, frozen and processed chicken products as well as other food producers in the broader market for fresh, frozen and processed food. Rainbow also supplies retail, wholesale and food service customers in the South African market with fresh and frozen chicken products. According to the merging parties Rainbow competes in numerous market segments with different brands and other food types that meet the specific needs and requirements of consumers. The Commission has defined the relevant upstream market as the national market for the producing and processing of poultry products, and for the purpose of this analysis we will accept that definition, which is narrower than that suggested by the merging parties.
12. Vector is involved in the market for the provision of general contract logistic services to *inter alia* the food and food-related industries across the retail, wholesale and food service sectors, throughout South Africa. Vector is able to provide a wide range of transport services

including frozen, chilled and ambient temperature zones. At the narrowest level, the downstream product market can be defined as the market for the provision of contract logistic services to producers of fresh, frozen and processed food products, nationally.

Impact on competition

13. Vector acts as a *del credere*² agent for Rainbow and distributes Rainbow branded products to customers in the local retail, wholesale, food service and export channels with two of the three Rainbow brands – “Farmer Brown” and “Rainbow”.³ Effectively, the transaction formalises the current vertical arrangement between Rainbow and its distributor in regard to the distribution of Rainbow branded chicken products. Vector will continue to service all of its current customers outside the Rainbow Group.
14. Both the upstream and downstream market are fragmented with a number of participants. While Rainbow has the largest market share in the market for the supply of fresh, frozen and processed chicken products in South Africa, its share of the broader market for the supply of fresh, frozen and processed food products is very small.
15. Vector is a relatively small player in the downstream market segment for the provision of contract logistic services to producers of fresh, frozen and processed food products. This market is highly fragmented with a number of participants. Vector market share is approximately 2% of the market with bigger players like Imperial Holdings limited, Super Group Limited, Tibbett and Britten, and Clover Logistics holding larger shares of the market.
16. According to the parties,⁴ the largest barriers to entry in the upstream market relate to the capital cost to become a vertically integrated producer. The parties however, submit that easier entry can be gained by becoming an importer and processor of chicken, as this circumvents the agricultural supply chain and processing costs can be optimized by importing cut chicken. Barriers to entry in the downstream market relate primarily to capital costs and food handling regulations. These are however not insurmountable, as is evidenced by the recent entry of Digistics (Pty) Ltd which was awarded a contract to manage Kentucky Fried Chicken’s inbound store distribution.⁵
17. According to the parties, market foreclosure in the upstream market is unlikely since firstly, all of Vector’s key principals have agreements in place that ensure access to the Vector distribution network for between four to five years. Secondly, no other direct competitor to Rainbow in the market segment for the production and supply of fresh and frozen chickens currently uses the services offered by Vector. Thirdly, there are a number of independently owned contract logistic service providers in the downstream market to whom suppliers of fresh and frozen food products can turn to for distribution services, and finally, there are no prohibitive barriers to entry into the downstream market that would prevent producers and suppliers of fresh and frozen food products from entering this market themselves.

² A *del credere* agent is one who guarantees the solvency of the third party with whom the agent makes a contract for the principal. A *del credere* agent receives possession of the principal’s goods for purposes of sale and guarantees that anyone to whom the agent sells the goods on credit will pay promptly for them. For this guaranty, the agent receives a higher commission for sales – Black’s Law Dictionary, 7th edition. (1999)

³ Competitiveness Report

⁴ *ibidem*

⁵ Vector previously provided distribution services to KFC but subsequently lost the contract.

18. With regard to the downstream market, prior to the merger a large percentage of Rainbow's products were distributed by Vector, the remainder being distributed by Clover Logistics. However, should Rainbow terminate its contract with Clover, this will not negatively effect the competitive position of Clover in the downstream market, as the Rainbow business constitutes a very small portion of Clover's turnover.

Conclusion

19. Having regard to the above, we conclude that the merger will not lead to a substantial lessening of competition and there are no significant public interest concerns. Accordingly, we agree with the Commission's recommendation that the transaction be unconditionally approved.

D Lewis

05 November 2004
Date

Concurring: N Manoim and M Mokuena

For the merging parties: J. Katz and R.Hollingworth (Webber Wentzel Bowen)

For the Commission: M. van Hoven and E Mtantato (Mergers and Acquisition)