COMPETITION TRIBUNAL
REPUBLIC OF SOUTH AFRICA

Case no: 78/LM/Oct04

In The Large Merger Between:

Plaaskem (Pty) Ltd **Acquiring Firm**

And

UAP Agrochemicals KZN (Pty) Ltd

UAP Crop Care (Pty) Ltd **Target Firms**

Reasons for Decision

Approval

1. On 9 December 2004 the Competition Tribunal issued a Merger Clearance Certificate approving the transaction between Plaaskem (Pty) Ltd and UAP Agrochemicals KZN (Pty) Ltd and UAP Crop Care (Pty) Ltd. The reasons for this decision follow.

The Parties

2. The primary acquiring firm is Plaaskem (Pty) Ltd ("Plaaskem"). Plaaskem is controlled by Chemical Services Ltd ("Chemserve")[1], which is ultimately controlled by AECI Ltd ("AECI")[2], a public company listed on the JSE Securities Exchange South Africa. No one shareholder directly or indirectly controls AECI. Plaaskem directly or indirectly controls the following firms: Plaaskem Italia s.r.l, Fertiplant (Pty) Ltd, Plaaskem Intellectual Property and Nalesco 88 (Pty) Ltd.

3. The primary target firm is UAP Agrochemicals KZN (Pty) Ltd ("UAP KZN") and UAP Crop Care (Pty) Ltd ("UAP Cape"). UAP KZN is a wholly owned subsidiary of Lager Commodity Trading (Pty) Ltd ("Lager").[3] Lager is a subsidiary of ConAgra Foods Inc.[4] At the time of notification, UAP Cape was 80% owned by Lager and 20% owned by AstraZeneca Pharmaceuticals (Pty) Ltd. However, at the hearing, the Tribunal was informed that AstraZeneca had already sold its stake in UAP Cape to Plaaskem. Neither UAP KZN nor UAP Cape has control over any firms, nor do they have any subsidiaries.

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[1] A list of Chemserve's subsidiaries can be found on pages 14 to 51 of Chemical Services Limited's Publication of March 2004, pages 214-251 of the record.
[2] A list of AECI's principal consolidated subsidiaries can be found on page 80 of its 2003 Annual report, page 188 of the record.
[3] A company incorporated in South Africa.
[4] A company incorporated in the United States of America.

The Transaction

4. Plaaskem is acquiring UAP's Cape and KwaZulu-Natal businesses, UAP Cape and UAP KZN, respectively. The sale includes the operating assets and liabilities of said businesses. In terms of the Sale of Business Agreement, the acquisition by Plaaskem of the UAP KZN business is conditional upon Plaaskem's acquisition of UAP Cape and visa versa. The acquisition therefore constitutes one indivisible transaction.

Rationale for the Transaction

5. According to Plaaskem[5] the agricultural industry in South Africa is dynamic, overtraded and therefore extremely competitive, and these factors are forcing both distribution networks and manufacturers to integrate both vertically and horizontally. The integration of UAP's existing distribution infrastructures will result in, *inter alia* cost and operating efficiencies and provide Plaaskem with a more efficient and effective route to market its products.[6] From UAP's perspective, ConAgra, its parent company, has made the strategic decision to withdraw from all non-core food-processing activities and as such, to exit the agricultural chemicals business.[7]

The Parties' Activities

6. Plaaskem manufactures and supplies agricultural products to the local and export markets. Plaaskem's activities are broadly divided into the following product divisions: agricultural chemicals (or "agrochemicals"), foundry chemicals, animal health products, industrial products, water treatment and mining chemicals. However, the division relevant to the assessment of the proposed transaction is agrochemicals division.

7. In its agrochemicals division, Plaaskem manufactures and supplies plant protection products, plant nutrition products and adjuvants. According to the parties[8], plant protection products are designed to protect crops from various forms of damage or disease caused by insects, weeds or fungi. Plant protection products include insecticides, fungicides and herbicides. Plant nutrition products impact a grower's yield and comprise foliar products and soil fertilizers (fertigation products). Adjuvants are surfactant (surface-active substance) chemicals that are added to a tank mix to adjust the water quality in order to improve or prolong the performance of the agrochemical. Adjuvants are added mainly to plant protection solutions.

8. UAP KZN and UAP Cape distribute a complete line of agrochemicals, including plant protection chemicals, plant nutrition chemicals and adjuvants, from a range of manufacturers including Plaaskem. None of Plaaskem's other divisions use the target firms as distributors.

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[5] Management summary at page 269 of record
[6] Page 7 of the parties' competitiveness report
[7] ibid.
[8] Page 9-11 of the parties' competitiveness report

The Relevant Market

9. The transaction has a vertical effect in that it involves a manufacturer and supplier of agrochemicals, acquiring a distributor of agrochemicals. The transaction must therefore be analysed at two levels of the supply chain viz. the manufacturing level (upstream) and the distribution level (downstream).

10. It is important, at this point, to understand the supply chain in the South African agrochemical industry. Manufacturers of agrochemicals develop and formulate agricultural products.[9] The manufacturers then supply these chemicals to the agrochemical distributors. Manufacturers typically supply more than one distributor. Similarly, distributors tend to source and stock a range of agrochemical products from a number of research-based and generic companies. Distributors employ agents who serve the farmer directly. Agents make recommendations to the farmers regarding which products and services they should utilize, in order to develop a comprehensive spray programme. Usually[10], farmers are offered a "complete solution" of various agrochemical products,[11] from a number of agrochemical manufacturers.

11. The Commission refrained from defining the relevant upstream market.[12] However, we accept the parties' submission that the relevant markets for the purpose of assessing the vertical aspects of the transaction are:
    - the manufacture and supply of herbicides;
    - the manufacture and supply of fungicides;
    - the manufacture and supply of insecticides;
    - the manufacture and supply of plant nutrition products; and
    - the manufacture and supply of adjuvants.

12. Both the Commission and the parties define the relevant downstream market as the market for the distribution of agrochemicals. While the parties submit that the downstream markets are regional, the Commission did not conclude on the relevant downstream geographic market.

Evaluating the merger

13. Although generally, vertical mergers raise fewer competition concerns and generate larger pro-competitive gains than their horizontal counterparts,[13] vertical mergers may impact negatively on competition. In analyzing the effect on competition from

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[9] Companies like Plaaskem base their product development and formulation on the patented products of multi-national companies. These generic companies produce products that are exact copies of original patented products or modified derivatives of the original. This occurs once the patent has expired.
[10] Page 8 of the parties' competitiveness report
[11] These are adjusted in intensity and in the types of active ingredients required for local weather conditions, type of diseases, pests or weeds present, soil conditions as well as the type of crop. At page 9 of the parties competitiveness report.
[12] At page 7 of the Commission's report, "…no competition concerns prevail when defining the markets… narrowly."
[13] *Schumann Sasol (SA)(Pty)Ltd and Price's Daelite (Pty)Ltd* 89/LM/Oct00, decision on 30 January 2001.

vertical integration, effects in two markets usually have to be considered—the market in which the integrating firm already competes i.e. the upstream market and the market into which it is vertically integrating i.e. the downstream market. As with all vertical transactions, market shares in the upstream and downstream markets do not increase as a direct result of the transaction. In the ***Schumann Sasol and Price's Daelite***[14] matter, the Tribunal stated[15] that instead the question to be asked is "…whether the transaction allows the parties or one of the parties to prevent competition in the relevant market(s) thus maintaining or extending the anti-competitive structure of both or one of the markets."[16]

14. To this end, it is necessary to examine the likelihood of the merged entity raising its rivals' costs by means of input or customer foreclosure. This approach is confirmed by our previous decisions.[17]

Customer foreclosure

15. According to the parties, customer foreclosure is not likely because a very small portion of both UAP KZN and UAP Cape's turnovers is derived from distributing Plaaskem's products. Post-merger UAP will continue to distribute the products of other manufacturers. There are a number of distributors in the agricultural chemicals industry. Many of Plaaskem's competitors have their own distribution networks and/or alternative routes to market. The Commission's investigation revealed that there were other distributors who not only had the capacity but the incentive to serve any supplier that would be cut off from UAP's distribution.[18]

16. Plaaskem supplies a range of agricultural chemicals to various distributors and neither target firm is a significant customer of Plaaskem. According to the parties' competitiveness report, a relatively small percentage of Plaaskem's total sales were supplied through UAP during the past year. In the Cape region, the remainder of Plaaskem's sales is conducted through two other distributors, Wenkem and Terason, and it is expected that these distributors will continue to distribute for Plaaskem in future. Plaaskem's sales account for approximately 1% of both Wenkem and Terason's businesses and the parties submit that even if the merged entity were to cancel these distribution contracts, this would not cause them (Wenkem and Terason) to exit the market.

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[14] Supra, footnote 13.
[15] ibid. Paragraph 31.
[16] Areeda, Hovenkamp and Solow, Antitrust Law Vol. IVA, p.137: "A vertical merger, standing alone, does not alter concentration … Accordingly, any anticompetitive effects of a vertical merger must arise from other structural or behavioural consequences such as increased entry barriers, the elimination of non-integrated rivals by foreclosure, or the raising of rivals' costs".
[17] *Mondi Limited and Kohler Cores and Tubes* 06/LM/Jan02 decision on 20 June 2002 as well as *Inzuzo Furniture Manufacturers (Pty) Ltd and PG Bison Holdings (Pty) Ltd* 12/LM/FEB04 decision on 31 August 2004.
[18] At page 14 of the Commission's Report.

17. Similarly in the KZN region, Plaaskem's remaining sales are conducted through another distributor, Farmers Agricare. These sales also constitute an insignificant part of Farmers Agricare and will not cause it to exit the market should the merged entity self-deal in KZN. The Commission's investigation confirmed the parties' contention that Plaaskem represented a small percentage of the other distributors' total annual revenue in the downstream market. Furthermore, since UAP does not have a national distribution network, the merged entity would have to use other distributors in the regions where UAP is not located.

18. The Commission's investigation revealed that farmers and agents regularly attend symposiums and presentations by independent consultants, co-operatives, chemical companies, research councils and industry trusts. At these occasions, new product developments (patented and generic) are discussed. Thus the farmer and agent are familiar with continuous developments at manufacturing level.

19. If a distributor refused to supply a particular product, the farmer could, via the agent, approach a multinational directly. The agent could even recommend products and services of competitor distributors not available on its list. According to the parties, there are also various substitutes available to downstream distributors for the products supplied by Plaaskem.

20. The barriers to entry into the manufacturing market are low.[19] However, entry into the distribution and agent levels of the market is relatively difficult since all distributors must be registered with Agrochemicals Dealers Association of Southern Africa (ACDASA).[20] The agent-farmer relationship is critical to the distributor, therefore for a distributor to have a sustainable presence in this market, it is vital to attract and secure good quality staff.[21] The "buying" of competitor agents could be an effective entry strategy. UAP followed this approach and reaped an additional 54% share in a particular area.[22] We agree with the Commission that customer foreclosure is unlikely as a result of the transaction.[23]

Input foreclosure

21. Both the Commission and the parties agree that input foreclosure would not be likely as a result of the transaction.

22. As mentioned before, barriers to entry into the market for the manufacturing of agricultural chemicals are low. According to the parties,[24] while certain products do

[19] At page 25 of the parties' competitiveness report.
[20] Distributors also have to undergo a two-year course in The Fertilisers, Farm Feeds, Agricultural Remedies and Stock Remedies Act 36 of 1947 as well as in entomology. The course also involves intense product training. Ultimately though, the manufacturer would carry the responsibility for the mistreatment of its chemicals albeit by any person.
[21] UAP Cape's strategic plan 2002-2005.
[22] At page 14 of the Commission's Report.
[23] According to an industry association (ACDASA) fair competition prevails at both levels.
[24] At page 25 of the parties' competitiveness report.

have to go through a registration process in terms of The Fertilizers, Farm Feeds, Agricultural Remedies and Stock Remedies Act,[25] the requirements for registering a product becomes less detailed if the product has already been registered by another entity and particularly if the product is regarded by the Registrar[26] as a commodity. There are a number of manufacturers of agricultural chemicals and distributors typically source from a range of these national suppliers including Dow, Exportos, Bayer, Volcano, Du Pont and Syngenta.

23. In the manufacturing markets for insecticides, herbicides and fungicides, Plaaskem is a relatively small player with market shares of less than 10% in all three markets.[27] Even though Plaaskem is currently a relatively large player in the adjuvant manufacturing market, there are at least seven other players that have a market share ranging from 4% to 9% while 21% of the market is made up of a number of smaller players.[28] In the plant nutrition manufacturing market, although Plaaskem has the highest market share, the other players, according to the Commission, have sufficient capacity to supply the residual of customers.[29] Phosyn, one of the three largest local competitors, frequently imports and distributes finished plant nutrition products from England. Therefore customers are sufficiently exposed to international manufacturers to import without the need to formulate the product themselves.

24. Furthermore, a number of Plaaskem's upstream rivals are multinational companies who have a strong market presence in a number of the relevant upstream markets.[30] There are therefore, various substitutes available to downstream distributors for the products supplied by Plaaskem, thereby eliminating the possibility of harm, should the merged entity attempt to raise prices or engage in price discrimination.

25. The parties submit and we accept, that the ability to raise prices or restrain competition is constrained by the potential of distributors in the downstream market to substitute products from other manufacturers.

26. According to an industry player, it is "very easy" for distributors to change suppliers as no distribution agreements exist between supplier and distributor.[31] This coupled with the fact that Plaaskem is a relatively small player in both the Cape and KZN regions and that the majority of sales in these regions are derived from other upstream players, further decreases the likelihood of input foreclosure.

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[25] Supra, footnote 22.
[26] Registrar of Fertilizers, Farm Feeds and Agricultural Remedies as designated by section 2 of the Fertilisers, Farm Feeds, Agricultural Remedies and Stock Remedies Act.
[27] Parties' competitiveness report.
[28] Plaaskem's market share for adjuvants in the identified geographic markets remain under 15%.
[29] According to the Commission's investigator, HyperAgro indicated "…that they would keep supplying to whoever falls out of the bus afterwards…", at page 5 of the transcript.
[30] For example, amongst others Dow, Syngenta, Bayer, Du Pont and BASF are all active in the plant protection chemicals market in most instances, higher market shares than Plaaskem.
[31] Business is reserved by good service and relationships. Footnote 51 at page 15 of the Commission's Report.

27. The parties' competitiveness report made reference to a proposed joint venture between Plaaskem and Terason (a competitor of UAP) relating to the "…joint manufacturing and marketing of plant products and more specifically fertigation products."[32] During the hearing the Plaaskem stated that the joint venture related to a specific product that Plaaskem was providing to Terason.[33] However, Mr. Hugo Minnaar, Plaaskem's representative, indicated that Terason and UAP were "fierce competitors" and would continue to be so, post-merger. It was also pointed out that the areas, geographic or product, in which Terason was active was different in some cases to that of UAP, and that they would continue to compete to the extent that there was any overlap in those areas.[34] Furthermore, the plant nutrition product which is the subject of the joint venture is one which UAP itself does not distribute nor does it have a competing product that performs the same function. Mr. Jacobus Kriel, Managing Director of UAP Cape, in fact, stated that they specialised in plant protection (in the combating of pests and diseases) and not in the plant nutrition market. However, Mr. Kriel did confirm that in future they might be looking for another supplier to get a similar product, which they would sell in competition with the Terason product.[35]

28. According to Plaaskem's Management Summary, Plaaskem would through the proposed transaction, "…seek increased alignment with BASF", a multinational company, which, according to the Commission, competes with Plaaskem to some extent. BASF previously had an exclusive relationship with UAP, where it supplied UAP with the full range of products on an exclusive basis. According to Mr. Kriel, from the beginning of 2005, this would change into a "semi-exclusive relationship" as BASF will also supply another distributor Viking.[36] However, BASF still remains UAP's "most important supplier".[37] The Tribunal, during the hearing sought clarification from Plaaskem, as to the difference between *its* products and BASF's. According to Mr. Minnaar, BASF manufactures specialized patented products while Plaaskem focuses on generic products. Furthermore, most of BASF's products are imported into South Africa, while Plaaskem is a local formulator of active ingredients into the final product. Plaaskem also offers a wide range of plant nutrition products and "adulants" which supplement the pesticides that companies like BASF (and Plaaskem) or any other multinational would spray, and which increase the efficacy of the product.[38] The product offerings are therefore complimentary and not competitive with each other.

29. According to the Commission, BASF-like relationships were not only general practice, but also a key success factor in the industry. The desired result of such relationships would be to offer a comprehensive spray program to the farmer. We

[32] At page 24 of the parties' competitiveness report.
[33] At page 6 of the transcript.
[34] Plaaskem's legal representative, at page 7 of the transcript.
[35] ibid.
[36] According to Mr Kriel, at BASF's request, UAP has already started sub-distributing to Viking, as part of a "phasing-in" process.
[37] Mr Kriel, at page 8 of the transcript. See also Management Summary at page 274 of the record.
[38] At page 2-3 of the transcript.

accept the Commission's view that the planned arrangement would not likely prevent or lessen competition in the relevant markets.

30. It is our finding that the merged entity will not be in the position to foreclose its rivals in either of the vertically related markets in which it operates.

Public Interest

31. All the employees of UAP KZN and UAP Cape will be transferred to Plaaskem. There are no other significant public interest issues.

Conclusion

32. Having considered the Competition Commission's recommendation and the merging parties' submissions, we conclude that the merger will not lead to a substantial lessening of competition and therefore approve the transaction unconditionally.

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D Lewis	**Date**

Concurring: N Manoim and Y Carrim

For the Acquiring firm: N Hlatshwayo, N Pennel (Webber Wentzel Bowens)
For the Target firms: L.Mtanga, A.Forman (Bowman Gilfillan Inc)
For the Commission: O.Strydom (Mergers and Acquisitions)