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COMPETITION TRIBUNAL OF SOUTH AFRICA

Case No: 91/LM/Oct12

In the matter between:

CALULO INVESTMENTS (PTY) LTD
INVESTEC BANK LIMITED Acquiring Firms

And

FFS REFINERS (PTY) LTD Target Firm

Panel	:	A Wessels (Presiding Member)
		M Mazwai (Tribunal Member)
		A Roskam (Tribunal Member)
Heard on	:	19 February 2013
Order issued on	:	19 February 2013
Reasons issued on	:	19 April 2013

Decision

Conditional approval

1. On 19 February 2013, the Competition Tribunal ("Tribunal"), in terms of section 16(2)(b) of the Competition Act of 1998[1], conditionally approved the proposed transaction involving Calulo Investments (Pty) Ltd ("Calulo") and Investec Bank Limited ("Investec"), the primary acquiring firms, and FFS Refiners (Pty) Ltd ("FFS"), the primary target firm.

2. The reasons for conditionally approving the proposed transaction follow.

[1] Act No. 89 of 1998, as amended.

Merging parties and their activities

3. The primary acquiring firms are Calulo and Investec, both of which companies are incorporated in accordance with the company laws of the Republic of South Africa. Investec holds 29.47% of the issued share capital in Calulo. Calulo controls *inter alia* Calulo Petrochemicals (Pty) Ltd ("Petrochem") which holds a 25.1% shareholding in FFS via FFS Calpet (Pty) Ltd ("FFS Calpet") (also see paragraph 7 below).

4. Calulo is an investment holding company which has a portfolio of investments in companies/businesses within the petroleum, chemicals and logistics sectors in Southern Africa. Calulo, through the companies/businesses in which it holds investments, provides the following products and services: (i) shipping and freight brokerage; (ii) shipping services; (iii) crude oil and petroleum product commercial marketing and distribution; (iv) ships agency and clearing and forwarding; (v) liquid fuel storage and facilities management; and (vi) rural electrification utilising solar energy systems.

5. Investec is a wholly owned subsidiary of Investec Limited, a company listed on the Johannesburg Stock Exchange ("JSE"). Investec is the main banking subsidiary of Investec Limited. The Investec group provides a diverse range of financial products and services to a niche client base in two principal markets, namely South Africa and the United Kingdom, as well as in eight other countries, including Australia.

6. Of relevance to the competition assessment of this transaction is that Investec holds a shareholding in Corobrik (Pty) Ltd ("Corobrik"). Corobrik is a manufacturer, distributor and exporter of bricks and allied products. From a vertical competition assessment perspective, we note that Corobrik uses light fuel oil (known as Light Oil 2 or LO2[2]) supplied by FFS. FFS also

[2] LO2 is a cost effective low flashpoint, low sulphur fuel suitable for larger applications that require a clean and light fuel where the risks associated with the low flashpoint can be properly mitigated.

supplies a variety of fuel oils, including the supply of LO2, to other brick manufacturers in South Africa (also see paragraph 8 below).

7. The primary target firm is FFS. FFS is directly controlled by Fuelmark Investments (Pty) Ltd ("Fuelmark"), which owns 51% of the shares in FFS. The other shareholders of FFS are FFS Calpet, which owns 25.1% of the shares in FFS, and FFS Management Company (Pty) Ltd, which owns 23.9% of the shares in FFS. FFS Calpet is a wholly owned subsidiary of Petrochem which, in turn, is a wholly owned subsidiary of Calulo. FFS directly or indirectly controls a number of firms.[3]

8. FFS is mainly involved in the procurement, processing and blending, refining, distribution and marketing of industrial fuel oils ("IFOs"). It also provides ancillary, technical and support services to its IFO customers. FFS's technical support services are provided to assist customers in choosing and using the IFO product best suited to their needs and ensuring that the IFO is used in the most efficient and optimal way.

9. IFOs of desired customer specificities are produced through the processing and blending of heavy fuel oils (HFOs) from refinery residuals, used waste oils and marine waste oils. IFOs are fuels or fuel blends used to produce energy which is used in (i) manufacturing and industrial facilities such as glass and brick making factories; (ii) the production of steam from boilers; (iii) road-mix heating; (iv) heating of lime kilns; and (v) sand and stone drying.

10. As stated above, of specific relevance to the competition assessment of this transaction is that FFS sells LO2 to *inter alia* Corobrik.

Proposed transaction and rationale

11. The proposed transaction comprises a number of interdependent steps, which ultimately result in Investec jointly controlling FFS Calpet with a shareholding of between 40% and 49% and Calulo (via Petrochem) jointly controlling FFS Calpet with a minimum shareholding of 50% and FFS

[3] See merger record, pages 45 and 46.

Calpet owning a 100% equity shareholding interest in FFS.[4] The exact shareholding will be confirmed post the finalisation of the funding structure for the transaction.

12. Investec and Calulo will thus post-merger control FFS Calpet which will solely control FFS.

13. The merging parties submitted that FFS is a profitable business that demonstrates attractive growth potential and the proposed transaction increases Calulo’s exposure to the oil and energy sectors. The merging parties further submitted that FFS requires superior BEE credentials to effectively compete in the South African market and Calulo’s increased shareholding will provide FFS with the requisite previously disadvantaged shareholding profile.

14. From Investec’s perspective, FFS is an attractive investment in the energy sector which has been identified as a strategic focus area.

15. FFS is concluding the transaction for two reasons. First, the percentage of IFO sales dependent on public tenders is increasing and FFS needs to improve its broad-based black economic empowerment score in order to improve its chances of effectively competing for these opportunities. Second, Fuelmark has made a decision to dispose of its investments in South Africa, but retain FFS’s activities in Australia and the United Kingdom and grow its investments elsewhere in the globe.

Impact on competition

16. The Commission found that Investec’s increased shareholding in FFS as a result of the proposed transaction brings about a change in the control of FFS. The Commission concluded that Investec will have at least joint control of FFS post-merger due to (i) its increased shareholding in FFS and associated rights; and (ii) Calulo acquiring the shares of Fuelmark that currently exercises control over FFS. The Commission further found that Investec has [...] of Corobrik.

[4] See page 71 of the merger record.

17. The main theory of competitive harm advanced by the Commission was that of post-merger input foreclosure in the downstream market for the production and sale of face bricks. We shall only deal with this theory of harm in these reasons since we found no other likely competition concerns resulting from the proposed transaction.

18. As stated above, pre-merger FFS sells LO2 to Corobrik. Given Investec's post-merger (joint) control over FFS and its relationship with Corobrik, the Commission was concerned that Investec may cause FFS to foreclose Corobrik's rivals in the downstream bricks market(s) in respect of the supply of LO2.

19. The Commission further found that pre-merger FFS has market power in the market for the processing and blending of LO2 in the geographic markets affected by the proposed merger, i.e. in KwaZulu-Natal, the Eastern and the Western Cape.

20. From a customer and potential substitution perspective, we note that the available evidence suggests that HFO is significantly more expensive than LO2.[5]

21. The Commission's analyses of profit margins and market dynamics suggest that there is a likely incentive for the merged entity to foreclose brick competitors of Corobrik in KwaZulu-Natal, the Eastern and the Western Cape. This ultimately would cause likely harm to end-customers in the bricks market(s) through consequent price increases and/or a reduction in choice.

22. In order to address this input foreclosure concern raised by the Commission, the merging parties agreed[6] to a behavioural condition (i.e. a supply condition) which in essence guarantees the post-merger non-foreclosure of competitors of Corobrik in respect of the supply of LO2. The Commission was of the view that the foreclosure concerns raised by the

[5] See page 52 of the Commission's Report.
[6] See transcript, page 16.

proposed merger were sufficiently addressed by these tendered conditions.

23. We concur with the Commission's finding that the merging parties' tendered conditions are warranted to address the identified competition concern. We further find that the tendered conditions are proportionate to the concern. We therefore have approved the proposed transaction subject to the following conditions:

23.1. FFS shall continue supplying its existing brick customers with LO2 on terms and conditions which do not discriminate in favour of Corobrik in terms of trading conditions, price, volume and quality, other than reasonable allowances made to reflect (a) differences in cost or likely cost of manufacture or distribution, sale, promotion, storage or delivery resulting from the differing places to which, methods by which or quantities in which, the LO2 is supplied to different customers; or (b) variations in the quality and available volumes of the raw materials used to make the LO2. In this regard, it is noted that LO2 is a low flash point product produced by blending and processing raw materials from a variety of waste products emanating from refinery slops, by-products, contaminated and off specification materials. Due to the unsecured, variable and *ad hoc* supply of these raw materials, the availability and cost to FFS of these raw materials varies continuously and is not fixed or related to any index. In addition, because the nature of the raw materials varies so much, the processing requirements and associated processing costs also vary accordingly. In addition, due to the very nature of the origin of these raw materials waste streams the generators of these raw materials cannot give any supply commitments to FFS. Because the raw materials used to make LO2 are waste streams and vary considerably, the quality of the LO2 supplied also varies; and

23.2. In the event of an unanticipated reduction in the production of LO2 for whatever reason, such that FFS is unable to fully fulfil its commitments to its existing brick customers, FFS shall apply any reduction in volumes of supply on pro rata terms based on the volume of its LO2 supplies to existing brick customers during the consecutive 12 months period preceding such anticipated reduction.

Restraint of trade

24. The Confidentiality Agreement between the merging parties contains a restraint of trade clause in terms of which the seller, Fuelmark, its shareholders and certain employees of FFS are restrained from entering the African market for the processing and blending of IFOs for a period of five years. The merging parties stated that they view this restraint as being pro-competitive as FFS will be prepared to make investments in expansion and technological improvements knowing that it will not face competition from erstwhile shareholders and employees.

25. The Commission assed the restraint and concluded that it was both reasonable and justifiable in the circumstances and necessary to protect the value of the investment made by the acquiring firms.

26. The Tribunal questioned the merging parties with regards to the rationale for and the scope of the restraint of trade and requested them to explain the relevant know-how and intellectual property that the acquiring firms wish to protect.[7] We were satisfied with the answers provided and have no reason to doubt the Commission's conclusion concerning the restraint being reasonable and justifiable.

Public interest

27. The merging parties confirmed that the proposed merger will not result in any retrenchments and that employment will not be affected.[8]

28. The proposed merger raises no other public interest issues.

[7] See pages 20 to 22 of the transcript.
[8] See pages 8 and 100 of the merger record.

CONCLUSION

29. We approve the proposed transaction subject to the conditions as per the attached "**Annexure A"**.

____________________ 19 April 2013

Andreas Wessels **DATE**

Mondo Mazwai and Anton Roskam concurring

Tribunal Researcher:	Thabo Ngilande
For the merging parties:	Werksmans Attorneys
For the Commission:	Werner Rysbergen