



Australian
Competition &
Consumer
Commission

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Statement of Issues — Baiada Poultry Pty Ltd - proposed acquisition of Bartter Enterprises Pty Ltd

1. Outlined below is the Statement of Issues released by the Australian Competition and Consumer Commission (ACCC) in relation to the proposed acquisition of Bartter Enterprises Pty Ltd by Baiada Poultry Pty Ltd (**proposed acquisition**).
2. A Statement of Issues published by the ACCC is not a final decision about a proposed acquisition, but provides the ACCC's preliminary views, drawing attention to particular issues of varying degrees of competition concern, as well as identifying the lines of further inquiry that the ACCC wishes to undertake.
3. In line with the ACCC's *Merger Review Process Guidelines* (available on the ACCC's website at www.accc.gov.au) the ACCC has established a secondary timeline for further consideration of the issues. The ACCC anticipates completing further market inquiries by 27 January 2009 and anticipates making a final decision by 11 February 2009. However, the anticipated timeline can change in line with the *Merger Review Process Guidelines*. To keep abreast of possible changes in relation to timing and to find relevant documents, market participants should visit the Mergers Register on the ACCC's website at www.accc.gov.au/mergersregister.
4. A Statement of Issues provides an opportunity for all interested parties (including customers, competitors, shareholders and other stakeholders) to ascertain and consider the primary issues identified by the ACCC. It is also intended to provide the merger parties and other interested parties with the basis for making further submissions should they consider it necessary.

Background

5. On 12 November 2008 the ACCC commenced its informal review of Baiada Poultry Pty Ltd's acquisition of Bartter Enterprises.

The parties

Baiada Poultry Pty Ltd

6. Baiada is a privately owned Australian company which supplies poultry products throughout Australia. Baiada is vertically integrated (with the exception of contracted growing farms) and its business operations include broiler¹ and breeder farms, hatcheries, processing plants, feed milling and protein recovery. Its products include live poultry including breeding stock, poultry feed, fertile eggs, day old chickens, primary processed chicken (raw) and further processed chicken products and pet food.
7. Baiada currently has processing plants located in Sydney, Tamworth, Adelaide and Laverton (Victoria). It has approximately 2200 employees.
8. Baiada is a one-third owner (together with Red Lea and Cordina) of Hi-Chick, a breeding company.
9. Baiada is currently Australia's third-largest producer of chicken meat in Australia, which it supplies nationally.

Bartter Enterprises Pty Ltd

10. Bartter is also privately owned and is the second largest processor of primary processed and further processed chicken products in Australia which it sells under the Bartter and Steggles brands.
11. Bartter's Steggles Foods Products division supplies cooked, semi-cooked and further processed chicken and turkey products into the retail and food service channels. Bartter employs over 4500 people throughout its farming, processing, distribution and marketing and sales operations.
12. Bartter is also vertically integrated and has six processing facilities in Australia one located in Victoria, Western Australia and Queensland and three located in New South Wales. Bartter is the second largest producer of chicken meat in Australia, which it supplies nationally. Bartter also operates a number of feed mills and broiler hatching facilities.

Other industry participants

Inghams Enterprises

13. Inghams is the largest producer of chicken meat in Australia. It has over 7,000 employees and operates facilities in all states of Australia.
14. Inghams is vertically integrated (with the exception of contracted chicken growing) and operates 10 primary processing plants and six further processing plants. Inghams also operates 10 feed mills and has breeder farms located in New South Wales, Victoria, South Australia, Queensland and Western Australia.

¹ *Broiler* is the industry term for chicken grown for the purpose of chicken meat consumption

15. Inghams supplies chicken meat nationally.

State-based processors

Golden Cockerel (Queensland)

16. Golden Cockerel Pty Ltd is based in South East Queensland. It is fully integrated, comprising feed mills, hatcheries, parent farms, broiler farms, processing plant and distribution.
17. Golden Cockerel processes in excess of 15 million broilers per year and also supplies several independent processors throughout south east Queensland.

La Ionica (Victoria)

18. La Ionica operates a processing facility in Thomastown, Victoria and acquires the services of contract growers in Victoria. La Ionica is a major supplier of whole dressed birds to Victorian customers.
19. La Ionica is currently not completely vertically integrated as it does not operate hatching facilities of its own. La Ionica also does not currently operate any feed mill facilities and sources its feed from third parties.
20. La Ionica currently processes over 300,000 birds per week at its Thomastown plant and utilises a chemical-free processing method.

Hazeldene (Victoria)

21. Hazeldene is based in Bendigo, Victoria. It is a major supplier of chicken meat to Victorian customers and also supplies some products to customers located in Adelaide, South Australia and Tasmania.
22. Hazeldene operates its own hatching and breeder farms to produce day old chicks. Hazeldene also operates its own company growing farms as well as contracting some of its growing requirements to growers located in the Bendigo area.

Sunnybrand Chickens (New South Wales)

23. Sunnybrand Chickens is based in Byron Bay, New South Wales. Sunnybrand's customer base predominantly includes customers located in northern New South Wales and south east Queensland.
24. Sunnybrand is a vertically integrated chicken processor as it produces its own fertilised eggs and day-old chicks. Its processing facility is located in Byron Bay and produces 95% fresh and 5% frozen chickens at 250,000 chickens per week. The company has contracts with growers located in the Byron Bay area.

Red Lea (New South Wales)

25. Red Lea Chickens Pty Ltd is located in Blacktown, Sydney and Red Lea employs processes in excess of 300,000 chickens per week.

26. Together with Baiada and Cordina, Red Lea is a part owner of Hi-Chick, which owns a distribution licence for the Cobb breed of chicken. Red Lea has its own breeder rearing farms which are located at Menangle, Tamworth, Wellington & Cooranbong in New South Wales.
27. Red Lea Chickens produces more than 100 product lines that are sold on to wholesalers, supermarkets, butchers, restaurants, hotels and clubs. Red Lea also has 24 retail outlets of their own that sell direct to the public. More than 60% of the products produced by Red Lea have been value-added.²

Cordina Chicken Farms (Cordina) (New South Wales)

28. Cordina is located in Girraween, Sydney. Cordina processes approximately 340,000 chickens per week, which are then distributed to Sydney, Newcastle, Wollongong, ACT and parts of Queensland, Victoria and South Australia.
29. Cordina is also a part owner in Hi-Chick which owns a distribution licence for the Cobb breed of chicken.
30. Cordina supplies a range of products including, whole birds, fillets and pieces. The ACCC understands that Cordina markets its products through major supermarket chains, specialist chicken shops, delicatessens, restaurants and other food outlets.

Market inquiries

31. On 12 November 2008 the ACCC commenced market inquiries regarding the proposed acquisition. A range of interested parties provided responses, including industry representative bodies, growers, wholesale and retail customers, and other chicken processors.

Areas of overlap

32. From its inquiries, the ACCC understands that the primary areas of overlap between Bartter and Baiada are:
 - a. The acquisition of growing services in growing regions in Victoria and New South Wales; and
 - b. The supply of chicken meat to wholesale customers including:
 - National supermarket chains;
 - National quick service restaurants; and
 - State-based wholesale customers.

² 'Value-added' refers to chicken that has been processed into pieces such as chicken nuggets, chicken drumsticks, or marinated.

33. The ACCC considers that in relation to (a) the relevant growing regions where there are overlaps between the parties are:
- Geelong/West Victoria region in Victoria;
 - The Hunter Valley/Newcastle region in New South Wales; and
 - The Central Coast region in New South Wales.

Market definition

Chicken processors

34. Processors of chicken meat fall into two groups:
- national or multi-state processors who produce on a large scale using a number of processing facilities located in more than one state
 - state-based processors who tend to produce on a smaller scale from one processing facility located in one state

The acquisition of chicken grower services in regional areas in Victoria and NSW

35. The ACCC considers that chicken growers situated in different parts of each state would be impacted uniquely by the merger, and that consequently, these growers are unlikely to operate in the same markets for the purpose of competition analysis.
36. The ACCC has defined the approximate grower regions based on feedback received from market participants during the market inquiry process. In defining the geographic scope of the markets for the acquisition of grower services, the ACCC considers that the chicken processors' locations relative to growers' locations would determine the likelihood of the growers being able to supply their services to processors in particular regions. The ACCC considers that processors located geographically close to a growing region are the most likely acquirers or potential acquirers of growers' services from that region.
37. Market participants informed the ACCC that, due to the cost of transporting live birds over distances and the deterioration in quality resulting from dehydration and increased mortality rates during long distance transport, chicken processors have a preference for growers to be located within close vicinity of the processing facility. Market inquiries and advice received from processors suggested that ideally a grower should be located within an hour to an hour and a half travel time from the processing facility. The ACCC also took account of advice from individual processors as to what they regarded as their effective grower catchment areas.

Supply of chicken meat to wholesale customers

38. Market inquiries have indicated that buyers of processed chickens from processors primarily fall into one of two groups:

- state-based wholesale customers
- national buyers

39. State-based wholesale customers include:

- distributors of wholesale chicken to be on-sold to other smaller buyers such as chicken retailers, take-away shops, caterers, and restaurants
- boning rooms which process fresh whole chickens, also to be on-sold to other smaller buyers such as those listed above; and
- customers who purchase wholesale chicken directly from processors.

40. For the purposes of this Statement of Issues, all such customers will be referred to as 'State-based wholesale customers'.

41. Market inquiries have indicated that state-based customers operate in one state. For the distributors and boning rooms, prices and volumes tend to be negotiated on a daily or weekly basis for immediate delivery to their customers.

42. Relative to national buyers, state-based wholesale customers buy smaller volumes and it appears that state-based and national processors can both readily meet the requirements of state-based wholesale customers. Given the purchase volumes involved and the products supplied, state-based and national processors appear to be close substitutes for these customers.

43. National buyers tend to be supermarkets or fast food chains who service outlets located nationally or in more than one state. Generally, these buyers prefer to deal with national processors. This enables the buyer to obtain chicken of uniform quality, in the volumes necessary to supply their outlets, and processed to certain specifications in some cases. Dealing with national processors also avoids the additional costs of negotiating and dealing with multiple state-based processors.

44. Market inquiries have indicated that state-based and national processors do not appear to be close substitutes in the eyes of many national buyers. This is mainly to do with the limited ability for state-based processors to supply the necessary volumes of the specified products required by large national customers. The ACCC notes that there are some national buyers who utilise state-based processors for certain volumes, these buyers tend to acquire products that are homogenous and can be readily supplied by both state-based and national processors. Market participants voiced concern that these state-based processors are only able to impose limited competitive constraints on the national processors as state-based processors do not have the capabilities to supply the substantial volumes required by the national buyers.

45. Therefore, it appears there are varying degrees of available substitutes for the two customer groups.

Statement of issues

46. For the purposes of this Statement of Issues, the issues in this matter are divided into three categories, 'issues of concern', 'issues that may raise concerns' and 'issues unlikely to raise concerns'.

Issues of concern

47. The ACCC's preliminary view is that the proposed acquisition is likely to result in a substantial lessening of competition in:
- The market for the acquisition of chicken grower services in the west Victoria region; and
 - The market for the supply of chicken meat to national wholesale customers.

The market for the acquisition of broiler growing services - Geelong/West Victoria

48. Market inquiries suggested that for growers located in the Geelong area or West Victoria region, most of which are currently contracted to Bartter or Baiada, the main constraint in terms of alternative processor options to a merged Bartter/Baiada is La Ionica.
49. The ACCC considers that growers in this region would face a significant reduction in the number of processors situated within close proximity that would be likely to compete to acquire their growing services. Currently both Baiada and Bartter are the processors most likely to compete to acquire for these services.
50. The ACCC is concerned that the removal of Bartter from the region as a buyer option for growers could provide an incentive for the remaining processors to put downward pressure on grower fees in the region post acquisition.
51. The ability for La Ionica in the future to act as a strong competitive constraint to Baiada in this region will be an important aspect of the ACCC's competition assessment.
52. The ACCC is concerned that processors in Victoria other than La Ionica are not in a position to act as a constraint in the region. Market inquiries have suggested that the locations of other processors in Victoria relative to the Geelong/West Victoria region are such that for reasons including transport cost and convenience and possible deterioration in bird quality those processors are unlikely to acquire the services of growers in that region.

The ACCC invites market participants to comment on the following and preferably provide specific examples in relation to:

- Further information on whether, in the event that Baiada acquires Bartter, La Ionica, or any other processor, would be in a position to act as an effective competitive constraint to Baiada for the acquisition of growing services in the Geelong/west Victoria region.
- Information that would suggest that, in the event of Baiada acquiring Bartter, Baiada or other processors in the region would be in a position to decrease grower fees in a sustainable manner without facing any competitive constraints.

Market for the supply of chicken meat to national wholesale customers

53. As noted above, the availability of alternative suppliers appears to vary depending on the type of customer within the national buyer category. In addition, the ACCC recognises that some customers may have strong buyer power that enable them to negotiate favourable terms and price relative to other buyers. Alternatively some buyers may possess countervailing power if they are able to bypass their upstream suppliers either by sponsoring new entry or expansion by an existing smaller processor.
54. Further inquiries are needed to determine the availability and nature of substitutes and bargaining or countervailing power for customers within this category, and it may be the case that for some customers, the proposed acquisition will have less of a detrimental impact than for others. However, the ACCC is concerned that the proposed acquisition would result in increased prices for a substantial proportion of the volume of chicken meat sold in Australia. Therefore, for the purposes of this Statement of Issues, the ACCC has highlighted this matter as an issue that is likely to raise competition concerns.
55. The ACCC understands there to be a number of wholesale customers that are exclusively supplied by two or more of the three major processors at one time, and for whom the three large major processors are the only credible alternative suppliers of fresh chicken. This is because the major suppliers have the scale and distribution networks to produce large volumes of fresh chicken to at a consistent quality level, at prices that enable these customers to price on a nationally-consistent basis.
56. Market inquiries to date suggest that smaller processors may not be adequately substitutable for the three major processors, due to limited production or distribution capacities, current inability to produce the required products to a satisfactory standard required by QSRs, and concerns regarding smaller processors' abilities to expand their production capacities.

57. Market inquiries have also suggested that the majority of state-based chicken processors are currently capacity-constrained and are only able to provide limited competitive pressure on the large national processors.
58. Market participants have also indicated that barriers to entry and expansion for chicken processors are high due to a range of factors including:
 - the shortage of available chicken growers;
 - high barriers to entry and expansion for chicken growers;
 - access to additional vertical inputs and/or barriers to vertical integration;
 - the capital costs of investing in new equipment and transport infrastructure to accommodate national supply; and
 - availability of suitable land for both growers and processing facilities, particularly for processors located in urban areas.
59. The ACCC is therefore concerned that the proposed merger will result in the aggregation from three to two large national chicken processors, leading to increased prices for a large proportion of the wholesale chicken meat that is sold to many national wholesale buyers. This is particularly the case if state-based processors are not considered to be viable alternative suppliers for chicken meat to such customers.

The ACCC is seeking further information in relation to:

- The nature of barriers to expansion for existing processors and the ability of small state-based suppliers to expand production capacity;
- Smaller regional processors' ability to meet national wholesale customers' product quality standards should the merged entity seek to increase prices upon these customers post-acquisition;
- Whether Red Lea and Cordina are unlikely to act as effective competitors to Baiada for these customers;
- The likelihood that Inghams would constrain the merged entity's attempts to increase prices to these customers;
- The ability or inability for QSRs to sponsor expansion of a smaller state-based chicken processor who could act as a potential substitute supplier of chicken products to the QSR;
- The ability of QSRs to disaggregate their current supply arrangements such that they could switch volumes to smaller state-based chicken processors in order to constrain the large national processors from increasing prices or lowering the quality of chicken meat products; and
- Any other strategies which a QSR could use to mitigate the risk of a potential price increase or decrease in quality which may arise as a consequence of the proposed transaction proceeding.

Issues that may raise competition concerns

60. On the basis of market inquiries conducted to date, the ACCC's preliminary view is that competition concerns may arise in the following markets:

- the acquisition of growing services in the Newcastle/Hunter Valley growing region of NSW;
- the acquisition of growing services in the Central Coast region of NSW; and
- the supply of chicken meat to wholesale customers in New South Wales.

The market for the acquisition of growing services – Newcastle/Hunter Valley, NSW

61. Currently three processors acquire grower services from growers in the Newcastle/Hunter Valley region in New South Wales. Most of the growers

provide services to Bartter, and a small number provide services to each of Baiada and Red Lea.

62. Bartter is the only processor with a processing facility in the Hunter Valley. Inghams has a processing facility in Cardiff, New South Wales which is in relatively close proximity to Bartter's Beresfield processing facility and is approximately 40 kilometres on average from growers in the Hunter Valley region. However, Inghams appears to currently source most if not all of its growers from the Central Coast, New South Wales region and does not acquire chicken growing services from the Hunter Valley region. Hence, it appears that Inghams is a potential, rather than actual acquirer of Hunter Valley growers' services.
63. Baiada's closest processing facility is in Pendle Hill, in the greater Sydney region, which is on average approximately 190km away from the growers in the Hunter Valley region. Red Lea's processing plant is also a substantial distance away in Sydney.
64. The ACCC considers that the removal of Bartter from this grower region could result in a significant reduction in the number of processors positioned to acquire the services of growers in the Hunter Valley, with Baiada being one of the only other three processors actively acquiring growing services from the area.

The ACCC invites market participants to comment on the following and where possible provide specific examples in relation to:

- the likelihood that Inghams' Cardiff processing facility would provide a strong competitive constraint to the merged entity for the acquisition of services from growers located in the Hunter Valley; and
- whether processors located in the Sydney basin should be properly considered to be included in the market for Hunter Valley growers and the likelihood and extent to which those processors might be prepared to acquire the services of growers approximately 190 kms away in the Hunter Valley on a long term basis.

The market for the acquisition of growing services – Central Coast, NSW

65. The Central Coast area (encompassing the Mangrove Mountain, Peats Ridge, Castle Hill, Kulnura, Somersby and surrounding regions) currently comprises growers who provide grower services to Baiada, Cordina, Inghams and Red Lea.
66. This region is relatively close to the Sydney Basin processors and also the Hunter Valley/ Newcastle region. In effect these growers are located midway between Sydney and Newcastle. Although Bartter does not currently acquire grower services from this region, these growers are located on average approximately 100km away from Beresfield, the location of the Bartter processing facility. The ACCC considers that accordingly these growers could potentially supply growing services to Bartter.

67. Market inquiries have suggested that vertical supply arrangements between Baiada, Cordina and Red Lea (mainly for the supply of day old chicks and their participation in the Hi-Chick joint venture) may compromise the ability of Cordina and Red Lea to act independently as strong competitive constraints to Baiada. If such a view is correct, potential competition issues may arise in the Central Coast as the removal of Bartter will leave only one significant competitive constraint in the market being Inghams.

The ACCC invites market participants to respond on the following and preferably provide specific examples in relation to:

- Any factors likely to prevent Bartter from acquiring growers' services in the Central Coast region;
- The ability of Cordina and Red Lea to act as strong competitive constraints to Baiada and Inghams in the event Baiada acquires Bartter; and
- Any examples of Cordina or Red Lea acquiring grower services in the region in competition with Baiada or Inghams.

The market for supply of wholesale chicken meat to wholesale customers in New South Wales

68. In New South Wales, market participants identified the following processors as suppliers of chicken meat to wholesale customers: Baiada, Bartter, Cordina, Red Lea, Sunnybrand and Inghams.
69. Market participants informed the ACCC that they did not consider Inghams to be a significant participant in this segment, mainly because their focus was on supplying high volume wholesale customers.
70. Furthermore, concerns were raised in market inquiries that Cordina and Red Lea's participation in the Hi-Chick joint venture may limit or provide disincentives for these processors to compete vigorously against the merged entity post acquisition.
71. The ACCC considers that competition issues may arise in relation to this market if the competitive constraint offered by Inghams, Cordina and Red Lea are weak or limited.

The ACCC invites market participants to comment on the following and preferably provide specific examples in relation to:

- The effectiveness of state-based chicken processors to impose competitive constraints upon the large national chicken processors, particularly in relation to price and quality of product.
- Any other information which would suggest that the proposed acquisition is likely to result in a substantial lessening of competition.

Issues unlikely to raise concerns

72. The ACCC's preliminary view is that competition issues are unlikely to arise in the following markets for the acquisition of grower services :

- The markets for the acquisition of chicken growing services in the following regional areas:
 - Bendigo/North Victoria
 - Mornington Peninsula/South East Victoria
 - Yarra Valley/East Victoria
 - Sydney Basin, NSW
 - Tamworth, NSW
 - Griffith, NSW
 - Western Australia
 - South Australia
 - Queensland; and
- the market for the supply of chicken meat to state-based wholesale customers in Victoria, Queensland, South Australia, and Tasmania.

Supply of wholesale chicken meat to state-based wholesale customers in Victoria

73. In Victoria, market participants identified the following processors as suppliers of chicken meat to wholesale customers: Baiada, Bartter, Inghams, La Ionica and Hazeldene.
74. Market inquiries suggested that both La Ionica and Hazeldene appeared to have a strong presence in the supply of chicken to these types of customers.
75. The ACCC considers that competition issues are unlikely to arise in this area.

Supply of wholesale chicken meat to state-based wholesale customers in Queensland

76. In Queensland market participants identified the following chicken processors as suppliers of chicken meat to wholesale customers: Bartter, Baiada, Ingham, Golden Cockerel and Sunnybrand.

77. Market participants contacted in Queensland in general did not convey any concerns to the ACCC in relation to the proposed acquisition. These market participants informed the ACCC that they considered strong competition to exist within Queensland amongst the state-based processors and the three major large national processors.
78. The ACCC therefore considers that competition issues are unlikely to arise for wholesale customers in Queensland as a result of this acquisition.

The ACCC will accept further submissions from industry participants and will further consider this area if it considers that such an assessment is warranted.

In particular, market participants who do have concerns may wish to provide information on the strength of the alternative regional processors to act as a strong competitive constraint on the merger parties post acquisition.

Supply of chicken meat to state-based wholesale customers in other states

79. Market inquiries to date have not revealed competition concerns arising from the proposed acquisition in South Australia, Western Australia or Tasmania. The ACCC therefore seeks any further comment from market participants who consider that competition issues are likely to arise in relation to these states for bulk-buying wholesale customers.

- The ACCC will accept further submissions from industry participants and will further consider this area if it considers that such an assessment is warranted.
- In particular, market participants who do have concerns may wish to provide information on the strength of the alternative regional processors to act as a strong competitive constraint on the merger parties post acquisition.

ACCC's future steps

80. The ACCC will finalise its view on this matter after it considers market responses invited by this Statement of Issues.
81. The ACCC now seeks submissions from market participants on each of the issues identified in this Statement of Issues and on any other issue that may be relevant to the ACCC's assessment of this matter.

82. Submissions are to be received by the ACCC no later than 27 January 2009. The ACCC will consider the submissions received from the market and the merger parties in light of the issues identified above and will, in conjunction with information and submissions already provided by the parties, come to a final view as to the appropriate course of action to take to resolve any competition concerns that remain.
83. The ACCC intends to publicly announce its final view by 11 February 2009. However the anticipated timeline may change in line with the *Merger Review Process Guidelines*. A Public Competition Assessment for the purpose of explaining the ACCC's final view may be published following the ACCC's public announcement.