



Australian  
Competition &  
Consumer  
Commission

16 January 2008

## **Statement of Issues — Proposed acquisition of certain assets of Carter Holt Harvey's Woodproducts Australia business by Sumitomo Forestry Co. Ltd**

1. Outlined below is the Statement of Issues released by the Australian Competition and Consumer Commission (ACCC) in relation to the proposed acquisition (**proposed acquisition**) of certain assets of Carter Holt Harvey's (CHH) Woodproducts Australia business by Sumitomo Forestry Co. Ltd (SFC).
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](http://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 **30 January 2008** and anticipates making a final decision by **13 February 2008**. 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, interested parties should visit the Mergers Register on the ACCC's website at [www.accc.gov.au/mergersregister](http://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 29 November 2007 SFC sought an informal review by the ACCC of the proposed acquisition.

## **The parties**

### **Sumitomo Forestry Co. Ltd**

6. SFC has numerous wood and housing related businesses internationally including timber land management, production and sales of timber and building materials, the construction and sales of wooden housing and remodelling and sales of previously owned homes.
7. Alpine MDF Industries Limited (**Alpine**) is a wholly owned Australian subsidiary of SFC purchased in December 2002. Alpine is a manufacturer and supplier of raw medium density fibreboard (**MDF**), with a plant located near Wangaratta Victoria. Other than MDF, SFC does not manufacture any products in Australia.
8. SFC also has particleboard, plywood, and value added timber product manufacturing assets in Indonesia and owns Nelson Pine Industries Ltd (**Nelson**) in New Zealand, which manufactures raw MDF and laminated veneer lumber (**LVL**).

### **Carter Holt Harvey Pty Limited**

9. CHH is a privately owned New Zealand forest products company with significant interests in wood products, pulp, paper and packaging throughout Australasia.
10. Carter Holt Harvey Woodproducts Australia Ltd (**CHH Woodproducts**) is a wholly owned subsidiary of CHH which is involved in the manufacture and supply of wood based building products, including timber, plywood, LVL, particleboard, MDF and a range of interior decorative products. CHH Woodproducts services both domestic and export markets.

## **Proposed acquisition**

11. SFC is proposing to acquire the following assets from CHH Woodproducts:
  - raw MDF manufacturing plant located in Oberon NSW;
  - MDF mouldings manufacturing plant located in Oberon NSW;
  - particleboard manufacturing plants located in Gympie QLD, Tumut and Oberon NSW and Mt Gambier SA;
  - decorative panel manufacturing plants located in Tumut and Oberon NSW and Mt Gambier SA; and
  - chemical resins manufacturing plant located in Oberon NSW.
12. The primary area of overlap between the assets of SFC and CHH Woodproducts in Australia is in relation to the manufacture and supply of raw MDF.

## **Market inquiries**

13. On 3 December 2007 the ACCC commenced market inquiries regarding the proposed acquisition. A range of interested parties provided responses, including MDF customers, suppliers of wood products, distributors, secondary MDF manufacturers, retailers and industry associations.

## **Industry background**

14. MDF is formed by breaking down softwood into wood fibres, combining it with wax and resin, and forming panels by applying high temperature and pressure.
15. MDF comes in a variety of forms and can generally be divided into raw and value added. Raw MDF is the product of the primary manufacturing processes described above and is supplied in a range of sizes for particular applications.
16. Value added MDF is raw MDF to which secondary manufacturing processes have been applied. Value added MDF includes MDF mouldings used for commercial and residential fit-outs and laminates such as melamine, veneers and vinyl used for kitchen and bathroom cabinets, wall units, wardrobes, doors and office desks.
17. The main customers of raw MDF are secondary MDF manufacturers such as:
  - residential and commercial fit-out suppliers (including decorative and shop fittings);
  - cabinet makers (including kitchen and bathroom cabinets); and
  - furniture manufacturers (including dining tables and wardrobes).
18. There are currently three manufacturers of raw MDF in Australia, namely CHH Woodproducts, SFC and The Laminex Group Pty Ltd (**Laminex**). The proposed acquisition would see the number of manufacturers of MDF in Australia reduce from three to two.

## **Statement of issues**

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

### **Issues likely to raise concerns - Supply of raw MDF**

20. Based on market inquiries, the ACCC considers that the proposed acquisition is likely to give rise to substantial competition concerns with respect to the supply of raw MDF in Australia.
21. There are a variety of alternative wood panel products available to consumers of raw MDF including particleboard, plywood, hardboard, and solid and veneered timber. However, market inquiries indicated that for a significant number of raw MDF customers these alternatives are generally not close substitutes for the uses

of raw MDF due to the unique characteristics of raw MDF with regard to finishing, cutting ability and strength. These unique characteristics are reflected in the difference in price between raw MDF and other wood panel products.

22. The proposed acquisition would lead to the merged entity supplying a significant share of the raw MDF supply in Australia as there are limited alternative suppliers. Post acquisition, the only alternative domestic manufacturer and supplier of raw MDF would be Laminex. Laminex is a significant manufacturer of raw MDF in Australia and supplies raw MDF in Australia and in export markets.
23. However, interested parties expressed concerns that Laminex may not impose a significant competitive constraint on the merged entity because Laminex is likely to focus its supply of raw MDF to its vertically integrated secondary manufacturing and distribution operations. Interested parties indicated that Laminex does not currently supply significant volumes of raw MDF to independent distributors and secondary MDF manufacturers that compete with Laminex in the downstream supply of value added MDF products (some of which are significant purchasers of raw MDF). As a result, Laminex may not be a viable alternative manufacturer and supplier of raw MDF for many independent MDF distributors and secondary MDF manufacturers post acquisition.
24. Market inquiries indicated that raw MDF imports would have a limited ability to constrain the merged entity because there are limited imports of raw MDF entering Australia and the volume of raw MDF imports has declined in recent years, in particular because New Zealand manufacturers are now related to Australian manufacturers. The two most likely sources of imported raw MDF identified were New Zealand and Asia. Market inquiries indicated that:
  - other than the SFC and CHH related entities, the only alternative manufacturer of raw MDF in New Zealand is Dongwha Patinna NZ Ltd (**Dongwha**). Dongwha is part owned by entities related to an incumbent Australian manufacturer, Laminex. Market inquiries indicated that as a result of this interest, Dongwha may have a reduced incentive to impose a significant competitive constraint on the merged entity and Laminex in Australia; and
  - while it may be viable to import raw MDF manufactured in Asia to Australia (in particular from Malaysia and China), raw MDF imported from Asia is not an alternative for some raw MDF customers in Australia because it:
    - is inferior in quality, as it is frequently manufactured from rubber trees instead of radiata pine and can have higher formaldehyde levels than permitted by Australian standards; and
    - may not be available on a reliable basis.
25. Interested parties also indicated that there are high barriers to entry with respect to the manufacture of raw MDF, including:

- high capital costs (including significant sunk costs) to establish a raw MDF manufacturing plant;
- only large scale entry would be profitable given the minimum efficient scale requirements to effectively compete; and
- difficulties purchasing sufficient supply of necessary radiata pine inputs for the manufacture of raw MDF, given the existence of long term exclusive supply contracts held by incumbent wood product manufacturers.

26. The ACCC invites further information and views as to:

- the extent to which alternative wood products such as particleboard and plywood may be considered a close substitute for raw MDF;
- the extent to which Laminex supplies raw MDF to independent MDF distributors and secondary MDF manufacturers;
- the extent to which Laminex would be likely to have the ability and incentive to expand its manufacturing and supply of raw MDF to impose a significant competitive constraint on the merged entity;
- the extent to which Laminex would be likely to divert the supply of raw MDF from export markets to domestic markets in Australia in response to an increase in the price or a reduction in the quality of raw MDF supplied by the merged entity;
- the extent to which Dongwha would be likely to have the ability and incentive to supply significant volumes of raw MDF to Australia in response to an increase in the price or a reduction in the quality of raw MDF supplied by the merged entity;
- the extent to which raw MDF imports from China and Malaysia could be a close substitute for raw MDF manufactured in Australia;
- the landed cost of raw MDF imported from each of New Zealand, Malaysia and China;
- lead times required for importing raw MDF from each of New Zealand, Malaysia and China;
- the nature and amount of capital costs required to establish a raw MDF manufacturing plant;
- the minimum efficient scale requirements to effectively compete in the manufacture and supply of raw MDF; and
- the extent to which existing long term supply agreements with respect to radiata pine supplies may hinder entry by prospective entrants or expansion by existing suppliers of raw MDF in Australia.

## **Issues that may raise concerns - Ability and incentive to foreclose competition**

27. Based on market inquiries to date, the ACCC considers that the proposed acquisition may lead to substantial competition concerns with respect to the potential for the merged entity to limit the supply of raw MDF to downstream distributors and secondary MDF manufacturers which compete with the merged entity in the manufacture and supply of value added MDF products, namely, MDF mouldings.
28. Market inquiries indicated that competition for the supply of MDF mouldings may be substantially reduced if the proposed acquisition resulted in the merged entity having the ability and incentive to effectively foreclose rival MDF mouldings suppliers from competing for a material proportion of demand.
29. For example, the merged entity could seek to use its strong position with respect to the supply of raw MDF in Australia to:
  - restrict the supply of raw MDF to rival MDF mouldings suppliers;
  - supply rival MDF mouldings suppliers at inflated prices; and/or
  - impose unfavourable conditions upon the supply of raw MDF to rival MDF mouldings suppliers.
30. These examples, which are necessarily a non-exhaustive account of the types of conduct that may foreclose competition, may significantly foreclose the ability of rival MDF mouldings suppliers to compete, reduce their ability to achieve economies of scale and raise their costs.
31. The ACCC invites further information and views as to the extent to which:
  - CHH Woodproducts currently supplies raw MDF to its downstream rivals in the supply of MDF mouldings;
  - the merged entity would have the ability to foreclose competition with respect to the supply of MDF mouldings by limiting the supply of raw MDF to rival MDF mouldings suppliers having regard to:
    - the ability and incentive of Laminex to expand its supply of raw MDF to rival MDF mouldings suppliers;
    - any alternative overseas sources of supply of raw MDF to rival MDF mouldings suppliers (i.e. import competition); and
  - the merged entity would have the incentive to foreclose competition with respect to the supply of MDF mouldings by limiting the supply of raw MDF to rival MDF mouldings suppliers having regard to:
    - the relative profit margins of raw MDF and MDF mouldings;
    - the likely capacity utilisation of the merged entity;

- the nature and extent of competition from imported MDF mouldings;
- the extent to which MDF mouldings may be differentiated from other MDF products and other building products; and
- the extent to which the merged firm is likely to have the capacity to expand the manufacture and supply of MDF mouldings.

### **Issues unlikely to pose concerns – Particleboard, decorative panels and resins**

32. Based on market inquiries, the ACCC considers that the proposed acquisition is unlikely to pose substantial competition concerns in relation to the supply of particleboard, decorative panels and chemical resins.
33. Nonetheless, the ACCC will accept further submissions from interested parties and will further review these product areas if it considers such an assessment is warranted.

### **ACCC's future steps**

34. The ACCC will finalise its view on this matter after it considers market responses invited by this Statement of Issues.
35. The ACCC now seeks submissions from interested parties 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.
36. Submissions are to be received by the ACCC no later than **30 January 2008**. 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.
37. The ACCC intends to publicly announce its final view by **13 February 2008**. 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.