



Public Competition Assessment

24 December 2009

Gunns Limited - proposed acquisition of ITC Timber Pty Ltd

Introduction

1. On 25 November 2009, the Australian Competition and Consumer Commission (**ACCC**) announced its decision to oppose the proposed acquisition of ITC Timber Pty Ltd (**ITC Timber**) by Gunns Limited (**Gunns**) (**proposed acquisition**). The ACCC was of the view that the acquisition by Gunns of ITC Timber's 50 per cent interest in the SmartFibre Pty Ltd (**SmartFibre**) wood chip joint venture would be likely to have the effect of substantially lessening competition in the market for the acquisition of hardwood pulpwood in north-eastern Tasmania in contravention of section 50 of the *Trade Practices Act 1974* (the **Act**).
2. On 26 November 2009, Gunns submitted a revised proposal to acquire ITC Timber that did not include the SmartFibre wood chip joint venture asset. The ACCC subsequently announced on 27 November 2009 that it would not oppose the revised proposed acquisition of ITC Timber by Gunns after the ACCC's competition concerns were addressed with the exclusion of the SmartFibre wood chip joint venture asset.
3. The ACCC formed its view on the basis of the information provided by the merger parties and information arising from its market inquiries. This Public Competition Assessment outlines the basis on which the ACCC has reached its decision on the proposed acquisition and the subsequent revised proposal, subject to confidentiality considerations.

Public Competition Assessment

4. To provide an enhanced level of transparency and procedural fairness in its decision making process, the ACCC issues a Public Competition Assessment for all transaction proposals where:
 - a merger is opposed;
 - a merger is subject to enforceable undertakings;
 - the merger parties seek such disclosure; or

- a merger is not opposed but raises important issues that the ACCC considers should be made public.
5. This Public Competition Assessment has been issued because the original proposed acquisition was opposed by the ACCC. The ACCC did not oppose the revised proposed acquisition following a restructure which excluded the SmartFibre joint venture asset from the acquisition.
 6. By issuing Public Competition Assessments, the ACCC aims to provide the public with a better understanding of the ACCC's analysis of various markets and the associated merger and competition issues. It also alerts the public to circumstances where developments in particular markets have led, or are likely to lead, to changes in the ACCC's assessment of competition conditions in those markets.
 7. Each Public Competition Assessment is specific to the particular transaction under review by the ACCC. While some transaction proposals may involve the same or related markets, it should not be assumed that the analysis and decision outlined in one Public Competition Assessment will be conclusive of the ACCC's view in respect of other transaction proposals, as each matter will be considered on its own merits.
 8. Many of the ACCC's decisions will involve consideration of both non-confidential and confidential information provided by the merger parties and market participants. In order to maintain the confidentiality of particular information, Public Competition Assessments do not contain any confidential information or its sources. While the ACCC aims to provide an appropriately detailed explanation of the basis for the ACCC decision, where this is not possible, maintaining confidentiality will be the ACCC's paramount concern, and accordingly a Public Competition Assessment may not definitively explain all issues and the ACCC's analysis of such issues.

The parties

The acquirer – Gunns Limited

9. Gunns is an ASX-listed company and is Australia's largest fully integrated hardwood forest products company. Gunns is comprised of three operating divisions:
 - *Forest Products*: including forest plantations, sawmilling and production of timber products and wood chip exports;
 - *Managed Investment Schemes*: offering investors the opportunity to invest in forestry and horticultural development; and
 - *Other businesses*: including wineries, construction and Mitre 10 retail outlets in Tasmania.

10. Gunns manages over 275,000 hectares of freehold land, with 200,000 hectares under plantation. Gunns plantations include 150,000 hectares of hardwood eucalyptus plantations in Tasmania and 50,000 hectares of radiata pine softwood plantations in South Australia and Victoria.
11. Gunns produces a range of hardwood and softwood timber products including solid timber and timber veneers. Gunns operates eight sawmills in Australia including six hardwood mills (located in Smithton, Austins Ferry, Launceston, Western Junction and Deloraine, Tasmania, and Manjimup, Western Australia). Gunns also operates two softwood sawmills (located in Mt Gambier, South Australia and Scottsdale, Tasmania). Gunns' sawmill operations have the capacity to process 950,000 cubic metres of sawlog per annum.
12. Gunns also supplies wood chips to customers in Japan, Korea, China and Indonesia. Gunns operates four wood chip facilities and loading ports (located in Burnie, Tamar and Triabunna in Tasmania and Portland in Victoria). Gunns is currently constructing a \$2.5 billion pulp mill in Bell Bay Tasmania. Gunns exports an estimate of 3.1 million tonnes of wood chip per annum.
13. Gunns also currently holds a 13.37 per cent interest in Forest Enterprises Australia Ltd (**FEA**).

The target – ITC Timber Pty Ltd

14. ITC Timber Pty Ltd is a wholly owned subsidiary of ITC Limited, which in turn is wholly owned by Elders Limited. ITC Limited is a vertically integrated forestry company, with approximately 170,000 plantation hectares under management across Australia.
15. ITC Timber manufactures hardwood timber and value-added timber products for a wide range of applications including construction, flooring and furniture. ITC Timber has four hardwood processing facilities in Australia – two in Victoria (Alexandra and Heyfield) and two in Tasmania (Huonville and Launceston). ITC Timber has the capacity to process approximately 250,000 cubic metres of sawlogs per annum.
16. ITC Timber also holds a 50 per cent share of SmartFibre, a wood chip joint venture with FEA, formed in 2003. SmartFibre exports plantation hardwood and softwood wood chips for paper and paperboard production, to customers in mainly Japan and China. SmartFibre processes hardwood and softwood timber not suitable for sawlogs into wood chips for export, at its wood chip facility in Bell Bay, Tasmania. SmartFibre also uses residual timber in its wood chip production, sourced from independent sawmills and the joint venture parties' own sawmill operations. It currently exports on average 500,000 tonnes of wood chips per annum.
17. The revised proposed acquisition excludes ITC Timber's 50 per cent interest in SmartFibre from the transaction, such that ITC Timber's parent, Elders, retains ownership of the 50 per cent interest.

Other industry participants

Forest Enterprises Australia

18. FEA is an ASX-listed forestry and forest products company. FEA's principal activities include acquiring hardwood and softwood timber from log suppliers for the manufacture of sawn timber and value-added timber products, such as timber veneer, at its saw milling and timber processing facilities situated at Bell Bay, Tasmania. FEA's Bell Bay sawmill has the capacity to process approximately 400,000 cubic metres of sawlog per annum.
19. FEA is also responsible for the establishment and management of approximately 72,000 hectares of hardwood plantations in Tasmania, northern New South Wales and south-eastern Queensland, for over 11,000 investors.
20. FEA holds the remaining 50 per cent share of the SmartFibre wood chip export joint venture with ITC Timber (now with Elders after the SmartFibre interest was excluded from the transaction).
21. ITC Timber's parent company Elders Limited currently holds a 13.5 per cent shareholding in FEA.

Forestry Tasmania

22. Forestry Tasmania is established under the *Forestry Act 1920* (Tas) and is the manager of Tasmania's state-owned forests. Forestry Tasmania has statutory responsibility for the management of 1.5 million hectares of State forest land, including approximately 105,000 hectares of plantations comprising both softwood and hardwood species. Of the area managed, 685,400 hectares are available for wood production, with the remainder designated for conservation and recreation.
23. Forestry Tasmania currently harvests native forests and plantations to supply the industry with approximately 300,000 cubic metres of high quality saw and veneer logs per annum. Forestry Tasmania also supplies lower quality logs as pulpwood.

Industry background

24. Gunns and ITC Timber manufacture hardwood timber products and wood chips. Hardwood timber products are typically classified as either 'appearance grade' or 'structural grade' products. Appearance grade hardwood timber products are used in timber flooring, panelling, interiors, joinery and furniture. Structural grade hardwood timber products are typically used for timber framing in residential construction. The primary input for the manufacture of hardwood timber products is hardwood sawlog.
25. Wood chips are used in the manufacture of paper products. The primary inputs for the manufacture of wood chips are pulpwood and residual timber. Pulpwood is produced from native or plantation logs that are not of a sufficient standard to supply to sawmills for the manufacture of timber products. Residual timber is a

by-product from the production of timber products or the harvesting of native or plantation forests. In addition to its use as an input in wood chip manufacturing, residual timber is used as a bio-fuel as well as in agricultural and landscaping applications.

26. Pulpwood and hardwood sawlog suppliers in Tasmania include Forestry Tasmania, private property owners and private plantation owners, which include project growers that are part of Managed Investment Schemes. There are approximately 885,000 hectares of privately owned native forests and 150,000 hectares of plantation forests on private land in Tasmania.

ACCC review timeline

27. The following table outlines the timeline of key events in this matter.

Date	Event
14-Sep-2009	ACCC commenced review under the Merger Process Guidelines.
25-Sep-2009	Closing date for submissions from interested parties.
29-Sep-2009	ACCC requested further information from Gunns Limited. ACCC indicative timeline suspended.
14-Oct-2009	Former proposed date for announcement of ACCC's findings, deferred to allow additional time for Gunns to respond to the ACCC information request of 29 September 2009. ACCC received further information from Gunns. ACCC timeline recommenced.
28-Oct-2009	ACCC published a Statement of Issues outlining preliminary competition concerns.
03-Nov-2009	ACCC requested further information from Gunns and ITC Timber. ACCC timeline suspended.
09-Nov-2009	ACCC received further information from ITC Timber.
11-Nov-2009	Closing date for submissions from interested parties in response to Statement of Issues.
12-Nov-2009	Gunns provided a partial response to the ACCC's information request of 3 November 2009.
16-Nov-2009	Gunns provided the balance of the information requested by the ACCC on 3 November 2009. ACCC timeline recommenced.
25-Nov-2009	ACCC announced it would oppose the proposed acquisition.
26-Nov-2009	Gunns submitted a revised proposal that did not include the SmartFibre wood chip joint venture asset.
27-Nov-2009	ACCC announced it would not oppose the revised proposed acquisition.

Market inquiries

28. The ACCC conducted extensive market inquiries in relation to the proposed acquisition. A range of interested parties provided responses including competing producers of hardwood sawn timber products and wood chips, key customers of Gunns and ITC Timber, suppliers of sawlog, pulpwood and residual timber, government bodies and industry associations.

Statement of Issues

29. On 28 October 2009, the ACCC published a Statement of Issues regarding the proposed acquisition. The Statement of Issues identified a number of competition concerns arising with respect to the proposed acquisition, including one issue categorised as an issue of concern, three issues categorised as issues that may raise concerns requiring further analysis, and three further issues categorised as issues that are unlikely to pose concerns
30. The ACCC formed the preliminary view that the proposed acquisition was likely to have the effect of substantially lessening competition in the market for acquisition of hardwood pulpwood in north-eastern Tasmania. The ACCC's preliminary view was that, post-acquisition, there would remain only one significant wood chip manufacturer independent of the merged firm, Artec Pty Ltd, acquiring pulpwood in the region, where entry appeared unlikely.
31. The ACCC also formed the preliminary view that the proposed acquisition may raise competition concerns in relation to the market for the acquisition of residual timber in north-eastern Tasmania and the markets for the acquisition of appearance grade and structural grade hardwood sawlog in southern and north-eastern Tasmania. It was considered that suppliers of residual timber and hardwood sawlog in these markets would face a significant reduction in the number of actual and potential buyers available to them.
32. Finally, the ACCC formed the preliminary view that the proposed acquisition was unlikely to pose competition concerns in the following markets:
 - the national market for the manufacture and supply of appearance grade hardwood timber products;
 - the national market for the manufacture and supply of structural grade hardwood and softwood timber products; and
 - the global market for the manufacture and supply of wood chips.
33. The Statement of Issues is available on the ACCC's website at www.accc.gov.au/statementsofissues.
34. This Public Competition Assessment will focus on the areas identified as raising concerns in the Statement of issues, namely the market for the acquisition of hardwood pulpwood in north-eastern Tasmania, the market for the acquisition of residual timber in north-eastern Tasmania and the markets for the acquisition of hardwood sawlog in southern and north-eastern Tasmania.

Areas of overlap

35. The operations of Gunns and ITC Timber overlap in the following areas:
- the manufacture and supply of appearance grade and structural grade hardwood timber products in Australia;
 - the manufacture and supply of wood chips to overseas customers;
 - the acquisition of hardwood sawlog in southern and north-eastern Tasmania for the manufacture of appearance grade hardwood timber products;
 - the acquisition of hardwood pulpwood in north-eastern Tasmania;¹ and
 - the acquisition of residual timber in north-eastern Tasmania.

Market definition

36. Having regard to the areas of overlap between the parties, the ACCC considered the proposed acquisition and the revised proposed acquisition in the context of the following relevant markets:
- the national market for the supply of appearance grade hardwood timber products;
 - the national market for the supply of structural grade timber products (comprising both softwood and hardwood structural timber products);
 - the global market for the manufacture and supply of wood chips;
 - the southern Tasmanian market for the acquisition of hardwood sawlog that is suitable for the manufacture of appearance grade hardwood timber products;
 - the north-eastern Tasmanian market for the acquisition of hardwood sawlog that is suitable for the manufacture of appearance grade hardwood timber products;
 - the north-eastern Tasmanian market for the acquisition of hardwood pulpwood; and
 - the north-eastern Tasmanian market for the acquisition of residual timber.

Acquisition of hardwood pulpwood in north-eastern Tasmania

37. As outlined above, hardwood pulpwood is produced from native or plantation logs and used for the manufacture of wood chips.
38. The ACCC took the view, based on market inquiries, that there are no close supply-side substitution possibilities for hardwood pulpwood. The ACCC found that it would take a considerable length of time for suppliers of hardwood

¹ There was also a small *de minimus* overlap between the operations of the parties in the acquisition of softwood pulpwood.

pulpwood to change their stock of logs or the output of their land. Accordingly, it was found that a small but significant decrease in prices for pulpwood was unlikely to result in suppliers switching a significant proportion of production to a different category of log or another agricultural output.

39. Similarly, the ACCC took the view, based on market inquiries, that there are no close demand side substitutes for hardwood pulpwood. The ACCC considered it unlikely that acquirers of other timber products, such as acquirers of softwood pulpwood, rotary veneer mills, bio-fuel customers or hardwood sawmills would switch to acquiring hardwood pulpwood in response to a small but significant reduction in its price. Market inquiries indicated that quality differences, distinct production processes and the need for significant capital investment would prevent such acquirers from switching in response to a small but significant price reduction. Accordingly, the ACCC considered the appropriate product dimension to be the acquisition of hardwood pulpwood.
40. Market inquiries indicated freight costs generally prohibit transporting logs beyond distances of 200km. Accordingly, the ACCC considered the appropriate geographic dimension to be confined to the market for the acquisition of hardwood pulpwood in north-eastern Tasmania, centring around wood chip mills in the Bell Bay area.

Acquisition of residual timber in north-eastern Tasmania

41. As residual timber is a by-product of sawn timber production and timber harvesting, the ACCC took the view that there are no close supply-side substitution possibilities for residual timber. Suppliers are unlikely to switch their production processes in response to changes in the price they receive for a by-product. Similarly, market inquiries did not identify any categories of customer that could commence acquiring residual timber if there was a small but significant reduction in its price. Accordingly, the ACCC considered the appropriate product dimension to be residual timber.
42. Market inquiries indicated freight costs generally prohibit transporting residual timber beyond distances of 200km. Accordingly, the ACCC considered that the relevant geographic dimension of this market was confined to the market for the acquisition of residual timber in north-eastern Tasmania.

Acquisition of appearance grade hardwood sawlog in southern and north-eastern Tasmania respectively

43. Hardwood sawlog which is used in the production of appearance grade hardwood timber products is usually the highest quality or grade of sawlog, containing a consistent grain with limited knots or natural markings. While such sawlog is harvested together with logs of inferior quality, sawmills with a focus on the production of appearance grade timber products (such as those of Gunns and ITC Timber) typically acquire the highest quality category of logs available for

harvest. Accordingly, the ACCC's analysis focused on hardwood sawlog that is suitable for the manufacture of appearance grade timber products.²

44. Market inquiries confirmed that there were unlikely to be any close supply-side substitution possibilities for suppliers of hardwood sawlog that is suitable for the manufacture of appearance grade timber products. The ACCC found that it would take a considerable length of time for suppliers of hardwood sawlog to change their stock of logs or the output of their land. Accordingly, it was found that a small but significant decrease in prices for hardwood sawlog that is suitable for the manufacture of appearance grade timber products was unlikely to result in suppliers switching a significant proportion of production to a different category of log or another agricultural output.
45. Similarly, the ACCC took the view, based on market inquiries, that there are no close demand side substitutes for hardwood sawlog that is suitable for the production of appearance grade hardwood timber products. The ACCC considered it unlikely that other categories of customer, such as acquirers of pulpwood, peeler log or other categories of sawlog, would commence acquiring hardwood sawlog that is suitable for the production of appearance grade hardwood timber products in response to a small but significant reduction in price due to significantly different production processes and equipment used.
46. Accordingly, the ACCC considered the appropriate product dimension of this market to be hardwood sawlog that is suitable for the manufacture of appearance grade timber products.
47. Market inquiries indicated freight costs generally prohibit transporting logs beyond distances of 200km. Accordingly, the ACCC considered the appropriate geographic dimensions of these markets to be confined to the regional market in southern Tasmania and the regional market in north-eastern Tasmania.

Other markets

48. Given that no competition concerns were identified in relation to the other areas of overlap between the merger parties, irrespective of the market definition adopted, the ACCC did not consider it necessary to reach a concluded view with respect to the relevant markets for those areas of overlap. Nevertheless, the ACCC's inquiries indicated the following with respect to market definition.

² The ACCC considered that the markets for the acquisition of structural grade hardwood sawlog identified in the Statement of Issues were not relevant to its consideration of the proposed acquisition after it became apparent that there was no overlap between the merger parties. While the parties produce some structural grade timber products in Tasmania, it is only as a by-product of manufacturing appearance grade timber products.

Manufacture and supply of appearance grade hardwood timber products

49. Appearance grade hardwood timber products are used for application in timber flooring, joinery, panelling, interiors and furniture. The ACCC took the view, based on market inquiries, that there are no close demand or supply side substitutes for appearance grade hardwood timber products. For example, most customers would be unlikely to switch to softwood timber products if there was a small but significant increase in the price of hardwood products, since softwood timber is more susceptible to scratching and indentation.
50. Given that both Gunns and ITC Timber distribute their appearance grade hardwood timber products nationally, the ACCC considered that the relevant market was likely to be the national market for the supply of appearance grade hardwood timber products.

National market for the supply of structural grade timber products

51. Structural grade hardwood timber products are used primarily in residential construction for timber framing. In contrast to appearance grade hardwood timber products, market inquiries indicated that softwood structural grade timber products are likely to be a close demand side substitute for hardwood structural grade timber products.
52. Given that both Gunns and ITC distribute their structural grade hardwood products nationally, the ACCC considered that the relevant market was likely to be the national market for the supply of structural grade timber products (comprising both softwood and hardwood timber products).

Global market for the manufacture and supply of wood chips

53. Given that wood chips are frequently shipped vast distances from the place of production to the pulp and paper mill and approximately 80% of all wood chips manufactured in Australia are supplied to export markets, the ACCC considered that the relevant market was likely to be the global market for the manufacture and supply of wood chips.

Competition analysis

Acquisition of hardwood pulpwood in north-eastern Tasmania

54. The ACCC found that the proposed acquisition was likely to have the effect of substantially lessening competition in the market for the acquisition of hardwood pulpwood logs in north-eastern Tasmania. In particular, the ACCC found that the merged firm would have been likely to be able to impose a significant and non-transitory reduction in prices paid to private land and private plantation owners, which constitute a significant section of the relevant market.

55. The merged firm would have accounted for a substantial share of the hardwood pulpwood acquired in north-eastern Tasmania. Post acquisition, there would have remained only one significant wood chip manufacturer independent of the merged firm acquiring pulpwood in the relevant area, Artec Pty Ltd (**Artec**).

Availability of substitutes

56. The ACCC took the view that competitors such as Artec were unlikely to effectively constrain the merged firm from achieving a significant and sustained reduction in prices being paid to independent pulpwood suppliers in north-eastern Tasmania. Competitors typically acquire lower priced, lower quality native pulpwood, for the manufacture of a lower grade wood chip. Furthermore, the ACCC's market inquiries indicated that competitors were unlikely to commence acquiring higher quality pulpwood or higher volumes of pulpwood in competition with the merged firm, due to difficulties in obtaining customer contracts without access to a secure supply of higher quality logs from Forestry Tasmania or large plantation managers such as Gunns or FEA.
57. The ACCC considered that FEA was unlikely to constrain the merged firm due to its 50-50 SmartFibre joint venture with the merged firm. The ACCC considered it likely that FEA would independently recognise a mutual incentive for the merged firm to assume responsibility for purchasing the pulpwood SmartFibre requires from independent suppliers, having regard to Gunns' existing purchasing volumes and contacts. Gunns' 50 per cent ownership of SmartFibre would also have given Gunns access to competitively sensitive information regarding SmartFibre's pulpwood purchasing arrangements (including prices and volumes).

Barriers to entry

58. The ACCC also considered it unlikely that new entry in the manufacture of wood chips would provide an effective competitive constraint on the merged firm. Notwithstanding the example of SmartFibre's entry in the manufacture of wood chips in 2003, market inquiries indicated that sunk costs, access to ports, obtaining overseas customer contracts, lead times and regulatory approvals (including environmental approvals) are likely to limit any constraint provided by the threat of entry in the foreseeable future. Entry would be particularly unlikely in the absence of a secure supply of hardwood pulpwood logs from Forestry Tasmania or large plantation managers such as Gunns or FEA, and as such the ACCC considered the threat of entry to be unlikely to prevent a significant and sustained reduction in prices being paid to independent pulpwood suppliers in north-eastern Tasmania.

Countervailing power

59. The ACCC found that Forestry Tasmania, as the largest supplier of hardwood pulpwood in the region, may have the ability to guarantee the volumes of hardwood pulpwood and the certainty of supply to underwrite prospective entry or expansion in wood chipping. Accordingly, the ACCC found that Forestry Tasmania has some countervailing power that would insulate it from any attempt by the merged firm to reduce the price it pays Forestry Tasmania for hardwood pulpwood. In contrast, the ACCC found that the remaining smaller private land and private plantation owners, which supply a material proportion of the demand for pulpwood in the region, are unlikely to have any countervailing power.

Removal of a vigorous and effective competitor

60. Market inquiries strongly suggested that Gunns and SmartFibre are each other's closest competitors for the acquisition of pulpwood in the relevant region and rivalry between Gunns and SmartFibre tends to increase the prices received by private land and private plantation owners for the hardwood pulpwood logs they supply. The proposed acquisition of SmartFibre by Gunns would have removed or significantly diminished this rivalry, resulting in lower prices.

Conclusion

61. Since independent pulpwood suppliers constitute a significant section of the relevant market, the ACCC considered that the reduction in competition resulting from the proposed acquisition would constitute a substantial lessening of competition in the market for the acquisition of hardwood pulpwood logs in north-eastern Tasmania for the purposes of section 50. Accordingly, the ACCC opposed the proposed acquisition. The ACCC was less concerned about the likely impact of the proposed acquisition on Forestry Tasmania.
62. By excluding ITC Timber's 50 per cent stake in the SmartFibre joint venture, the revised proposed acquisition addressed the ACCC's competition concerns in relation to the market for the acquisition of hardwood pulpwood in north-eastern Tasmania. Under the independent joint ownership of Elders and FEA, SmartFibre will continue to provide competition to Gunns in the acquisition of hardwood pulpwood in north-eastern Tasmania.

Acquisition of residual timber in north-eastern Tasmania

63. Given that the proposed acquisition was likely to substantially lessen competition in the market for hardwood pulpwood in north-eastern Tasmania and would be opposed on that basis, the ACCC did not consider it necessary to form a concluded view on the impact of the proposed acquisition on competition in the acquisition of residual timber in north-eastern Tasmania. However, the ACCC's inquiries indicated that the proposed acquisition was less likely to raise concerns in this market.

64. The merged firm would have accounted for a significant proportion of the residual timber consumed in north-eastern Tasmania. However, both Gunns and SmartFibre source the vast majority of their residual timber requirements internally. Market inquiries also indicated that suppliers of residual timber have access to a greater number of outlets for the sale of their product than do suppliers of hardwood pulpwood. In particular, agricultural, landscaping and industrial customers (which use residual timber as bio-fuel) were likely to continue to compete with the merged firm for the acquisition of residual timber from sawmills.
65. In any event, by excluding ITC Timber's 50 per cent stake in the SmartFibre joint venture, the revised proposed acquisition addressed the ACCC's competition concerns in relation to the market for the acquisition of residual timber in north-eastern Tasmania. Under the independent joint ownership of Elders and FEA, SmartFibre will continue to provide competition to Gunns in the acquisition of residual timber in north-eastern Tasmania.

Acquisition of appearance grade hardwood sawlog in north-eastern and southern Tasmania

66. The ACCC considered that the revised proposed acquisition³ was unlikely to have the effect of substantially lessening competition in the north-eastern and southern Tasmanian markets for the acquisition of hardwood sawlog suitable for the manufacture of appearance grade hardwood timber products.

Availability of substitutes

67. The merged firm would be a significant acquirer of hardwood sawlogs suitable for the manufacture of appearance grade hardwood timber products in both north-eastern and southern Tasmania. However, the majority of the hardwood sawlogs acquired by the merged firm would be sourced from Forestry Tasmania.
68. In relation to the potential impact of the revised proposed acquisition on Forestry Tasmania, the ACCC found that the merged firm would face competition in the acquisition of hardwood sawlog suitable for the manufacture of appearance grade hardwood timber products from several smaller alternative buyers in both north-eastern and southern Tasmania. Market inquiries indicated that these alternative buyers have both the desire and the capacity to significantly increase the volumes of hardwood sawlog they acquire from Forestry Tasmania.
69. The ACCC also found that competition from these smaller alternative buyers would constrain the prices paid by the merged firm to private land and private plantation owners for the small volumes of hardwood sawlog suitable for the manufacture of appearance grade timber products that they supply in the relevant regions.

³ The revision to the transaction did not impact on the market for the acquisition of appearance grade hardwood sawlog in north-eastern and southern Tasmania. Accordingly the ACCC's views on these markets apply equally to the original proposed acquisition.

70. As a consequence, the ACCC took the view that suppliers would be well placed to resist any attempt by the merged firm to achieve a significant and sustained reduction in the prices it pays for hardwood sawlog in north-eastern and southern Tasmania.

Countervailing power

71. The ACCC also considered Forestry Tasmania likely to have some degree of countervailing power arising from its scale and its ability to guarantee sufficient volumes of hardwood sawlog to a prospective entrant to hardwood sawmilling. As discussed below, the ACCC found that Forestry Tasmania's countervailing power in hardwood sawmilling was not likely to be limited by the presence of other barriers to entry as was the case for hardwood pulpwood.

Barriers to entry

72. In contrast to entry into hardwood wood chipping, market inquiries indicated that there is a credible threat of entry in hardwood sawmilling (with Forestry Tasmania sponsorship) which is likely to provide an effective competitive constraint. Entry into hardwood sawmilling can be done on a smaller scale and with less sunk cost than entry into hardwood wood chipping and does not require port access or overseas contracts.

Conclusion

73. The ACCC considered that the merged firm would be constrained in the southern and north-eastern Tasmanian markets for the acquisition of hardwood sawlog that is suitable for the manufacture of appearance grade timber products by several alternative buyers as well as the credible threat of entry in hardwood sawmilling. Moreover, the major supplier of hardwood sawlog, Forestry Tasmania, is likely to have some degree of countervailing power.
74. The ACCC therefore concluded that the proposed acquisition and revised proposed acquisition would be unlikely to result in a substantial lessening of competition in the markets for the acquisition of hardwood sawlog that is suitable for the manufacture of appearance grade timber products in southern and north-eastern Tasmania.

Other markets

75. The ACCC considered that the revised proposed acquisition would be unlikely to have the effect of substantially lessening competition in the following markets:
- the national market for the supply of appearance grade hardwood timber products;
 - the national market for the supply of structural grade timber products (comprising both softwood and hardwood structural timber products); and
 - the global market for the manufacture and supply of wood chips.

76. The ACCC considered that there are a large number of alternative suppliers in these markets which would continue to provide an effective competitive constraint on the merged firm post-acquisition.

Conclusion

77. The ACCC concluded that the proposed acquisition by Gunns of ITC Timber's 50 per cent stake in the SmartFibre wood chip joint venture would be likely to substantially lessen competition in the market for the acquisition of hardwood pulpwood in north-eastern Tasmania. On this basis, the ACCC announced its intention to oppose the proposed acquisition on 25 November 2009.
78. As a result of the parties' restructuring the proposed acquisition to address the ACCC's concerns, SmartFibre will remain an independent competitor to Gunns in the acquisition of pulpwood. With the exclusion of SmartFibre, the ACCC's competition concerns with the proposed acquisition have been addressed.
79. The ACCC concluded that both the proposed acquisition and revised proposed acquisition would be unlikely to result in a substantial lessening of competition in the markets for the acquisition of hardwood sawlog in southern and north-eastern Tasmania or any of the other relevant markets identified.
80. The ACCC was therefore satisfied that the revised proposed acquisition of ITC Timber by Gunns, after taking account of the exclusion of the stake in the SmartFibre wood chip joint venture, was unlikely to substantially lessen competition in any markets and on this basis, unlikely to breach section 50 of the Act.