



Public Competition Assessment

30 July 2009

Rheem Australia Pty Ltd – proposed acquisition of Aqua-Max Pty Ltd

A Introduction

1. On 23 June 2009, the Australian Competition and Consumer Commission (ACCC) announced its decision not to oppose the proposed acquisition by Rheem Australia Pty Ltd of the water heater business of Aqua-Max Pty Ltd, from Sietel Ltd (the **proposed acquisition**). The ACCC was of the view that the proposed acquisition would not be likely to have the effect of substantially lessening competition in any relevant market in contravention of section 50 of the *Trade Practices Act 1974* (the **Act**).
2. 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, subject to confidentiality considerations.

B Public competition assessment

3. 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.
4. This Public Competition Assessment has been issued because the proposed acquisition is considered to raise issues of interest to the public.
5. 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 the

circumstances where the ACCC's assessment of the competition conditions in particular markets is changing, or likely to change, because of developments.

6. 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.
7. 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.

C The parties

The acquirer – Rheem Australia Pty Ltd

8. Rheem Australia Pty Ltd (**Rheem**) is a wholly-owned subsidiary of Paloma Co Ltd (**Paloma**), a leading international producer of gas-fuelled water heaters, boilers and other consumer appliances based in Japan.
9. Rheem began manufacturing and supplying water heaters in Australia in the late 1930s, and is currently the largest manufacturer and supplier of water heaters in Australia. Rheem manufactures, imports and supplies a complete range of water heaters for residential and commercial use, including electric storage water heaters (**ESWH**), gas storage water heaters (**GSWH**), instantaneous gas water heaters (**IGWH**), solar water heaters and heat pump water heaters (together referred to as **renewable water heaters**). The water heater brands distributed by Rheem in Australia include *Rheem, Solahart, Edwards, Vulcan, Raypak, Paloma, and Everhot*.
10. Rheem distributes its water heater products to retail customers through plumbing and building supply merchants, energy retailers and plumbing supplies buying groups. Rheem's Australian manufacturing sites are located in Rydalmere and Liverpool in New South Wales, Welshpool and Canning Vale in Western Australia, and Scoresby in Victoria.

The target – Aqua-Max Pty Ltd

11. Aqua-Max Pty Ltd (**Aqua-Max**) is a wholly-owned subsidiary of the Australian investment firm, Sietel Ltd (**Sietel**), which is listed on the Australian Stock Exchange (**ASX**).

12. Aqua-Max began manufacturing and supplying water heaters in Australia in the early 1990s. Aqua-Max manufactures and supplies a limited range of water heaters for residential use, including ESWHs, GSWHs (in the 5 star energy efficiency rated product range only) and a small volume of solar water heaters, under the *Aqua-Max* brand.
13. Aqua-Max distributes its water heater products to retail customers through plumbing and building supply merchants, energy retailers and plumbing supplies buying groups. Aqua-Max's only Australian manufacturing site is located in Moorabbin, Victoria.

D Other industry participants

14. In addition to Rheem and Aqua-Max, there are a number of water heater suppliers in Australia. These are discussed in turn.

Dux Pty Ltd

15. Dux Pty Ltd (**Dux**) is a wholly-owned subsidiary of the Australian firm GWA International Ltd, which is listed on the ASX. Dux is one of Australia's largest designers, manufacturers, importers and distributors of household consumer products.
16. Dux has been manufacturing and supplying water heaters in Australia since 1915, and is currently the second largest manufacturer and supplier of water heaters in Australia. Dux manufactures, imports and supplies a complete range of water heaters for residential and commercial use.
17. Dux distributes its water heater products under the *Dux* and *Radiant* brands to retail customers mainly through plumbing and building supply merchants, energy retailers and plumbing supplies buying groups.

Rinnai Australia Pty Ltd

18. Rinnai Australia Pty Ltd (**Rinnai**) is a wholly-owned subsidiary of Rinnai Corporation, which is a significant international manufacturer and supplier of gas appliances, including water heaters, based in Japan.
19. Rinnai manufactures, imports and supplies a limited range of water heater products for residential and commercial use, including significant volumes IGWHs (in respect of which it is currently the leading Australian supplier), as well as smaller volumes of ESWHs and solar water heaters.
20. Rinnai distributes its water heater products under the *Rinnai* brand to retail customers through plumbing and building supply merchants, energy retailers and plumbing supplies buying groups.

Robert Bosch (Australia) Pty Ltd

21. Robert Bosch (Australia) Pty Ltd (**Bosch**) is a wholly-owned subsidiary of Robert Bosch GmbH, a significant international manufacturer and supplier of products

and services to a range of industries (including the automotive, industrial and building sectors) based in Germany. Robert Bosch GmbH is a significant international manufacturer and supplier of commercial and consumer goods, including water heaters.

22. Bosch imports and supplies a limited range of water heaters for residential and commercial use, including IGWHs (in respect of which it is currently the second largest Australian supplier).
23. Bosch distributes its water heater products under the *Bosch* brand to retail customers through plumbing and building supply merchants, energy retailers and plumbing supplies buying groups.

Chromagen Solar Australia Pty Ltd

24. Chromagen Solar Australia Pty Ltd (**Chromagen**) is a private Australian company that holds the Australian rights to import and distribute the water heater products of Chromagen Ltd, a significant international manufacturer and supplier of solar water heaters based in Israel.
25. Chromagen imports and supplies a limited range of water heaters for residential use, including solar water heaters and a small volume of IGWHs (typically for use as boosters for their solar water heater systems, but also as stand-alone water heaters). Chromagen currently has no manufacturing facilities in Australia.
26. Chromagen distributes its water heater products under the *Chromagen* brand to retail customers, mainly through large volume builders and direct-to-public retail outlets.

Peter Sachs Industries Pty Ltd

27. Peter Sachs Industries Pty Ltd (trading as **Saxon**) is a private Australian company involved in the manufacture and supply of water heating products for residential, commercial and marine applications.
28. Saxon manufactures and supplies a limited range of water heaters, including ESWHs and renewable water heaters.
29. Saxon distributes water heaters under the *Saxon* brand to retail customers, mainly through plumbing and building supply merchants, energy retailers and plumbing supplies buying groups.

Quantum Energy Technology Pty Ltd

30. Quantum Energy Technology Pty Ltd (**Quantum**) is a wholly-owned subsidiary of Quantum Energy Limited, an Australian publicly listed company with patented proprietary heat pump water heater technology.
31. Quantum manufactures and supplies a range of heat pump water heaters for residential and commercial use, pool heaters, and space heaters for residential, commercial and industrial use.

32. Quantum distributes water heaters under the *Quantum* brand to retail customers, mainly through mainly through plumbing and building supply merchants, energy retailers, plumbing supplies buying groups, and large volume builders.

Table 1: Summary of the types of water heaters supplied in Australia, by supplier

<i>Supplier</i>	ESWH	GSWH	IGWH	Solar	Heat Pump
Rheem	✓	3 and 5 ★	✓	✓	✓
Aqua-Max	✓	5 ★ only	✗	✓	✗
Dux	✓	3 and 5 ★	✓	✓	✓
Rinnai	✓	✗	✓	✓	✗
Bosch	✗	✗	✓	✗	✗
Chromagen	✗	✗	✓	✓	✗
Saxon	✓	✗	✗	✓	✓
Quantum	✗	✗	✗	✗	✓

Areas where the water heater businesses of Rheem and Aqua-Max overlap

33. As highlighted in Table 1 above, Rheem and Aqua-Max overlap in relation to the manufacture and supply of ESWHs, GSWHs (in the 5-star rated product range only) and, to a lesser extent, solar water heaters, for residential use.

E ACCC review timeline

34. The ACCC’s timeline for the review of the proposed acquisition is outlined in Table 2 below.

Table 2: Timeline of key events

Date	Event
23 February 2009	ACCC commenced its review under the Merger Review Process Guidelines.
6 March 2009	Closing date for submissions from interested parties.
20 March 2009	ACCC timeline suspended pending receipt of further information from the merger parties.
3 April 2009	ACCC received further information from the merger parties, ACCC timeline recommenced.
22 April 2009	ACCC published a Statement of Issues outlining preliminary competition concerns.
13 May 2009	Closing date for submissions relating to Statement of Issues.
19 May 2009	ACCC timeline suspended pending receipt of further information from the merger parties.
12 June 2009	ACCC received further information from the merger parties. ACCC timeline recommenced.
23 June 2009	ACCC announced it would not oppose the proposed acquisition.

F Market inquiries

35. As a part of the ACCC’s investigation, submissions were sought in relation to each of the substantive competition issues from the merger parties, customers, competitors, importers, representative industry bodies, Commonwealth and state and territory government departments, and other relevant market participants.

G Regulatory environment

36. In its review of the proposed acquisition, the ACCC had regard to the regulatory environment surrounding the water heater industry in Australia. In particular, the ACCC considered the Renewable Energy Certificates (RECs) Scheme¹ as well as rebate programs offered by the Commonwealth and state and territory governments.
37. The ACCC also took into account the existing regulatory environment and proposed regulatory developments with respect to the phasing out of ESWHs and lower efficiency GSWHs at the Commonwealth Government and state and territory government levels, in relation to certain categories of consumers.

Government rebates

38. As indicated above, there are a number of rebates currently available at the Commonwealth and state and territory government levels designed to encourage the take-up of more energy efficient water heater options.
39. Under the 'Energy Efficient Homes Package – Solar Hot Water Rebate', the Commonwealth Government offers a \$1600 rebate for the installation of a renewable water heater to replace an existing ESWH, subject to certain eligibility requirements.²
40. Each state and territory government offers rebates for replacing less energy efficient water heater types with more energy efficient water heater types in certain types of households, subject to meeting certain eligibility requirements.³

The existing regulatory environment and proposed regulatory developments

State governments

41. There are existing (and some proposed) regulations banning the installation of particular water heater types at the state level, as outlined below.
42. Existing and proposed state government prohibitions on the installation of all GSWHs with an efficiency rating of less than 5 stars currently only apply to detached, semi-detached, row and terrace homes (**Class 1 homes**) in certain states, as outlined in Table 3 below.

¹ RECs are established under the *Renewable Energy (Electricity) Act 2000 (Cth)*. RECs are an electronic, tradeable commodity equivalent to one megawatt hour of renewable energy generation. Typically, the value of the RECs attributable to a renewable water heater is deducted from the upfront purchase price of the relevant water heater by retailers (who then trade the RECs on their own account).

² The Commonwealth's "Energy Efficient Homes Package – Solar Hot Water Rebate" was made available from 3 February 2009. The Commonwealth previously offered a \$1000 rebate for the replacement of an existing ESWH with an eligible solar or a heat pump heater under the "Solar Hot Water Rebate Program", which was made available between 18 July 2007 and 3 February 2009.

³ The relevant dates from which the specific state and territory government commenced offering rebates are as follows: New South Wales from 1 October 2007, Victoria from 1 July 2007, Queensland from 7 January 2006, South Australia from 1 July 2008, Western Australia from 31 May 2006, the Australian Capital Territory from 1 January 2005, the Northern Territory from 28 June 2009, and Tasmania from 1 July 2007.

Table 3: Summary of existing and proposed state government prohibitions on the installation of GSWHs rated less than 5 stars

State	Prohibition Start Date		Areas where prohibitions apply
	New Class 1 Homes	Established Class 1 Homes	
Queensland	1 March 2006	1 January 2010	Areas with access to reticulated gas
South Australia	1 July 2008	1 July 2008	Areas with and without access to reticulated gas
Western Australia	1 September 2007	Not applicable	Areas with and without access to reticulated gas

43. Existing and proposed state government prohibitions on the installation of ESWHs currently only apply to Class 1 homes in certain states, as outlined in Table 4 below.

Table 4: Summary of existing and proposed state government prohibitions on the installation of ESWHs

State	Prohibition Start Date		Areas where prohibitions apply
	New Class 1 Homes	Established Class 1 Homes	
Queensland	1 March 2006	1 January 2010	Areas with access to reticulated gas
South Australia	1 July 2006	1 July 2009 (for Adelaide only)	Areas with access to reticulated gas (for new homes), and in both areas with and without access to reticulated gas (for established homes)
Western Australia	1 September 2007	Not applicable	Areas with access to reticulated gas
Victoria	1 July 2005	Not applicable	Areas with access to reticulated gas

44. Additionally, in Victoria (since 1 July 2007), the installation of renewable water heaters has been actively encouraged for new homes, with all new Class 1 dwellings required to install either a water tank or a solar water heater.

The Commonwealth Government

45. The ACCC noted that there are currently no regulations in place at the Commonwealth Government level imposing restrictions on the types of water heaters that consumers are permitted to install in their homes.
46. The Ministerial Council on Energy (MCE)⁴ has indicated that certain proposed regulatory developments are likely to occur in the short to medium term in relation to the water heater industry, and which are intended to apply on a national basis (the **proposed regulatory developments**). The likely form of the proposed regulatory developments is outlined below.

⁴ The MCE was established by the Council of Australian Governments (COAG) in 2001 to deliver the economic and environmental benefits for Australia from implementation of the COAG national energy policy framework. The MCE is the national policy and governance body for the Australian energy market, including for electricity and gas (see <http://www.ret.gov.au/Documents/mce/about/default.html>).

Minimum Energy Performance Standards for GSWHs

47. The MCE proposes to impose Minimum Energy Performance Standards on gas water heaters. The new regulation proposes to phase out 3 star rated GSWHs by imposing a minimum 4 star rating standard, which will impact all new and established homes. It is proposed that the regulation will take effect during the second half of 2010.

ESWHs in new homes

48. During 2010, the Australian Building Codes Board (**ABCB**) proposes to introduce regulations into the Building Code of Australia (**BCA**) to phase out ESWHs in all new Class 1 homes.
49. The ABCB will also consider the introduction of new regulations into the BCA to phase-out ESWHs in all new homes categorised as flats and apartments (**Class 2 homes**) with access to reticulated gas. These new regulations may come into effect during 2012.

ESWHs in existing homes

50. During 2010, the MCE proposes to begin phasing out ESWHs in all existing Class 1 homes with access to reticulated gas, with the exception of Tasmania. It is also probable that Class 2 homes may be excluded from this phase out.
51. During 2012, the MCE proposes to phase out ESWHs in all established Class 1 homes without access to reticulated gas, with the exception of Tasmania. It is also probable that Class 2 homes may be excluded from this phase out.

Interaction between the Commonwealth Government and state government regulations in relation to water heaters

52. Importantly, inquiries conducted by the ACCC indicated that where the regulations of a state government differ from those enacted at the Commonwealth Government level, the regulations referable to that state or territory may continue to apply, particularly where a higher standard applies. For example, where a state government already applies a higher minimum star rating standard for the installation of GSWHs (such as in Queensland, South Australia and Western Australia), the higher minimum star rating standard may continue to apply in that state or territory.

H Statement of Issues

53. The ACCC published a Statement of Issues on 22 April 2009 identifying a number of potential competition issues. The Statement of Issues sought further comments from market participants on the market definition adopted by the ACCC (see below) and on the ACCC's preliminary view that the proposed acquisition:
 - *was likely to raise concerns* in the ESWH segment of the national water heater market; and

- *may raise concerns* in the GSWH segment of the national water heater market.

54. The Statement of Issues in relation to this matter is available on the ACCC website at <http://www.accc.gov.au> under the Mergers Register.

I With/without test

55. In assessing a merger pursuant to section 50 of the Act, the ACCC must consider the effects of the transaction by comparing the likely future state of competition if the transaction proceeds (the “with” or “factual” position) to the likely future state of competition if the transaction does not proceed (the “without” or “counterfactual” position).
56. The ACCC focuses on the foreseeable future when considering both the factual and counterfactual, the market definition, and any likely competitive harm attributable to the proposed acquisition.
57. In considering the likely state of competition in the future without the proposed acquisition, the ACCC had regard to, among other things, the likely impact of the proposed regulatory developments. Although these proposed regulatory developments are anticipated to occur independently of the proposed acquisition, manufacturers of ESWHs and 3 star rated GSWHs are likely to be impacted on by the proposed regulatory developments in the foreseeable future (that is, from 2010 to 2012). However, the ACCC ultimately came to the view that this would be unlikely to have a significant impact on the ongoing viability of market participants in the future without the proposed acquisition.
58. Accordingly, the ACCC considered that, absent the proposed acquisition, Aqua-Max would have remained a viable independent player.
59. The ACCC also considered the possibility that, if the proposed acquisition by Rheem did not proceed, Aqua-Max would be acquired by an alternative party. However, on the basis of available information, the ACCC formed the view that this was unlikely and that, instead, it was likely that Aqua-Max would continue to be owned by Sietel.
60. On this basis, the ACCC concluded that both Rheem and Aqua-Max would continue to compete in the relevant market in the future without the proposed acquisition, albeit with a different product mix as a result of proposed regulatory developments.

J Market definition

61. The ACCC concluded that the relevant market in which to consider the likely effect on competition of the proposed acquisition is the national market for the manufacture and supply of water heaters (the **water heater market**) for the reasons outlined below.

Product dimension

62. Market inquiries suggested that, while most householders replace their existing water heaters with a water heater of the same type, significant substitution between water heater types is occurring. For example, there has been a shift toward IGWH and renewable water heaters driven in part by the different features of IGWH, the environmental benefits of renewable water heaters, government rebates and existing regulatory requirements. The ACCC also considered that substitution between water heater types is likely to increase in the short to medium term as the proposed regulatory developments (should they be enacted as proposed) start to take effect from 2010.
63. The ACCC also recognised, however, that the substitution possibilities between water heater types are not uniform across consumer groups and vary according to switching costs likely to be incurred by specific consumer types and due to other factors such as the ability to access a particular type of fuel source (such as reticulated gas). In this regard, market inquiries indicated that consumers most commonly considered the upfront capital cost as the most important factor in deciding what type of water heater to purchase. A range of other factors, such as the relative ongoing running costs attributable to different fuel sources and water heater types, were also considered by consumers, but to a lesser extent.
64. By way of example, the cost to consumers living in Class 2 homes of replacing an ESWH or a GSWH with an IGWH can be substantial. Likewise, the cost to consumers living in areas without access to reticulated gas of replacing an ESWH with an IGWH can be substantial. These consumers are therefore likely to consider ESWHs and IGWHs as weaker substitutes than those consumers who do have access to reticulated gas.
65. However, despite the lack of uniform substitution possibilities outlined above, recent industry survey evidence scrutinised by the ACCC confirmed that significant consumer switching is occurring across the different water heater types. In particular, inquiries indicated that significant switching is occurring from ESWHs and GSWHs to IGWHs and renewable water heaters (reflecting growth products within the water heater market), primarily due to the factors outlined at paragraph 62 above.
66. On balance, the ACCC formed the view that the information available supported the adoption of a single product market for water heaters.

Geographic dimension

67. Given the national approach to pricing and distribution adopted by water heater manufacturers, the ACCC considered the proposed acquisition in the context of a national market.

K Competition analysis

The water heater market

68. The proposed acquisition will result in the removal of an independent competitor, in the form of Aqua-Max, from the national water heater market. As highlighted in Table 1 above, the operations of Rheem and Aqua-Max overlap primarily in relation to the manufacture and supply of ESWHs, 5 star rated GSWHs and, to a lesser extent, solar water heaters, for residential use.
69. In the course of its review of the proposed acquisition, the ACCC identified the following key characteristics of the water heater market:
- new entry in relation to the manufacture and supply of water heaters was unlikely, mainly due to the presence of very large established incumbent suppliers, the lead time and cost associated with establishing new domestic manufacturing facilities, and obtaining the requisite regulatory water heater product approvals (for both domestic and imported products). Additionally, the mature nature of the ESWH and 3 star rated GSWH segments of the water heater market, meant that new entry or expansion in those segments was unlikely;
 - imports of water heaters, other than IGWHs and smaller capacity ESWHs (significant volumes of which are currently imported), comprise a small proportion of the national market for water heaters; and
 - customers for the supply of water heaters appear to have limited or no countervailing power.
70. However, inquiries indicated barriers to expansion for existing market participants in relation to the manufacture and supply of water heaters (other than ESWHs and 3 star rated GSWHs) were not high, mainly since existing market participants:
- operate domestic water heater manufacturing facilities that would be likely to be in a position to readily expand. Inquiries indicated that the associated time and cost for the expansion of existing manufacturing facilities are not significant, given that regulatory approvals have already been obtained for the water heater products currently supplied by those existing market participants; and/or
 - have the ability to readily increase water heater import volumes.
71. The ACCC therefore considered that the merged firm is likely to be constrained in its post-acquisition pricing for water heaters as a result of the ability of consumers to switch to an independent domestic manufacturer or importer in the event of a significant price increase by the merged firm. Relevantly, the ACCC's inquiries indicated that Dux, with its product mix spanning the complete range of water heaters, would be likely to act as a significant competitor to the merged firm post-acquisition. Additionally, Dux would be likely to be in a position to

readily expand its supply of water heaters through increased imports and production at its domestic manufacturing site at Moss Vale, New South Wales.

72. The ACCC considered that other existing independent importers and niche suppliers would also be in a position to constrain the merged firm from raising prices in the water heater market post-acquisition. Specifically, the ACCC noted that:
- Rinnai and Bosch are Australia's leading suppliers of IGWHs, imports of which account for more than 20 per cent of the water heater market;
 - Rinnai would be likely to be in a position to readily expand its supply of IGWHs and ESWHs (in particular its smaller capacity ESWHs of 90L or less (**smaller capacity ESWHs**)) through increased imports. Rinnai would also be in a position to expand its supply of solar water heaters through increased production at its domestic manufacturing site at Devon Park, South Australia;
 - Bosch would be likely to be in a position to readily expand its supply of IGWHs, through increased imports;
 - Chromagen would be likely to be in a position to readily expand its supply of solar water heaters, through increased imports;
 - Quantum would be likely to be in a position to readily expand its supply of heat pump water heaters through increased imports; and
 - Saxon would be likely to be in a position to readily expand its supply of ESWHs (in particular, its smaller capacity ESWHs) and renewable water heaters, through increased production from its domestic manufacturing site at Zillmere, Queensland.
73. As noted above, the ACCC recognised that there is significant growth in both IGWHs and renewable water heaters (see paragraph 62 above).

Products within the water heater market

74. While the ACCC did not identify significant competition concerns in relation to the market for water heaters as a whole, certain preliminary issues were identified in relation to particular products within the water heater market. As indicated above (see paragraph 53 above), the ACCC's inquiries identified preliminary competition concerns in the water heater market as a result of the removal of Aqua-Max as an independent supplier of ESWHs, and due to the reduction in the number of available suppliers of GSWHs in the water heater market as a result of the proposed acquisition.
75. Given these concerns, and the fact that the proposed regulatory developments would likely impact particular products within the water heater market and different consumers of these products in distinct ways, the ACCC considered separately the effect of the proposed acquisition on the supply of ESWHs and GSWHs. In this regard, it is noted that the ACCC considers that firms would generally be deterred from instituting a price increase, or only be able to institute

it for a transitory period, where effective competitive constraints exist or where constraints are likely to become effective within a period of one to two years (see the ACCC's *Merger guidelines*).

Supply of ESWHs

76. As noted above, the proposed acquisition would result in a reduction in the number of available suppliers of ESWHs in the water heater market, with the merged firm and Dux remaining as significant suppliers post-acquisition in addition to the other smaller independent ESWH suppliers.
77. Under the proposed regulatory developments outlined above, ESWHs will be phased out for certain categories of consumers, including those living in Class 1 homes in all states and territories (with the likely exception of Tasmania) by around 2012 (and noting that certain categories of consumers are currently not permitted to install ESWHs in Queensland, South Australia, Western Australia and Victoria, as highlighted in Table 4 above). Therefore, the proposed acquisition is expected to have different effects on competition in the supply of water heaters for each of the following categories of consumers, which are considered separately below:
- established Class 1 homes with access to reticulated gas—where ESWHs are proposed to be phased out from around 2010;
 - established Class 1 homes in areas without access to reticulated gas—where ESWHs are proposed to be phased out from around 2012;
 - established Class 2 homes—where no phase out of ESWHs is proposed for the foreseeable future; and
 - Tasmania—where no phase out of ESWHs is proposed for the foreseeable future.

Established Class 1 homes with access to reticulated gas

78. Taking into account the proposed regulatory developments, consumers in established Class 1 homes with access to reticulated gas (which represent the majority of Australian homes) will not be permitted to install ESWHs after 2010. It is noted, in this context, that any anti-competitive effects likely to arise prior to the proposed regulatory developments and as a result of the consolidation of Rheem and Aqua-Max as suppliers of ESWHs, are likely to be transitory for this consumer category.
79. However, the ACCC considered that the potential for transitory anti-competitive effects to arise prior to the proposed regulatory developments would be limited by the presence of Dux, which would act as a significant constraint on the merged firm in relation to ESWHs during this period. Additionally, the ACCC considered that, to a more limited extent, other independent smaller suppliers of ESWHs, including Rinnai and Saxon would continue to constrain the merged firm, particularly in relation to the supply of smaller capacity ESWHs.

80. Additionally, in light of increased switching from ESWHs to IGWHs and renewable water heaters, and noting that existing incentives in the form of rebates available to certain consumers (such as those replacing existing ESWHs) are likely to continue into the foreseeable future, the ACCC also considered that independent suppliers of IGWHs (such as Rinnai and Bosch) and renewable water heaters (such as Rinnai, Chromagen, Quantum and Saxon) would be likely to constrain the merged firm post-acquisition.
81. The ACCC considered that, if the proposed regulatory developments proceeded as anticipated, customers with access to reticulated gas seeking to replace an existing ESWH beyond 2010 will continue to have a range of alternatives to the merged firm's (non-ESWH) product offering in the form of higher efficiency (5 star) GSWHs, IGWHs and renewable water heaters supplied by existing competitors including Dux, Rinnai, Bosch, Saxon and Chromagen.
82. Accordingly, the ACCC considered that, in relation to this consumer type, the merged firm would be likely to be constrained in its post-acquisition pricing behaviour both prior to and subsequent the proposed regulatory developments, such that the proposed acquisition would be unlikely to result in a substantial lessening of competition.

Established Class 1 homes in areas without access to reticulated gas

83. Taking into account the proposed regulatory developments, consumers in established Class 1 homes without access to reticulated gas (which represent a significant proportion of Australian homes) will not be permitted to install ESWHs from around 2012. It is noted, in this context, that any anti-competitive effects likely to arise prior to the proposed regulatory developments and as a result of the consolidation of Rheem and Aqua-Max as suppliers of ESWHs, are likely to be transitory for this consumer category.
84. However, the ACCC formed the view that the potential for transitory anti-competitive effects prior to the proposed regulatory developments would be limited, as the merged firm would likely be constrained in its post-acquisition pricing for ESWHs given the ability for this category of consumers to switch to alternative suppliers of non-gas-fuelled water heaters during this period.
85. Prior to the proposed regulatory developments, a number of independent water heater suppliers would remain including Dux, Rinnai and Saxon (as suppliers of ESWHs). Additionally, in light of increased switching from ESWHs to renewable water heaters, and noting that existing incentives in the form of rebates available to certain consumers (such as those replacing existing ESWHs) are likely to continue into the foreseeable future, the ACCC also considered that independent suppliers of renewable water heaters including Dux, Rinnai, Chromagen, Quantum and Saxon would likely constrain the merged firm post-acquisition.
86. While the proposed regulatory developments are not anticipated to occur for a further three years, the ACCC also acknowledged that, if the proposed regulatory developments proceeded as anticipated, it would be likely that those customers without access to reticulated gas would continue to have alternatives to the

product offering of the merged firm in the form of renewable water heaters supplied by existing competitors including Dux, Rinnai, Bosch, Saxon and Chromagen.

87. Accordingly, the ACCC considered that, in relation to this consumer type, the merged firm would be likely to be constrained in its post-acquisition pricing behaviour both prior to and subsequent the proposed regulatory developments, such that the proposed acquisition would be unlikely to result in a substantial lessening of competition.

Established Class 2 homes

88. The ACCC also considered the expected competition impact of the proposed acquisition on established Class 2 homes (which represent a smaller proportion of Australian homes than the Class 1 homes noted above), where no phase out of ESWHs is anticipated in the foreseeable future under the proposed regulatory developments.
89. Inquiries indicated that, for the supply of water heaters to this category of consumers, the merged firm was not likely to be constrained in its pricing for ESWHs by the availability of independently sourced gas-fuelled water heaters (IGWHs and GSWHs) due to the specific difficulties associated with replacing an ESWH with a gas-fuelled water heater in Class 2 homes. However, inquiries indicated that the merged firm would likely be constrained in its post-acquisition pricing for ESWHs by the ability for this category of consumers to switch to an independent supplier of ESWHs in the event of a significant price increase by the merged firm. As indicated above, a number of alternative suppliers were identified as having the ability to readily expand their supply of ESWHs, including Dux as a significant competitor to the merged firm for the supply of ESWHs.
90. It is also noted that the ACCC's inquiries indicated that Class 2 homes typically install smaller capacity ESWHs, which take up significantly less space and do not require any other external components. In this context, the ACCC noted that smaller capacity ESWHs are able to be imported on a more commercially viable basis than larger capacity ESWHs. Consequently, smaller independent suppliers of ESWHs, including Rinnai and Saxon, are likely to be in a position to constrain the merged firm's pricing of ESWHs post-acquisition.
91. Accordingly, the ACCC considered that, in relation to this consumer type, the merged firm would be likely to be constrained in its post-acquisition pricing behaviour such that the proposed acquisition would be unlikely to result in a substantial lessening of competition.

Tasmania

92. The ACCC also considered the expected competition impact of the proposed acquisition on households located in Tasmania, where no phase out of ESWHs is proposed for the foreseeable future under the proposed regulatory developments.

93. In the course of its review, the ACCC noted that ESWHs are currently the most common type of water heater in Tasmania due to the availability of hydro-electricity, and may remain so for the foreseeable future should Tasmania be exempt from the proposed regulatory developments to phase out ESWHs.
94. The ACCC considered that the existing levels of competition in Tasmania would be unlikely to change to any significant extent as a result of the proposed acquisition. This was mainly due to Aqua-Max's relatively limited presence in Tasmania for the supply of water heaters, as well as the competitive constraint provided by other independent suppliers of ESWHs (such as Dux, Rinnai and Saxon) in that state, which inquiries indicated was likely to continue post-acquisition.

Supply of GSWHs

95. As noted above, the proposed acquisition would result in a reduction in the number of available suppliers of GSWHs in the water heater market, with only the merged firm and Dux remaining post-acquisition.
96. Taking into account the proposed regulatory developments, consumers living in all areas and all classes of homes will not be permitted to install GSWHs with an efficiency rating of less than 4 stars from around 2010. However, the ACCC also noted that certain categories of consumers in Queensland, South Australia and Western Australia are currently not permitted to install GSWHs rated less than 5 stars (see Table 3 above). It is noted, in this context, that any anti-competitive effects likely to arise prior to the proposed regulatory developments and as a result of the consolidation of Rheem and Aqua-Max as suppliers of GSWHs, are likely to be transitory for consumers.
97. The ACCC did, however, consider the likely competitive impact prior to the regulatory change (while consumers still have access to 3 star rated GSWHs as a water heater option) and formed the view that Dux would act as a significant constraint on the merged firm. While Dux would be the only other remaining supplier of GSWHs post-acquisition, the ACCC noted the increased incidence of switching from GSWHs to IGWHs and renewable water heaters, and that existing incentives in the form of rebates available to certain consumers (such as those installing higher efficiency gas-fuelled water heaters and renewable water heaters) are likely to continue into the foreseeable future. Accordingly, the ACCC considered that independent suppliers of IGWHs (such as Rinnai and Bosch) and renewable water heaters (such as Rinnai, Chromagen, Quantum and Saxon) would be likely to constrain the merged firm post-acquisition.
98. The ACCC also considered that, taking into account the proposed regulatory developments, customers seeking to replace an existing 3 star rated GSWH beyond 2010 will continue to have a range of alternatives to the merged firm's (non-GSWH) product offering in the form of higher efficiency (5 star) GSWHs, IGWHs and renewable water heaters supplied by existing competitors including Dux, Rinnai, Bosch, Saxon and Chromagen.

99. Accordingly, the ACCC considered that, the merged firm would be likely to be constrained in its post-acquisition pricing behaviour both prior to and subsequent the proposed regulatory developments, such that the proposed acquisition would be unlikely to result in a substantial lessening of competition.

Conclusion

100. On the basis of the above, the ACCC formed the view that the proposed acquisition by Rheem of the water heater business of Aqua-Max from Sietel would not be likely to result in a substantial lessening of competition in the national market for the manufacture and supply of water heaters in contravention of section 50 of the Act.