



Australian
Competition &
Consumer
Commission

12 August 2009

Statement of Issues — Pact Group Pty Ltd - proposed acquisition of certain assets from Huhtamaki Australia Pty Ltd

1. Outlined below is the Statement of Issues released by the Australian Competition and Consumer Commission (ACCC) in relation to the proposed acquisition of certain assets of Huhtamaki Australia Pty Ltd by Pact Group Pty Ltd (proposed acquisition).
2. A Statement of Issues published by the ACCC is not a final decision about a proposed acquisition, but provides the ACCC's preliminary views, drawing attention to particular issues of varying degrees of competition concern, as well as identifying the lines of further inquiry that the ACCC wishes to undertake.
3. In line with the ACCC's *Merger Review Process Guidelines* (available on the ACCC's website at www.accc.gov.au) the ACCC has established a secondary timeline for further consideration of the issues. The ACCC anticipates completing further market inquiries by 28 August 2009 and anticipates making a final decision on 16 September 2009. However, the anticipated timeline can change in line with the *Merger Review Process Guidelines*. To keep abreast of possible changes in relation to timing and to find relevant documents, market participants should visit the Mergers Register on the ACCC's website at www.accc.gov.au/mergersregister.
4. A Statement of Issues provides an opportunity for all interested parties (including customers, competitors, shareholders and other stakeholders) to ascertain and consider the primary issues identified by the ACCC. It is also intended to provide the merger parties and other interested parties with the basis for making further submissions should they consider it necessary.

Background

5. On 29 June 2009, the ACCC commenced its informal review of the proposed acquisition.

Relevant parties

The target – Huhtamaki Consumer Goods Australia

6. Huhtamaki Group is a multinational consumer and speciality packaging company. Huhtamaki Group undertakes its Australian operations through Huhtamaki Australia Pty Ltd (Huhtamaki Australia). The parent company, Huhtamaki Oyj, is based in Finland and is listed on the NASDAQ OMX Helsinki Ltd.
7. Huhtamaki Australia's operations include:
 - consumer goods rigid packaging;
 - food services packaging;
 - moulded fibre packaging; and
 - flexible food packaging.
8. The proposed acquisition relates to Huhtamaki Australia's consumer goods rigid packaging business known as Huhtamaki Consumer Goods Australia (HCGA). HCGA supplies a variety of thin-walled plastic containers manufactured using injection moulding (IM) and extrusion and thermoforming (E&T) processes. These containers are typically used by dairy customers for products including ice cream, yoghurt and table spreads. HCGA also manufactures and supplies extruded plastic roll stock to customers for in-house manufacture, as well as other types of packaging manufactured from paper and paper-plastic composites.
9. HCGA operates three manufacturing sites in Australia: Mulgrave, Victoria; Bankstown, NSW; and Wacol, Queensland.

The acquirer – Pact Group Pty Ltd

10. In Australia, Pact Group's plastic packaging business is managed through several wholly-owned subsidiaries: VIP Plastic Packaging Pty Ltd (trading as VIP Packaging) (VIP), Alto Packaging Australia Pty Ltd (Alto) and Summit Manufacturing Pty Ltd (trading as Signum) (Signum). Through VIP, Pact Group wholly owns several other subsidiaries including Baroda Packaging Pty Ltd (Baroda), a number of entities trading as PlasPak (PlasPak), Salient Asia Pacific Pty Ltd and Atlas Plastics Pty Ltd (together Pact Group).
11. These subsidiaries manufacture a diverse range of plastic packaging products for the food and retail industries including:
 - containers, such as bottles, jars and tubs;
 - trays (for meat and bakery products) and bowls (for fruit and salads);
 - closures; and
 - large plastic containers, such as jerry cans, cubes, pails and drums.

12. Pact Group also manufactures a variety of thin-walled plastic containers designed for the food industry, manufactured by E&T and IM.
13. Pact Group is privately owned by the Geminder family through a family trust. In 2002, a Pact Group related entity Salvage Pty Ltd acquired the industrial packaging operations of Visy Industries Australia Pty Ltd (Visy). As part of the purchase of the Visy industrial packaging business, Visy entered into an agreement for the provision of corporate and shared services to Pact Group.

Visy Industries Australia Pty Ltd (Visy)

14. Visy is Australia's largest packaging and recycling company. Visy's operations include:
 - the manufacture and supply of beverage and food containers, including bottles, jars, paperboard cartons and corrugated cardboard boxes;
 - the manufacture and supply of extruded plastic roll stock, which can be used in the manufacture of form-fill-seal food containers; and
 - the collection and processing of recyclable materials and the manufacture and supply of recycled paper.
15. Visy is privately owned by the Pratt family through a family trust.

Relationship between Pact Group and Visy

16. In previous matters, the ACCC has had regard to the commercial and family relationships between Pact Group and Visy, and the impact of these relationships on the likely effectiveness of competition between Pact Group and Visy post-acquisition.
17. In assessing the competitive effects of the proposed acquisition, the ACCC will have regard to the commercial and family arrangements between Pact Group and Visy, where relevant.

Other industry participants

NCI Packaging

18. National Can Industries Limited (NCI) was established in 1954, and is listed on the ASX, with operations in Australia, New Zealand, Fiji and Papua New Guinea.
19. One of NCI's businesses, NCI Packaging, specialises in supplying steel and plastic packaging products for application in a range of industries, including paint, chemicals and food packaging. Its product range includes IM pails, ranging from 250 millilitres to 20 litres in capacity, and IM food containers up to 5 litres in capacity.
20. NCI has eight manufacturing plants in Australia, and produces, among other forms of packaging, IM containers for ice cream and table spreads.

Cryovac

21. Cryovac Australia Pty Ltd (Cryovac) was established in 1934, and has offices in five Australian states. It operates as a manufacturer and importer of rigid and flexible packaging materials, specialising in plastic food containers, bubble wrap and padded envelopes, using both E&T and IM processes.
22. The parent company of Cryovac is Sealed Air Corporation (Sealed Air), a leading global manufacturer of materials and systems for protective, presentation and fresh food packaging, with operations in 52 countries.
23. Cryovac has five manufacturing plants in Australia and produces, among other forms of packaging, a large range of E&T containers predominantly for the dairy industry.

Manufacturing processes

24. There are two broad manufacturing processes relevant to the proposed acquisition — E&T and IM.

Extrusion and thermoforming

25. E&T food containers are made from extruded plastic roll stock, which is moulded into shape by heat and pressure. The manufacturing process consists of two stages — extrusion and thermoforming.
26. The first stage involves feeding raw materials or resin into an extruder, which heats the plastic to a desired temperature, which is then extruded to create a continuous strip of plastic. The second stage is known as thermoforming, whereby the strip of plastic is re-heated and stretched, and pressure is then applied to force the heated plastic strip into a moulded cavity. E&T food containers tend to be used to package a large range of food products such as yoghurt, cream, dips, dairy desserts, butter and other spreads.
27. The extruded plastic roll stock produced in the first stage of the E&T process (as described above) can also be supplied by packaging manufacturers to large food and dairy customers. The extruded plastic roll stock is used by these customers as an input for the in-house manufacture of form-fill-seal products.
28. Form-fill-seal is a specific thermoforming process — essentially, small containers are thermoformed from the extruded plastic roll stock, filled with yoghurt or preserved fruits, for example, and then sealed with plastic or foil.

Injection moulding

29. IM food containers are made by melting plastic polymer granules in a heated barrel and then injecting these into a mould which cools and solidifies the plastic into the finished product. IM food containers are often in-mould labelled (IML), which involves the application of labels during the moulding process. IM can be used to manufacture a wide variety of products including food containers. In the

food industry, common uses are tubs for ice cream and yoghurt, and take away containers.

Market inquiries

30. On 29 June 2009, the ACCC commenced market inquiries regarding the proposed acquisition. A range of interested parties provided responses, including other manufacturers and suppliers of IM and E&T food containers and customers.

Areas of overlap and market definition

Areas of overlap

31. The operations of Pact Group and HCGA overlap in relation to the manufacture and supply of thin-walled plastic food containers manufactured by E&T (E&T food containers) and thin-walled rigid plastic food containers manufactured by IM (IM food containers).
32. The ACCC understands that there is also overlap between HCGA and Visy in the manufacture and supply of extruded plastic roll stock to large food customers. On the information available, the ACCC understands that, apart from Visy and HCGA, Cryovac is the only other significant supplier of extruded plastic roll stock.
33. Given the commercial and family arrangements between Pact Group and Visy, in assessing this matter the ACCC will also have regard to any overlap between Visy and HCGA in relation to the manufacture and supply of thin-walled plastic food containers manufactured using E&T and IM.

Market definition

34. For the purposes of reviewing the proposed acquisition, the ACCC considers that the potential relevant markets are:
- the national market for the manufacture and supply of thin-walled plastic food containers manufactured using E&T and IM (up to 5L in capacity) (food container market); and
 - the national market for the manufacture and supply of extruded plastic roll stock (extruded plastic roll stock market).

Food container market

35. At this stage, the ACCC understands that the main customers of E&T and IM food containers are 'large volume customers'. Large volume customers tend to demand large volumes of containers and/or a wide variety of container types. They also tend to demand containers across a number of different site locations. These types of customers also expect high levels of service from suppliers in terms of the service provided by relationship managers and in terms of the quality of the packaging products.

36. The ACCC notes that it has received mixed views from these customers over the course of its market inquiries as to whether E&T food containers and IM food containers should be considered to be part of the same market, or form separate product markets.
37. Some market participants indicated that there is limited demand-side substitutability between the two types of thin-walled food containers. Differences between the two containers include:
- *structural integrity* – IM food containers are more dense than E&T food containers and, therefore, IM food containers can hold larger volume products;
 - *temperature tolerance properties* – IM food containers, by being more dense are able to withstand high and low temperatures, whereas E&T food containers may become brittle at colder temperatures;
 - *design flexibility* – IM food containers can be manufactured in a larger range of shapes and sizes than E&T food containers, with additional features including tamper evidence, tear openings and pouring spouts;
 - *price points* – IM food containers are more expensive than E&T food containers on a per unit basis due to slower production rates and higher input costs;
 - *printing quality* – IM food containers, through the use of IML allow for more intricate printing than dry offset printing typically used on E&T food containers;
 - *marketing difference* – IM food containers tend to be used in premium product segments with smaller production runs, while E&T food containers are used for standard products with large production runs; and
 - *tooling requirements* – different tooling is required for filling processes using IM versus E&T food containers, therefore customers may incur switching costs in re-tooling their machines when switching between the different packaging types.
38. However, the ACCC also received information from other customers that suggested that IM and E&T food containers were two segments within the same product market. Some customers took the view that there is demand-side substitution across the two types of containers. In this regard, the ACCC notes that the main customers —large dairy and food customers — tend to use both types of containers for the same products, such as yoghurt.
39. On the supply-side, inquiries to date indicate that there may be some substitutability between the two production processes. The ACCC understands that an E&T manufacturer who wished to switch to manufacturing IM food containers (and vice versa) would have to purchase additional equipment to produce the containers but is likely to have the relevant technical and marketing expertise.

40. On balance, the ACCC's preliminary view is that there is one product market with two market segments — IM and E&T food containers.
41. Market inquiries to date have indicated that the appropriate product dimension of the relevant market is better characterised as containers designed for 'food' products rather than the narrower product dimension being containers designed for 'dairy' products. Although dairy customers represent a large portion of demand for thin-walled food containers, there does not appear to be a significant distinction between the manufacturing processes used to produce dairy containers and the manufacturing processes used to produce food containers. While the ACCC notes that dairy containers tend to be more decorated than other types of food containers, market inquiries indicated that basic printing capabilities can be readily acquired or outsourced to a third-party.
42. Market inquiries to date have also indicated that the product dimension should be limited to IM food containers up to 5L in capacity given that larger container sizes would require a significantly larger and more expensive IM machine to produce. A similar limitation for E&T food containers on the basis of size is not necessary as a manufacturer is unlikely to be able to manufacture a container larger than 1L in capacity, given the weaker structural integrity of E&T food containers.

Extruded plastic roll stock market

43. At this stage, the ACCC understands that several manufacturers, including HCGA and Visy, manufacture and supply extruded plastic roll stock to large dairy and food customers to be used in form-fill-seal processes. The ACCC preliminary view is that the manufacture and supply of extruded plastic roll stock forms a separate product market to the manufacture and supply of food containers.

The ACCC invites comments on the areas of overlap and market definition

The ACCC welcomes any comments from market participants regarding the proposed market definitions, including:

- whether or not IM food containers and E&T food containers should be considered to be in the same or separate product market(s).
- whether the product dimension of the market(s) is appropriately characterised as thin-walled containers designed for 'food,' or should be limited to thin-walled containers designed for 'dairy' products specifically.
- whether there should be separate product markets for containers that are 'decorated' and containers that are 'undecorated', or whether such containers should be considered part of the same market'.
- whether the product dimension of the market for E&T and IM food containers should be limited to a particular capacity/size of container.

The ACCC also welcomes any comments from market participants on the extruded plastic roll stock market. In particular, the ACCC is seeking views on whether the supply of extruded plastic roll stock should be included within the same product markets as the manufacture and supply of E&T and IM food containers, or whether it should be treated as a separate product market.

Statement of issues

44. For the purposes of this Statement of Issues, there are three issues in this matter that fall within the one category — 'issues that may raise concerns'.

Issues that may raise concerns

Competition for the manufacture and supply of food containers

45. The ACCC considers that the proposed acquisition may raise substantial competition concerns in relation to the manufacture and supply of thin-walled food containers manufactured using IM and E&T.
46. Post-acquisition, two significant manufacturers of IM food containers would remain in the relevant market — the merged entity and NCI Packaging — and two significant manufacturers of E&T food containers would remain — the merged entity and Cryovac.
47. The ACCC's preliminary understanding from its market inquiries is that the significant manufacturers noted in the paragraph above tend to focus on supplying the main customers of these types of containers — large volume customers.
48. Market inquiries also suggested that HCGA may be considered to be a vigorous and effective competitor in terms of product innovation and service levels in this market.
49. The ACCC notes that the level of constraint that would be posed on the merged entity from other competitors appears to vary across the two types of containers. Relevantly, the ACCC is of the view that if information is received that suggests that the two types of containers are in separate markets, then there may be serious competition concerns in the E&T food container market but less significant competition concerns in the IM food container market.

E&T food containers

50. Market inquiries to date suggested that there are a number of smaller E&T manufacturers supplying E&T containers in Australia. However, these inquiries revealed that these suppliers are 'niche' and would not pose a competitive constraint on the merged entity post-acquisition. Similarly, from market inquiries conducted to date, it appears that imports would not provide a competitive constraint on the merged entity.

51. The ACCC is of the view that barriers to entry and expansion in the E&T food container market segment are high. The ACCC understands that there have been no new E&T manufacturers over the past decade. The ACCC therefore considers it highly unlikely that a new E&T manufacturer to enter and pose a competitive constraint on existing manufacturers.

IM food containers

52. Market inquiries to date have indicated that there appear to be several smaller IM food container manufacturers who may have the ability to increase their production volumes to service large volume customers to compete more effectively against the merged entity post-acquisition. Manufacturers identified include Sunrise Plastics, Arrow Plastics, Genfac and Chanrol.
53. Although still limited in number, market inquiries to date indicate that there are several importers of IM food containers, including Cryovac. The ACCC is investigating to what extent these companies may be able to pose a competitive constraint on the merged entity post-acquisition.
54. Barriers to entry and expansion in the IM food container market segment, while high for large scale entry/expansion, appear to be moderate for smaller scale entry/expansion. The ACCC notes that there has been some recent entry by importers, including Tecpak and Allpak, which suggests barriers to importing may be lowering over time.

The ACCC seeks further information on competition for the manufacture and supply of food containers

The ACCC invites further comment from market participants in relation to:

- *smaller food container manufacturers* — whether it is likely that smaller manufacturers could expand production to provide an effective competitive constraint on the merged entity post-acquisition. The ACCC seeks further information on barriers to expansion, such as the capital costs associated with the installation of new machinery and the scale of expansion required to compete effectively with the merged entity in relation to each form of manufacturing process.
- *actual and potential importers* — whether it is likely that importers could increase current import volumes to provide an effective competitive constraint on the merged entity post-acquisition. The ACCC seeks further information on barriers to importing, such as the lead times and the need to stockpile containers.
- *HCGA's position in the market* — whether HCGA is a significant driver of price based and/or non-price based competition (such as product quality, product innovation and high customer service levels).

Competition for the manufacture and supply of extruded plastic roll stock

55. The ACCC considers that the proposed acquisition may raise competition concerns in relation to the manufacture and supply of extruded plastic roll stock.

Post-acquisition, three significant suppliers of extruded plastic roll stock to customers would remain – the merged entity, Visy and Cryovac.

56. From its market inquiries to date, the ACCC understands that HCGA supplies a large amount of extruded plastic roll stock to its large dairy customers. Although the ACCC understands that Pact Group currently only supplies a small amount of extruded plastic roll stock to third parties, market inquiries suggest that Visy is a significant supplier of these products to third parties. On the basis of information received to date, there appears to be only one other significant supplier of extruded plastic roll stock, Cryovac.
57. On the basis of preliminary market inquiries, the ACCC understands that this market is characterised by high barriers to entry and expansion. Further, imports in terms of volume do not appear to be significant and are therefore not likely to pose a strong competitive constraint on the merged entity post-acquisition.

The ACCC seeks further information on competition for the manufacture and supply of extruded plastic roll stock

The ACCC invites further comment from market participants in relation to:

- *extruded plastic roll stock manufacturers* — the ACCC seeks further information on key manufacturers of extruded plastic roll stock, including the approximate market shares, and the extent to which these manufacturers could increase their existing production to provide an effective competitive constraint on the merged entity post-acquisition.
- *actual and potential importers* — the ACCC seeks information on the extent to which imports would provide an effective competitive constraint on the merged entity post-acquisition, including information relating to current import volumes, lead times and costs.
- *HCGA's position in the market* — whether HCGA is a significant driver of price based and/or non-price based competition (such as product quality, product innovation and high customer service levels).

Conglomerate merger issues

58. The ACCC notes that some market participants had concerns that the proposed acquisition could increase the ability and incentive for Pact Group to raise conglomerate merger issues by offering packaging bundles to customers.
59. The ACCC's preliminary understanding is that the merged entity would be able to supply a large number of packaging products post-acquisition. On the basis of market inquiries to date, the merged entity appear to have a significant market share in the following food packaging segments:
- smaller plastic containers, such as bottles, jars, punnets and tubs;
 - large plastic containers, such as jerry cans, cubes, pails and drums;

- trays, commonly used for meat and bakery products;
 - bowls, commonly used for fruit and salads;
 - closures; and
 - extruded plastic roll stock, used for form-fill-seal processes.
60. Some of the packaging items listed above could be offered in a bundle to dairy customers, such as a bundle of packaging for white milk, long life milk, ice cream, dips, yoghurt, table spreads, cream and other dairy desserts.
61. Conglomerate mergers can raise competition concerns where they enable the merged firm to alter its operations or product offerings in a way that forecloses the merged firm's rivals and ultimately reduces the competitive constraint they provide. For example, foreclosure can occur through bundling or tying products in complementary markets. However, a conglomerate firm will generally only be able to engage in foreclosure if it has sufficient market power in one of the relevant markets (i.e the ability to tie products) and has the incentive to do so (i.e. it is profitable to do so).
62. On the evidence available to the ACCC, it considers that the proposed acquisition may result in an increased ability and incentive for the merged entity to foreclose its rivals by offering a packaging bundle.

The ACCC seeks further information on possible conglomerate effects

The ACCC invites further comment from market participants in relation to:

- whether the merged entity has a significant presence in other packaging segments.
- whether the merged entity currently bundles packaging products and whether the ability and incentive to bundle is increased with the proposed acquisition and if so, whether the bundle would be likely to foreclose actual and potential rivals.
- whether barriers to entry are significant in markets where the merged entity would have an incentive to bundle its products.
- whether the proposed acquisition will raise barriers to entry and expansion in relevant markets.

ACCC's future steps

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

65. Submissions are to be received by the ACCC no later than 28 August 2009. The ACCC will consider the submissions received from the merger parties and other 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.
66. The ACCC intends to publicly announce its final view by 16 September 2009. However the anticipated timeline may change in line with the Merger Review Process Guidelines. A Public Competition Assessment for the purpose of explaining the ACCC's final view may be published following the ACCC's public announcement.