



Statement of Issues

7 July 2016

The Borg Group's proposed acquisition of the manufacturing assets of Alpine MDF Industries Pty Ltd

Purpose

1. This Statement of Issues aims to:
 - give the Australian Competition and Consumer Commission's (**ACCC's**) preliminary views on competition issues arising from the proposed acquisition of the manufacturing assets of Alpine MDF Industries Pty Ltd (**Alpine**) by the Borg Group (**Borg**) (the **proposed acquisition**)
 - identify areas of further inquiry
 - give all interested parties an opportunity to comment
 - invite interested parties to submit information to assist us in our assessment of the issues.

Overview of ACCC's preliminary views

2. The legal test which the ACCC applies in considering the proposed acquisition is in section 50 of the *Competition and Consumer Act 2010* (the **Act**). Section 50 prohibits acquisitions that would have the effect, or be likely to have the effect, of substantially lessening competition in any market.
3. The ACCC divides its preliminary views into three categories, 'issues of concern', 'issues that may raise concerns' and 'issues unlikely to raise concerns'. For this matter the ACCC has two issues of concern and one issue that may raise concerns.

Issues of concern

- The proposed acquisition is likely to substantially lessen competition in the national market for the manufacture and supply of raw medium density fibreboard (**MDF**). The reduction in the number of raw MDF manufacturers from three to two and the removal of the only manufacturer without significant value-adding operations is likely to lead to higher prices and/or

reduced service quality given the lack of competitive constraints in the relevant market.

- The proposed acquisition is likely to substantially lessen competition in one or more national markets for the supply of value-added MDF products, by increasing the ability and incentive of Borg to increase prices, or foreclose the supply of raw MDF to competing manufacturers and suppliers of downstream value-added MDF products.

Issue that may raise concerns

- The proposed acquisition may substantially lessen competition in one or more national markets for the manufacture and supply of doorskins, mouldings or other particular value-added MDF products. In particular, the reduction in the number of manufacturers of doorskins from two to one may lead to higher prices and/or reduced service quality.

Making a submission

4. The ACCC is seeking submissions from interested parties, particularly on the following key issues:
 - The likelihood that the proposed acquisition would result in higher prices (or reduced service quality) for the supply of raw MDF.
 - In the event that prices for domestic raw MDF increase by a small but significant amount, whether Australian customers would import raw MDF to avoid the price increase.
 - Whether the proposed acquisition would reduce the intensity of competition between the remaining manufacturers of raw MDF in Australia. For instance, whether it would facilitate co-ordination by Borg and the Laminex Group (**Laminex**) of prices of raw MDF.
 - Whether the proposed acquisition is likely to increase the ability and incentive of Borg to increase prices or foreclose supply of raw MDF to competing manufacturers of value-added MDF products.
 - The likelihood that the proposed acquisition would result in higher prices (or reduced service quality) for the supply of doorskins, mouldings or other value-added MDF products.
5. Detailed discussion of these and other issues, along with specific questions, is contained in this Statement of Issues.
6. Interested parties should provide submissions by no later than 5pm on 21 July 2016. Responses may be emailed to mergers@accc.gov.au with the title: *Submission re: Borg Alpine – attention Mandy Bendelstein/Julie Chandler*. If you would like to discuss the matter with ACCC officers over the telephone or in person, or have any questions about this Statement of Issues, please contact Mandy Bendelstein on (02) 9230 3890 or Julie Chandler on (02) 9230 3877.
7. The ACCC anticipates making a final decision on 1 September 2016, however, this timeline can change. To keep abreast of possible changes in relation to

timing and to find relevant documents, interested parties should visit the Mergers Register on the ACCC's website at www.accc.gov.au/mergersregister.

Confidentiality of submissions

8. The ACCC will not publish submissions regarding the proposed acquisition. We will not disclose submissions to third parties (except our advisors/consultants) unless compelled by law (for example, under freedom of information legislation or during court proceedings) or in accordance with section 155AAA of the Act. Where the ACCC is required to disclose confidential information, the ACCC will notify you in advance where possible so that you may have an opportunity to be heard. Therefore, if the information provided to the ACCC is of a confidential nature, please indicate as such. Our [Informal Merger Review Process Guidelines](#) contain more information on confidentiality.

About ACCC 'Statements of Issues'

9. 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.
10. 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.

Timeline

| Date | Event |
|------------------|---|
| 26 April 2016 | ACCC commenced review of the proposed acquisition |
| 7 July 2016 | ACCC publication of Statement of Issues |
| 21 July 2016 | Closing date for submissions from interested parties in response to Statement of Issues |
| 1 September 2016 | Proposed date for announcement of ACCC's final decision. |

The parties

Borg

11. The Borg Group (**Borg**) manufactures and supplies raw MDF and a range of value-added MDF products (including mouldings and doorskins), from its plant in Oberon, New South Wales.

The Borg Group's proposed acquisition of the manufacturing assets of Alpine MDF Industries Pty Ltd

12. Borg also manufactures and supplies value-added MDF products from its plants in Charmhaven and Somersby in New South Wales.
13. Borg owns Polytec, a supplier of value-added MDF products throughout Australia.
14. Borg (including Polytec) generally distributes its raw and value-added MDF products through its national network of distribution centres and operates a fleet of trucks for providing deliveries.

Alpine, SFC and Nelson Pine

15. Alpine MDF Industries Pty Ltd (**Alpine**) manufactures and supplies raw MDF and value-added MDF products from its plant in Wangaratta, Victoria.
16. The only value-added MDF products made by Alpine are mouldings and doorskins.
17. Alpine is wholly-owned by Sumitomo Forestry Company Ltd of Tokyo, Japan (**SFC**).
18. SFC has a wholly-owned subsidiary in New Zealand, Nelson Pine Industries Limited, which manufactures raw MDF.

Other industry participants

Laminex

19. Other than Borg and Alpine, Laminex (i.e. the Laminex Group) is the only manufacturer and supplier of raw MDF in Australia. Its plant is located in Gympie, Queensland. If the proposed acquisition proceeds, Laminex will be the only other manufacturer and supplier of raw MDF in Australia.
20. Laminex also manufactures and supplies a range of value-added MDF products, including mouldings (but not doorskins).
21. Laminex distributes its raw MDF and value-added MDF products primarily through its network of branches and warehouses.
22. Laminex is part of the Fletcher Building Group which holds a 20% shareholding in Dongwha NZ Limited, a producer of raw MDF in New Zealand.

Manufacturers of value-added MDF products

23. There are many Australian manufacturers of value-added MDF products that purchase raw MDF. These manufacturers range from large-scale kitchen and wardrobe manufacturers, to smaller more specialist manufacturers, such as joineries and skirting board manufacturers.

Re-sellers/distributors of raw MDF

24. Several companies purchase raw MDF in order to resell it to small to medium-sized manufacturers of value-added MDF products and other customers. Sometimes these companies change the products slightly (for example, by

cutting the raw MDF sheets into smaller sizes). Many of these companies purchase raw MDF from Alpine and in some cases act as Alpine's distributors.

Industry background

25. Raw MDF is a wood-based panel product formed by breaking down woodchips into fibre, combining it with wax and resin, and forming panels by applying high temperature and pressure.
26. Raw MDF is used for multiple applications, such as DIY purposes, shop-fitting and making furniture. Raw MDF is purchased in different sizes and thicknesses. The most popular thicknesses in Australia are 16mm and 18mm.
27. All of the wood fibre used to make raw MDF in Australia and New Zealand comes from pine plantations located near manufacturing plants. Raw MDF made in Australia and New Zealand is considered to be of a high quality, and is generally regarded as superior to raw MDF made in Asia which often uses different types of wood fibres (often derived from rubberwood).
28. Value-added MDF is raw MDF to which secondary manufacturing processes have been applied. Value-added MDF products include doorskins, mouldings and laminated kitchen and bathroom cabinet doors.
 - a. *Doorskins* are thin pieces of MDF (primarily 3mm thick, but also up to 12mm thick) which are painted and glued to each side of the core of an interior or exterior door.
 - b. *Mouldings* include architraves and skirting boards found in residential and commercial premises.

The proposed acquisition

29. Borg proposes to acquire all of Alpine's assets for manufacturing raw and value-added MDF, which are located in Wangaratta, Victoria. Borg is not acquiring Alpine's goodwill, intellectual property rights, or sales or marketing assets.

Future with and without the proposed acquisition

30. Section 50 of the Act prohibits acquisitions that would have the effect or be likely to have the effect of substantially lessening competition in a market.
31. In assessing a proposed acquisition pursuant to section 50 of the Act, the ACCC considers the effects of the acquisition by comparing the likely future competitive environment if the acquisition proceeds (the "with" position) to the likely future competitive environment if the acquisition does not proceed (the "without" position).
32. On the basis of the information currently available, the ACCC considers that in the future without the proposed acquisition, Alpine's manufacturing assets would continue to be operated independently of Borg and Laminex.

Previous ACCC decisions

Sumitomo Forestry Company Limited (SFC) – proposed acquisition of certain assets of Carter Holt Harvey Limited's Woodproducts Australia business (2008) - opposed

33. In 2008 the ACCC opposed the proposed acquisition by SFC of certain assets owned by Carter Holt Harvey (**CHH**) including a raw MDF manufacturing plant at Oberon in New South Wales.
34. The proposed acquisition in 2008 was the reverse of the current proposed acquisition, with the owner of the raw MDF manufacturing facility at Wangaratta (SFC) proposing to acquire the raw MDF manufacturing facility at Oberon.
35. Similar to the current proposed acquisition, the proposed acquisition in 2008 would have reduced the number of manufacturers of raw MDF in Australia from three to two.
36. The ACCC was of the view that the proposed acquisition would be likely to have the effect of substantially lessening competition in the national market for the manufacture and supply of raw MDF, and was also likely to foreclose the supply of raw MDF to downstream competing manufacturers of value-added MDF products.
37. The ACCC did not consider that actual or potential import competition would effectively constrain SFC following the proposed acquisition. The ACCC considered that:
 - a. the majority of raw MDF traded globally was not of comparable quality to Australian raw MDF (in terms of the wood used and formaldehyde emission standards)
 - b. while New Zealand's raw MDF was of suitable quality, corporate links between Australian and New Zealand manufacturers meant that significant quantities of raw MDF were unlikely to be available for independent imports to Australia
 - c. the prices of Australian raw MDF would need to increase in excess of 5-10% before there was any possibility of significant and suitable quality raw MDF being imported into Australia from South-East Asia or South America, and
 - d. imported value-added MDF products would be unlikely to impose an effective constraint on SFC following the proposed acquisition.

The ACCC public register relating to this matter is available at:

<http://registers.accc.gov.au/content/index.phtml/itemId/811679/fromItemId/751043>

The Borg Group – proposed acquisition of raw MDF manufacturing plant of Carter Holt Harvey Woodproducts Australia Pty Ltd located at Oberon, NSW (2009) – not opposed

38. In 2009 the ACCC did not oppose Borg's proposed acquisition of CHH's raw MDF manufacturing plant at Oberon in New South Wales, and other assets.

39. At the time, Borg was not manufacturing raw MDF in Australia. This meant that following the proposed acquisition there continued to be three manufacturers of raw MDF.
40. The ACCC concluded that the proposed acquisition was unlikely to materially increase the ability and incentive for foreclosure of downstream rivals, such as by restricting supply of raw MDF, or hindering of rivals' alternative supply options.

The ACCC public register relating to this matter is available at:

<http://registers.accc.gov.au/content/index.phtml/itemId/903273/fromItemId/751043>

Market definition

41. For the purposes of this Statement of Issues, the ACCC considers that the relevant markets in which to assess the effects on competition arising from the proposed acquisition are:
 - a. a national market for the manufacture and supply of raw MDF
 - b. a national market for the manufacture and supply of doorskins, and
 - c. national markets for the manufacture and supply of value-added MDF products.
42. The ACCC's starting point for delineating relevant markets is to identify the products actually or potentially supplied by the merger parties. The ACCC then considers what other products constitute sufficiently close substitutes to provide a significant source of constraint on the acquirer (i.e. Borg) following the proposed acquisition.

National market for the manufacture and supply of raw MDF

Product dimension

43. Consistent with the ACCC's previous decision in relation to SFC's proposed acquisition of certain assets of CHH's Woodproducts Australia business in 2008, market feedback has indicated that there is a national market for the manufacture and supply of raw MDF.
44. Other wood-based panel products, such as particleboard and plywood, do not appear to be close substitutes for raw MDF in the context of many applications and therefore, do not form part of the relevant product market. In particular the ACCC considers that while other wood-based panel products may constitute functional alternatives to raw MDF in certain limited circumstances, they are generally not close substitutes for raw MDF.
45. On the demand side, market inquiries indicate that:
 - a. particleboard is not a close substitute for raw MDF in many applications. For instance, the structural characteristics of particleboard make it unsuitable for use in applications that require shaping or routing and it has a rougher surface which may produce an uneven finish when painted

- b. as particleboard is cheaper than raw MDF, to the extent that users of wood-based products are willing and able to use particleboard instead of raw MDF, many are likely to have already done so, and
 - c. while plywood may possess similar characteristics to raw MDF for some applications, plywood often costs much more than raw MDF, so it is unlikely to be a substitute for raw MDF, even in the event of a small but significant and non-transitory increase in the price of raw MDF.
- 46. On the supply side, market inquiries have indicated that different machinery is needed to produce particleboard, plywood and raw MDF. Manufacturers of particleboard and plywood would not be able to adapt their existing production facilities to produce raw MDF without significant capital investment and time. Different types of timber may also be needed to produce different wood-based products.
- 47. For the reasons set out above, the ACCC's preliminary view is that other wood-based panel products are not close substitutes for raw-MDF from a demand-side or a supply-side perspective.

Geographic dimension

- 48. Based on market feedback, the ACCC's preliminary view is that the geographic scope of the market for the manufacture and supply of raw MDF is national. The vast majority of raw MDF purchased by Australian customers is made in Australia. Market participants indicated that transport costs increase significantly when raw MDF is transported across long distances. The ACCC does not currently consider that there is a global or trans-Tasman market for the supply of raw MDF. The prices paid for raw MDF are not determined globally and there are currently no material imports of raw MDF into Australia. The ACCC's preliminary assessment of the constraint that imports, or potential imports, would impose on Borg post-acquisition is set out below.

National markets for the manufacture and supply of value-added MDF products

- 49. The ACCC is also considering the likely competitive effects of the proposed acquisition in the context of the downstream market (or markets) for the manufacture and supply of value-added MDF products in Australia (e.g. laminated kitchen and bathroom cabinet doors, mouldings and doorskins).
- 50. Alpine and Borg both manufacture mouldings and doorskins, and like Laminex, Borg also makes a wide range of other value-added MDF products.
- 51. The ACCC is seeking further information from market participants about the manufacture, supply and use of doorskins and mouldings, to determine whether there are separate markets for the supply of these types of value-added MDF products.
- 52. The ACCC is also considering whether the proposed acquisition is likely to raise competition issues in any national market for the manufacture and supply of a value-added MDF product in which Borg operates.

National market for the manufacture and supply of doorskins

53. The ACCC understands that in Australia only Borg and Alpine manufacture doorskins (and Laminex does not). As noted above, doorskins are thin pieces of raw MDF (primarily 3mm thick, but also up to 12mm thick) which are painted and glued to each side of the core of a door.
54. Market feedback suggests that doorskins are made on different machinery from other value-added MDF products. Therefore manufacturers of other value-added MDF products cannot switch to producing doorskins easily or without significant investment.
55. The ACCC is considering the extent to which doorskins made of different wood-based products, such as particleboard, are substitutes for doorskins made from MDF.
56. The ACCC understands that plywood is not a close substitute for MDF in the making of doorskins, due to the significant price difference between the two products.

The ACCC invites comments from market participants on its preliminary views about the definition of the relevant market(s). In particular, market participants may wish to comment on:

- Whether market participants agree that the relevant geographic markets are national, or whether they consider that should be broader.
- The extent to which particleboard, plywood or other wood-based products could be substituted for raw MDF if the prices of raw MDF rose.
- The appropriateness of considering separate markets for the manufacture and supply of (i) doorskins and (ii) mouldings, rather than a single market for the manufacture and supply of all value-added MDF products.
- Whether the machinery used to manufacture (i) doorskins and (ii) mouldings can be used to manufacture other value-added MDF products, or the reverse.
- Whether doorskins made of different wood-based products, such as particleboard, are close substitutes for raw MDF.

Issue of concern: Reduction in manufacturers of raw MDF

57. Based upon its inquiries to date, the ACCC's preliminary view is that the proposed acquisition is likely to substantially lessen competition in the national market for the manufacture and supply of raw MDF.
58. The proposed acquisition would reduce the number of raw MDF manufacturers in Australia from three to two and create a duopoly in the manufacture and supply of raw MDF. Borg and Laminex would be the only manufacturers of raw MDF in Australia.
59. The ACCC therefore considers that the removal of Alpine from the market for the manufacture and supply of raw MDF is likely to lead to unilateral effects and/or

coordinated effects in the national market for the manufacture and supply of raw MDF.

Unilateral effects

60. The ACCC's preliminary view is that by removing the close competition provided by Alpine, the proposed acquisition raises the concern that Borg would have the ability to unilaterally exercise market power, leading to higher prices and/or reduced service in respect of the supply of raw MDF.
61. The ACCC considers that there will be a lack of competitive constraints on Borg in the relevant market, given:
 - a. Borg would grow from controlling approximately one third to over half the raw MDF manufacturing capacity in Australia
 - b. the reduction in the number of raw MDF manufacturers and suppliers in Australia from three to two would reduce the choices available to customers and diminish their leverage in pricing negotiations with Borg (and/or Laminex)
 - c. Borg and Alpine are close competitors in relation to the supply of raw MDF, offering raw MDF in many of the same thicknesses and sheet sizes, and have been willing to lower their prices to win customers from each other. For customers in Victoria, South Australia or parts of New South Wales, Alpine and Borg represent much closer alternatives than Laminex which produces its MDF in Queensland
 - d. Alpine supplies a greater proportion of its output to third parties than Borg and Laminex which use significant proportions of their raw MDF to make value-added MDF products (Alpine only uses a very modest proportion of its output of raw MDF for making value-added MDF products)
 - e. the proposed acquisition would remove Alpine, which is currently the only manufacturer of raw MDF in Australia with a strong incentive to supply wholesalers and distributors of raw MDF and manufacturers of value-added products. Unlike Borg and Laminex, Alpine does not also produce many of the value-added MDF products supplied by those customers, and does not compete with these customers. Alpine is regarded as an 'independent' source of supply for those customers
 - f. Alpine is likely to be the manufacturer of raw MDF with the most spare capacity in Australia
 - g. There may be some limits on Laminex's willingness to supply all segments of customers buying raw MDF, so there may be customers for which Borg would be the only Australian-based supplier of raw MDF following the proposed acquisition
 - h. Laminex would be Borg's only rival manufacturer and supplier of raw MDF in Australia, and like Borg, Laminex is vertically integrated with sizable downstream value-added MDF operations. A significant proportion of the raw MDF produced by Laminex is used internally to manufacture value-added MDF products

- i. the actual or potential constraint provided by imports of raw or value-added MDF is likely to be limited
 - j. barriers to entry in the relevant market appear to be high, and
 - k. customers of raw MDF generally lack countervailing power.
62. The ACCC's consideration of these competitive constraints is also relevant to the concerns raised about coordinated effects, as discussed below.

No material current imports of raw MDF, and no likely credible threat of imports in the foreseeable future

63. The ACCC is not aware of any material volumes of raw MDF currently being imported into Australia other than by existing local manufacturers, and this has not changed in many years. Based on the information currently available to it, the ACCC considers that existing imports of raw MDF would appear unlikely to constrain Borg following the proposed acquisition.
64. In respect of the potential to import raw MDF in the future, a small number of market participants consider that imports of raw MDF are possible and others consider that it is a potential option they can explore further. However the majority of market participants consider that there is limited scope to obtain imports of suitable quality raw MDF in sufficient quantities.
65. The ACCC understands that customers have encountered the following specific difficulties when importing, or seeking to import, raw MDF from each of the following parts of the world which produce large volumes of raw MDF.

New Zealand

66. Many customers reported difficulties securing supply of raw MDF from New Zealand. The ACCC considers that New Zealand based manufacturers and suppliers of raw MDF are unlikely to have an incentive to divert raw MDF to Australia from their existing export markets in response to a small but significant increase in the price of raw MDF in Australia. The ACCC understands that this is a result of:
- a. Two of Australia's three manufacturers of raw MDF have parent companies with interests in two of the three manufacturers of raw MDF in New Zealand
 - b. Higher margins being attainable for New Zealand's raw MDF exported to Asian countries (primarily Japan) rather than Australia
 - c. High proportions of New Zealand's raw MDF being exported to Asia pursuant to longstanding customer relationships, and
 - d. Licensing restrictions on the sale of certain brands of raw MDF in Australia.
67. In spite of the short distance, it generally costs significantly more to ship products across the Tasman Sea than it does to move products between Australia and Asia or New Zealand and Asia (partly because of the relative infrequency of ships). As a result of more expensive shipping costs and lower prices attainable in Australia, the ACCC understands that New Zealand's

producers of raw MDF can obtain higher margins from selling their raw MDF to Asia rather than Australia.

68. Market inquiries suggest that New Zealand's producers of raw MDF would lack the incentive to supply Australia with raw MDF in the full range of sizes and thicknesses purchased by Australian customers.

South East Asia

69. The ACCC understands that the quality of raw MDF produced in South East Asia is of lower quality than that produced in Australia and New Zealand. The fibre blend is often of mixed or unknown origin, and it is generally made from rubberwood. Many market participants consider that raw MDF manufactured in South East Asia is unsuitable for making value-added MDF products, particularly if machining or routing is needed.

South America and South Africa

70. Customers who have considered buying raw MDF from South Africa or South America have reported difficulties in obtaining competitively priced supply.
71. Other customers suggested that they could not remain competitive importing raw MDF from South Africa or South America, as there were long lead times and shipping times, or they were uncertain whether suppliers could produce raw MDF of a suitable quality, in terms of density and formaldehyde emissions.

Other concerns with imports from all potential points of origin

72. The ACCC understands that many customers hold concerns about importing raw MDF due to the following potential difficulties and risks associated with the process:
- a. *Longer lead times and increased risks of delays:* Customers who have imported wood-based products suggested that in addition to allowing for the longer lead times and shipping times associated with imports, it can take significant additional time for products to clear the port and be transported to their warehouses compared with domestic supply.
 - b. *Warehousing:* Some customers have minimal warehousing and order raw MDF from their domestic supplier on a 'just in time' basis. These customers indicated that they would need to invest in extra warehousing at significant cost to import raw MDF.
 - c. *Limited sizes:* Customers indicated that they would be unable to buy all of the sizes and densities of raw MDF that they currently buy domestically from overseas suppliers. Some of the sizes used by Australian customers differ to the sizes produced by overseas manufacturers.
 - d. *Difficulties with containerisation and logistics:* Some customers indicated that they would rarely need an entire container load of raw MDF of an identical size, that some sizes of raw MDF are too difficult to remove from containers and that mixing sizes in one container results in the customer paying for the transportation of air which increases their per unit transportation costs. Further, because of Australian laws limiting the weight

that can be transported by road, imported containers often cannot be filled completely which increases shipping costs.

- e. *Price:* Customers have indicated that the landed price of imported raw MDF, of suitable quality, would be considerably higher than existing domestic prices.
73. The ACCC recognises that many of the logistical difficulties could be overcome, and often are by importers of other wood based panel products. However only a minority of customers (in particular distributors) have the experience and scale necessary to import raw MDF, and these customers have reported difficulty in securing competitively priced supply of suitable quality. Further, the ACCC understands that higher margins tend to be available for other wood-based panel products, making importation of these products more likely to be competitively possible than raw MDF.
74. The ACCC's preliminary view is that the prices of domestically produced raw MDF would need to increase before a significant proportion of customers could credibly threaten to switch to imports.

Imports of value-added MDF products

75. The parties to the proposed acquisition contend that if local manufacturers of raw MDF raise their prices too much, local downstream manufacturers of value-added MDF products (such as kitchens or furniture) will go out of business because their customers would import cheaper value-added MDF products into Australia.
76. The ACCC understands that certain types of value-added MDF products are being increasingly imported into Australia (e.g. flat pack kitchens for resale to consumers and installation in medium to high density apartment buildings). However, the ACCC understands that these imports remain a relatively modest proportion of all such products sold in Australia.
77. The ACCC does not currently consider that imports of value-added MDF products would indirectly act as a significant constraint on Borg following the proposed acquisition. If Borg increased the prices of its raw MDF, the increasing competitiveness of imported value-added MDF products would not be likely to reduce the volume of raw MDF sold by Borg or Laminex to such an extent that it would prevent Borg from profitably undertaking such a price increase. In addition, this may increase Borg's sales and profitability in that downstream value-added MDF market.

Barriers to entry are high

78. Consistent with the ACCC's previous review involving the manufacture of raw MDF, it considers that barriers to entry to the market for the manufacture of raw MDF are high.
79. The capital costs associated with establishing a greenfield raw MDF manufacturing plant are substantial, and sunk costs are likely to constitute a substantial proportion of those costs.

80. Further, Australian wood resources (and in particular, suitable pine) are generally already contracted for extended periods with existing manufacturers of raw MDF and other wood-based products.
81. The ACCC understands that Australia's capacity to manufacture raw MDF currently exceeds domestic demand. Accordingly, there is unlikely to be an incentive for a new entrant to establish a new raw MDF plant.
82. The ACCC currently considers that new entry is unlikely to occur in the foreseeable future and therefore, following the proposed acquisition, Borg would not be constrained by the threat of such entry.

Countervailing power

83. Given the likely height of the barriers to entry, and the difficulties reported by customers in relation to importing raw MDF, the ACCC considers that customers would be unable to credibly threaten to bypass Borg (e.g. by sponsoring new entry or importing raw MDF), if Borg sought to increase the prices of its raw MDF following the proposed acquisition.

Increased risk of coordination

84. As noted above, the proposed acquisition would reduce the number of raw MDF manufacturers in Australia from three to two and create a duopoly in the manufacture and supply of raw MDF. Borg and Laminex would be the only manufacturers of raw MDF in Australia.
85. The ACCC is concerned that the proposed acquisition is likely to increase the risk of coordinated effects in the national market for the manufacture and supply of raw MDF.
86. Consistent with its previous merger reviews, the ACCC does not consider that such coordination would require any explicit communication or commitment between rivals. Rather, rivals would act in their own self-interest, taking into account each other's likely actions and reactions.
87. The ACCC's preliminary view is that the reduction in competitive tension between the remaining raw MDF manufacturers could make it easier for them to coordinate key commercial decision-making, such as price increases, customer allocation, and output and/or production capacities, and would make it more likely that they would do so.
88. The ACCC considers that the market for the manufacture and supply of raw MDF has a number of characteristics that are likely to be conducive to coordination, such as:
 - a. The proposed acquisition will result in increased symmetry between the remaining raw MDF manufacturers, in terms of market shares and manufacturing scale.
 - b. Borg and Laminex are vertically integrated with significant downstream operations in value-added MDF manufacture and supply. Such similarly constituted firms, of similar size, may have reduced incentives to compete effectively to win market share.

- c. There are high levels of price and output transparency - prices charged by each supplier of raw MDF in Australia at any given time, proposals to increase prices and details of actual price increases are discussed widely in the industry and are well-known by most customers and suppliers.
 - d. There is limited product innovation (raw MDF products are relatively homogenous), limited fluctuations in costs (given the nature of the inputs required for raw MDF that are typically acquired through long term contracts), and demand from raw MDF customers is generally stable.
 - e. Interactions between suppliers of raw MDF further increases transparency in the market. Industry participants identified that manufacturers of raw MDF can and do seek supply from other manufacturers in the event that they experience a shortfall in production.
 - f. Customers of raw MDF tend to place frequent and small orders with manufacturers. Whilst some customers have a 12 or 18 month supply contract, generally long term supply contracts for raw MDF are rare. Customers can easily switch between suppliers so there would be little incentive for either supplier to deviate from a consensus to capture market share.
89. The ACCC is continuing to consider other aspects of the relevant markets to determine the likelihood of coordinated effects arising from the proposed acquisition.

ACCC's preliminary views

90. In summary, the ACCC is concerned that:
- a. The proposed acquisition will considerably reduce the bargaining power of customers when negotiating the prices of raw MDF by removing the third domestic manufacturer of the product.
 - b. Following the proposed acquisition, Borg would have a substantial, and considerably increased, market share and in the absence of constraints provided by Laminex or imports, Borg would be likely to increase prices or degrade other aspects of its offering (e.g. service or quality).
 - c. Following the proposed acquisition there would be insufficient competitive constraints on Borg and Laminex to prevent price increases or equivalent non-price degradation of their offers, including because:
 - i. Laminex may not be incentivised to compete vigorously against Borg in relation to the prices of its raw MDF
 - ii. Current imports of raw MDF into Australia are negligible, and customers are unlikely to be able to credibly threaten to switch to imports of raw MDF of suitable quality, in the sizes and thicknesses they require, and at competitive prices in the foreseeable future
 - iii. Imports of value-added MDF products appear unlikely to indirectly constrain Borg to a sufficient extent
 - iv. Barriers to entry appear to be high, and

- v. Customers appear to lack countervailing power.
- d. The proposed acquisition is likely to increase the risk of coordinated effects in the national market for the manufacture and supply of raw MDF, for instance by Borg and Laminex coordinating their prices of raw MDF.

The ACCC invites comments from market participants on its concern that the proposed acquisition would be likely to substantially lessen competition in the national market for the manufacture and supply of raw MDF. In particular, market participants may wish to comment on the following:

- Whether market participants would expect Laminex to compete vigorously with Borg following the proposed acquisition.
- By how much would the prices of Borg's raw MDF need to increase before customers would look to import raw MDF of a suitable quality? In responding to this question, please provide details of any overseas suppliers, and details of any quotes or responses received from overseas suppliers in relation to the supply raw MDF. Please also comment on lead times, warehousing needs, the availability of sizes and thicknesses, and logistics.
- If any New Zealand-based manufacturer of raw MDF has expressed a willingness to supply you with raw MDF, please identify the supplier, the available sizes and thicknesses, the anticipated shipping costs, the pricing at which that supply would occur, and the expected or actual duration from the placement of the order until receipt of the products.
- Whether actual or potential imports of value-added MDF products, including 'flat pack kitchens', would indirectly constrain Borg from raising the prices of its raw MDF.
- Have you observed any behaviour by manufacturers of raw MDF which may suggest that price-based coordination between such manufacturers would be likely following the proposed acquisition?
- How price-based coordination may occur between Borg and Laminex, having regard to customer experience of price increases by raw MDF manufacturers.

Issue of concern: Vertical foreclosure of rival manufacturers of value-added MDF products and intermediaries

- 91. Customers who compete with Borg and Laminex in the manufacture and supply of value-added MDF products have raised strong concerns that the proposed acquisition would remove the only manufacturer and supplier of raw MDF in Australia which is not also a significant manufacturer and supplier of value-added MDF products and therefore, is not one of their direct competitors. Customers expressed strong concerns that the proposed acquisition would provide Borg with an increased ability and incentive to foreclose and/or discriminate against them in the supply of raw MDF.
- 92. The ACCC's preliminary view is that the proposed acquisition is likely to provide Borg with market power in relation to the manufacture and supply of raw MDF

because it will not be sufficiently constrained. If so, Borg may have the ability and incentive to foreclose and/or discriminate against its downstream rivals in the manufacture and supply of value-added MDF products.

93. Borg and Laminex are vertically integrated into the downstream manufacture and supply of value-added MDF products. Alpine is currently the only manufacturer of raw MDF in Australia which does not produce a significant range or volume of value-added MDF products. For instance, Alpine does not produce any laminated MDF products. The removal of Alpine will therefore increase Borg's ability, and possibly its incentive, to engage in foreclosure or discrimination of those downstream rivals. For instance, by raising the prices they pay for raw MDF which is required to make value-added MDF products.
94. The ACCC notes that foreclosure and/or discrimination by Borg would only be successful if Laminex was unable or unwilling to supply the customers that Borg sought to foreclose and/or discriminate against. The ACCC is still considering Laminex's ability and incentive to supply raw MDF in response to an increase in the price or reduction in the volume of supply by Borg.
95. At this stage, the ACCC considers that Borg would be likely to have an incentive to engage in foreclosure and/or discrimination of those customers (e.g. by raising the costs of its downstream rivals), as the ACCC understands that Borg and Laminex earn greater margins from value-added MDF than raw MDF.
96. The ACCC understands that some distributors of raw MDF and manufacturers of value-added MDF products may already be unable to buy the raw MDF they require from Borg and/or Laminex on competitive terms.
97. Although Borg and Laminex may currently supply some of their downstream competitors with raw MDF, it is the ACCC's preliminary view that by removing the only manufacturer of raw MDF which has a strong incentive to supply wholesalers, distributors and manufacturers of value-added MDF products which compete with Borg and Laminex, the proposed acquisition is likely to increase Borg's incentive to foreclose supply to these customers, including competing suppliers of higher margin value-added MDF products.
98. The ACCC is therefore concerned that the proposed acquisition would provide Borg with an increased ability and incentive to:
 - a. restrict the supply of raw MDF to competing manufacturers of value-added MDF products, and/or
 - b. raise the costs of competing manufacturers of value-added MDF products by increasing the prices they must pay for raw MDF.
99. The ACCC currently considers that such foreclosure and/or discrimination would be likely to result in a substantial lessening of competition in national markets for the manufacture and supply of value-added MDF products.

ACCC's preliminary views

100. In summary, the ACCC is concerned that:
 - a. If the proposed acquisition proceeds, raw MDF will only be manufactured and supplied in Australia by Borg and Laminex, which produce significant

volumes of value-added MDF products, in favour of its own downstream operations and customers will no longer be able to buy suitable raw MDF from a supplier that they do not compete with downstream.

- b. The proposed acquisition may increase Borg's ability and incentive to foreclose supply of raw MDF to competing downstream manufacturers of value-added MDF products, which generate higher margins, regardless of whether it currently supplies these customers. This is likely to substantially lessen competition in national markets for the manufacture and supply of value-added MDF products.

The ACCC invites comments from market participants on its concerns in relation to the risk of foreclosure and/or discrimination of downstream competitors of Borg seeking to buy raw MDF. In particular, market participants may wish to comment on the following:

- Whether there are particular types of customers that Borg has refused to supply, or is likely to refuse to supply after the proposed acquisition, with competitively priced raw MDF. Please provide specific examples of any past refusals to supply, including the timing, reasons given and any pricing quoted.
- Whether it is likely that raw MDF manufacturers would have the incentive to reduce supply in order to foreclose to downstream rivals in the manufacture and supply of value-added MDF.
- Whether Laminex would be a willing and able supplier of competitively priced raw MDF, if Borg sought to raise its prices or reduce supply volumes after the proposed acquisition.
- The importance of Alpine in providing a source of competitively priced raw MDF for manufacturers of value-added MDF products, including those that compete with Borg (through Polytec) and Laminex.
- The relative margins generated by supplying raw MDF compared with the various value-added MDF products.

Issue that may be of concern: Aggregation in value-added MDF markets

101. As discussed above, Borg and Alpine overlap in relation to the manufacture and supply of two value-added MDF products, doorskins and mouldings, and the ACCC is considering whether there are separate product markets for different types of value-added MDF products.
102. Market participants have indicated that Borg and Alpine are the only manufacturers and suppliers of doorskins in Australia. The ACCC understands that Laminex does not supply doorskins in Australia, and that a producer of raw MDF or other value-added MDF products would need to make significant additional investment and have sufficient available space in order to begin making doorskins. As a result, the ACCC currently considers that Borg is likely to be the only manufacturer of doorskins in Australia following the proposed acquisition.

103. A number of market participants have identified concerns that as a result of the proposed acquisition, they will have no alternative but to purchase doorskins from Borg which will have the ability and incentive to increase prices.

ACCC's preliminary views

104. The ACCC's preliminary view is that this change in market structure may substantially lessen competition in the market for the manufacture and supply of the doorskins in the event that Borg does not face any effective competitive constraints.
105. The ACCC is seeking further information in relation to the manufacture and supply of doorskins to understand whether there will be any issues of concern.
106. The ACCC is also considering whether any competition issues are likely to arise in relation to the manufacture and supply of mouldings.

The ACCC invites comments from market participants on the aggregation in value-added MDF markets arising from the proposed acquisition, in particular doorskins. Market participants may wish to comment on the following:

- The likelihood of new entry for the supply of doorskins. For example, could existing manufacturers of other value-added MDF products begin making doorskins?
- The extent to which customers of doorskins could import doorskins or complete doors into Australia if domestic prices increased. Please provide reasons and identify any obstacles where relevant.
- Whether customers can purchase thin raw MDF and manufacture their own doorskins. Please describe the process that would be involved, including any special equipment that would be needed.
- The likelihood of new entry for the supply of mouldings. For example, could existing manufacturers of other value-added MDF products begin making mouldings?
- Whether customers of mouldings could import mouldings into Australia if domestic prices increased. Please provide reasons and identify any obstacles where relevant.

ACCC's next steps

107. The ACCC will finalise its view on this matter after it considers submissions invited by this Statement of Issues.
108. As noted above, 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. Submissions are to be received by the ACCC no later than 21 July 2016 and should be emailed to mergers@accc.gov.au.
109. The ACCC intends to publicly announce its final view by 1 September 2016. However the anticipated timeline may change in line with the *Informal Merger*

The Borg Group's proposed acquisition of the manufacturing assets of Alpine MDF Industries Pty Ltd

Review Process Guidelines. A Public Competition Assessment may be published following the ACCC's public announcement, to explain its final view.