Summary of Commission Decision of 9 January 2009 declaring a concentration compatible with the common market and the functioning of the EEA Agreement

(Case COMP/M.5153 — Arsenal/DSP)
(notified under document C(2008) 8439 final)
(Only the English text is authentic)
(Text with EEA relevance)
(2009/C 227/11)

On 9 January 2009 the Commission adopted a Decision in a merger case under Council Regulation (EC) No 139/2004 of 20 January 2004 on the control of concentrations between undertakings, and in particular Article 8(2) of that Regulation. A nonconfidential version of the full Decision can be found in the authentic language of the case and in the working languages of the Commission on the website of the Directorate-General for Competition, at the following address:

http://ec.europa.eu/comm/competition/index_en.html

I. JURISDICTION

(1) This case concerns a notification of a proposed concentration received by the Commission on 17 June 2008 following a referral request pursuant to Article 22(1) of the Merger Regulation, by which the undertaking Arsenal Capital Partners (‘Arsenal’, US) acquires, within the meaning of Article 3(1)(b) of the Merger Regulation, control of the whole of the undertaking DSM Special Products B.V. (‘DSP’, the Netherlands), a subsidiary of Royal DSM N.V. (‘DSM’, the Netherlands), by way of a purchase of shares.

(2) The Commission’s jurisdiction in this case is based on the referral request of 2 April 2008 submitted by the Spanish Competition Authority pursuant to Article 22(1) of the Merger Regulation. This request was joined on 28 April 2008 by the German Competition Authority. The Commission accepted the referral by decision of 16 May 2008, which was communicated to the notifying party on 29 May 2008.

II. THE PARTIES

(3) Arsenal is a private equity firm which controls, via its Arsenal Capital Partners QP fund, the undertaking Velsicol Chemical Corporation (‘Velsicol’, Estonia). Velsicol produces plasticisers, food additives and industrial intermediates. It is the only Arsenal business with activities in the sector affected by the transaction.

(4) DSP, a subsidiary of DSM, produces food additives and industrial intermediates.

(5) Both Velsicol and DSP are active in the manufacture and supply of benzoic acid and sodium benzoate. Velsicol also manufactures benzoate plasticisers, a downstream product to benzoic acid, in the EEA (Estonia), the United States and China. In China, Velsicol produces this product in a joint venture with Wuhan Youji Industries Company Limited (‘Wuhan’, China), the parties’ largest Chinese competitor for the production of benzoic acid. In the United States, Velsicol purchases benzoic acid for the production of plasticisers from Emerald Kalama Chemical LLC (‘Emerald’, United States), the parties’ only US competitor for the production of benzoic acid, sodium benzoate and benzoate plasticisers.

III. THE OPERATION

(6) The operation relates to the acquisition of control by Arsenal of DSP. DSP is a wholly owned subsidiary of DSM, the seller. The transaction, which concerns the manufacture of base chemicals, consists in the acquisition by Arsenal of 100% of the shares of DSP.

(7) However, the VevoVitall trade mark will continue to be owned by DSM Nutritional Products (‘DNP’, the Netherlands), a subsidiary of the DSM group. Under a supply agreement signed between DNP and DSP on 5 February 2008, DSP will continue to manufacture and sell VevoVitall to DNP. VevoVitall is the trade mark given to high purity benzoic acid for use in animal feed, currently protected by a patent owned by DSP.

(8) As the transaction will give Arsenal sole control of DSP through the acquisition of its entire issued share capital, it constitutes a concentration as defined in Article 3(1)(b) of the Merger Regulation.
IV. EXPLANATORY MEMORANDUM

1. Relevant markets

(9) The transaction relates to the production of solid technical grade benzoic acid, sodium benzoate and benzoate plasticisers. These products are produced by using liquid benzoic acid as an input. The parties to the transaction are the only producers of liquid technical grade benzoic acid, solid technical grade benzoic acid and sodium benzoate in the EEA. Velsicol also produces benzoate plasticisers in the EEA.

(10) While both DSP and Velsicol produce liquid technical grade benzoic acid, solid technical grade benzoic acid and sodium benzoate in their respective plants in Rotterdam and Estonia, the activities of the parties to the transaction only overlap with regard to solid benzoic acid and sodium benzoate as Velsicol produces liquid benzoic acid only for captive use.

1. Market for solid technical grade benzoic acid

1.1. Product market

(11) In line with the notifying party’s submission, the Commission concluded that technical grade benzoic acid constitutes a distinct product market from higher purity grade benzoic acids, i.e. ultra pure benzoic acid and animal feed benzoic acid, considering the limited demand and supply-side substitutability between these products. In addition, there is no overlap between the parties with regard to higher purity grade benzoic acid as only DSP produces this product.

(12) The Commission also confirmed the notifying party’s submission that technical grade benzoic acid should be further sub-divided into liquid and solid benzoic acid considering the limited demand and supply-side substitutability. In particular, liquid technical grade benzoic acid can only be transported to a limited degree, because it requires specialised transportation technology in order to remain liquid. Solid technical grade benzoic acid is produced using a ‘flaker’ in which the liquid benzoic acid is solidified and packaged. The different forms of technical grade benzoic acid (liquid vs. solid) imply that customers need different on-site handling and processing facilities for these products, and thus switching from one product to the other is not instantaneous and requires process adjustment and equipment investments (1).

(13) Based on the above, the Commission concluded that solid technical grade benzoic acid (hereafter ‘solid benzoic acid’) constitutes a separate product market.

(1) For example, a customer that uses solid benzoic acid requires a melting equipment that melts the benzoic acid before it can be further used in the production process.

1.2. Geographic market

(14) The notifying party submitted that the relevant geographic market for solid benzoic acid covers at least the EEA, the US and Asia, with these regions accounting for virtually all global production. This submission is based inter alia on the fact that significant trade flows take place between different areas in the world.

(15) The Commission’s market investigation showed, unlike the notifying party’s submissions, that the market for solid benzoic acid is EEA-wide for the following reasons: (i) the market for technical grade benzoic acid in the EEA is to a very large extent dominated by EEA-based producers, there are only marginal imports coming from China and the USA, and this trend has been constant at least for the last nine years; (ii) transport costs and a custom tariff of 6,5 % constitute important barriers to entry for non-European producers; (iii) the quality of Chinese benzoic acid is perceived by customers as low compared to the one produced by EEA-based producers; and (iv) prices in the different regions, i.e. the EEA, Asia and North America, are not moving closely together as would be expected if there was a wider global market. The Commission thus concluded that the relevant geographic market for solid benzoic acid is EEA-wide.

1.3. Product market

1.2. Market for sodium benzoate

1.2.1. Product market

(16) The notifying party submitted that the relevant product market for sodium benzoate should include potassium benzoate, calcium benzoate and sorbates. The investigation revealed that the transaction does not give rise to competition concerns on the narrowest possible market of sodium benzoate. The Commission thus leaves open the question whether calcium benzoate and potassium benzoate belong to the same product market as sodium benzoate. However, with regard to sorbates and in view of the results of the investigation, the Commission considers that sodium benzoate constitutes a separate market from sorbates.

1.2.2. Geographic market

(17) The notifying party considered that the relevant geographic market for sodium benzoate covers at least producers in the EEA, the US and Asia, which account for virtually all global production.

(18) The results of the Commission’s market investigation are not conclusive: while there are some factors that point towards an EEA-wide market, there are also factors that are consistent with a market wider than the EEA. However, as the transaction does not give rise to any competition concerns even on the narrowest EEA-wide market, the Commission leaves open the question whether the geographic market is wider than the EEA.
1.3. Market for benzoate plasticisers

1.3.1. Product market

(19) The notifying party submitted that all plasticisers (including for instance phthalates, polymeric, trimellitates, epoxy or benzoate plasticisers) should be considered to constitute one single product market as most plasticisers could be substituted by another plasticiser falling in a different category. As the notifying party produces benzoate plasticisers, the Commission evaluated whether benzoate plasticisers are part of a wider plasticiser market or form a market of their own.

(20) The results of the Commission’s investigation showed that benzoate plasticisers are not technically substitutable with all other plasticisers but only with a limited proportion thereof (the so-called phthalate plasticisers). However, given that phthalates are subject to new EU regulations due to their toxicity, there are only very few applications (such as PVC flooring) for which phthalates and benzoate plasticisers are substitutable. The Commission thus concluded that benzoate plasticisers form a product market of their own.

(21) Within benzoate plasticisers, there are various types of this product, such as mono-benzoates, di-benzoates, tri-benzoates, tetra-benzoates and various blends of benzoates. The majority of Velsicol’s plasticiser products fall within the category of di-benzoate plasticisers.

1.3.2. Geographic market

(22) The geographic market for di-benzoate plasticisers is subject to the same constraints, such as transport costs and customs tariffs, as the markets for benzoic acid and sodium benzoate. Transport costs account for approximately 8-10% of the cost of the product shipped between the US and Europe. Di-benzoate plasticisers entering the EEA are, like benzoic acid and sodium benzoate, subject to a 6.5% customs tariff.

(23) In addition, the US producer Emerald is the only non-EEA competitor of Velsicol that exports di-benzoate plasticisers to the EEA and currently has a market share of [5-10] % (1). There are no exports of this product from China to the EEA.

(24) The Commission thus concluded that the market for di-benzoate plasticisers is EEA-wide in scope, and that the competitive constraint exerted by the US producer Emerald is very limited.

2. Competitive assessment

2.1. Market for solid technical grade benzoic acid

(25) The main worldwide producers of solid benzoic acid are Velsicol, DSP, Emerald (US) and Wuhan (China). Several other smaller Chinese producers are also active. However, as illustrated below, Velsicol and DSP are the only credible suppliers of benzoic acid in the EEA. The market shares of the parties to the transaction and of their competitors in 2007 for supplies of solid benzoic acid within the EEA are as follows:

<table>
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<tr>
<th></th>
<th>DSP</th>
<th>Velsicol</th>
<th>DSP + Velsicol</th>
<th>Emerald (US)</th>
<th>Wuhan (China)</th>
<th>Others</th>
</tr>
</thead>
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Source: Form CO and Commission analysis.

(26) Prior to the transaction, DSP and Velsicol are the only two EEA-based producers of solid benzoic acid with already very high market shares. Non-EEA based producers export only a very marginal volume of benzoic acid to the EEA and this has been constant during the last nine years.

(27) Post-transaction, the new entity would enjoy a near-monopoly position with a combined market share as high as 90-100 % in the EEA, whereas the other producers, such as Emerald (USA) and Wuhan (China), would only have a very marginal presence.

(28) The market investigation confirmed that the parties to the transaction are each other’s closest competitors considering the quality concerns raised by customers as regards Chinese products and the very limited presence of Chinese or US producers in the EEA. Accordingly, the transaction would lead to the elimination of important competitive constraints that the parties to the transaction have previously exerted upon each other.

(29) In addition to the very high market shares, the Commission’s market investigation showed that EEA producers are protected by important barriers to entry such as customs tariffs and transport costs that limit Chinese and US competitors’ entry or expansion in the EEA. US and Chinese products bear additional transportation costs and tariffs that represent approximately 10-15% of the price of solid benzoic acid.

(30) The Commission thus concluded that it is very unlikely that the US or Chinese producers of benzoic acid would substantially increase their sales in the EEA should the merged entity decide to increase prices or restrict output in the EEA.

(1) Benzoate plasticisers Velsicol’s worldwide market share was [60-70] % in 2007, versus [10-20] % for Emerald. Source: Form CO.
The lack of Wuhan’s and Emerald’s competitive pressure on the EEA producers is best illustrated by the fact that neither of these producers increased their sales into the EEA when the market conditions on the benzoic acid market were extremely tight in 2007 and in the beginning of 2008 due to the simultaneous and unusually long maintenance shut downs of the plants of the two EEA producers. Instead, Wuhan actually increased the prices of its benzoic acid. Accordingly, the competitive constraints exercised by competitors post-transaction seem to be very limited, and thus it is unlikely that the competitors of the merged entity could thwart any price increases in the EEA.

Based on the foregoing, the Commission concluded that the proposed transaction would lead to a significant impediment of effective competition in the EEA market for solid benzoic acid.

The horizontal overlap between the parties’ activities in the manufacture and supply of sodium benzoate would result in the merged entity becoming the sole producer of sodium benzoate in the EEA with a market share of [60-70] %, while around [30-40] % would be in the hands of Chinese producers.

The market share held by Chinese producers appears to be a significant constraint that would discipline the combined entity post-transaction should it intend to increase prices above competitive levels. This is best documented by the development of the percentage gross margins of both of the parties to the transaction in the EEA (that can be thought of as the measure of competition in the market) that have been steadily decreasing over time as the Chinese exports of sodium benzoate have been increasing.

Finally, the spare capacities of Chinese producers and Wuhan in particular indicate that Wuhan would have the ability to supply more output to the EEA if the merged entity increased prices of sodium benzoate above a competitive level.

In view of the foregoing, the Commission considered that the ability and incentive of the combined entity to unilaterally increase prices post-merger in the EEA above a competitive level would be largely constrained by imports of sodium benzoate from China as well as by the threat of an increase of imports from China. Thus, the Commission concluded that the proposed transaction would not lead to a significant impediment of effective competition on the market for sodium benzoate, irrespective of whether the geographic scope of this market is EEA-wide or worldwide.

The Commission also examined whether the proposed transaction would create or strengthen a collective dominant position on the market for sodium benzoate and found that it is unlikely that the transaction would lead to such an outcome. This is because the Chinese producers have increased their sales in the EEA by over 400 % from 1999 to 2007 and currently account for around [25-45] % of the EEA market. Any coordination scheme would thus require the participation of the Chinese producers, as if only the merged entity and the US producer engaged in a coordination scheme of any kind, it is likely that this would result in further increases of Chinese exports to the EEA given that the Chinese exporters managed to increase their market share to 35 % in the last nine years.

The question thus remains whether the Chinese producers would find it profitable to enter into a coordination scheme. As the Chinese producers managed to increase exports to the EEA by 400 % in the last nine years, it is unlikely that their behaviour would change post-transaction. Moreover, it is important to note that there are four Chinese producers, and thus any coordination scheme would require participation of most of them (if not all) as there appear to be large spare capacities in China.

The Commission thus ultimately concluded that the acquisition of DSP by Velsicol would not create nor increase any incentive for the producers of sodium benzoate to coordinate their activities.

Benzoic acid is the core component used to produce di-benzoate plasticisers, as 0.75 of a ton of benzoic acid is necessary to produce one ton of di-benzoate plasticisers. There are no substitutes for benzoic acid, and the merged entity would be the sole producer of liquid benzoic acid in the EEA and would have [90-100] % of the solid benzoic acid market. All producers of plasticisers currently have long-term contracts for the supply of liquid benzoic acid, with one of the four producers (Ferro) having been recently offered a new long-term contract for the supply of liquid benzoic acid.

The Commission concluded that, while the merged entity would have market power vis-à-vis its downstream competitors with regard to the supply of benzoic acid, its ability to foreclose the downstream competitors would be limited due to the existence of long-term contracts.
2.3.2. Incentive to foreclose

(42) Pre-transaction, DSP is not in competition with the producers of benzoate plasticisers and has an incentive to supply these producers with benzoic acid at a price which is sufficiently competitive to enable them to profitably remain on the market. The acquisition of DSP by Velsicol changes the incentive of DSP as the latter would then be part of a vertically integrated company supplying benzoic acid but also producing di-benzoate plasticisers. DSP/Velsicol’s incentive to foreclose its downstream competitors would thus depend on the profitability of such a foreclosure strategy.

(43) The Commission’s analysis showed that the merged entity would have no incentive to foreclose any of the four benzoate plasticiser companies (Caffaro, Ferro, Evonik and Exxon Mobil), as the gains that it would make on the downstream market for benzoate plasticisers would be more than outweighed by the losses on the upstream market for liquid benzoic acid.

2.3.3. Impact on customers

(44) As Velsicol/DSP would have limited ability to foreclose and in any case no incentive to foreclose any of its competitors in the EEA, the transaction would have no impact on the downstream market.

3. Remedies

3.1. First set of remedies

(45) On 6 November 2008 the notifying party proposed remedies to address the Commission’s concerns regarding the market for solid benzoic acid. The notifying party offered as remedies the divestment of all the solid benzoic acid and sodium benzoate capacity production in the Estonian plant as well as the worldwide customer lists for benzoic acid and sodium benzoate. As regards liquid benzoic acid, the main input for the production of solid benzoic acid and sodium benzoate, the notifying party proposed the creation of a Joint Venture (JV) in the same Estonian plant. Each partner to the JV would be allocated 50% of the current production capacity of liquid benzoic acid. While the JV would be jointly controlled by the two partners, the notifying party would own 51% of the shareholding and the remaining share would be owned by the purchaser.

(46) The vast majority of the respondents (12 out of 15) to the Commission’s market test on the remedies proposed considered that the latter would not ensure the viability of the divestment business and would not restore competition on the market for solid benzoic acid.

(47) The main opposition to the commitments related to the JV for liquid benzoic acid. In particular, respondents emphasised that the notifying party, by having joint control over liquid benzoic acid, which is the main input for the production of solid benzoic acid, would continue to have influence over the production of solid benzoic acid. In a duopoly market, such a structural link between the purchaser of the divestment business and the merged entity, the only two producers of solid benzoic acid in the EEA, would be likely to impede effective competition. Some respondents also expressed concerns that (i) the principle of common decision-making would jeopardise the everyday running of the business; and (ii) the JV would increase transparency in the market for solid benzoic acid as the notifying party would be aware of the cost structure of its only competitor in the EEA.

(48) Moreover, some respondents submitted that the notifying party would not have an interest to undertake capacity extension in the Estonian plant (jointly with the purchaser) but rather at the Rotterdam site. Accordingly, the purchaser would have to invest unilaterally in increasing the production capacity in Estonia and thus bear all related costs for the increased capacity, which according to the notifying party would have to be for at least 20 Kp. The respondents considered that the purchaser would not undertake such an investment unless it obtained in return the majority in the shareholding of the JV and the control of the JV.

(49) In light of the above, it was concluded that the first set of remedies submitted by the notifying party had been rejected by the market. The JV structure was not considered of a kind to ensure the viability of the divested business, and there was a consensus on the market to consider that the notifying party would keep a de facto control of the production of solid benzoic acid. The first remedy proposal, while removing some of the competition concerns raised by the transaction, did not fully remove them. The Commission thus concluded that the first set of remedies could not be accepted.

3.2. Second set of remedies

(50) On 3 December 2008 Arsenal submitted an amended set of remedies consisting in the divestment of the upstream liquid benzoic acid plant at the Estonian site and the divestment of the two downstream solid benzoic acid and sodium benzoate plants at the Estonian site along with the transfer of Arsenal’s worldwide customers for solid benzoic acid and sodium benzoate.

(51) The third remaining downstream plant at the Estonian site for the production of benzoate plasticisers would remain in Arsenal’s ownership, and its requirements for liquid benzoic acid would be served by an evergreen long-term contract with the purchaser of the divested business. Through this long-term supply contract, Arsenal would...
be entitled to 50% of the liquid benzoic acid capacity of the plant. The price of the liquid benzoic acid under the supply agreement would be determined on the basis of current costs and a pricing formula index.

(52) This second remedies proposal would overcome the concerns reflected on the remedies market test, in particular the most significant concerning the JV to be created by the purchaser and Arsenal under the first set of commitments. Under the new set of remedies, the structural link between the divestment business and Arsenal (via the upstream liquid benzoic acid JV) would disappear. The new remedies would also resolve the concern revealed by the market test that the purchaser of the divested assets would be unlikely to undertake any capacity expansion in Estonia in the framework of a JV in which it only had a minority shareholding.

V. CONCLUSION

(53) In the light of the second set of commitments submitted by Arsenal, the decision concludes that the proposed concentration will not significantly impede effective competition in the Common Market or a substantial part of it.

(54) Consequently, the decision declares the concentration compatible with the Common Market and the functioning of the EEA Agreement, in accordance with Article 2(2) and Article 8(2) of the EC Merger Regulation and Article 57 of the EEA Agreement.