

**COMPETITION TRIBUNAL
REPUBLIC OF SOUTH AFRICA**

Case No: 36/LM/Jul03

In the large merger between:

Chemical Services Limited

and

Ondeo Nalco SA (Pty) Limited

Reasons for Decision [Non-Confidential Version]

APPROVAL

On 18 September 2003 the Competition Tribunal issued a Merger Clearance Certificate in terms of Section 16(2)(a) of the Act approving the merger Chemical Services Limited and Ondeo Nalco SA (Pty) Ltd. The reasons for the approval of the merger appear below.

The Parties

1. The acquiring firm is Chemserve Services Limited (“Chemserve”), a holding company for Chemical Services Group. Chemserve, as a holding company, does not itself engage in activity in South Africa but its subsidiaries are engaged in the business of chemical supply to various local industries.
2. Chemserve is a subsidiary of AECI Limited (“AECI”), a public company listed on the JSE. AECI is described as a “speciality product and service solutions organization active in the chemical industry”. It operates in South Africa through five subsidiaries:
 - ?? African Explosives
 - ?? Sans Fibres
 - ?? Dulux
 - ?? Heartland Properties
 - ?? Chemserve

3. Only Chemserve is relevant to this transaction. All the chemical activities of AECl are consolidated in Chemserve.
4. Chemserve has a variety of subsidiaries operating in South Africa. For our purposes, only Pelichem (Pty) Ltd ("Pelichem") is relevant. Pelichem serves the water and mining industries by supplying various chemicals and equipment to the extractive, sewerage treatment and water service industries.
5. The target firm is Oudeo Nalco SA (Pty) Ltd ("ON"). ON is jointly controlled by its holding company, Oudeo Nalco Company, ("Oudeo Nalco USA"), and Chemserve. Each currently hold a 50% stake in ON. Oudeo Nalco USA is incorporated in the USA and ultimately controlled by the French-based Suez Group.

The Merger Transaction

6. In terms of the Shares Agreement, Chemserve is acquiring the additional 50% shareholding held by Oudeo Nalco USA. Post-merger, ON will be a wholly-owned subsidiary of Chemserve.

Rationale for the Transaction

7. The parent company of Oudeo Nalco USA, the Suez Group, wants to withdraw from its emerging market operations worldwide.

The Relevant Market

8. Chemserve's 19 autonomous SMME businesses market specialty chemicals to many industries within Southern Africa.¹ Its website describes it as "*the largest specialty chemical operation in southern Africa. The group comprises a number of autonomous subsidiaries and joint ventures, supplying a diverse range of specialties, raw materials and related services to a broad spectrum of industries.*"
9. ON is involved in the manufacture and supply of chemicals to the petroleum industry and the in the provision of water treatment solutions to customers in SA and the Indian Ocean islands². This latter service will comprise chemical products, the service component and sometimes,

¹ Speciality chemicals are defined as those products which act as additives to enhance the process efficiencies of most manufacturing industries.

² Amongst other functions, which include the manufacture and supply of chemical products to the petroleum industry; supply of ion exchange resins; supply of water treatment plants and lab equipment, which are not relevant for the purpose of this transaction

equipment.³ On its website it describes itself as “the leading water management, energy and process chemicals supplier in SA.”

10. The overlap occurs insofar as Chemserve’s subsidiary, Pelichem and ON are active in the market for the supply of water treatment solutions⁴. The Commission defines this more narrowly, as being the market for water clarification and solid liquid separation solutions in RSA.
11. The parties tried to explain away the overlap by contending that the merging parties focus on different customer segments – Pelichem (Chemserve) on customers in coal and diamond mining and ON on customers in industrial, food and heavy industries. They also state that the applications of each firm’s products are different. One is involved in surface applications, the other in underground applications, servicing the supply chain to the mining industry. According to the parties therefore, if one analyses the market closely, the primary and target firms do not compete head-on. The MD of ON remarked at the hearing that although similar technology is available to both merging firms, they are focused on different markets.
12. The Commission maintained that the market for the supply of water clarification and solid liquid separation market does constitute one market, since they had interviewed competitors and a chemical consultancy who confirmed that there is no distinction between the two firms’ applications and in fact, each firm can change their operations to conduct either application.
13. It therefore appears that the market could be defined as two separate ones. It could either be defined according to the differing surface or underground applications to which the firm’s technology could be applied. Alternatively, it could be defined as one market for the provision of water clarification and solid liquid separation solutions in RSA, as the Commission have done. However, as appears from the competitive analysis below, it is not necessary for us to decide on the precise ambit/parameters of the market.

Geographic Market

³ On page 379 of bundle, in Competitiveness Report, page 7, ONSA is stated to be involved in the “manufacture and supply of chemical products to the petroleum industry”. However, for the purposes of this transaction, this is irrelevant because there is no overlap with Chemserve in respect of the petroleum industry as it does not source inputs for use in petroleum industry products from Chemserve.

⁴ There is no overlap insofar as the manufacture and supply of petrochemicals is concerned.

14. The parties suggest that the **upstream market** (for the supply of chemical products for use in water treatment solutions) could be international in that there are significant imports into the market, but proceed to evaluate this transaction on the basis of the narrower, national market.
15. As far as the **downstream market** (for the provision of water treatment solutions) is concerned, it is also national since the total product is provided nationally by service providers.
16. The relevant market is therefore national.

Impact on competition

Horizontal Effect

17. The Commission evaluated the horizontal overlap in the downstream market in that Chemserve's subsidiary, Pelicham, is also active in the provision of water clarification and solid water separation solutions. Assuming we accept that the acquiring and target firms belong to the same relevant market, the combined market share in the market for provision of water clarification and solid liquid separation solutions in RSA is 30%.

Market Shares for water clarification and solid liquid separation

<u>Firm</u>	<u>Market Share</u>
Zetachem	[]%
<i>Pelichem</i>	[]%
BHT Drew (aka Sud -Chemie)	[]%
<i>ON</i>	[]%
Others	[]%

18. The parties and the Commission maintain that barriers to entry into this market are low. The chemicals are described by the parties as homogenous commodity products that can be easily sourced from other suppliers. Because such products are easily obtainable, many small firms have recently entered the market.
19. At the hearing, the Managing Director of ON confirmed the ease of entry into the market and the nature of competitors who could enter. On the one hand, small to medium-sized enterprises could import the materials via the Internet from any supplier in the global supply chain and compete.

Secondly, ON competes with global technology suppliers, such as Sud-Chemie, all international companies with international technology.

20. Potential competition also exists in that supply side substitution is easy by firms in the water treatment solution market generally.
21. Customers (particularly in the mining and steel industries) can switch easily between suppliers of water clarification and solid liquid separation solutions.
22. Post-merger, ON and Chemserve's subsidiary Pelichem will remain separate autonomous firms, each focussing on their respective specialities.

Vertical Effect

23. The vertical integration issue is that the acquiring firm, Chemserve, through its subsidiaries, supplies Ondeo Nalco with various chemical products which ON in turn uses as inputs into its chemical water treatment solutions. Furthermore, Ondeo Nalco has in the past provided water treatment solutions to Chemserve subsidiaries. The Commission interviewed other customers and suppliers of the parties who maintain there is no chance of foreclosure.
24. As far as backward integration is concerned, (ON integrating with a supplier of chemicals) the parties argue that it would not be economically feasible for Chemserve to foreclose other customers the supply of chemicals, as only []% of its total sales are accounted for by ON. The remaining []% of its sales is to other customers. Therefore, it would not make sense to foreclose this market which would reduce the viability of Chemserve's business.
25. Furthermore, ON only buys []% of its chemical requirements from Chemserve, the rest from a variety of other suppliers in SA and abroad. There is apparently an active trading sector whereby agents handle the importation and marketing of chemicals.
26. In further defence of this transaction, the parties state that this is merely a change in shareholding and doesn't affect competitive conditions in the industry. Chemserve had management control pre-merger anyway so the parties state that there will be no management change in ON post-merger as Chemserve will continue to manage it.

We accordingly conclude that this merger will not lead to a substantial lessening of competition. There are no public interest concerns which would alter this conclusion. The merger is therefore approved unconditionally.

N. Manoim

14 October 2003
Date

Concurring: D. Lewis, M. Madlanga

For the merging parties:	Webber Wentzel Bowens Attorneys
For the Commission:	R. Labuschagne, Competition Commission