ANGLO AMERICAN/LAFARGE MERGER INQUIRY

Summary of hearing with Aggregate Industries held on Monday 10 October 2011

Background

1. Aggregate Industries (AI) was formed in the late 1990s through a merger of Bardon and CAMAS. It remained a public company until early 2005 when it was purchased by the Swiss heavy building materials company, Holcim. The group was primarily UK- and US-based, but also had operations in Norway. After the acquisition by Holcim, the company purchased Foster Yeoman which enabled the group to sell into the northern European market.

2. Some of AI's main customers were Travis Perkins, B&Q, the Highways Agency, Transport Scotland, and major national contractors such as Balfour Beatty, BAM Group and Carillion.

3. AI has four different operating divisions—Aggregate Products, Concrete Products, Overseas and Cementitious. Turnover and profitability had broadly decreased over the last couple of years across all divisions (although there were some variations with the Overseas division) and AI expected the trend to be flat over the next couple of years. It noted considerable uncertainty in the market and difficulties in particular with the reduction in public spending. A further issue concerned an exponential increase in energy and hydrocarbon-related input costs. It was not aware of any significant regulatory issues affecting the industry over the last five years.

4. AI was a member of the Minerals Product Association (MPA) and the Construction Product Association (CPA).

Market definition and competition

5. AI produced a range of aggregates (rock, sand and gravel and secondary aggregates), ready-mix concrete (RMX), asphalt, and a range of concrete products (such as blocks and paving), and it also imported CEM1 cement.

6. It did not produce or import CEM2 or CEM3. It did, however, blend CEM1 mainly with Pulverized Fly Ash (PFA) but also with Ground Granulated Blast-furnace Slag (GGBS), at its RMX plants and concrete products factories (PFA was preferred on grounds of cost and AI would be willing to consider more cost-effective alternatives). A minimal amount of GGBS was bought from Civil and Marine (Hanson) and was also imported from Holcim Germany, whilst PFA was predominantly purchased from Drax. AI confirmed that Hanson was the only source of domestically produced GGBS.

7. The overall cement market in the UK was approximately 8–9 million tonnes a year and it did not see anyone willing to invest in capacity expansion. Cement was a product that could be supplied globally and the location of manufacture did not matter; all that mattered was being able to provide a competitive offer. AI did not believe that it faced any disadvantages compared with domestic producers of cement and did not consider that there were any issues about quality (it used the same UK testing regime).

8. Broadly speaking, secondary and recycled aggregates could be substituted for primary aggregates in a limited way in low-specification applications (such as sub-base and fill-type applications). However, recycled aggregates included material (for example, asphalt planings, incinerator bottom ash and crushed glass) that could be used as substitutes in fairly high-specification areas. Further, china clay by-products from Devon and Cornwall, a secondary aggregate, were pretty much used as a complete substitute for primary aggregates across all applications (for example block manufacture and RMX in the South-West).

9. There were no major issues with the availability of secondary and recycled aggregates and they formed around 25 per cent of the total demand for UK aggregates. This indicated a regular and consistent source of supply.

10. Volumetric trucks were generally substitutable with RMX, although it did not meet with high-specification requirements and was generally a lower-grade product, which was not strong enough for projects like a nuclear power plant or a skyscraper. Volumetric trucks now accounted for 10 per cent of the concrete market despite only entering the market around 10 to 15 years ago, although this was likely to be accounted for by low-specification projects requiring smaller volumes.

11. RMX site plants were only suitable for large-volume jobs and there was a minimum volume requirement over a long contract period before using RMX site plants was cost-effective. Mobile asphalt plants were similar and viable only for fixed contracts, which required a very high level of service (such as airfield resurfacing).

12. Some of AI's asphalt plants had permission to operate 24 hours a day, seven days a week, reflecting the need that some of its customers required this degree of access to such plants. These plants were used to supply jobs that needed to be carried out at night (for example, road resurfacing—the Highways Agency was a major user of 24/7 asphalt plants) and the asphalt produced tended to be more expensive, reflecting the increased labour costs of night-time work.

13. AI had a range of aggregate competitors, both nationally (CEMEX, Hanson, Lafarge and Tarmac) and at a regional level (ranging from small family-owned SMEs to large plc businesses such as Breedon). There were regional areas where Tarmac and Lafarge were seen as particularly strong, such as the supply of sand and gravel in the South-East, asphalt in the South-East and limestone in Derbyshire and the Manchester/South Yorkshire/West Yorkshire areas.

14. AI had a number of rail depots in and around south-east England and London, and taking the low-cost route to market was key to any manufacturing site. Opening a new rail depot was not as difficult as a sand and gravel quarry, although it did take some time. However, there were some issues concerning access to the railway network as there were only a limited number of paths available. Obtaining the right path at the right cost was as important as developing a new railhead.

15. AI was also involved in road surfacing and paving throughout Scotland and England. Its main competitors for road surfacing were Tarmac, Lafarge, Hanson and CEMEX, as well as hundreds of local and regional companies such as Breedon, Tillicoultry, Colas, Eurovia and Conway.

AI as a customer

16. AI only purchased aggregates for asphalt and concrete from Tarmac and Lafarge (although it also had a joint venture with Tarmac for the M74 contract in Scotland, through which AI jointly supplied RMX and asphalt with Tarmac to one scheme). AI

had purchased these products from Tarmac and Lafarge for four to six years. Some of its sub-divisions might purchase materials from other companies where they were competitive (geographically) for a particular job.

17. AI purchased aggregates where it did not have its own plant or quarry with sufficient proximity to demand. A significant proportion of cement purchased by AI was supplied by Holcim Germany. In the event that Holcim Germany did not have the capacity to supply AI, where it was cost-effective to do so (for example, taking account of fuel costs, distance of site from the coast and exchange rates), AI purchased the balance of the required cement mainly from Lafarge, but also from CEMEX and Hanson. Due to the UK's geographical location and its need for cement to be transported by sea, the UK experienced a lack of supply capacity from Europe due to and as a result of the EU emissions trading scheme, which resulted in cement producers preferring not to produce cement and instead trade their excess CO2 allowance.

18. AI stated that it generally had no problems obtaining the materials that it required although there had been localized problems at periods of peak demand in 2006 and 2007. Given the overall drop in demand (by about 30 to 50 per cent) this was now less of a problem except for where reserves had run out.

Purchasing process

19. AI tried to maintain flexibility and obtain the best commercial price. It treated its sourcing of materials like any other product and would look at all suppliers, find the best price, and use benchmarks in negotiations. AI purchased aggregates from Tarmac, Hanson, CEMEX, Lafarge and other companies on a spot basis, in accordance with geographical requirements.

20. Its customers mainly bought products on a spot basis, with no fixed supply contracts. Prices were set by negotiation and whilst it was told by customers of prices offered by other suppliers, it had no idea if they were accurate or not.

21. AI was not aware of suppliers refusing to provide customers with quotes or indeed supply them; however, there might be occasions when this occured where customers had a poor credit rating or a poor credit history. Given the current reduction in demand, suppliers such as AI had every incentive to take on as many customers as were looking for supply.

Barriers to entry/expansion

22. A new supplier would have to assess the cost of any investment, planning consent and of the area. For example, it took about five to six years to get consent for a new quarry or for an extension to a sand and gravel quarry, for which expertise was required. It was not beneficial having a quarry in Cornwall if the customers were in Hampshire.

23. The cost of a new cement plant in the UK would be around £500–700 million.

The counterfactual

24. Should the joint venture not go ahead the market would nonetheless get more and more concentrated. It was aware that Anglo American was looking to divest Tarmac and that it would find a way to do so.

Views on the joint venture

25. AI had no concerns relating to road surfacing or cement. Its concerns related to the supply of aggregates, asphalt and RMX in local markets. In particular, this related to limestone aggregates in Derbyshire, sand and gravel in the Home Counties, and rail-linked positions in Derbyshire and Leicestershire.