15 November, 2013
1. This Response is submitted by Lafarge Tarmac ("LT") in response to the Competition Commission’s ("CC") Addendum to the Provisional Findings\(^1\) providing further analysis on GGBS and GBS ("GGBS Addendum") in connection with its market investigation into the acquisition or supply in GB of aggregates, cement and ready-mix concrete (the “MIR”). This Response also addresses the CC’s GBS remedy proposals outlined in its Provisional Decision on Remedies (“PDR”).\(^2\)

2. LT considers that a remedy affecting the supply of GGBS in GB has the potential to address both the adverse effect on competition ("AEC") that the CC has identified in the supply of cement in GB and in the supply of GGBS. LT does not consider that the CC’s analysis (on which it has further commented in detail in the response to the PDR) at all supports its conclusion that there is an AEC in the supply of cement resulting from coordination. Furthermore, were any remedy in fact justified, a remedy focused on the supply of GGBS alone would be a more effective and more proportionate remedy than a cement plant divestment by LT (see section 4 of RBB Annex to LT’s Response to the PDR).\(^3\)

3. LT has encouraged the CC to consider the way in which a break-up of the GGBS supply arrangements, together with a possible divestment of GGBS grinding facilities, might increase the volume of cementitious material supplied in GB such that it would have the effect of placing downward pressure on the price of cementitious material, including grey cement.

4. It is incumbent upon the CC to consider whether a possible remedy in relation to GGBS in GB would be adequate and appropriate to address the alleged AEC that the CC has identified in both the supply of GGBS and the supply of cement. The CC is required when selecting remedies in the context of a market investigation to ensure that these are proportionate to the harm identified.

5. LT has already made submissions that the divestment of one of LT’s Tunstead or Cauldon cement plants would not be appropriate (i.e., effective), in particular given that both of those cement plants are already operated at full capacity. Such a divestment would therefore not increase cement output but would be almost certain to

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\(^1\) Published 10 October 2013.  
\(^2\) Published 10 October 2013.  
\(^3\) “Consumer detriment and profitability: a response to the Provisional Decision on Remedies”, dated 11 November 2013.
increase unit production costs for both LT and for the acquirer of the divested cement plant (relative to LT’s current cost of operation), putting upward pressure on prices.

6. In its response of 25 June 2013 to the CC’s Remedies Notice, LT outlined that the divestment of a cement plant already operating at capacity would not be an effective remedy, and also suggested an alternative remedy in relation to GGBS arrangements in GB. This alternative remedy would prove effective by making available to any willing purchasers GBS produced on an ongoing basis in addition to large amounts of GBS that are currently stockpiled, thereby increasing the supply of cementitious material available in GB, which would be equivalent to the construction of a new standard-sized cement plant (but without incurring the associated capital expenditure). Unlike a divestment of a cement plant, a GBS/GGBS remedy would immediately place considerable downward pressure on cement and cementitious material prices in GB.

7. This Response document considers three main points arising from the CC’s GGBS Addendum and PDR:

(a) **Market definition.** LT considers that the CC has incorrectly defined as a separate product market the supply of GGBS. LT continues to consider that the functional substitutability between GGBS, CEM I and PFA means that all of these materials should form part of a broader cementitious market.

(b) **The incentives of LT (since its formation in January 2013), and the incentives of the legacy Tarmac and legacy Lafarge businesses prior to the formation of the joint venture in January 2013.** LT disputes the characterisation cast by the CC that prior to the formation of LT in January 2013, the legacy Lafarge and Tarmac businesses had any ability or incentive to influence the price of GGBS in GB.

(c) **LT’s alternative proposal to address the CC’s alleged AEC in cement (and GGBS).** LT considers that an alternative remedy (similar to arrangements currently in place in Germany) in which LT would retain its position in GBS, but would auction tranches of GBS to any willing purchasers would be more proportionate and more effective in addressing the AEC that the CC has identified in both the supply of cement and the supply of GGBS in GB.

8. Each of these is considered in turn below.

**A. MARKET DEFINITION**

9. In the GGBS Addendum, the CC concluded that although “on the face of it” evidence available to it suggests that “**GGBS is part of wider product market including CEM I as well as PFA (a broad cementitious market)**”, the CC considered that this may only be due to the “cellophane fallacy”.

10. After assessing and then concluding that Hanson earns excess profits in the production and supply of GGBS, the CC then concludes that “**current prices are likely to be above the prices that would prevail in a well-functioning market**” which is likely to result **“in a product market definition, at current GGBS prices, which is broader”**
(i.e., in which there would appear to be more substitutability with non-GGBS alternatives) than that which would prevail in a well-functioning market with several competing producers of GGBS in GB in which GGBS prices would be lower and substitutability with non-GGBS alternatives would be much more limited” (GGBS Addendum, paragraphs 42-43).

11. The CC then concludes that “if there were several competing producers of GGBS in GB, we would expect these to be more focused on competing between themselves for selling GGBS to GB customers, rather than on competition with CEM I and PFA. We would therefore expect that, if prices for GGBS were at competitive levels, the extent of substitution between GGBS on the one hand and CEM I and PFA on the other would be significantly more limited than that which we observe at current GGBS prices” (paragraph 42).

12. LT notes that the cellophane fallacy occurs only when competitively priced products are analysed in relation to a product which at prevailing prices is priced at monopolistic or above-competitive prices, potentially leading to too broad a market being defined. However, the CC has provisionally concluded that GGBS prices are not competitively priced (due to the monopoly on domestic supply) and that CEM I prices are not competitively priced due to the alleged presence of coordination in the cement industry.

13. Furthermore, LT considers that the CC is wrong to conclude that Hanson’s current profitability in GGBS does not prove that there would be no inter-relationship between GGBS and CEM I and PFA even if the price of GGBS were set at “competitive” rates. If the price of GGBS were lower (i.e., more competitive), LT expects that substitution between CEM I, GGBS and PFA would continue because the functional inter-relationship between these products would remain. As is the case now, substitutability between the products will be dynamic and driven by a range of factors.

(a) **Functional substitutability**: There is functional substitutability between the different inputs to produce a unit or cubic metre of concrete. Under the relevant standards, GGBS is substitutable at a rate of 50-95% with CEM I. A concrete or blended cement manufacturer will consider the alternative costs of different inputs and choose the inputs that allow him to produce at the lowest cementitious cost per cubic metre of concrete.

(b) **Environmental considerations (including regulations, the cost of CO₂ and consumer preferences for sustainability) incentivise the use of CEM I alternatives**: Environmental legislation including, for example, the cost of CO₂, influences the decision to use CEM I relative to PFA and GGBS, depending on the differing impact of these regulations on the cost of producing these alternatives. For example, if CO₂ costs increase, the costs of CEM I will also increase, thereby incentivising greater use of GGBS than

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4 Please note that under EN 197, CEM II cements can contain up to 35% of either GGBS or PFA (among other additives). In this respect, please see attached a document setting out the blends under the EN 197 standard. This also shows that CEM III can contain up to 95% GGBS.
CEM I. There is also increased demand for sustainable products which must be produced using greater quantities of CEM I substitutes.

14. The CC’s position that the inter-relationship between GGBS, CEM I and PFA would not continue if GGBS were priced competitively is premised on the view that the relationship is static. But it is not: the inter-relationship between these additions is dynamic. This best is illustrated in the use of cementitious materials in Europe.

15. LT submitted to the CC on 31 July 2013 evidence of the use of GGBS in other countries within the EU27. This evidence was contained in a Cembureau report detailing levels of GGBS/PFA substitution. Published in 2010, the report provides the most up-to-date overview of blended cements used in the EU27 and in other countries included in the scope of the report. The report identifies how significant blended cements are in other European countries: 74% of all domestic deliveries are accounted for by blended cements, while only 26% are accounted for by CEM I. The data covers the full range of blended cement classifications (i.e., CEM II, III, IV and V) and therefore highlights the use of GGBS, PFA, limestone, silica fume, natural pozzolana (and combinations thereof) that are used as additions to replace clinker in cements according to standard EN 197. This evidence shows there are still different rates of substitution of GGBS/PFA and CEM I in Europe as a consequence of the different dynamics at play. Accordingly, even if the price of GGBS were set at a lower level, LT expects that the inter-relationship between CEM I and GGBS/PFA would continue, such that it is appropriate to consider that they form part of one and the same relevant product market.

16. The CC has taken a very superficial approach to market definition, overlooking the practical reasons and dynamic considerations that might drive substitutability between CEM I, GGBS and PFA in the industry at any one point in time. LT considers that the CC has not engaged in a thorough and rigorous analysis of the product definition and has therefore incorrectly concluded that there is no broader “cementitious” market in GB.

17. We also note that the CC concedes that there is a relationship between the prices of GGBS and cement. In the PDR, the CC said that “we expect the overall impact of these measures will be to put downward pressure on GGBS prices, driving them towards competitive levels. This in turn would address the distortion caused by the current operation of the GGBS supply chain in the GB cement markets and hence would also be expected to reduce the price of cement” (paragraph 6.12). This is clearly inconsistent with the position that the CC adopts in relation to the product market definition.

B. INCENTIVES OF LT, AND OF THE LEGACY LAFARGE AND TARMAC BUSINESSES

18. As to the AEC in GGBS identified by the CC, LT considers that the AEC in the supply of GGBS in GB arises not from LT’s position in the supply chain, but from the position that Hanson has in the supply chain, by which it has the exclusive right to purchase all GBS for cementitious applications in GB. Indeed, LT is merely a price-taker under the agreements that LT has in place with Hanson for the supply of GBS. The CC acknowledges this: “the price of GBS which Lafarge Tarmac receives from
Hanson is currently set under the GBS agreements as a percentage of Hanson’s selling price of GGBS” (PDR, paragraph 134).

19. LT therefore considers that the CC has mischaracterised LT’s position and incentives in relation to its activities in GBS. Most importantly, the CC considers that coordination between LT and Hanson in cement acts as a further disincentive on LT and Hanson to seek lower GGBS prices (GGBS Addendum, paragraph 83). This is problematic for a number of reasons:

(a) **First**, as the CC concedes, LT (and the legacy Tarmac business) has no ability whatsoever to influence the pricing of GGBS under its GBS supply agreements with Hanson. Moreover, although given the absence of any ability it is not relevant to the assessment, Tarmac was not a member of the purported coordinating group in cement and yet the CC has found that competition in the supply of GGBS has not been effective even before Tarmac became LT i.e., before January 2013.

(b) **Second**, Lafarge had no position in GBS prior to 7 January 2013 when the joint venture between Lafarge and Tarmac was formed (this was cleared by the CC less than twelve months ago and the CC raised no concerns about the combination of Tarmac’s GBS position with Lafarge’s cement position). Tarmac did have a position in GBS, but was not, based on the CC’s theory, a part of the coordinating group. Accordingly, Lafarge’s purported coordination with Hanson is of no consequence: Lafarge had no ability to influence prices of GGBS.

C. **ALTERNATIVE REMEDY PROPOSAL**

20. To remedy the AEC that the CC has identified in GGBS, the CC proposes that LT should divest two of its three GBS facilities, and that Hanson should divest two GGBS plants.

21. Section 138 of the Enterprise Act 2002 provides that, where the CC has identified an AEC, it should take such action “as it considers to be reasonable and practicable” and “shall, in particular, have regard to the need to achieve as comprehensive a solution as is reasonable and practicable to the adverse effect on competition concerned and any detrimental effects on customers.”

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5 Although the CC notes that there are limited imports of GGBS into GB, the CC has overlooked the fact that Lafarge also imported quantities of GGBS from Spain, albeit very small quantities of GGBS (in 2012 approximately 50kt).

6 In that respect, where the CC cites in paragraph 83 of the GGBS Addendum an “instance” in which “in response to Hanson’s 2009 internalisation, Lafarge internalised its own purchases from Hanson, some of which were GGBS purchases switched to PFA”, LT notes that at this point Lafarge was not present in GGBS or GBS. Furthermore, if anything, this is evidence that the three materials should form one and the same product market, rather than separate product markets, given the relative ease with which Lafarge switched from purchasing GGBS to using PFA/CEM I. LT continues to assert that this was not evidence of “retaliation” as part of any alleged coordination, but a unilateral decision by LT to implement its PFA strategy and self-supply its cement needs given significant levels of over capacity at the time in the face of a large drop in demand.
22. In determining what is reasonable and practicable, and in light of the protection of property rights enshrined in the Human Rights Act 1998, the Competition Appeal Tribunal (the “CAT”) has made clear that any remedies:

“(1) must be effective to achieve the legitimate aim in question (appropriate),

(2) must be no more onerous than is required to achieve that aim (necessary),

(3) must be the least onerous, if there is a choice of equally effective measures, and

(4) in any event must not produce adverse effects which are disproportionate to the aim pursued.”

23. The CC Guidelines themselves recognise this, and also note that the CC will consider “remedy options both relative to other effective measures as well as relative to taking no action” and will “apply these principles to the evaluation of individual measures within a package of remedies as well as to the package taken as a whole.”

24. LT does not consider that the CC’s remedy proposal involving LT divesting two of its GBS facilities is either effective or proportionate.

Not effective

25. LT does not consider that the CC’s remedy proposal will actually materially improve competition in the supply of GGBS. Instead, LT considers that the practical effect of the CC’s remedy proposal would be a move from a one-party controlled market to a proposed two-party controlled market.

26. As an alternative, LT proposes that, instead of requiring the divestment of LT’s GBS facilities, LT would retain ownership of GBS facilities but would sell GBS that it produces through an open auction process conducted on a periodic basis (e.g., annually). LT notes that this model is currently used in Germany, as LT outlined to the CC in its submission of 24 July 2013. Under this proposal, GBS would be made available to any willing purchasers by the auction of individual tranches, i.e., through a bidding process. Both individual undertakings and consortia would be able to bid, making it possible, for example, for independent RMX producers to “club” together to bid for tranches of GBS. This would have the potential to create a multi-player market in the supply of GGBS by giving access to GBS to any willing purchaser.

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9 Please refer to, Bundeskartellamt, Tätigkeitsbericht 2007/08 [Report on Administrative Action in 2007 and 2008], page 84. The Tätigkeitsbericht is a report that the Bundeskartellamt edits and publishes every two years to inform the German Federal Government and the public about its activities. A copy of this report can be found online.
27. LT does not consider that the sale of GBS and GGBS facilities to two buyers would introduce the same level of competition in the supply of GGBS. The consequence of this remedy would only increase the number of supplies to two or three, at a maximum. In contrast, an auction remedy would make GBS available to any willing purchasers, and would incentivise investment in grinding facilities. As a consequence of this, there would be much greater competition between suppliers of GGBS, thereby increasing price competition. LT considers that this would provide a more effective remedy since it would ensure equality of access to GBS to any willing purchaser. It would, moreover, eliminate entirely the possibility of exclusive supply relationships between GBS and GGBS producers.

**Disproportionate**

28. LT considers that it would be disproportionate for the CC to order a divestment of any its GBS facilities. This is for the following reasons:

(a) The CC has not identified that LT has earned excess profits as a result of its position in GBS under the current structure of arrangements.

(b) Given the uncertainties associated with how GBS would be sold and priced under the CC’s proposed remedy arrangements, there is a high risk that it would be difficult for LT to extract fair market value from any prospective purchaser for the sale of the granulators. In addition, the forced nature of the sale would be likely further to depress the likely price that LT could achieve for the sale of the GBS facilities.

(c) Associated costs of divesting the GBS facilities would also need to be borne by LT, including the cost of appointing lawyers, bankers and accountants to run, value and draw up the legal documentation to give effect to the sale. These costs would come despite the fact that the CC has not identified that LT achieves profits in excess of its cost of capital in relation to its GBS activities.

(d) LT’s GBS operations are part of a broader relationship with the steel facilities at those locations. LT’s operations also include the handling, processing and removal of aggregates (made from air-cooled slag and steel slag) (both of which form part of the LT aggregates business and which generate a significant contribution to LT’s EBITDA). By being forced to divest the GBS facilities, LT would be forced to undergo an extensive and costly process to separate these activities. Therefore, LT could be required to incur the costs of separation despite the CC having failed to identify not only any excess profits in LT’s GBS operations, but also having examined and failed to identify any competition issues in relation to the supply of aggregates.

29. Since a more proportionate and more effective option is available to the CC by LT retaining its position in GBS but by introducing an auction mechanism for the sale of GBS to any willing purchaser, it would be disproportionate for the CC to order that LT divest any of its GBS facilities.

**Proposal if the CC continues to consider that LT should divest GBS facilities**
30. If, however, the CC continues to consider that the divestment by LT of two of its GBS facilities is more effective, LT would (subject to any wider review of the CC’s decision) propose to divest different plants to those identified by the CC.

31. The CC has provisionally identified that LT should divest LT’s Port Talbot and Scunthorpe GBS plants, as these present the fewest divestiture risks (see PDR, paragraph 4(d)(ii)). However, the CC also said that it would be prepared to consider the divestiture of the Teesside GBS plant if LT were able to address the additional divestiture risks associated with this plant.

32. LT considers that Teesside is a more appropriate candidate for divestment than Port Talbot. The following factors make the divestment of Scunthorpe and Teesside a more compelling proposal than the divestment of Scunthorpe and Port Talbot:

(a) Teesside has better access to non-road logistics (rail and ship) subject to agreement with third parties (LT has used rail for distribution of air-cooled and steel slag aggregate). In contrast, access to rail and sea at Port Talbot is more restricted. The distance by sea to South East England from Teesside is significantly shorter than from Port Talbot (a voyage which can only be made by navigating around Cornwall).

(b) To the extent that the CC wishes to create a dynamic competitive market for GBS, selling a granulator whose output is not all consumed on site would have benefits as this would require the purchaser of Teesside to sell some GBS into the open market, potentially introducing an additional supplier of GGBS.

(c) LT’s GBS activities at Teesside and Scunthorpe are part of the same legal entity (East Coast Slag Products) whereas Port Talbot is separate (Cambrian Stone). This would simplify and reduce the costs borne by LT in the execution of any remedy.

(d) The divestment of Teesside with Scunthorpe provides greater synergy opportunities for a single buyer:

(i) the sites are closer geographically (than Scunthorpe and Port Talbot) and accordingly, it is easy to move granulate between them. This means that granulate can be moved between the plants during periods when the steel works are shut down.

(ii) The two plants have historically been operated together which means existing connections and practical operational connections are pre-existing. As such, a two plant GBS (and GGBS) divestment of Teesside and Scunthorpe would give the new entrant a more secure and flexible footprint than Scunthorpe and Port Talbot.

(iii) For East Coast Slag Products (covering both Scunthorpe and Teesside), a single quality contract is already in place that assures quality of the granulate produced from the two facilities. A consistent product can then be supplied from both plants. Accordingly, a customer can easily substitute the material produced from both facilities.
33. The divestiture risk that the CC identifies at Teesside (i.e., that Hanson’s grinding facility is not currently active) is, LT considers, not insurmountable for the following reasons:

(a) Teesside is currently operated successfully by LT despite the fact that LT has no ability to sell GBS to the open market.

(b) The situation at Teesside (granulator capacity with no on-site grinding capacity) is, to an extent, no different from Port Talbot where the on-site grinding capacity is only approximately 50% of the granulation capacity.

(c) In the event that Hanson or the prospective purchaser does not re-activate the grinder at Teesside, any buyer of the granulator would have a strong incentive to invest in its own grinding facilities given that the Teesside slag facilities have the capacity to produce c.750kt of water-cooled slag.

(d) If the fact that the granulator is not currently active is considered problematic by prospective purchasers, LT considers either that Hanson could re-activate this or that this fact would be reflected in the purchase price.

34. Accordingly, if the CC continues to consider that LT should divest two of its three GBS facilities, LT considers that the divestment of Scunthorpe and Teesside presents a more compelling alternative than the divestment of Scunthorpe and Port Talbot.

D. CONCLUSION

35. Irrespective of the failures in the CC’s analyses with respect to market definition, the characterisation of LT’s contribution to the AEC in GGBS, and without prejudice to LT’s position that there is no AEC in the supply of cement, LT considers that its alternative remedy proposal by which LT, retaining its position in GBS, auctions in tranches GBS to any willing purchasers would be more effective in introducing greater competitiveness into the supply of GGBS in GB. The prospect of making GBS available to any willing purchasers would ensure that any third party, regardless of size, capacity or capability, could bid for and secure GBS to grind, sell and/or use as it were to choose. This has the potential to introduce a greater number of alternative suppliers of GGBS than the CC’s current remedy proposal envisages, thereby improving the prospects for price competition in the supply of GGBS.

36. Even if the CC continues to consider that GGBS forms a separate product market, the CC has acknowledged that there is a pricing inter-relationship between GGBS and cement. LT considers that the effect of this remedy would be to place considerable downward pressure on the price of cement.

37. LT reiterates the comments put forward in its response to the PDR that a remedy in GGBS would address the consumer detriment identified by the CC in cement, and thereby would single-handedly address the AECs identified by the CC in both cement and GGBS.

38. Although LT disputes the CC’s calculations that the AEC in cement results in consumer detriment of £3.20 per tonne, even assuming that this is correct, when each of the remedies should be taken in turn the incremental effect of these remedies
addresses the alleged £3.20 per tonne detriment without the need to resort to a cement plant divestment.

(a) The starting point must therefore be with measures designed to address market transparency. The CC concludes that its other remedies will undermine features that contribute to the “Coordination AEC”, namely reduced market transparency from the prohibition on the supply and publication of recent data (PDR, paragraph 3.210) and the prohibitions on price announcement letters (PDR, paragraph 3.250). But it does not adequately address why it supposes that these alone would be insufficient to undermine coordination. Given that the CC’s allegation is coordination on market share on the basis of very high levels of market transparency, the CC must displace the natural presumption that measures which significantly reduce that transparency would themselves be sufficient.

(b) It is then necessary to consider the effect of a GGBS remedy on consumer detriment. Like remedies designed to address market transparency, the CC considers that remedies in relation to GGBS would increase competition (and LT’s alternative proposal of a GBS auction mechanism would further increase competition in the supply of GGBS). The CC acknowledges the effect that the price of GGBS has on the price of cement and that there is a level of competitive interaction between the two products (PDR, paragraph 3.286 (b)). The CC must, with sufficient precision and detail, articulate why it does not consider that GGBS remedies alone would be sufficient to remedy the AEC identified.

(c) RBB Economics (see the independent report annexed to LT’s response to the PDR) has conducted its own analyses to consider the effect of a GGBS remedy on the price of cement, and consequently the ability to eliminate the consumer detriment of £3.20 estimated by the CC.

(i) As the CC is aware, there is spare capacity in the supply of GGBS. The proposed GGBS remedy would be expected to increase the supply of cementitious materials in GB by up to 0.8MT based upon LT’s submission in Annex H to the PDR.

(ii) There will be a greater incentive to lower the price of GGBS to sell the additional capacity. In order to sell the additional amounts, the price of GGBS will have to fall. As noted by the CC in Appendix D to the PDR, in a situation where GGBS is supplied by a non-cement producer there would be a greater incentive to reduce the price of GGBS because the new operator would not risk cannibalising some of its cement sales.

(iii) There is considerable scope for the price of GGBS to fall. [8].

(iv) As the price of GGBS falls, so will the price of CEM I. Since GGBS is a substitute for CEM I (the former can replace the latter to a considerable degree, e.g., 40-50% on average), a lower price of GGBS will reduce the price of CEM I. [8].
Accordingly, the GGBS remedy would cause a sufficient reduction in the cement price to remove the CC’s estimated overcharge in cement. In the same way that Hanson currently has a limited incentive to reduce the price of GGBS (given that this would cannibalise sales of cement), it also has a weakened incentive to reduce the price of cement (because it would cannibalise sales of GGBS). The latter “cost of cannibalisation” is substantially reduced as a result of the GGBS remedy. First, the impact of divesting grinding stations reduces the diversion ratio from Hanson cement to Hanson GGBS. Second, as the price of GGBS falls, the benefit of diverting sales from Hanson cement to Hanson GGBS also falls (since Hanson earns a lower margin on whatever GGBS it sells post divestment). Both factors work to incentivise Hanson to lower the price of its cement. Under some assumptions, the incentive to lower price could be sufficient to reduce the cement price by £3 per tonne.

39. Together, the market transparency measures and LT’s alternative GGBS remedy proposal represent an effective and proportionate way to address the alleged consumer detriment of £3.20 per tonne without incurring the substantial costs (to LT, to the industry, and to the new entrant) of a cement plant divestment.