
Completed acquisition by Bobst Group SA of the Valmet Converting Business of Metso Corporation

The OFT's Decision on reference under section 22 of the Enterprise Act 2002 given on 11 March 2004

Please note text in square brackets indicates range inserted at request of parties.

PARTIES

1. **Bobst Group SA (Bobst)**, a Swiss company, is a global producer and distributor of machines used in the production of packaging, consisting of solid fibre board, corrugated board and foils. In 2002 Bobst had total sales of CHF 1478 million (approx £634 million).
2. The **Valmet Converting Business (Valmet)** is part of Metso Corporation, a Finnish company. Metso is a global supplier of process industry machinery and systems with a worldwide turnover of EUR 4.7 billion. The Valmet business concerns the manufacture, sale and servicing of machines and equipment for the manufacture of plastic film and flexible packaging as well as the conversion of paper, which had total sales of EUR 170 million. In 2002, Valmet's UK turnover was approximately (see note 1).

TRANSACTION

3. The transaction involves the acquisition of the Valmet business which comprises Metso's subsidiaries Valmet Atlas plc (GB), Valmet Rotomec SpA (Italy) and Valmet Converting Center GmbH (Germany), including their respective subsidiaries, and certain assets used or related to Valmet located in the US, Indonesia, Singapore and China. The consideration was approximately EUR 75 million.
4. OFT considers that a complete submission was received on 17 December 2003 and that the 40-day administrative timetable expired on 16 February 2004. The parties state that the transaction completed on 21 October 2003¹. The statutory deadline for considering this merger has been extended in accordance with section 25(1) of the Enterprise Act 2002 (the Act).

¹ The parties state that the parties ceased to be distinct within the meaning of Section 26 of the Enterprise Act 2002 on 21 October 2003 although completion of the transaction took place on 30 January 2004.

BACKGROUND

5. Bobst's rationale for the transaction is to broaden the printing machine products range and develop its business activities in other geographic areas e.g. Asia where Bobst does not have a presence.
6. The transaction was notified in Brazil in December 2002, and has also been notified and cleared in Turkey, Germany and Spain. The Spanish competition authority considered that it was not necessary to distinguish between the different types of flexible packaging machines because the transaction did not raise any significant anti-competitive effects. Following previous cases relating to the machinery for packaging² and the production of flexible packaging products³, it considered the geographic scope for supplies should be at least EEA-wide.

JURISDICTION

7. As a result of this transaction Bobst and Valmet have ceased to be distinct. The parties overlap in the supply of flexible packaging machines and the share of supply test in section 23 of the Act is met in respect of the supply of slit rewinding machines in the UK. A relevant merger situation has therefore been created.

RELEVANT FRAME OF REFERENCE

8. The parties overlap in the manufacture and sale of machines used in the process of producing flexible packaging. Flexible packaging is malleable i.e. it changes shape when pressure is applied, in contrast to other types of packaging like carton or solid plastic. It is used for containing food, pharmaceutical, and cosmetic products. There are three key processes in the manufacture of flexible packaging:
 - manufacturing – the substrate e.g. plastic, paper is made into a certain thickness (only Valmet is active at this stage in the production of slitting and film vacuum coating machines);
 - finishing – images are printed on film or substrate, laminated or coated, cut into rolls (both parties are active here and manufacture gravure and flexography printing machines; coating and laminating machines; and slitting rewinding machines);
 - conversion – the substrate is shaped or glued into its final form (neither party is active at this stage).

² Case N-03010 of the Spanish Competition Service and Case IV/M.478.

³ Case N-236 and N-03044 of the Spanish Competition Service and Cases IV/M.2441, IV/M.2840, IV/M.2843 and IV/M.3049.

Product scope

Gravure and Flexographic printing machines

9. Gravure and flexographic printing machines are used to print images on flexible packaging. This raises the question whether, on the demand side, customers' view them as interchangeable. Since the underlying technology is different, supply side substitution appears unlikely. Bobst and third parties have confirmed that gravure printing is of much higher quality than flexographic printing. One third party thought flexographic machines, which cost around £300,000-400,000, were suitable for lower quality larger production runs, while gravure machines, which cost £1-2 million, were used for smaller scale higher quality production. Third parties indicated they would be unlikely to consider switching between gravure and flexographic machines. The evidence suggests, therefore, that these types of machines should be considered separately.
10. Bobst submits that the characteristics of gravure and flexographic machines may need to be adapted depending on the substrate and that most competitors manufacture presses for different types of substrates. However, this, in itself, does not necessarily suggest that supply-side substitution is possible. Third parties thought that, in general, it would be difficult to quickly and at minimal cost switch production from other substrates to flexible packaging. One third party cited environmental considerations as the principal reason for this because flexible packaging machines use dangerous inks and solvents.

Coating and Laminating machines

11. These are used to improve the appearance and barrier properties of a substrate. The parties claim that customers increasingly demand machines that combine coating and laminating functions. An estimated 40 per cent of all laminating machines sold can carry out coating and laminating functions, such that the parties consider that coating and laminating machines form part of the same frame of reference. On the supply-side, Bobst maintains that the technology for coating machines and laminating machines is similar and that it is possible to switch production without incurring additional costs in a very short time.
12. The parties also manufacture machines used to coat or laminate shopping bags, labels and industrial packaging. The machines require some adaptation for different substrates, but most competitors manufacture machines for various substrates. Again, as discussed above this is not necessarily indicative of supply-side substitution.

Slitting-Rewinding machines

13. These are used to cut rolls of printed/coated/laminated substrate into the required number of smaller reels ready for form and filling machines, after which the reels are wound back into a rolled form. There do not appear to be any demand-side or supply-side substitutes.

Geographic scope

14. Customers in the UK are supplied through Bobst Group Ltd, located in Redditch. Valmet manufactures some products in the UK and sells these directly to UK customers, while products not manufactured in the UK are sold by one sales person in the UK.
15. Bobst submits that suppliers do not need to have a presence in any country or region to supply into it; suppliers tend to have one manufacturing site and compete for contracts and supply customers around the world from that single site. The only requirement to supply a country is the ability to provide technical assistance, which can be achieved by sending technicians from abroad. Manufacturers can also supply through local providers. Local agents typically represent a range of suppliers. In addition, transport costs are low in relation to the value of the product, at less than 5 per cent of selling price. The sales price of flexible packaging machines does not vary significantly or systematically between countries and there are generally no variations in technical characteristics or national customer preferences. However, customers in Asia may have preference for certain brands. Bobst contends that there are numerous examples of suppliers competing for and winning contracts around the world. For example, Fuji-Kikai and Toshiba (who are based in Japan) have both supplied European customers (e.g. Print Pack). Given all these factors, the parties consider that the geographic scope is world-wide.
16. Evidence from third parties, however, suggests that they tend only to consider suppliers in Europe because of the need for relatively local technical assistance.
17. For the purposes of this analysis, the relevant frames of reference will be taken to be the supply in Europe of the following flexible packaging machines: Gravure printing machines; Flexographic printing machines; Coating & Laminating machines; and Slitting-Rewinding machines.

HORIZONTAL ISSUES

Shares of supply

18. From the data supplied by Bobst, shares of supply in this sector are 'lumpy' - customers make infrequent purchases of flexible packaging machines which have a life of 10 to 20 years. A relatively small number of machines are sold each year, largely for replacement purposes. Machines are sold either through competitive tender or individual negotiations. These characteristics suggest that shares of supply in any one year are unlikely to be a reliable indicator of possible market power.
19. Post-merger, the parties' combined share of supply in Europe is estimated to be [20-30 per cent], increment [10-15 per cent], for gravure printing machines; [10-20 per cent], increment [0-5 per cent], for flexographic printing machines; [10-15 per cent], increment [0-5 per cent], for coating and laminating machines; and [10-15 per cent], increment [0-5 per cent], for slitting-rewinding machines. These figures are based on the average shares over the period 1998-2002.
20. Some third parties were concerned that the merger reduced from three to two the number of major suppliers of gravure printing machines; the other major

supplier being Cerutti (Italy). However, evidence provided by Bobst and a number of third parties consulted by OFT suggests that over the last five years both itself, Valmet, Cerutti, Windmoeller & Hoelscher, Chadwick, Andreotti and DCM have made sales of gravure printing machines in the UK⁴.

21. There is also evidence of European customers switching between a number of suppliers, including but not confined to the parties and Cerutti. The parties also contend that there are other suppliers of gravure printing machines such as Giave (Spain) and Uteco (Italy)⁵. On the basis of the evidence, therefore, there are at least a number of other suppliers of gravure printing machines.
22. For flexographic printing machines the main competitors appear to be Fischer & Krecke, Comexi, Windmoeller & Holscher, Flexotecnica, Bielloni and Uteco. For coating and laminating machines the main competitors appear to be Max Kroenert, Nordemeccanica, Polytype and Bachofen & Meier. While for slitting rewinding machines the main competitors appear to be Ashe Conrols, Kampf, Parkland, SRC Systems and WT Wickeltechnik.
23. Overall, there appear to be a number of other suppliers within Europe in each category of flexible packaging machine, which should act as a constraint on the parties post-merger.

Barriers to entry and expansion

24. The parties submit that the costs of entry are not significant for a new entrant to start supplying UK customers with gravure, flexographic, coating & laminating and slitting-rewinding machines. The key requirement for a *de novo* entrant is to have knowledge of the industry and some customer contacts. The cost of appointing a local agent is minimal.
25. In addition to *de novo* entry, Bobst submits that there is the potential for entry from manufacturers in related sectors: a manufacturer of one type of flexible packaging machine could start manufacturing another type. Manufacturers active outside Europe, including Asia, could also start supplying European customers through appointing a local distributor.
26. Overall, the OFT does not believe there to be significant barriers to entry to the supply of flexible packaging machines.

Buyer power

27. Most suppliers use a list price for the majority of their standard equipment but these are mainly internal. The prices quoted to customers are as a result of

⁴ It should be noted Chadwick no longer manufacture gravure printing machines but instead are active in the supply of refurbished machines (which could operate as a constraint) and Andreotti is now in receivership.

⁵ There are also a number of other European suppliers such as CMR, Chesnut, Kochsiek, Fuji-Kikai, Toshiba, Polytype and Emerson.

competitive price negotiations and technical changes required by the customer. The majority of customers contacted by the Office considered that they purchased bespoke products.

28. Evidence provided by the parties suggests that customers typically invite 5 or 6 bids to supply a new flexible packaging machine and then negotiate with these suppliers, playing them off against each other, before choosing the best final offer. The number of machines sold per year is not large, they are expensive purchases, and machines are replaced infrequently (every 10-20 years) so the loss of one sale can have a significant effect on a manufacturer's sales (as demonstrated by the significant year-on-year variations in suppliers' share of sales and revenue). The parties have supplied a number of examples where customers have exercised negotiating strength to extract lower prices from manufacturers. Overall, there is some evidence to indicate customers are able to exercise some buyer power.

Portfolio effects

29. Bobst has stated that one rationale for the transaction is to broaden its printing machine product range. This raises the question whether the merger might enhance the ability of the parties to tie purchases of flexible packaging machines. However, it appears that both parties, and other manufacturers already supply the full range of flexible packaging machines. The possibility therefore, of this transaction raising any substantive portfolio issues is negligible.

VERTICAL ISSUES

30. Valmet manufacture machines used in the manufacture of flexible packaging, upstream of the finishing process for flexible packaging. The machines associated with each of the three key processes go to different types of customers and there is very little overlap in the customer base. Therefore the transaction does not appear to raise any vertical competition issues.

THIRD PARTY VIEWS

31. A number of third parties were contacted in the usual way. Some raised concerns that the number of major suppliers of flexible packaging machines, in particular gravure printing machines, would be reduced from three to two. This has been discussed under horizontal issues and, overall, the evidence presented to the OFT shows that alternative suppliers are present and have supplied customers in the UK for each type of machine.

ASSESSMENT

32. This completed merger qualifies on the share of supply test of the Act. At a horizontal level, the parties overlap in the manufacture and sale of machines used to apply the finishing process to flexible packaging. At a vertical level, Valmet is active in the upstream manufacture of machines used to manufacture flexible packaging but the OFT believes this does not raise any substantive competition issues. Supply and demand side considerations indicate that the

relevant frames of reference for analysing this transaction are the manufacture and sale in Europe of: gravure printing machines, flexographic printing machines, coating and laminating machines and slitting-rewinding machines.

33. The shares of supply and accretions to those shares are not significant and a number of competitors remain post-merger. Some third parties raised concerns about a reduction in the number of major suppliers of flexible packaging machines but enquiries have confirmed that there are a number of existing and potential suppliers. In addition, the OFT believes that some buyer power is present and barriers to entry are not insurmountable.
34. Accordingly the OFT does not believe that it is or may be the case that the creation of the relevant merger situation has resulted or may be expected to result in a substantial lessening of competition within a market or markets in the United Kingdom for goods or services.

DECISION

35. This merger will therefore **not be referred** to the Competition Commission under section 22(1) of the Act.

NOTES

1. Figures removed at the request of parties