OFFICE OF FAIR TRADING

Completed acquisition by Arcelor SA of Corus UK Limited's UK hot-rolled steel sheet piling business

The OFT's decision on reference under section 22 given on 9 September 2004

Please note square brackets indicate text either deleted or replaced by a range at the request of the parties for reasons of commercial confidentiality

PARTIES

1. **Arcelor SA (Arcelor)** is headquartered in Luxembourg. It has four core businesses: flat carbon steel; long carbon steel; stainless steel; and steel distribution. Arcelor has a world wide turnover of €25.9 billion, of which €20.1 billion was achieved in the EU. Arcelor's total UK turnover in the last four years has been less than £[] million.

2. **Corus UK Limited (Corus)** is a subsidiary of Corus Group PLC. Its UK turnover for sheet piling for year end 3 January 2004 was £[<70] million.

TRANSACTION

3. On 30 April 2004, Arcelor acquired Corus' UK hot-rolled steel sheet piling ('sheet piling') business ('the Arcelor transaction') consisting of[1]:

   - goodwill and a small number of employees;
   - supplier and customer lists including UK mailing lists, customer credit limits, customer payment history and UK transport rates;
   - product development and design information, including specifications, drawings, data, instruction and training manuals, handbooks, plans instructions, formulae, test results, reports, project reports, testing procedures and tables of operating conditions;
   - sales, marketing and promotional information, and market forecast;

[1] Arcelor wishes to confirm that this makes up the commercial part of Corus' UK hot-rolled steel sheet piling business.

- technical or other expertise; and
- a [] year non-compete clause.

4. The assets acquired by Arcelor did not, therefore, include Corus' production facilities at its Scunthorpe mill. Corus ceased production of sheet piling at its Scunthorpe mill as part of its UK restructuring programme and 'Restoring Success' initiative and closed the operation on 6 July 2004.

5. The total consideration for the acquisition was £[] million, []. The transaction was notified to the OFT on 21 June 2004 by way of an informal submission. The administrative timetable expired on 3 September and the statutory period was extended to 27 September 2004 under section 25(2) of the Enterprise Act 2002.

JURISDICTION

6. The OFT considers that the combination of assets that have been acquired by Arcelor under this transaction constitutes an 'enterprise' for the purposes of the Enterprise Act 2002. The assets acquired by Arcelor form a crucial part of the sheet piling business and the transaction prevents Corus from re-entering the market for a period of [] years and thereafter with any relative ease. As a result of the acquisition the Corus enterprise has ceased to be distinct with the enterprise carried on by or under the control of Arcelor. The transaction qualifies as a relevant merger situation on the basis that the parties' combined share of supply for sheet piling in the UK exceeds the jurisdictional threshold under the Enterprise Act 2002.

RELEVANT MARKET

7. The parties overlap in the supply of sheet piling. Sheet piling is used as a retaining structure, typically, in terrestrial excavations (acting as a barrier to earth) or maritime/river applications (acting as a barrier to water). Arcelor manufactures and supplies sheet piling from its Esch-Belval production plant, Luxembourg. Corus manufactured and supplied sheet piling from its Heavy Sections Mill ('HSM') at Scunthorpe, UK.

8. In relation to demand side substitution, Arcelor submits that the appropriate frame of reference should be retaining structures as a whole. It maintains that a variety of materials (such as concrete, masonry, diaphragm walls and cold formed sheet piling) can be used as an alternative to sheet piling. In particular, Arcelor submits that such alternative materials account for around 90 per cent of retaining structure installations, typically based on concrete products, while sheet piling

accounts for around 10 per cent. Arcelor further submits that there are no projects or types of work where sheet piling cannot be substituted by alternative retaining structures and that concrete products are a particularly strong constraint.

9. The evidence gathered by the OFT from third parties is mixed. Third parties indicate that, in terrestrial applications, substitution to other types of retaining structures is possible but depends on the needs of the specific project, with consideration being given to technical, installation and pricing factors. Some third parties have said that sheet piling is typically used in marine and river work even though concrete can be used. Others maintain that sheet piling is the only viable option in temporary excavation works where the retaining structure is often removed after the work is completed. Although third parties agree that concrete can be used in terrestrial and marine works, some say that they would not switch to an alternative product in the event of a 5-10 per cent increase in the price of sheet piling.

10. Arcelor has provided evidence of marine and coastal projects using concrete retaining structures. However, despite Arcelor's contention that concrete is a strong constraint on the pricing of sheet piling, the price of sheet piling is markedly lower than the price of concrete. In addition no evidence was produced to show that Arcelor monitors the price of concrete on a systematic basis.

11. In relation to supply side substitution, the manufacturing process of each type of retaining structure is different. The closest possible substitute to sheet piling is cold-formed sheet piling, but this involves an entirely different manufacturing process and Arcelor has not argued that any supply side substitution exists. Supply side substitution is therefore unlikely.

12. Although concrete is a major material used in retaining structures and although it does exert a degree of competitive constraint on sheet piling, given the mix of evidence received it is difficult to reach a view on the strength of that constraint. Therefore, the appropriate frame of reference is considered to be sheet piling.

13. Historically, competition in sheet piling has taken place on a national basis. This was evidenced by the high share of supply held by Corus in the UK. In 1995, Corus held a 95 per cent share of UK sheet piling supply. However, in recent years it appears that imports from Europe have placed competitive pressures on UK sheet piling prices resulting in a steady fall in the price of UK sheet piling and a steady decrease in Corus' share of UK

sheet piling supply. This is evidenced by the presence of Salzgitter (Germany) and, to a more limited extent, Arcelor as well as the Eastern European suppliers, Vitkovice and Huta Katowice in the UK. Third parties have also indicated that the sheet piling segment is European wide. It is, therefore, considered that competition now takes place on a European level.

COUNTERFACTUAL

14. In order to assess whether post-merger, a substantial lessening of competition is, or may be, likely to occur, it is necessary to consider what the competitive situation would be absent the merger (referred to as the counterfactual). In this case, Arcelor has submitted that, in its view, Corus' sheet piling activities were loss-making and that it would have closed the Scunthorpe mill and exited even in the absence of the Arcelor transaction. In order to treat this change to the prevailing conditions of competition as the appropriate counterfactual for assessment of the merger situation, the OFT considers that compelling evidence is required, particularly in circumstances where the postulated counterfactual involves the exit of one of the merging parties together with a non-compete agreement.

15. Corus' submissions give some support to Arcelor's view that the closure of the Scunthorpe mill would have happened even without this merger. Corus submits that there were a number of pre-existing factors that led to the decision to close the HSM at Scunthorpe unconnected to the acquisition of its sheet piling business by Arcelor. Corus confirmed that the HSM was loss-making and said that competition from European suppliers and a weak product range, together with an inability to develop and produce the innovative 'Z' type sheet piling which is becoming the industry standard, meant that Corus would not be in a position to compete with the European suppliers. Corus further submits that given its forecast of falling prices[2] for sheet piling it could not envisage the HSM becoming profitable nor could it justify the substantial amount of investment required to bring the HSM up to competitive levels. Furthermore, Corus submits that various joint venture configurations were considered as well as the possibility of switching production to another mill. However, such options were not found to be workable.

16. The OFT considers the corroborating evidence to be short of compelling. On the one hand, there is material to show that Corus actively considered joint ventures [] which involved the switching of production to [] European plants. On the other hand, the OFT has found []

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[2] Addendum – Corus states its reference was to falling margins.

17. While profitability graphs for 2003 show that Corus' European (excluding the UK) and world-wide sales of sheet piling from the mill were loss-making, Corus' UK sheet piling sales were making a profit of [] per tonne []. Corus' UK sheet piling sales made annual profits of around £[] million. Furthermore, demand for sheet piling may be cyclical, and so the overall performance of the Scunthorpe HSM mill might have recovered.

18. It is also difficult to reconcile the fact that Arcelor agreed to pay around £[] million for the purchase of various non-production assets, listed above, relating to Corus' UK sheet piling business if closure of this business was 'inevitable'. Arcelor submits that the payment was to allow it a smooth transition into the UK where its previous presence had been sporadic. This is evidenced by its pre-merger UK share of supply figures (2001 ([<5 per cent), 2002 ([<5 per cent]) and 2003 ([10-15 per cent])). However, Arcelor clearly had some pre-merger presence in the UK and its ability to gain UK share of supply is evidenced by the increase in its share from [<5] to [10 -15 per cent] in one year. Questions also arise as to the rationale for the [] year non-compete commitment obtained by Arcelor from Corus. The inference could be made that Arcelor was concerned that Corus could re-enter the UK market without such a commitment. Corus has confirmed that it had no intention of doing so and Arcelor submits that the non-compete clause is a standard contract term.

19. Even if the correct counterfactual is Corus' exit from the sheet piling business, it is not necessarily the case that Arcelor's acquisition of the Corus business does not result in a substantial lessening of competition relative to what would otherwise have happened. A Corus decision to exit would have presented the alternative suppliers to the UK with an opportunity to compete for that business. Market exit can provide an opportunity for vigorous price competition as the remaining players seek to gain share in competition with rivals. Often, this is a time when competition is at its most fierce and, as a result, customers can benefit through the lower prices that this competition brings. However, Arcelor has pointed out that it acquired no on-going contracts from Corus and so any existing customers were free to switch suppliers if they wished. Also, contracts for supply tend to be gained by competitive tender and the merger does not prevent competitors from bidding for, and winning, such contracts as they arise. However, the evidence has shown that, following the Arcelor transaction, Arcelor has obtained business from nine of the ten top UK customers of Corus, which suggests that the transaction may at least have had a dampening effect on the competition that would otherwise have taken place.

20. In conclusion, while the closure of the HSM at Scunthorpe is a plausible counterfactual, the OFT does not consider that the parties have provided sufficiently compelling evidence to substantiate it as the reference point that the OFT should adopt in assessing whether it may be the case that the merger may result in a significant lessening of competition. Moreover, even if the counterfactual was substantiated by the parties, there might have been a more competitive alternative outcome had the Arcelor transaction not occurred.

HORIZONTAL ISSUES

Shares of supply

21. Tables 1 and 2 below show the parties' European and UK shares of supply for sheet piling. The figures show that in 2003 the parties' European combined share of sales was [50 per cent-60 per cent] (increment [10 per cent-15 per cent]). Corus' [10 per cent-15 per cent] European share is made up of [5 per cent-10 per cent] UK sales and [5 per cent-10 per cent] non-UK sales. The combined share of UK supply is [75 per cent-85 per cent] (increment [10 per cent-15 per cent]).

Table 1: EU 2003 share of supply of sheet piling.

Firm	Capacity (tonnes)	Sales (tonnes)	Share of sales %
Arcelor (Luxembourg)	[450,000 – 550,000]	[250,0000 - 350,000]	[40-50%]
Corus (UK)	[150,000 – 250,000]	[50 – 150,000]	[10-20%]
Combined	*[650,000 – 750,000]*	*[400,000 – 500,000]*	*[50 – 60%]*
Salzgitter (Germany)	[300,000 – 400,000]	[150,000 – 250,000]	[25-35%]
Vitkovice (Czech Repub)*	[100,000 – 200,000]	[0 – 100,000]	[0-10%]
Huta Katowice (Poland)*	[100,000 – 200,000]	[0 – 100,000]	[0-10%]
Others	-	[0 – 50,000]	[0-10%]
TOTAL	[1,000,000-1,500,000]	[700,000 – 800,000]	100

Source: The parties (based on Eurofer, amtiliche Ausfuhrstatistik and Arcelor's estimates).

*Arcelor has submitted that it is unable to provide capacity volumes for Vitkovice and Huta Katowice. However these estimates are sourced from Arcelor's board papers. Vitkovice submits its capacity is [].

Table 2. UK shares of sales 2001 – 2003 for sheet piling.

Company	2001		2002		2003	
	Sales (t)	Share	Sales (t)	Share	Sales (t)	Share
Arcelor	[350-400]	[0-5%]	[0-5,000]	[0 - 5%]	[5,000 – 15,000]	[5-15%]
Corus UK Business	[45,000-55,000]	[70% - 80%]	[45,000 –55,000]	[70% - 80%]	[45,000 – 55,000]	[65 - 75%]
Salzgitter	[5,000 – 15,000]	[10% - 20%]	[5,000 – 15,000]	[10% - 20%]	[5,000 – 15,000]	[10-20%]
Vitkovice	[0-5,000]	[0-5%]	[0-5,000]	[0-5%]	[1,000 – 2,000]	[0-5%]
Others	[0-5,000]	[0-5%]	[0-5,000]	[0-10%]	[50-150}	[0-5%]
Total	[65,000-75,000]	100%	[65,000 -75,000]	100%	[65,000 – 75,000]	100%

Source: The parties (based on Eurofer, amtliche Ausfuhrstatistik and Arcelor's estimates).

22. Arcelor submits that the combined European share of [50-60 per cent] overstates its post-merger share of supply because the transaction did not cover Corus' Continental European sales: the customer information Arcelor has acquired only relates to Corus' UK customers. Accordingly, it contends that the combined European share of supply arising as a result of the merger is [45 -50 per cent] ([35-45 per cent] + [0-10 per cent]).

23. Nonetheless, the transaction results in greater concentration of European sheet piling suppliers. Arcelor now has a share of supply in the region of at least [45-50 per cent] with Salzgitter the nearest competitor with [25-35 per cent] share of supply. The composition of competition may have changed as a result of the transaction from a three to two-firm dynamic, with a potentially weak constraint from fringe players such as the Eastern European suppliers. Some UK customers have questioned the quality of the Eastern European producers' product, although it is expected that they will be more competitive now given the lifting of import tariffs following Polish and Czech accession into the EU.

24. The transaction also results in a particularly high share of supply for Arcelor in the UK ([75-85 per cent]) with Salzgitter again the nearest competitor with [10-20 per cent] share. This may already be having an adverse effect on prices for sheet piling in the UK. Evidence from Arcelor indicates that UK prices have increased post-merger by around [5 per cent-15 per cent] (some customers submitting that the price increase is around [10-20 per cent]). This increase appears to be greater than an equivalent rise in European prices. Arcelor submits that the increase in the price of sheet piling, post-merger, is explained by the dramatic increase in the price of scrap metal, the raw material used to produce sheet piling. The increase in the price of steel products generally has been well documented. Evidence of this has been provided by Arcelor, together with evidence of price increase announcements by Corus on other steel products.

25. More generally, as to the importance of Corus for the maintenance of rivalry, Arcelor contends that Corus was never an effective competitor (due to its weak product range and decline in efficiency) within Continental Europe and that the competition dynamic was between Arcelor and Salzgitter. Arcelor further maintains that its prices are constrained by Salzgitter which, Arcelor claims, prices its product aggressively. Furthermore, Salzgitter is said to have spare capacity greater in volume than total UK demand.

Barriers to entry and expansion

26. De novo entry requires substantial investment in the construction of a manufacturing mill which is estimated by some third parties to cost several million pounds. In addition, low margins in this sector appear to be characteristic, nothwithstanding Corus' UK margin, and given that no new entry has been experienced in the last five years, the cost of entry would appear to be high and prohibitive.

27. Arcelor maintains that the cost of expansion by existing players into new territories is low. This is supported by Arcelor's own experience of entry into the UK where in 2003 it obtained a share of supply of [5 per cent-15 per cent] from [<5 per cent] the previous year. Arcelor further maintains that its main competitor, Salzgitter, has excess capacity capable of supplying annual UK demand for sheet piling. The OFT have been unable to confirm what actual usable excess capacity there might be in this sector and there is conflicting evidence as to the degree of excess capacity available to the Eastern European suppliers. The Eastern European suppliers' ability to constrain the activities of the merged entity is uncertain

in view of the mixed evidence received from third parties concerning the quality of their product.

28. It has also been suggested that supplies from the USA and countries such as Japan can enter and supply the European sector. As regards suppliers from the USA entering the European sector, Corus has provided evidence that the interlocking system of USA sheet piling is different from the European system used. Corus said that it had itself tried to develop the USA system of interlocking ('ball and socket') but felt that the European sector was not ready for it and would take a long time to 'convert' customers. Consequently, further development was shelved. It is also unclear as to the extent of non-European products entering the European sector. Some third parties have said that they are rare or very limited at most.

Buyer power

29. Evidence of buyer power has been mixed. Arcelor estimates that a supplier's top ten customers account for approximately [85 per cent-95 per cent] of sales and due to the tendering procedure customers have negotiating strength. Although some customers confirmed this point particularly because of the volumes they purchase, others said that they had little or no negotiating strength. The ability of customers to switch may be limited if Arcelor's only feasible competitor is Salzgitter but Arcelor maintains that Corus was never considered to be a strong competitor outside the UK before the transaction took place.

THIRD PARTY VIEWS

30. There have been varied views about the competitive effects of this acquisition. Some customers are clearly concerned that the loss of Corus as a manufacturer of sheet piling limits their options to switch supplier. Concern has also been raised at the increase in the price of sheet piling since the merger. Other third parties had no concerns about any competitive effects resulting from the acquisition. As noted above there was also a mixture of third party views in relation to the substitutability of sheet piling with concrete and other retaining structures. Most recognised that the type of retaining structure used depended on the type and nature of the project. Generally the deeper the excavation the more likely the use of concrete would be and generally sheet piling would be the typical choice of retaining structure in marine and river work.

CONCLUSION

31. Arcelor, the largest European supplier of sheet piling, has acquired the sheet piling business of Corus, historically the main UK supplier, with which Arcelor had recently been competing directly. Arcelor's share of an already concentrated market has risen significantly.

32. Alternative retaining structures such as concrete may exert a competitive constraint in some applications, but it is unclear that this constraint is strong generally.

33. It is plausible that Corus would have exited in any event, but the parties have not advanced sufficiently compelling evidence for this to be an assumption upon which the OFT can rely in judging whether it may be the case that the merger may result in a substantial lessening of competition. Even if Corus was going to exit in any event, it is possible that a more competitive outcome than acquisition by Arcelor could have come about.

34. In conclusion, therefore, the OFT believes that it may be the case that the merger has resulted or may be expected to result in a substantial lessening of competition within a market or markets in the United Kingdom.

UNDERTAKINGS IN LIEU

35. []

DECISION

36. This merger will therefore **be referred** to the Competition Commission under section 22(1) of the Act.