

***Case No COMP/M.2926 -
EQT/H&R/DRAGOCO***

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**REGULATION (EEC) No 4064/89
MERGER PROCEDURE**

Article 6(1)(b) NON-OPPOSITION
Date: 16/09/2002

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COMMISSION OF THE EUROPEAN COMMUNITIES

Brussels, 16.09.2002

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In the published version of this decision, some information has been omitted pursuant to Article 17(2) of Council Regulation (EEC) No 4064/89 concerning non-disclosure of business secrets and other confidential information. The omissions are shown thus [...]. Where possible the information omitted has been replaced by ranges of figures or a general description.

PUBLIC VERSION

MERGER PROCEDURE
ARTICLE 6(1)(b) DECISION

To the Notifying Parties

Subject: Case No COMP/M.2926 - EQT/H&R/Dragoco

Notification of 12 August 2002 pursuant to Article 4 of Council Regulation No 4064/89

1. On 12 August 2002, the Commission received a notification of a proposed concentration pursuant to Article 4 of Council Regulation (EEC) No 4064/89¹ by which the undertaking Isis Vermögensverwaltung GmbH ("Isis") belonging to the EQT group, which is ultimately controlled by the Swedish Investor AB acquires within the meaning of Article 3(1)(b) of the Council Regulation control of the whole of the undertakings Dragoco Gerberding & Co AG ("Dragoco") and Haarmann & Reimer GmbH ("H&R") by way of purchase of shares and assets.
2. After examination of the notification, the Commission has concluded that the notified operation falls within the scope of Council Regulation (EEC) No 4064/89 and does not raise serious doubts as to its compatibility with the common market and with the EEA Agreement.

I. THE PARTIES' ACTIVITIES AND THE OPERATION

3. EQT Northern Europe ("EQT"), an investment fund active in the north of Europe and ultimately controlled by the Swedish Investor AB, an investment company listed on the OM Stockholm Stock exchange. Both H&R and Dragoco are based in Holzminden, Germany and are active in the areas of fragrances, flavours, aroma chemicals and cosmetic ingredients.

¹ OJ L 395, 30.12.1989 p. 1; corrigendum OJ L 257 of 21.9.1990, p. 13; Regulation as last amended by Regulation (EC) No 1310/97 (OJ L 180, 9. 7. 1997, p. 1, corrigendum OJ L 40, 13.2.1998, p. 17).

Both companies are globally active through their world-wide production sites and client bases.

4. EQT will acquire the two companies through Isis, which has been set up for this purpose. EQT will hold a stake of 75.9% in Isis. EQT's intention is to exploit the synergies resulting from the combination of both companies in view of a stock exchange listing after [...] years.
5. H&R is currently owned by the German Bayer group, who wants to sell this business since it is not part of its core activities. Bayer will sell the entire H&R business to EQT.
6. Dragoco is currently controlled by its CEO, Mr. Gerberding, who will sell his share in the company in return for a minority stake of 22% in Isis. He will be the CEO of the newly formed company resulting from the transaction. . A remaining 2,1% stake in Isis will be hold by the German Braunschweig GmbH.

II. CONCENTRATION

7. The concentration consists of two transactions: the acquisition by EQT of H&R from Bayer and of Dragoco from Mr. Gerberding. Both transactions constitute a single concentration in the sense of Article 3 Merger Regulation. The following reasons are relevant for this assessment:
 8. The two transactions are linked by a legal conditionality that is laid down in the contracts between the parties, which is based on the economic considerations of the parties for entering into the transactions in the first place.
 9. EQT wants to generate returns for its investors by combining H&R and Dragoco, which is considered to lead to the realisation of significant synergies. These synergies could not be realised if either of the companies were acquired on a stand-alone basis. EQT's business objective regarding this transaction is reflected by the purchase price paid for Dragoco and H&R. This price was not motivated solely by the profit potential of either company on a stand-alone basis but only by the combination potential of the two entities.
 10. For Mr. Gerberding, the current majority shareholder of Dragoco, it has been a non-negotiable precondition for the transaction that he would not be willing to give up the control of Dragoco to EQT unless EQT also acquires H&R.
 11. Furthermore the facilities agreement with the financing banks demonstrates the interdependence of the acquisition of the two targets, where the joint acquisition is prerequisite for the financing.
 12. These legal and economic links are underlined by the fact that the closing for the acquisition of H&R and Dragoco will occur on the same day.

III. COMMUNITY DIMENSION

13. The undertakings EQT, H&R and Dragoco have a combined aggregate world-wide turnover in excess of EUR 5,000 million² (EQT, EUR [...]; H&R, EUR [...] and Dragoco, EUR 356

² The turnover is calculated in accordance with Article 5(1) of the Merger Regulation and the Commission Notice on the calculation of turnover (OJ C 66, 2.3.1998, p. 25).

million). Two of them have a Community-wide turnover in excess of EUR 250 million (EQT, EUR [...]; H&R, EUR [...] with Dragoco having EUR [...]), but they do not achieve more than two-thirds of their aggregate Community-wide turnover within one and the same Member State. The notified operation therefore has a Community dimension, but does not constitute a cooperation case under the EEA Agreement, pursuant to Article 57 of that Agreement.

IV. COMPETITIVE ASSESSMENT

A. Relevant product markets

14. Both target companies, H&R and Dragoco, are primarily producers and suppliers of flavours and fragrances – both consisting of complex blenders of aromatic materials – as well as aroma chemicals which principally serve as one type of the compounding agents in the production of flavours and fragrances. H&R and Dragoco also produce and supply cosmetic ingredients. EQT is not active in any of these areas.
15. Furthermore H&R is active in the downstream market for fruit juice compounds, where flavours are used in the production. The EQT group is active in the market for frozen foods through a subsidiary, Findus AB (“Findus”), which also uses flavours in its production.

1. Flavours

16. Flavours are compounds of naturally occurring and/or synthetically manufactured ingredients to impart flavour to materials designated for human consumption or animal feeding. The natural flavours (ex. berries) are commonly regarded as an inherent part of the creation of a flavour compound. There is no market for these natural raw materials. By contrast the synthetically manufactured ingredients are the below (IV.A.3.) described aroma chemicals which constitute an upstream market. Flavours are manufactured by blending the ingredients and diluting them with solvents to the desired concentration.
17. Flavours are used for a wide range of products, such as processed foods, drinks, chewing gums, pharmaceutical products, tobacco and fodder. The function of the flavour is to simulate the flavour, to maintain its character and to enhance the flavour impression and its acceptability.
18. Flavours are almost always customised, i.e. designed for a specific end product, which very often is defined at a very late stage of the product development on the basis of tenders. Thus, a particular flavour composition may not be interchangeable with another flavour composition from the demand side. However, due to the very high degree of supply side substitutability, which characterises the flavours industry, the parties submit that the relevant product market includes all flavour compositions.
19. It results from both the parties’ submissions and the market investigation that most flavour companies have the ability to design and manufacture a wide range of flavours for a multiplicity of end products. The production of flavours is essentially low-tech and based on a common applicable production methodology, equipment and know-how. Flavour manufacturers are able to convert the production of one flavour composition to the manufacture of another without any significant delay or expense or the need for technical adjustments. It is the “inputs” (i.e. ingredients) which vary according to the required specifications. Consequently, it is capability rather than actual production that creates competitive pressure in the market, which in turn makes supply-side substitutability the

decisive factor when defining the relevant product market. It should also be observed that there are no capacity restraints that prevent supply-side substitution. The parties estimate that the capacity utilisation rate in the F&F industry is around 60-80%.

20. It follows from the above that flavours as a whole constitute a relevant product market.

2. Fragrances

21. Fragrances are compounds of natural and synthetic origin giving scent to or masking bad odour of a wide range of products. They are manufactured by blending natural and/or synthetic ingredients and diluting them with solvents to the desired concentration. Natural fragrance ingredients are extracted from herbs or animals (ambra, musk), whereas semi-synthetic or fully synthetic ingredients are manufactured by using aroma chemicals instead of natural ingredients.

22. Fragrances are used for the manufacture of fine perfume products, cosmetic products and other kinds of products such as laundry detergents, fabric softeners, and dish wash detergents, cleaners and air fresheners.

23. Even though various fragrance compositions are often developed individually by manufacturers in close co-operation with their customers, it is normally possible to get the same or a very similar product from a new supplier. The market investigation has shown that for some sophisticated products such a change could be a relatively important expenditure, and therefore customers tend not to switch supplier for a specific composition developed in co-operation between customer and supplier. However, this does not reduce competition between suppliers, but creates incentives for them to compete on winning customers' orders for the development of new compositions.

24. Therefore, the considerations leading to the definition of a single product market for flavours apply to fragrances accordingly, so it can be concluded that fragrances as a whole constitute a relevant product market.

3. Aroma Chemicals

25. Aroma chemicals are chemical substances (molecules) with a distinctive flavour and/or odour. They are used as raw materials for the manufacture of flavour and fragrance compositions. The production of aroma chemicals, which are manufactured by physical methods (extraction, steam distillation etc.), by chemical modification of isolates from natural sources or by chemical synthesis (usually starting with petro-chemical raw materials), is more sophisticated than the blending of flavours and fragrances.

26. Aroma chemicals are either consumed captively or sold to third parties as a raw material for the production of flavours (around 30% of world-wide production) and fragrances (around 70% of world-wide production).

27. With regard to aroma chemicals the parties also refer to the very high degree of supply-side substitutability, which characterises the aroma chemicals business in order to make the point for a single product market which would include all aroma chemicals. The considerations are similar to those made with regard to flavours and fragrances: each of the major manufacturers of aroma chemicals has the capacity, know-how and the technical capabilities to supply its customers (flavour and fragrance manufacturers) with a wide range of aroma chemicals and can convert the production of a certain aroma chemical substance to the

manufacture of another one without any significant delay or expense or the requirement for technical adjustments. In their replies to the Commission's market investigation, customers explained that although the replacement of some specific aroma chemicals is not necessarily easy and chemical molecules might not be identical in the offer of two distinct suppliers, the replacement of some aroma chemicals by others is quite common in their business. Suppliers are regularly confronted with such requests, and are used to finding appropriate solutions to this.

28. It can be concluded that, also with regard to aroma chemicals, it is capability rather than actual production that creates competitive pressure in the market and is the decisive factor when defining the relevant product market. The Commission therefore concludes that aroma chemicals as a whole constitute a distinct relevant product market.

4. Cosmetic Ingredients

29. Cosmetic ingredients are chemical agents used in the manufacture of cosmetics, e.g. surfactants/emulsifiers, cosmetic oil components, waxes, polymers, water-soluble plant extracts, cooling agents, sunscreen agents and anti-dandruff agents. Cosmetic ingredients are either synthetic or natural substances.
30. Supply-side considerations also lead the parties to define a single market for all cosmetic ingredients. On the one hand, distinguishing between cosmetic ingredients depending on the ultimate end product in question would be inappropriate for market definition purposes as one chemical agent often could be used for very different products and/or have several functions/effects. On the other hand, the very high degree of supply side substitutability in this sector enables competitors to supply easily the various cosmetic ingredients in question to the market. The results of the market investigation underline the existence of a single product market for cosmetic ingredients.

5. Fruit juice compounds

31. H&R, but not Dragoco, is active on the downstream market for fruit juice compounds. Those highly concentrated fruit juice mixes contain small quantities of flavours, less than 5% of the final fruit juice compound mix by weight and less than [5-10%] in terms of value. On this basis flavours amount to well below 1% of the final beverage product. As upstream almost all producers of flavours and downstream almost all producers of fruit juices have the know-how and technology to produce fruit juice compounds supply-side considerations lead to the definition of fruit juice compounds as one single product market.

6. Frozen foods

32. One of the portfolio companies controlled by the EQT-Group is the frozen food manufacturer Findus. It uses flavours in its production to a small extent. Since this vertical relationship does under no possible market definition give rise to any competition concern, the exact definition of the market(s) for frozen food can be left open.

B. Relevant geographic markets

33. The parties consider the geographic market for flavours, fragrances, aroma chemicals and cosmetic ingredients to be at least EEA-wide. The general conditions for the production are

homogeneous world-wide, transport costs are insignificant and there are no significant price differentials. There are no tariffs or other non-tariff barriers within the EEA or elsewhere which might affect the cross-border trade. The general conditions of competition for the production and trade of the products are homogeneous and the raw materials are widely available all over the world. Cross-border supplies of the four products in question within the EEA but also on a wider European and indeed global basis are common place.

34. Moreover, the flavours and fragrances businesses are based on formulation knowledge and do not require high-value technical investments. Production can therefore be established anywhere around the world and requires little technical sophistication. The compositions are generally not protected by intellectual property and can therefore be duplicated by any competitor. As their competitors, the parties produce world-wide and sell their products to a world-wide customer base.
35. H&R manufactures flavours in more than 20 countries world-wide, including Germany, France, Spain, the UK, USA, South Africa, South America, Australia etc. The company supplies flavours to its EEA customers from its production facilities in Europe and the USA; on a case by case basis even from Asia and Australia. Dragoco manufactures flavours in 7 countries world-wide, including Germany, Austria, USA, India, China etc. The EEA customers are supplied from the Dragoco's production facilities in Europe or – on a case by case basis – from the US, China and Singapore production plants.
36. The same is true for the fragrances market. All major producers – including H&R and Dragoco - supply customers in all European States. H&R manufactures fragrances 16 facilities world-wide, including in Germany, Spain, Switzerland and the US; Dragoco manufactures fragrances in 7 facilities, including Germany, Austria, the US, Brazil, Singapore, China.
37. Aroma chemicals and cosmetic ingredients involve a chemical process, which is somewhat more sophisticated, but still basic compared to other production technologies used in the chemical industry. H&R and Dragoco produce their aroma chemicals only in Holzminden, Germany but sell them to customers world-wide, such as do all major producers. Cosmetic ingredients are produced by Dragoco in Germany, Austria, Brazil and Singapore, H&R produces only in Germany, but both of them serve customers worldwide.
38. The existence of an at least EEA-wide, if not world-wide geographic market for flavours, fragrances, aroma chemical and cosmetic ingredients has been confirmed by all respondents, both customers and competitors, in the market investigation.
39. The geographic scope of the markets for fruit juice compounds and frozen food can be left open, since the vertical relationship between the parties concerning these markets does not give rise to competition concerns under any possible geographic market definition.

C. Assessment

1. Horizontal relationships

40. The combined market shares of the parties do not exceed 15% in any of the above mentioned markets in which both H&R and Dragoco are active.

a. Flavours

41. The flavour market (2001) is estimated to amount to around EUR [...] world-wide and to around EUR [...] million in the EEA..
42. H&R's 2001 turnover in flavours amounted to around EUR[...] world-wide and to around EUR[...] in the EEA, corresponding to a market share of [5-10%] and [5-10%] respectively. Dragoco's 2001 turnover in flavours amounted to around EUR [...] world-wide and to around EUR [...] in the EEA, corresponding to a market share of [0-5%] in each geographic area.
43. The following table sets out the market shares for the leading global suppliers of flavours (in 2001).³

Flavour suppliers	World-wide	EEA-wide
IFF	[15-20%]	[15-20%]
Givaudan	[15-20%]	[10-15%]
Quest	[10-15%]	[10-15%]
Firmenich	[5-10%]	[5-10%]
H&R	[5-10%]	[5-10%]
Dragoco	[0-5%]	[0-5%]
Takasago	[5-10%]	(not available)

44. Other major flavours suppliers include, Bell Flavours and Fragrances (USA), Belmay Inc. (USA), Degussa (Germany), Doehler (Germany), Frutarom (Israel), Hasegawa (Japan), Lucta (Spain), V. Mane Fils (France), Mannheimer (USA), Ogawa & Co. (Japan), Robertet (France), Sensient Technologies (USA), Soda Aromatic (Japan), and Wild (Germany).
45. The combined market share of H&R and Dragoco would be around [5-10%] on a world-wide flavour market and around [10-15%] on an EEA-wide flavour market.
46. On the basis of these market shares and in absence of any indications to the contrary, the addition of H&R's and Dragoco's activities in the flavours market does not give reason for competitive concerns.

b. Fragrances

47. The world-wide fragrances market (2001) is estimated to amount to around EUR [...] and that the EEA-wide fragrances market to amount to around EUR [...].
48. H&R's 2001 turnover in a world-wide fragrances market amounted to around EUR [...] and in an EEA-wide market to around EUR [...], corresponding to a market share of [5-10%] and [5-10%] respectively.
49. Dragoco's 2001 turnover in the world-wide fragrances market amounted to around EUR [...] and in the EEA-wide market to around EUR [...], corresponding to a market share of [0-5%] and [0-5%] respectively.

³ Source: IAL Consultants, February 2000 and the parties' best estimates.

50. The following table sets out the market shares for the leading global suppliers of fragrances (in 2001)⁴.

Fragrance suppliers	World-wide	EEA-wide
IFF	[15-20%]	[15-20%]
Givaudan	[10-15%]	[15-20%]
Firmenich	[10-15%]	[10-15%]
Quest	[10-15%]	[10-15%]
Mane	[5-10%]	(not available)
H&R	[5-10%]	[5-10%]
Takasago	[0-5%]	(not available)
Dragoco	[0-5%]	[0-5%]

51. Other major fragrance producers include, Bell Flavours and Fragrances (USA), Belmay (USA), Charabot (France), Drom Fragrances International KG (Germany), Hasegawa (Japan), International Speciality Products (USA), Lucta (Spain), Manheimer (USA), Millennium Speciality Chemicals (USA), Ogawa (Japan), Robertet (France), Sensient Technologies (USA), Soda Aromatic (Japan), Treatt (UK), Wild (Germany).

52. The combined market share of H&R and Dragoco would be around [5-10%] on a world-wide fragrance market and around [10-15%] on an EEA-wide fragrance market.

53. On the basis of these market shares and in absence of any indications to the contrary, the combination of H&R's and Dragoco's activities in the fragrances market does not give reason for competitive concerns.

c. Aroma Chemicals

54. The world-wide aroma chemicals market (2001) is estimated to amount to around EUR [...] and the EEA-wide aroma chemicals market to around EUR [...].

55. H&R's 2001 turnover in the world-wide aroma chemicals market amounted to around EUR [...] and in the EEA-wide market to around EUR [...] corresponding to a market share of around [5-10%] on either geographic area. Dragoco's 2001 turnover in aroma chemicals world-wide amounted to around EUR [...] and in the EEA to around EUR [...] corresponding to a market share of around [0-5%] in either geographic area.

56. The following table sets out the market shares for the leading global suppliers of aroma chemicals (in 2001).⁵

Aroma chemicals suppliers	World-wide	EEA-wide
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⁴ Source: IAL Consultants, February 2000 and the parties' best estimates.

⁵ Source: IAL Consultants, February 2000 and the parties' best estimates.

IFF	[5-10%]-[10-15%]	[5-10%]-[10-15%]
Firmenich	[5-10%]-[10-15%]	[5-10%]-[10-15%]
Givaudan	[5-10%]-[10-15%]	[5-10%]-[10-15%]
Quest	[0-5%]-[5-10%]	[0-5%]-[5-10%]
H&R	[5-10%]	[5-10%]
Takasago	[0-5%]-[0-5%]	[0-5%]-[0-5%]
Dragoco	[0-5%]	[0-5%]

57. The combined market share of H&R and Dragoco for aroma chemicals would be [5-10%] both world-wide market as well as EEA-wide.
58. On the basis of these market shares and in absence of any indications to the contrary, the possibility of dominance due to the combination of H&R's and Dragoco's activities in the aroma chemicals market does not give reason for competitive concerns.

d. Cosmetic Ingredients

59. The world-wide turnover for cosmetic ingredients (2001) is estimated to amounts to around EUR [...] and EEA-wide to around EUR [...].
60. H&R's 2001 turnover for cosmetic ingredients world-wide amounted to around EUR [...] and to around EUR [...] in the EEA corresponding to a market share of around 2% in both geographical areas. Dragoco's 2001 turnover in cosmetic ingredients world-wide amounted to around EUR [...] and to around EUR [...] in the EEA corresponding to a market share of around [0-5%] and [0-5%] respectively.

61. The following table sets out the market shares for the leading global suppliers of cosmetic ingredients (in 2001).⁶

Cosmetic ingredients suppliers	World-wide	EEA-wide
Dow Chemical	[10-15%]	[5-10%]
ISP	[10-15%]	[10-15%]

⁶ Source: IAL Consultants, February 2000 and the parties' best estimates.

BASF	[5-10%]	[10-15%]
Cognis	[5-10%]	[10-15%]
Degussa Goldschmidt	[0-5%]	[5-10%]
ICI	[0-5%]	[0-5%]
Clariant	[0-5%]	[0-5%]
Merck (Dortmund)	[0-5%]	[0-5%]
Dragoco	[0-5%]	[0-5%]
H&R	[0-5%]	[0-5%]

62. The combined market share of H&R and Dragoco on a world-wide cosmetic ingredients market would be [0-5%] and on an EEA-wide cosmetic ingredients market [5-10%].
63. On the basis of these market shares and in absence of any indications to the contrary, the possibility of dominance due to the combination of H&R's and Dragoco's activities in the cosmetic ingredients market does not give reason for competitive concerns.

2. Vertical relationships

a. Fruit juice compounds

64. H&R downstream activities in fruit juice compounds amounted to a 2001 turnover of about EUR [...] in total. The flavours used to produce fruit juice compounds constitute less than 5% of the product value. As flavours are used in a multitude of food products, fodder, pharmaceutical products etc. and in the light of the combined market shares of Dragoco and H&R in an upstream flavours market of around [10-15%] EEA-wide, any risk of foreclosure resulting from the existing vertical relationship can be excluded.

b. Frozen foods

65. EQT's downstream activities in the frozen food sector through Findus do not carry the risk of a foreclosure either. Findus' total expenditure on the purchase of flavours is less than EUR [...], which amounts to less than 5% in terms of volume of its total production and less than 5% of its purchasing value. A combination of EQT with H&R and Dragoco would in light of their market share in flavours and the use of flavours in many diverse products not be likely to create a foreclosure effect.

3. Result of the assessment

66. On the basis of the markets definitions proposed by the parties and confirmed by the market investigation the overlap of H&R and Dragoco would not exceed 15% in any of the four identified markets where horizontal overlaps exist (flavours, fragrances, aroma chemicals and cosmetic ingredients). On these markets competitors with an important market position are present. The merged entity H&R/Dragoco will be able to compete with these companies placing itself among the 4 to 6 more important players on these markets. Due to the limited market share of the merged entity on the flavours market on the one hand and the use of flavours in a multitude of products on the other hand, the vertical relationship with the markets for fruit juice compounds and frozen foods does likewise not give rise to any possible foreclosure effect.

V. CONCLUSION

For the above reasons, the Commission has decided not to oppose the notified operation and to declare it compatible with the common market and with the EEA Agreement. This decision is adopted in application of Article 6(1)(b) of Council Regulation (EEC) No 4064/89.

For the Commission

Mario MONTI
(Member of the Commission)