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Case No IV/M.331 - FLETCHER CHALLENGE / METHANEX

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REGULATION (EEC) No 4064/89
MERGER PROCEDURE

Article 6(1)(b) NON-OPPOSITION
Date: 31.03.1993

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COMMISSION
OF THE EUROPEAN
COMMUNITIES

Brussels, 31 March 1993

PUBLIC VERSION

MERGER PROCEDURE
ARTICLE 6(1) (b) DECISION

Registered with advice of delivery

1. Notifying party
2. Notifying party

Dear Sirs,

Subject: Case No. IV/M.331 - Fletcher Challenge/Methanex
Notification of 01.03.1993 pursuant to Article 4 of Council Regulation No. 4064/89

1. The above operation concerns the acquisition by Fletcher Challenge Ltd of joint control over Methanex Corporation, the other controlling shareholder being Metallgesellschaft AG.

2. After examination of the notification, the Commission has concluded that the notified concentration falls within the scope of Council Regulation No. 4064/89 and does not raise serious doubts as to its compatibility with the common market.

I. THE PARTIES

3. Fletcher Challenge ("FC") is a company based in New Zealand whose activities include the manufacture of pulp and paper, and building materials, construction, agriculture and energy. Its methanol and synthetic fuels production activities are located in New Zealand and Chile, but most of the methanol is subsequently sold in the EC, Japan and the US.

4. Metallgesellschaft ("MG") is a German company principally active in trade and financial services, the processing of base materials and engineering services, as well as chemistry, mining and environmental technology. After MG transferred its European marketing division to Methanex in 1992 in exchange for a 32% shareholding in the latter, it is no longer present in the methanol industry for its own account.

5. Methanex is a Canadian-based company active in the production and marketing of methanol and ammonia. Its production facilities are situated in Canada and the methanol produced is sold in Canada, the US and the Far East. In Europe, Methanex does not sell its own production but has a wholly owned subsidiary called Methanex GmbH that operates as a trader, re-selling methanol only purchased from independent producers.

Rue de la Loi 200 - B-1049 Brussels - Belgium

Telephone: direct line 29..... exchange 299.11.11 - Telex COMEU B 21822 - Telegraphic address COMEUR Brussels telefax 29.......

II. THE OPERATION

6. Methanex' current shareholding structure is the following: 32% of the capital is held by Metallgesellschaft (see point 4), the rest being widely dispersed amongst the public. In addition to the voting rights attached to its shareholding, MG has the right to appoint the Chairman and the Vice Chairman of Methanex' 7-member board.

7. FC and Methanex have entered into an agreement whereby FC transfers its methanol and synthetic fuels businesses to Methanex in exchange for shares and cash. As a result of this transfer of assets and increase of Methanex capital, the new shareholding structure of Methanex will be as follows:

   FC 44%
   MG 10%
   Public 46%

8. FC and MG have concluded a Shareholders Agreement providing for, inter alia, the following:

   (i) The number of directors on the Methanex board will be increased to 11, of whom 5 will be FC designees, 3 MG designees and the remaining 3 will be independent directors but jointly nominated by FC and MG. Both parties have agreed on the identity of the directors and will jointly support their nominations when submitting them for approval to the shareholders' meeting. Two of the three independent directors have already been jointly nominated. They are a partner and a counsel from the law firm advising Methanex. Both have been directors of Methanex since December 1991.

   (ii) FC and MG agree on the identity of the Chairman and Deputy Chairman, who will initially be an MG and an FC designee respectively. The Chairman and the Deputy Chairman have co-ordination roles.

   (iii) Methanex board decisions are taken by simple majority. This implies that either party can act without the other provided it obtains the support of at least one - in the case of MG all - of the independent directors. However, both parties are obliged to vote together in favour of any proposal adopted by the board on submission to the shareholders' meeting (even if they had voted against it in the board).

   (iv) Both parties have mutual rights of first offer and refusal in respect of share transfers. MG also has certain "take along" rights in the event that FC wishes to transfer any of its shares.

III. CONCENTRATION

9. As a result of the present operation, Methanex will become a joint venture of FC and MG. Methanex will perform on a lasting basis all the functions of an autonomous economic entity. Methanex' activities will be enlarged and it will continue to hold all the production and distribution assets necessary to carry out its business in the methanol and ammonia sectors.

10. As to joint control the following elements have to be taken into account:

    - FC and MG together will command the majority of shares and voting rights (54%) in Methanex.

- FC and MG have concluded a shareholder agreement which provides that they exercise their voting rights to a large extent, including important resolutions, jointly.

- FC and MG agreed to decide jointly on the composition of the enlarged board of directors of Methanex. They will also jointly fill any vacancy created by the resignation or removal of a director. All future independent directors must be mutually acceptable to FC and MG.

- The parties also agreed on the internal board appointments. The Chairman of the executive board of MG shall be Chairman of Methanex and an FC designee shall be deputy Chairman until the end of 1994. Thereafter an FC designee shall be Chairman of Methanex and an MG designee Deputy Chairman.

- FC and MG will define their common position in shareholder meetings by resolutions taken by the board of directors of Methanex. They agreed to vote in favour of all transactions and proposals approved by the board by simple majority.

- FC and MG complement each other as substantial shareholders in Methanex. FC has developed significant experience as a producer of methanol with natural gas as a feedstock. MG has become an important marketer of methanol with access to the big US and European markets. After transferring their methanol businesses to Methanex they have a common interest in using their complementary expertise in order to make Methanex a major player in the worldwide methanol industry.

11. Taking into account all the above elements, it is concluded that FC and MG will jointly control Methanex.

12. Both parent companies will withdraw from the sector on completion of the operation. Therefore, the creation of the joint venture does not give rise to co-ordination of the competitive behaviour of the parties and constitutes a concentration within the meaning of Article 3 of Regulation 4064/89.

IV. COMMUNITY DIMENSION

13. The present operation has a Community dimension within the meaning of Article 1(2) of the Regulation. The combined aggregate worldwide turnover of FC, MG and Methanex exceeded 17,000 million ECU in 1992(1). Both FC and MG attained a Community-wide turnover of more than 250 million ECU in the same financial year, of which they did not achieve more than two-thirds within one and the same Member State.

V. COMPATIBILITY WITH THE COMMON MARKET

Relevant product market

14. The main effects of the transaction concern the production and distribution of methanol, a basic liquid petrochemical, primarily obtained from natural gas. It is a homogeneous product once it reaches the minimum quality standard internationally accepted and is generally traded as a commodity. It has two major uses: the production of resins for building materials and engineering plastics and fuel applications, in particular the production of unleaded gasoline. Methanol is usually converted into MTBE (methyl tertiary butyl ether) which is used for the production of unleaded gasoline.

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(1) In the case of FC, the figures correspond to the financial year ending 30 June 1992.

Methanol itself constitutes a product market because it has no realistic substitutes in terms of applications and price.

15. FC is a multinational producer of methanol. In New Zealand it also converts crude methanol directly into unleaded gasoline and produces small quantities of durene, a by-product of gasoline. Most of FC's gasoline is sold in New Zealand's domestic market and the remainder is exported, primarily to Australia and countries in the Far East. FC does not sell gasoline in the EC. All these businesses will be transferred to the joint venture.

Methanex produces and distributes methanol and, to a lesser extent, ammonia. It does not sell ammonia in Europe. FC is not engaged in the production of ammonia.

<u>Geographic reference market</u>

16. Methanol is internationally traded as a commodity. The fact that certain production plants - especially in developing countries have very low production costs and sometimes benefit from more favourable import duties, helps to explain why methanol can be profitably transported over long distances, even if transport costs are not low. This is usually the case for those plants situated in remote locations whose local demand by no means absorbs production and where there is easy access to transport by sea (for example, plants in Chile, Malaysia or Trinidad). Such production is shipped to areas of the world where demand exceeds production.

However, the situation is not such as to conclude that there is a world market, since conditions of competition vary between the three main demand areas of the world: EC/Europe, North America and Asia. In the EC the current system of tariffs and ceilings imposes a 13% duty on the CIF value of all imports of methanol except for those originating in countries that benefit from preferential status (such as Chile, Trinidad or Malaysia). In the US there is an 18% import tariff, but as a result of the Canada-US Free Trade Agreement, Canadian methanol is exempt. Finally, in Asia, Japan is by far the most important net importer (accounting for around 50% of total Far East and Asian demand) and imports to Japan are only subject to a 2.8% import duty.

17. Overall it can be concluded that due to tariff barriers, transport costs and the different demand conditions of the three main geographic areas described, the latter have not yet achieved sufficiently homogeneous conditions for competition to consider that there is a world market. This is confirmed by the fact that methanol producers usually sell in the market closest to their plant (for example, Saudi Arabian, Libyan and Russian production tends to be exported to the EC).

However, a precise definition of the relevant geographic market does not need to be established as the concentration will not create or strengthen a dominant position even on the basis of the narrowest geographic market. Although there are grounds to consider that this market could be wider, ie comprising the whole of Western Europe, the market analysis of the present transaction will focus on the EC, the narrowest area where conditions of competition are homogeneous.

<u>Assessment</u>

18. The Community market for methanol has undergone considerable structural changes in the last decade. Due to demand growth the market is now much more open and captive production has become less important. In addition, the average production capacity per plant has increased and natural gas has replaced oil and coal as the major feedstock for methanol production. Several production facilities within the EC had to be closed down and

have been replaced by imports. Market growth is expected to continue, but will only be 10% in the period between 1991 and 1995.

19. The Community market is moderately concentrated. No supplier holds a market share of more than 25%; the five major suppliers serve around two-thirds of EC demand. There are three categories of suppliers for methanol: EC producers, non-EC producers and marketers who purchase from both for resale to end users. End users are mainly large chemical companies.

20. EC production plants are owned by Methanor in the Netherlands; Leunawerke, RWE DEA, VEBA and BASF in Germany; ICI in the UK and Chemie Linz in Italy. BASF produces methanol exclusively for internal consumption but all the others sell part of their production on the open market. Neither FC nor Methanex own plants in the EC (see points 3 and 5).

21. Since demand exceeds production in the EC by a considerable amount, imports (in particular from Saudi Arabia, Libya, Russia and Chile) account for around 60% of the total sales in the Community. FC sells methanol from its Chilean plant and a small amount from New Zealand. Methanex does not import methanol from its refineries. Its German subsidiary sells the petrochemical from EC producers as well as from other non-EC producers.

22. Price fluctuations in the past in the different areas of the world where methanol is sold show that these areas are closely interlinked. A price rise in one area has usually led to a rapid increase in supply, thereby bringing prices back to a uniform level.

23. The proposed concentration will have horizontal as well as vertical effects. Although it will create one of the world's largest methanol producers (approximately 10% of world capacity) and marketers, the operation will not fundamentally change conditions of competition within the common market.

24. As to the horizontal effect, Methanex appears to become the leading supplier with an overall market share (including the sales of its trade subsidiary Methanex GmbH) not higher than 25%.

25. The present supply structure within the Community may very well change further with the continuing growth of demand and the interest of countries far away from the industrial centres to make use of their resources of natural gas. FC's Chilean plant is itself an example of the dynamics of the industry. It began operating in 1988 and has since become one of the largest suppliers to the EC. Currently, new methanol production facilities are under construction in Trinidad and Venezuela. The EC already imports methanol from Trinidad. Additional market entry is being considered by Norway. A new methanol plant, which is costly to build (costs can exceed US$ 300 million), could be constructed in two and a half to four years.

26. Moreover, EC producers, non-EC producers and marketers have very divergent cost structures. Non-EC producers are subject to different import regulations depending on the country from which they import (some are totally free to import). It appears, therefore, unlikely that they will be able to arrive at a common supply policy which serves their divergent interests. This will not be altered through the operation since it only increases the market concentration moderately.

27. As to the vertical effects of the operation, foreclosure may occur given the fact that Methanex GmbH belongs to the leading group of traders within the Community. FC will have better access to EC chemical companies. However, in view of the overall supply structure of the Community market, which is moderately concentrated, the possible foreclosure effect will not lead to the creation or strengthening of a dominant position.

28. It can, therefore, be concluded that the proposed operation does not create or strengthen a dominant position as a result of which effective competition will be significantly impeded in the common market or in a substantial part of it.

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

For the Commission