EN

Case No COMP/M.3535 - VAN DRIE / SCHILS

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REGULATION (EC) No 139/2004
MERGER PROCEDURE

Article 6(1)(b) NON-OPPOSITION
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PUBLIC VERSION

MERGER PROCEDURE
ARTICLE 6(1)(b) DECISION

To the notifying party

Subject: **Case No COMP/M.3535 - Van Drie/ Schils**
Notification of 17 September 2004 pursuant to Article 4 of Council Regulation No 139/2004[1]

1. On 17 September 2004, the undertaking Van Drie Holding B.V. ("Van Drie") notified its intention to acquire control of the whole of the undertaking Schils Holding B.V ("Schils", The Netherlands) within the meaning of Article 3(1)b of the Merger Regulation. Due to incompleteness, the file was resubmitted to the Commission on 3 November 2004.

2. Prior to the notification, the concentration was referred to the Commission by the Member States under Article 4(5) to be reviewed under the EC Merger Regulation.

I. THE PARTIES

3. **Van Drie** is a Dutch company, active in the wholesale of whey powder and skimmed milk powder, the production and sale of calf milk replacer, the purchase of young calves, the trade and the slaughter of fatted calves as well as in the sale of veal to wholesalers and industrial processors. Van Drie is mainly specialized in the production of veal products and has slaughterhouses in France and in The Netherlands. The company sells its veal products all over Europe.

4. **Schils** is also a Dutch company, producing and selling a range of dry dairy products (like whey powder, skimmed milk powder, whey fat concentrates and calf milk replacers). To a more limited extent Schils is involved in activities related to veal

1 OJ L 24, 29.1.2004 p. 1.

production (like purchase of young calves, trading and the slaughtering of fatted calves and the sale of veal to industrial processors and wholesalers). However, Schils's core business is in dry dairy products supplied to customers in various European countries.

II. THE OPERATION

5. The entire operation of Schils will be acquired by the Van Drie Group by way of purchase of shares. After the transaction Schils will be integrated in Van Drie and will continue its activities.

III. CONCENTRATION

6. Van Drie will acquire sole control over Schils. The transaction is therefore an acquisition within the meaning of Article 3(1)b of the EC Merger Regulation.

IV. COMMUNITY DIMENSION

7. The concentration does not have Community dimension within the meaning of Article 1 of the Merger Regulation. On 5 August 2004 the notifying parties submitted a Reasoned Submission under Article 4(5) of the Merger Regulation, claiming that the operation is capable to be reviewed under the national competition laws of at least three Member States and that the Commission is best placed to review the concentration. Since no Member State objected to the request, the case was referred to the Commission.

V. RELEVANT MARKETS AND COMPETITIVE ASSESSMENT

A. Overview

8. Both Van Drie and Schils are active along a vertical chain that leads to veal as a final product. Skimmed milk and whey powder are among the main ingredients of calf milk replacers used for the fattening of slaughter calves.

9. Calves may be fattened directly by companies who also assume the associated economic risk or under fattening contracts, whereby farmers act essentially as service providers. After a period of 6 months of fattening, the calves are collected by slaughterhouses. Finally, the calf and veal processing ends with the sale of veal to wholesalers, industrial processors and other customers.

10. While the parties are vertically integrated to a large degree along the entire veal production chain, numerous competitors cover only one or a few production steps. As a result, extensive market interaction takes place between non-integrated players, such as independent slaughterhouses, farmers, calf milk replacer manufacturers and dairies (who supply whey and skimmed milk). Integrated players also participate in this market, for example by selling calf milk replacer to less-integrated producers or by buying fattened calves to fill their slaughterhouse capacity.

B. Relevant product markets

(i) Whey powder and skimmed milk powder

11. Whey powder and skimmed milk are among the main ingredients, in terms of value, of calf milk replacer. Whether each constitutes a separate relevant product market within

the veal production chain or is part of a wider product market[2], can be left open, as no affected market arises even under the narrowest possible market definition.

(ii) Calf milk replacer

12. Calf milk replacers are feeds developed especially for calves. They are mainly composed of whey powder, whey fat concentrates, skimmed milk powder, vitamins […]. The quality of calf milk replacer depends on the content of protein and digestibility. The protein is provided by the whey powder and skimmed milk powder mixed in the feed. The digestibility is the outcome of research, done by most producers in-house.

13. Based on the content of skimmed milk powder, two major types of calf milk replacers can be identified: the 0% product and 50% product. Both of them are marketed on the European markets and used during the fattening process of young calves. According to the parties, many farmers mix the two types to obtain their individually desired skimmed-milk content. Formulations vary, in addition, between calf milk replacers used for the fattening of slaughter calves and the rearing of calves which are later used as milk cows. Most suppliers of calf milk replacer offer a range of different formulations and little, if any, barriers to supply-side substitution appear to exist between the different varieties. It can therefore be concluded that there exists a single relevant product market for calf milk replacers.

(iii) Purchase of young calves

14. In its Best Agrifund/Nordfleisch decision[3], the Commission concluded that the purchase of live cattle for slaughtering constitutes a separate product market. Following this reasoning, the notifying parties argue that there exists a separate market for the purchase of young born calves. This market comprises the ten days old young calves bought by the cattle traders for fattening purposes from the dairy farmers.

(iv) Fattening of calves

15. Subsequently, the young animals are fattened either by their purchasers directly or fattened under contract by third parties. Some of the vertically integrated groups combine their own husbandry activities with contract fattening. The service of fattening calves under contract may therefore constitute a separate relevant product market for purposes of competition analysis. .

(v) Trading of fattened calves

16. Either by independents or by integrated producers without slaughtering facilities or with insufficient in-house slaughtering capacities, the fattened calves may be sold on the trading markets. The trading of fattened calves, therefore, may constitute a separate relevant product market, although significant interaction would seem to exist between trading and direct sale to a slaughterhouse. The exact market definition can, however, be left open in this case, as no competition concerns arise under any possible market definition.

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2 Whey powder and skimmed milk are, to some extent, substitutable in the production of calf milk replacer.

3 Decision of the European Commission dated 19 March 2004, case number M. 3337, paragraph 17.

(vi) Slaughtering of fatted calves

17. The slaughterhouses are buying fatted calves ready to be slaughtered. Before slaughtering, the quality of the animal (race, colour of the meat, fat content) is confirmed by an independent authority and the price is set accordingly. Slaughterhouses are designed for the slaughtering a specific species and cannot change their intake without substantial refurbishment. The slaughtering of fattened calves, therefore, constitutes a separate relevant product market.

(vii) Sale of veal to wholesalers

18. The sale of meat to wholesalers has been identified in the Commission's Best Agrifund/Nordfleisch decision[4] as a distinct market. The notifying parties based their delineation for veal wholesale on this decision. The market investigation in the present case has confirmed the findings of the Commission in the Best Agrifund/Nordfleisch decision.

(viii) Sale of veal to industrial processors

19. In the same decision, the Commission also identified a separate market for the sale of fresh meat to industrial processors. Industrial processors transform the meat and sell the processed food to retailers. As a luxury product, the processing and the catering markets play a smaller role than for the pork and beef production. The market investigation in the present case has confirmed the findings of the Commission in the Best Agrifund/Nordfleisch decision.

C. Relevant geographic markets

(i) Whey powder and skimmed milk powder

20. Whey powder and skimmed milk powder are commodity products. Being easily transported and sold all over Europe the geographical market appears to be EEA-wide in scope. However, it is not necessary to conclude definitively on this question, as no competition concerns would arise even under a narrower, national, market definition.

(ii) Calf milk replacer

21. The market investigation indicates that the market for calf milk replacers is European-wide in scope. Production is concentrated in five Member States, Belgium, France, Germany, Italy and The Netherlands, where most of the veal production in Europe takes place. Calf milk replacer is traded extensively throughout Europe and some manufacturers appear to export even over intercontinental distances (e.g. to Latin America). Quality concerns may, however, limit users' ability and willingness to import from outside the EU. Even smaller calf milk replacer manufacturers have confirmed that they supply their product across the EU, although smaller companies tend to concentrate on selected export markets where they have identified sales potential.

(iii) Purchase of young calves

4 Decision of the European Commission dated 19 March 2004, Best Agrifund/ Nordfleisch, case number M. 3337, paragraph 24.

22. The purchasing market for young calves is at least national in scope. The notifying parties argued that the transport of the baby calves may even reach 2,000 kilometres. However, such long transport distances require intermediate stops and additional care facilities for the animals and the market investigation could not confirm that such long-distance trade provides an effective constraint on local purchasing. For the purposes of this decision, the exact geographic market definition may, in any case, be left open.

(iv) Fattening of calves

23. Similarly, the geographic scope of the market for the fattening of calves is linked to the viable transport distance and can be left open, as no competition concerns arise even under a national market definition. The parties argue for European-wide markets, as several players are present in more countries and are dealing with different races of calves that may cover diverse consumer preferences.

(v) Trading of fattened calves

24. Concerning the market for the trade of fatted calves, the investigation did not provide conclusive evidence about the geographic scope of the market. Certain replies suggested that the trading market may be regional (cross-border) or European in scope; meanwhile, the existence of national markets or smaller regional markets could not be excluded either. Since under no circumstances the proposed transaction will give rise to competition concerns, the market definition can be left open.

(vi) Slaughtering of fatted calves

25. Similarly, the market investigation produced no conclusive evidence as to the geographic scope of the slaughtering market. The markets may be regional in scope, however, for smaller slaughterhouses the radius within which they are accessible may be smaller than national. Although the notifying parties argued for regional markets including Benelux, France, Northern Italy and Germany, for the purposes of the present investigation the geographical scope of the market may be left open as the parties slaughtering activities do not overlap on a national or smaller than national basis.

(vii) Sale of veal to wholesalers

26. With regard to the markets of sale of veal to wholesalers, the geographic scope of the market may be EU-wide, however some customers underlined the presence of national preferences. For the purposes of the present transaction the market definition can be left open due to the lack of competition concerns even on a national basis.

(viii) Sale of veal to industrial processors

27. Likewise, the geographic market scope of the market for sale of veal to industrial processors, the retail of veal, the sale of veal to caterers and sale of processed veal will be left open too, as no competition concerns arise under any possible geographic market definition.

D. Competitive assessment

28. Van Drie already today is the largest player in an otherwise fragmented market. This position will be reinforced by the notified transaction. Due to the complementarity of the parties' operations, the acquisition will enlarge Van Drie's geographic footprint across the main veal producing countries in Europe (France, the Netherlands, Italy, Belgium, Germany), and it will also strengthen the group's level of vertical integration. Van Drie/ Schils will account for nearly [10-20%] of slaughtered calves in the EEA[5] and it will supply up to one-third of calf milk replacer volumes[6] to non-integrated veal producers. Most of the remaining competitors have production facilities only in one single country and their market shares at the European level are in the low single-digit percentage range.

29. A number of respondents to the Commission's market investigation raised concerns that smaller competitors and, particularly, independent farmers and small slaughterhouses, will find it increasingly difficult to compete against such a large, vertically-integrated group. It was argued that the parties' presence along the entire value chain enabled them to influence market prices by strategically withholding or releasing large quantities from/ into the market. The Commission's market investigation has confirmed the parties' powerful presence (relative to the fragmented competition) along the value chain. However, while the various vertical links may reinforce the horizontal effects of the notified transaction, the parties' combined market share in the markets identified above does not yet give rise to concerns that effective competition may be significantly impeded. The Commission has investigated, in particular, the calf milk replacer market, where Van Drie/ Schils' combined share is high and the merger's horizontal effects may be compounded by the fact that the parties also supply competitors who use it as an input to their veal production chain.

<u>(i) Whey powder and skimmed milk powder</u>

30. No affected market arises at the EEA level, as the parties' combined market shares is below [0-10%]. On a national basis, the parties would have [20-30%] and [20-30%] of hypothetical Dutch markets for whey powder and skimmed milk, respectively. In all remaining Member States the parties' activities do either not overlap or market shares remain below [0-10%].

<u>(ii) Calf milk replacer</u>

31. The calf milk replacer market (approximately 1.6 million tons EEA market volume in 2003) has to be considered as one of the most important input markets for the calf fatteners. It constitutes the main feed and a major cost item in fattening calves. A significant share of calf milk replacer is produced by integrated groups who use it captively, but also supply non-integrated calf fatteners. Dairies form another important group of suppliers of calf milk replacer to non-integrated farmers as they have no downstream veal operations. Skimmed milk powder and whey powder are the main

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[5] according to the parties' data

[6] according to the Commission's investigation

ingredients of calf milk replacer and they account for a significant share of the ingredient costs.[7]

32. According to the parties' figures, the combined entity would reach a market share of [30-40%] of total European calf milk replacer production (Van Drie [10-20%], Schils [10-20%]). The total market estimate is based on industry association statistics, which do not distinguish between captive production and quantities sold to third parties. Citing internal estimates, the notifying parties submit that on the merchant market (i.e. excluding captive production) their combined market would only be approximately [20-30%]. The parties arrived at their estimate by subtracting from the total market those quantities that are, in their view, used captively by integrated competitors. They also submitted to the Commission a list of companies who they considered to be active on the merchant market along with a rough estimate of potential quantities supplied by each competitor.

33. The Commission has been able only partially to confirm these estimates by the parties. Based on replies by most of the major vertically-integrated companies and a partial survey of smaller suppliers and dairy companies, it appears likely that the parties' share of the merchant market for calf milk replacer is higher than [20-30%], but is likely to be lower than [30-40%]. No other player is likely to have more than [0-10%] of the merchant market and a large number of small suppliers with market shares in the low single-digit range exist. These companies, which typically supply between 10.000 and 30.000 tonnes to the merchant market, are nevertheless active internationally within the EU. By contrast, a number of very small manufacturers with less than 5.000 tonnes annual sales listed by the parties are unlikely to act as credible competitors in a wider market. The market investigation confirmed that significant spare capacity exists in the market. Access to new customers, rather than capacity constraints, appears to be the main barrier for most non-integrated competitors to increase output.

34. As mentioned above, skimmed milk powder and whey powder are the main ingredients for calf milk replacer and account for the bulk of the production costs. Together with other ingredients, such as various fats, vitamins etc., they account for approximately […]% of the average sales price of calf milk replacer.[8] The value-added at the calf milk replacer level of the production chain, therefore, is relatively low and the sales price is, consequently, driven largely by the price of the ingredients. The prevailing prices for skimmed milk powder and whey powder are widely known, and the prices for calf milk replacer appear to track closely the input prices.

35. In the absence of a strong position in the upstream input markets, such as those for skimmed milk powder or whey powder and in the presence of spare capacity, the parties combined market share in the market for calf milk replacer, therefore, does not raise serious doubts with respect to a potential impediment to effective competition.

<u>(iii) Purchase of young calves</u>

36. On the market for purchase of young calves, with the exception of the Netherlands ([20-30]%) the parties' combined market share post-merger will stay below [10-20]%

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[7] up to approx. […]% for a 50% skimmed milk product, according to accounting data supplied by the parties.

[8] i.e. the gross margin before sales, marketing, logistics and administrative costs is approximately […]%.

in each Member State, as well as at EU level ([0-10]%). The increment on a national Dutch market would be less than [0-10]%.

(iv) Fattening of calves

37. Similarly, in fattening, the parties' mainly fatten their calves under contracts or buy them externally from third parties. The volumes of fattened calves that parties assemble are below [10-20]% on both national and EU markets with the exception of Belgium and the Netherlands, where the parties' market shares reach [30-40]% and [20-30]% respectively. In Belgium parties' face the competition of the integrated groups Vilatca/ Lornoy and Van Lommel, whose market shares were about the same size, ranging between [20-30]%. In the Netherlands, the structure of the market will not change substantially; the increment in parties' market share is de minimis ([0-10]%).

(v) Trading of fattened calves

38. Concerning the trading markets for fatted calves, high market shares would arise only if the markets are considered to be national in scope, however the competitive overlap is minimal on this basis. Post merger, the parties' market share in Belgium and in Germany would reach respectively [30-40]% and [30-40]%. However for both markets the increment is only 1%. In addition to that, in both countries the closest competitors, Van Lommel and Vilatca in Belgium and Brünninghoff and Bahlmann in Germany have similar market shares in trading. Considering regional markets (comprising the Benelux, France, Germany and Northern Italy) the parties' combined market share would remain below [0-10]%. Assuming that this regional market does not include Northern Italy, parties' share would remain below [0-10]%.

(vi) Slaughtering of fatted calves

39. On an EU market for the slaughter of fatted calves, Van Drie/ Schils' combined market share would be [10-20]% with an increment of only [0-10]%. On a wider regional market including the Benelux, Germany, France and Northern Italy, the parties' combined market share would amount to approximately [20-30]%. Excluding Northern Italy from this hypothetical market, the parties would have market shares not higher than [20-30]%, and the increment would remain below [0-10]%. Finally, considering national markets for slaughtering, there are no overlaps between Van Drie and Schils.

(vii) Sale of veal to wholesalers

40. On the veal markets, mostly the vertically integrated groups are competing with the parties. On an EU-wide market, the parties' combined market share would be [20-30]% and the increment [0-10]%. The market shares of the competitors would range from [0-10]% to [0-10]% on the EU level. These companies e.g. ESA (Alpuro group), Tendriade Collet, Vitelco, Van Lommel and some smaller players (Brünninghoff and Bahlmann) can be considered as the parties' closest competitors. The small increment in the market share of the merging parties would also indicate that the structure of the market would not change significantly.

41. Based on a national market definition, the parties increment will be below [0-10]% in Germany, Italy, France and the Netherlands. The highest market shares ([40-50]%) will be reached in the Netherlands, In Belgium, the combined entity would have [30-40]% share ([0-10]% increment).

42. Assessing parties' market position, the Commission has considered that the competitors are much closer followers of the merging parties on the veal markets . The two strongest competitors in almost all countries would have similar shares than parties combined market share (e.g. in the Netherlands: ESA ([10-20]%) and Vitelco ([10-20]%)). Also, mainly veal customers indicated that the merger will cause a limited change or no change at all on these markets. Moreover, even if the Netherlands and Belgium, were considered to constitute separate relevant markets, potential entry from neighbouring countries, such as France and Germany would be an important constraining factor for domestic competitors.

(viii) Sale of veal to industrial processors and other customers

43. For the remaining veal markets no affected markets arise, except for a hypothetical market for the sale of veal to industrial processors at EU level, where the parties' combined market share is [10-20]% with a minimal increment ([0-10]%).

VI. CONCLUSION

44. 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 (EC) No 139/2004.

For the Commission

signed
Neelie KROES
Member of the Commission