



EUROPEAN COMMISSION
DG Competition

***Case M.8096 - INTERNATIONAL PAPER COMPANY /
WEYERHAEUSER TARGET BUSINESS***

Only the English text is available and authentic.

**REGULATION (EC) No 139/2004
MERGER PROCEDURE**

Article 6(1)(b) NON-OPPOSITION
Date: 20/10/2016

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EUROPEAN COMMISSION

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In the published version of this decision, some information has been omitted pursuant to Article 17(2) of Council Regulation (EC) No 139/2004 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 Where possible the information omitted has been replaced by ranges of figures or a general description.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

To the Notifying Party

Dear Sir/Madam,

Subject: Case M.8096 – International Paper Company / Weyerhaeuser Target Business
Commission decision pursuant to Article 6(1)(b) of Council Regulation No 139/2004¹ and Article 57 of the Agreement on the European Economic Area²

(1) On 15 September 2016, the European Commission received notification of a proposed concentration pursuant to Article 4 of the Merger Regulation by which International Paper Company ("IP", United States) will acquire sole control over the pulp business of Weyerhaeuser Company ("WTB", United States) within the meaning of Article 3(1)(b) of the Merger Regulation, by way of purchase of assets and shares (hereafter the "Transaction"). IP are designated hereinafter as the 'Notifying Party' and together with WTB 'Parties' to the proposed transaction.

1. THE PARTIES

(2) **IP** is a packaging and paper company with manufacturing operations in North America, the EEA, Latin America, Russia, Asia and North Africa. Its portfolio includes the production of containerboard and corrugated boxes, pulp, consumer packaging (carton board), cups and white paper.

(3) **WTB** consists of the Weyerhaeuser Group's cellulose fibers (pulp) business. It comprises all the group's shares in Weyerhaeuser Poland Sp.zo.o. and all the real

¹ OJ L 24, 29.1.2004, p. 1 (the 'Merger Regulation'). With effect from 1 December 2009, the Treaty on the Functioning of the European Union ('TFEU') has introduced certain changes, such as the replacement of 'Community' by 'Union' and 'common market' by 'internal market'. The terminology of the TFEU will be used throughout this decision.

² OJ L 1, 3.1.1994, p. 3 (the 'EEA Agreement').

estate properties, assets, goodwill and rights that relate primarily to the manufacture and distribution of fluff pulp, softwood paper grade pulp and specialty chemical cellulose pulp currently owned by Weyerhaeuser Company ("WY"). WTB in particular includes five mills located in North America, and two converting facilities, one located in the United States (Columbus, Mississippi) and one in Poland (Gdansk).

2. THE OPERATION AND THE CONCENTRATION

- (4) The "Transaction" consists in the acquisition by IP of all the relevant assets and shares currently held by WY as cellulose fibers (pulp) business, which will be separately held by IP as WTB.
- (5) As a result of the Transaction, IP will, directly or indirectly, own all shares in Weyerhaeuser Poland Sp.zo.o, all shares of Weyerhaeuser Sales Europe, Inc. and all assets belonging to WTB as well as all assets composing five mills located in North America, and two converting facilities, one located in the United States (Columbus, Mississippi) and one in Poland (Gdansk).
- (6) As a result of the Transaction, IP will acquire sole control over WTB, and therefore, the notified operation constitutes a concentration within the meaning of Article 3(1)(b) of the Merger Regulation.

3. EU DIMENSION

- (7) The undertakings concerned have a combined aggregate world-wide turnover of more than EUR 5 000 million³ (IP: EUR [...] million; WTB: EUR [...] million). Each of them has an EU-wide turnover in excess of EUR 250 million (IP: EUR [...] million; WTB: EUR [...] million), but they do not achieve more than two-thirds of their aggregate EU-wide turnover within one and the same Member State. The notified operation therefore has an EU dimension within the meaning of Article 1(2) of the Merger Regulation.

4. COMPETITIVE ASSESSMENT

4.1. Market definition

- (8) The Parties' activities mainly overlap in the production and sale of fluff pulp. Fluff pulp is a type of bleached wood pulp made through a chemical process, generally from long fibre softwoods, such as pine. Due to its high absorbency and relatively low cost, fluff is used as raw material to produce the absorbent core of personal hygiene products such as adult and baby/toddler diapers (nappies) and feminine hygiene products (sanitary napkins/pads, tampons) and to manufacture airlaid absorbent toweling or wipes.
- (9) The production process of fluff pulp consists of the following steps. First, wood chips and side cuttings or other waste from sawmills are soaked and heated/cooked using an aqueous chemical solution. This process (known as the Kraft process) results in the separation of cellulose fibre from the wood by dissolving the lignin

³ Turnover calculated in accordance with Article 5 of the Merger Regulation.

that binds the fibres together. Second, the cooked wood chips are cleaned with the pulp being separated mechanically from large shives (pulp that is not fully cooked), knots and dirt (so-called screening). After screening, the pulp is washed to separate the cellulose fibres from the chemical solution used to cook the wood chips. Third, the pulp is bleached and, usually, screened once more. The pulp is then dried and packaged. The production processes for fluff and other chemical pulp differ primarily at this last stage of the production process. Most chemical pulp [confidential information regarding use by the Parties] is “market pulp” that is dried to about 10% moisture content and delivered as sheeted bales. Market pulp is generally used in the production of paper and tissue products. Fluff is dried to only about 6-10% moisture content and shipped on rolls.

- (10) Fluff is generally produced from southern pine wood, in particular the loblolly, longleaf, Slash and Virginia pine varieties that are grown primarily in the south-eastern part of the United States. With their long, coarse fibres, southern pines have both the absorbency and the strength required for use in personal hygiene products. Fluff produced from southern softwood in the United States currently accounts for approximately 90% of fluff production worldwide, with United States suppliers exporting approximately 85% of their production outside the United States. A minor proportion of fluff is also produced in South America (mainly Brazil and Argentina) and in northern Europe, this latter production using a different variety of wood as input (northern softwood).

4.1.1. Product market definition

- (11) In most of its past decisions concerning the wood pulp sector, the Commission has taken the view that there is a single product market encompassing all types of pulp.⁴ The Commission has explored different ways of segmenting the market, depending on (i) the type of wood used (softwood/hardwood); (ii) whether the pulp is bleached; and (iii) whether chemical or mechanical processing is used to produce the pulp. However, in almost all of its past decisions the Commission has concluded that there was no need to segment the market further along these lines.⁵ The overall market considered is thus the wood pulp market.
- (12) On the overall worldwide wood pulp market, the Transaction would lead to a combined market share of the Parties of [0-5]%.
- (13) With regard to a potential segmentation between chemical and mechanical pulp, the Parties are only active in the chemical pulp segment and do not produce

⁴ Commission, decision of 24.02.1992, IV/M.166 – Torras/Sarrio, para. 9; Commission, decision of 12.05.1992, IV/M.210 – Mondi/Frantschach, para. 12; Commission, decision of 30.10.1995, IV/M.646 – Repola/Kymmene, para. 30; Commission, decision of 09.12.1998, IV/M.1356 – Metsä-Serla/UK Paper, para. 11; Commission, decision of 15.02.2000, Commission, decision of 22.12.2000; Commission, decision of 16.02.2005; Commission, decision of 19.12.2005, COMP/M.4054 – Koch Industries/Georgia-Pacific, para. 9; Commission, decision of 28.07.2008, COMP/M.5150 – UPM RUS/BRIST/JV, para. 23.

⁵ See Commission decisions: IV/M.210 – Mondi/Frantschach, para. 11-12; IV/ M.1356 – Metsä-Serla/UK Paper, para. 11; COMP/M.2245 – Metsä-Serla/Zanders, para. 16; COMP/M.6682 – Kinnevik/Billerud/Korsnäs, para. 65.

mechanical pulp. Within the chemical pulp market, the Parties activities overlap on two segments, mainly market pulp and fluff pulp.⁶

4.1.1.1. Market pulp

- (14) The type of chemical pulp that is produced the most is market pulp, and approximately 90% of the total wood pulp produced consists of market pulp. This is delivered as sheeted bales and is generally used in the production of paper and tissue products.
- (15) The Notifying Party claims that market pulp can be regarded as a separate product market and that there is no demand-side substitutability with other types of wood pulp, especially with fluff pulp.
- (16) Notwithstanding the high degree of supply side substitutability, the Notifying Party claims that from a demand side market pulp and other types of pulp, including fluff pulp cannot be considered as substitutes. The Notifying Party submits that this is because, first of the significant price differences between particularly market pulp and fluff pulp and, second because market pulp and fluff pulp serve fundamentally different purposes. Therefore there is little overlap between the customer base for market pulp and the customer base for fluff pulp. Whereas fluff pulp is sold mainly to producers of absorbent personal hygiene and airlaid products, market pulp is sold to paper, tissue and towel producers that do not have sufficient integrated pulp production.
- (17) From a supply side analysis, it appears, in fact, that the production process of fluff pulp and market pulp is very similar and for the most part virtually identical, the difference only being at the last stage. Market pulp is typically dried to about 10% moisture content and is delivered in sheeted bales, while fluff pulp is dried to only about 6-10% delivered and shipped on rolls. Most importantly fluff pulp and market pulp can be manufactured on the same production assets.
- (18) Hence, if a production line is equipped properly, a pulp producer can easily decide to shift its market pulp production to fluff pulp (and vice versa) at minimal cost and in minimal time (so called "swing" production). Swings in production already occur on the market place and manufacturers generally perform these swings in order to follow the punctual demands of their clients.
- (19) The Commission notes that the market investigation supports the Notifying Party's view that market pulp and fluff pulp constitute distinct markets. However, both competitors and customers indicated that market pulp and fluff pulp have different moisture content and need to be delivered in different formats. Market pulp in fact generally has higher moisture contents, around 10%, and is delivered in in sheeted bales whereas fluff pulp has a moisture content of less than 10% (often around 6%) and is delivered in rolls. In conclusion, as to the supply side market analysis, it can be left open whether fluff pulp and market pulp are substitutable as the Transaction does not give rise to serious doubts even under the narrowest plausible market definition.

⁶ For the purposes of this decision the term "market pulp" refers to chemical pulp other than fluff pulp that is sold on the open market.

- (20) As to the demand side, the Commission notes that the respondents to the market investigation indicated that the intended use and customer base of market pulp differs significantly from those of fluff pulp. The market investigation in fact indicated that fluff pulp is a niche product that is only used in the personal hygiene business, whereas market pulp is used for paper and tissue.
- (21) In any case, for the purpose of this decision, the Commission considers that the exact scope of the product market definition can be left open, as the Transaction does not give rise to serious doubts even under the narrowest plausible market definition.
- (22) The Parties only sell small amounts of market pulp to paper, tissue and towel producers as [confidential information regarding use by the Parties].⁷ The Parties' sales of market pulp on the market are minimal and their estimated market share in volume on this plausible product market is [5-10]% globally and [0-5]% in the EEA. Therefore, the question of whether or not market pulp constitutes a distinct product market will not be further considered in the competitive assessment below.

4.1.1.2. Fluff pulp

- (23) As explained above in paragraph 9, fluff pulp is a type of bleached wood pulp made through a chemical process, generally from long fiber softwoods such as pine. Due to its high absorbency and relatively low cost, fluff pulp is used as a raw material to produce the absorbent core of personal hygiene products. The end use of fluff pulp is disposable absorbent hygiene products such as disposable baby diapers, feminine hygiene pads, adult incontinence products and airlaid nonwovens such as medical specialties and wipes.
- (24) Fluff pulp can be produced using different kind of tree-woods as input. Such inputs can be treated with a debonding agent during the production process in order to make it easier to work with in the customer's production line ("treated", "semi-treated" or "debonded" fluff pulp).⁸ Also, an array of different properties can be added to the fluff pulp, creating a so called "differentiated fluff".
- (25) The Notifying Party submits that the relevant product market encompasses all types of fluff and that it is not appropriate to further segment it.
- (26) As regards a potential sub-segmentation of fluff pulp, the Commission understands that the respondents to the market investigation indicated that treated and untreated fluff pulp are not entirely substitutable on the demand side, whereas they are from a supply side.

⁷ IP is a vertically integrated paper producer that uses internally the bulk of the pulp it produces for paper production. IP sells only limited amounts of market pulp produced [confidential information regarding use by the Parties]. WTB operates one non-integrated pulp mill in Canada that produces market pulp. WTB does not produce any paper as it produces liquid packaging board and (separately) printing paper and newsprint through a joint venture with Nippon Paper. However, it has announced the sale of this business to Nippon, http://tdn.com/news/local/weyerhaeuser-to-sell-longview-liquid-packaging-plant-to-nippon/article_cd2a04fd-2bf0-592d-b47f-5238acff0d6d.html

⁸ Such fluff pulp is referred to as "debonded" by WTB and as "treated" (50% debonded) or "semi-treated" (10% debonded) by IP. RISI does not distinguish between these different types of fluff pulp, but treats the fluff pulp market as a single market.

- (27) With regard to the demand side, the Commission considers from the market investigation that customers cannot generally use treated and untreated fluff pulp interchangeably in their production process. Respondents to the market investigation indicated that on the one side, untreated fluff pulp has a higher tensile strength and therefore it cannot be used on every production line. Secondly, respondents to the market investigation indicated that the chemical process applied to treated (or semi-treated) pulp caused the end product to have lower absorbency characteristics and therefore cannot be used in the manufacturing of the same end products. Typically producers of airlaid products would use exclusively treated fluff pulp.
- (28) The Commission notes that one competitor has, however, indicated that most customers use treated and untreated fluff pulp interchangeably in their production process without incurring significant costs and within a short timeframe. Furthermore, certain customers in developing economic areas may choose to use treated pulp because their machines are not able to process untreated pulp as quickly.
- (29) As regards the supply side, the Commission understands that the majority of manufacturers of untreated fluff pulp can easily produce semi-treated or treated fluff pulp. Indeed, respondent to the market investigation indicated that "the same assets can be used for the untreated, semi-treated and treated fluff pulp" and that switching only requires the addition of a chemical debonder at a certain stage of the production process.
- (30) The Commission considers that the respondents have also indicated that switching between untreated and treated fluff pulp can be made within a short timeframe and without incurring in any significant cost. One competitor responding to the market investigation indicated that "we can produce both untreated and treated fluff pulp in our production. Generally the cost of treated is somewhat higher, but the switch can be done within a short timeframe in our production" and another one indicated that switching production from fluff pulp to treated or semi treated pulp can happen in a matter of hours.
- (31) Both customers and competitors agreed that the vast majority of the fluff pulp market is comprised of untreated fluff pulp.
- (32) In view of the above and for the purpose of this decision, the Commission considers that, in any case, the exact scope of the product market definition can be left open, as the Transaction does not give rise to serious doubts even under the narrowest plausible market definition.

The Commission moreover stresses that IP only started selling treated fluff pulp in 2016 and has therefore [confidential information regarding IP's market share for treated fluff].⁹ Untreated fluff pulp accounts for 80 to 90% of the whole production of fluff pulp, and the Commission considers that the market for untreated fluff pulp should therefore be considered as the narrowest plausible market, which is accordingly further considered in the competitive assessment below.

⁹ IP has currently not sold more than [...] MT of treated fluff pulp.

Differentiated fluff pulp

- (33) The Commission understands that customer demand for thinner and lighter products, as well as for products with additional features such as odour control, is growing. In this respect, fluff pulp manufacturers have introduced modifications to their production processes so as to allow them to respond to specific customer requirements. Fluff pulp with such added properties is typically designated as "differentiated fluff pulp".
- (34) The Commission understands that fluff pulp producers do differentiate the products they sell and can accordingly add specific values to their productions differentiating them from an otherwise rather standardised production. WTB has for example developed [confidential information related to the Parties' know-how], and both WTB and Georgia-Pacific produce fluff pulp with odour reduction features.
- (35) The Notifying Party claims that differentiated fluff pulp is part of the same product market of fluff pulp. The Notifying Party claims that this is because differentiated fluff pulp and untreated fluff pulp are perfectly substitutable from both a supply and demand side. As to the supply side, differentiated fluff pulp is manufactured on the same production lines as untreated and treated or semi-treated fluff pulp. As to the demand side untreated and differentiated fluff are used for the same applications and this is evidenced by the fact that the customer base is the same.
- (36) As to the demand side substitutability, the Commission has taken note that the respondents to the market investigation have indicated that differentiated fluff pulp has specific value added properties which are specific to the end product the customer intends to manufacture and sell. However, a switch from using differentiated fluff pulp to using normal fluff pulp can be performed. Such a switch would however require a considerable time and investment to be performed.
- (37) As to the supply side, the Commission notes that the responses to the market investigation were partially inconclusive as to whether differentiated fluff pulp is substitutable with normal fluff pulp. The largest manufacturers of fluff pulp indicated that in fact switching production is not costly, can be performed within a limited time frame and without a need to change production assets. Other market participants with limited market presence indicated that starting production of differentiated pulp is indeed possible but would require some investment as regards the chemical formulation to be used.
- (38) In that respect, for the purpose of this decision, the Commission considers that the exact scope of the product market definition can in any case be left open, as the Transaction does not give rise to serious doubts even under the narrowest possible market definition.
- (39) In fact, the Commission understands that IP only has very limited preparatory activities with regard to differentiated fluff pulp [confidential information related to the Parties' marketing plans]. Differentiated fluff pulp will therefore not be further considered in the competitive assessment below.

*SBSK and NBSK*¹⁰

- (40) From the information provided, the Commission understands that most fluff pulp is produced from softwood from the south-eastern part of the United States. Additionally, southern softwoods grown outside the United States (for example in Brazil and Argentina) and northern softwoods (for example from Northern Europe) are used for the production of fluff pulp. Northern Bleached Softwood fluff pulp ("NBSK fluff pulp") has very similar product characteristics as Southern Bleached Softwood Kraft fluff pulp ("SBSK fluff pulp"), with northern softwood fluff pulp being somewhat less absorbent.
- (41) The Notifying Party claims that fluff pulp from southern softwood and northern softwood are part of the same market as customers in the EEA use southern softwood and northern softwood fluff pulp interchangeably because they have comparable characteristics.
- (42) Moreover, RISI¹¹ does not distinguish between fluff pulp produced either from southern and northern softwoods, but describes BSK fluff pulp as one fluff pulp grade; including fluff pulp produced both from southern and northern softwoods.¹²
- (43) The market investigation broadly supported the Notifying Party's views and indicated that most market players indeed consider fluff pulp or market pulp from either southern or northern pines as interchangeable. Competitors and customers confirmed that despite the fact that the northern and southern fibres each have their own characteristics in terms of length, absorption capacity etc., they are comparable as regards their application and performance, and are often both used by customers.
- (44) Also, the greater majority of suppliers are using southern softwood pines in their production process, so that only a small share of the total fluff pulp supply is made up by NBSK fluff pulp, amounting to circa 5% of the total fluff production. Reaching a definitive conclusion as to whether fluff pulp from NBSK and fluff pulp from SBSK are part of the same market does not substantially change the competitive assessment.
- (45) In light of the foregoing, for the purpose of this decision, the Commission considers that the exact scope of the product market definition can be left open, as the Transaction does not give rise to serious doubts even under the narrowest plausible market definition.

*BEK*¹³

- (46) From the data provided, the Commission understands that BEK is fluff pulp using Eucalyptus trees as raw material. Eucalyptus is a hardwood tree (as opposed to the

10 SBSK stands for "Southern Bleached Softwood Kraft" and NBSK for "Northern Bleached Softwood Kraft". SBSK and NBSK are used for the production of both fluff pulp and market pulp.

11 RISI is a leading information services provider for the forestry products industry. RISI publishes a biannual report on the worldwide fluff pulp market that sets out demand and production capacity figures by volume and by region.

12 RISI, Outlook for the World Fluff Pulp Market, Special Market Analysis Study, 2016, 1.

13 BEK stands for "Bleached Eucalyptus Kraft".

softwood trees) that grows very quickly compared to northern and southern softwoods. However, hardwood fibres usually do not absorb liquid as well as softwood fibres.

- (47) The Notifying Party argues that fluff pulp from BEK is part of the same market as fluff pulp from other raw materials. The Notifying Party acknowledges that fluff pulp from BEK is in itself less absorbent and resistant than fluff pulp from softwood pines, however it claims that it can be used in combination with the latter and achieve similar absorption and resistance properties. Therefore, the Notifying Party claims that fluff pulp from BEK and fluff pulp from other softwood pines are substitutable from a demand side.
- (48) The Commission draws from the results of the market investigation that BEK fluff pulp and the other types of fluff pulp are not interchangeable. Both customers and competitors confirmed that BEK fluff pulp is a distinct product from BSK fluff pulp, as it is less flexible, less absorbent and less distributive than fluff pulp. Respondents to the market investigation also indicated that in order to ensure that the end product is sufficiently absorbent, BEK fluff pulp would have to be used in a blend with BSK fluff pulp; products could not be entirely made out of BEK.
- (49) In conclusion the Commission considers that, whether BEK fluff pulp belongs to the same product market as fluff pulp, can in any case be left open as none of the parties manufactures BEK fluff pulp and fluff pulp from BEK represent only a marginal proportion of the global production of fluff pulp, accounting for less than 0.1% of total production.¹⁴ The Commission concludes that the competitive assessment would therefore not materially change under either alternative market definition. The market for untreated fluff pulp is therefore the narrowest affected market considered in the competitive assessment below.

SAP

- (50) From the information available, the Commission understands that, when manufacturing diapers and feminine hygiene products, the fibres are often combined with super absorbent polymer ("SAP"), a synthetic, granular substance that is made from petroleum products and can absorb approximately 3-5 times as much fluid as fluff pulp. Personal hygiene products manufactured from a blend of SAP and fluff pulp can be significantly thinner, lower in weight and more absorbent than those manufactured from fluff pulp alone, as SAP is significantly smaller and less bulky than fluff pulp and expands less when absorbing fluid.
- (51) The Notifying Party argues that SAP exerts competitive pressure on fluff pulp since there is a high degree of demand side substitutability, but believes that SAP and fluff pulp are not interchangeable given that there is likely to be residual demand for fluff pulp for different uses than SAP.
- (52) In any case, as the parties do not produce SAP, the Commission does not consider it necessary or relevant to establish whether SAP and fluff pulp belong to the same product market or not.

¹⁴ See RISI, Outlook for the World Fluff Pulp Market, Special Market Analysis Study, 2016, 13.

4.1.2. *Geographic Market*

- (53) In previous decisions concerning pulp markets, the Commission considered these markets to be at least EEA-wide.
- (54) The Notifying Party considers that the fluff pulp market is worldwide in scope because US-based suppliers export about 85% of their fluff pulp production and supply approximately 75-80% of fluff pulp demand in the EEA. Customers from all over the world source fluff pulp from producers located both inside and outside the EEA. In addition, many fluff pulp customers procure fluff pulp for their global operations based on global group-wide purchasing agreements.
- (55) The Commission understands from the market investigation that the market for fluff pulp is likely worldwide in scope and at least EEA-wide. Both competitors and customers indicated that the competition for fluff pulp sales within the United States is mainly limited to the producers residing in the United States itself given that import into the United States is limited, but that elsewhere competition is global given that customers are located all over the world.
- (56) In light of the above, the Commission considers that the exact geographic market definition can in any case be left open since the Transaction does not give rise to serious doubts under any alternative geographic market definitions considered.

4.2. **Competitive assessment**

4.2.1. *Horizontal, non-coordinated effects*

- (57) The Commission finds that the Parties' activities horizontally overlap on the worldwide (or at least EEA-wide market) for fluff pulp,¹⁵ and there are no vertically affected markets resulting from the Transaction.
- (58) The Commission also finds that as the sales of untreated fluff pulp account for circa 90% of the total sales of fluff pulp and the Notifying Party confirmed that the market structure in any plausible market is comparable to that of the market for untreated fluff pulp, it is appropriate that only the latter, and not the broader market encompassing all different types of fluff pulp, are further considered in the competitive assessment below.

4.2.1.1. *Competitive landscape*

- (59) The Commission understands that, on the worldwide market for untreated fluff pulp, the Parties will have a capacity share of [30-40]%, and will continue to face competition from Georgia-Pacific with comparable capacity share ([30-40]%) as

¹⁵ Both Parties produce also "black liquor derivatives" which are chemical compounds extracted from black liquor, which is the waste product from the Kraft process. Generally, there are three types of derivatives: (i) crude tall oil (a soap that has been treated with acidic compounds found in pine trees), (ii) black liquor soap (a mixture of mainly acidic compounds found in pine trees) and (iii) crude sulphate turpentine (mainly used as a solvent). WTB sells tall oil soap and turpentine, but not tall oil, while IP does not sell any of these derivatives on the market. Indeed, IP [confidential information on IP's activity in black liquor derivatives]. The Commission therefore considers that the Parties' activities do not overlap as regards black liquor derivatives.

well as competition from smaller competitors, such as Domtar, Resolute Forest Products and WestRock in the United States and Stora Enso and UPM in the EEA.

Company	Capacity share (2016)¹⁶
WTB	[20-30]%
International Paper	[10-20]%
COMBINED	[30-40]%
Georgia-Pacific	[30-40]%
Domtar	[5-10]%
Resolute Forest Products	[0-5]%
Stora Enso	[0-5]%
West Rock	[0-5]%
All other¹⁷	[10-20]%

Table 1: Estimates of market shares for 2016 on the fluff pulp market

- (60) In this respect, the Commission notes that, should the market for fluff pulp be defined as EEA-wide, the capacity share would not be an appropriate proxy to take into account as the largest majority of production assets are located in North America. Hence, the Notifying Party provided the following best estimates of market share in value for the EEA-wide market for fluff pulp

Company	Market share – Value (2015)¹⁸
WTB	[10-20]%
International Paper	[20-30]%
COMBINED	[30-40]%
Georgia-Pacific	[20-30]%
Domtar	[10-20]%
Resolute Forest Products	[0-5]%
Stora Enso	[10-20]%
UPM	[5-10]%
All other¹⁹	[5-10]%

Table 2: Estimates of market shares for 2015 on the EEA-wide fluff pulp market

- (61) Notwithstanding the significant capacity share of the combined entity and the concentrated structure of the market, the Commission ultimately considers that the Transaction does not raise serious doubts as to its compatibility with the internal market as a result of horizontal non-coordinated effects because, first, a number of market participants have already announced additional investments to increase their respective production capacities, second, customers can easily switch suppliers, and, third, margins realized on the sale of fluff pulp are significantly higher than margins realized for the sale of market pulp, so that it will be improbable for the merged entity to reduce output of fluff pulp by swinging production from fluff pulp to market pulp, and that additional investments in fluff pulp production are therefore more likely to occur.

¹⁶ RISI, Outlook for the World Fluff Pulp Market, Special Market Analysis Study, 2016, p. 79.

¹⁷ Others includes Stora Enso; Arauco; Klabin; Fujian Tengrongda; Rayonier; Suzano; and WestRock.

¹⁸ Best estimate of the Notifying Party.

¹⁹ Others includes Stora Enso; Arauco; Klabin; Fujian Tengrongda; Rayonier; Suzano; and WestRock.

4.2.1.2. Production capacity for fluff pulp exceeds demand

- (62) The Commission considers that the capacity for fluff pulp production exceeds and will continue to exceed the current and future demand of customers of fluff pulp.
- (63) The Commission understands that fluff pulp is one of the very few products in the pulp and paper industry with a positive demand growth. According to public sources submitted by the Notifying Party demand for fluff pulp has grown steadily in the past years and is expected to increase further by 3-4% per year.²⁰
- (64) According to the Notifying Party, the main drivers for this growth are (i) an increased demand for disposable diapers and hygiene products in Asia, Central and South America and Africa and (ii) an increased demand for adult incontinence products globally, including in western countries and Japan.
- (65) The Commission also finds that the respondents to the market investigation broadly confirmed the Notifying Party's statement. All the competitors responding to the market investigation indicated that demand increased in the last 3 years and that they expect further increase in the next five years. Particularly, competitors responding to the market investigation on average confirmed that a yearly 4% increase in demand is to be expected.
- (66) The Commission takes note of the findings that, in reaction to the expected increase in demand of fluff pulp, several market participants have announced that they will significantly increase their total installed capacity in the near future. For example, in 2016, Klabin completed a new mill located in Ortigueira, Paraná, with an annual production capacity of inter alia 400 000 tons of bleached softwood pulp. As regards future capacity increase, several official announcements have been made:
- International Paper has announced that it plans to expand its fluff pulp production at its Riegelwood N.C. mill, adding an incremental 400 000 metric tons of capacity.
 - Domtar has announced a major investment at its Ashdown AR mill, to convert a paper machine to a fluff pulp line, allowing for an additional production of 516 000 metric tons of fluff pulp once the machine is in full operation.
 - Stora Enso will increase its fluff pulp production by approximately 160 000 metric tons annually.
- (67) More specifically, the Commission's findings as to the most recent and future increases of capacity resulting from expected setting up new fluff pulp mills are summarised in the table below:

²⁰ RISI estimates the global fluff pulp demand in 2015 was 5.8 million metric tons and that by 2020, global fluff pulp demand will be 6.9 million tons.

Company	Location	Country	Capacity (MT)	Expected start-up date	Type
Suzano	Suzano, São Paulo	Brazil	100 000	2015	Conversion
Klabin	Ortigueira, Paraná	Brazil	400 000	2015/2016	New build
International Paper	Riegelwood, North Carolina	US	350 000	2016	Conversion
Domtar	Ashdown, Arkansas	US	516 000	2016	Conversion
Stora Enso	Skutskär	Sweden	160 000	2018	Upgrade
Sun Paper²¹	Clark County, Arkansas	US	700 000	2019	New build

Table 3: Increased capacity of fluff pulp output; Source: Form CO

- (68) As a result of the planned increases, the additional capacity corresponding to an increase of 35% (by 2019) of the 2015 production capacity would only in a minor proportion (IP 350 000 Mt in Riegelwood) be owned by the Parties. As a result, the Commission expects that the combined capacity share of the Parties will significantly decrease in the foreseeable future and therefore competitors such as Domtar, Stora Enso and Sun Paper will significantly increase their market position.
- (69) Also, the Commission understands that there is current capacity that is not used for fluff pulp production at this time. Hence, if the current players on the market were to increase their utilization rates to 100 %, the Commission considers it likely that the currently unused capacity could be brought to the market as additional offer, in response to an increase of either demand or price. Hence, the Commission considers that, in this scenario, the Parties would likely also face potential competition from this capacity.
- (70) As to the current structure of supply, the Commission considers that respondents to the market investigation have reported that they have not experienced a capacity shortage on the fluff pulp market in the past years. Respondents to the market investigation also expect that production will exceed demand in the future. The expectation that capacity will exceed demand is also supported by public sources which foresee the following trend for demand and capacity of fluff pulp:

²¹ Full financing has not been announced for this project.

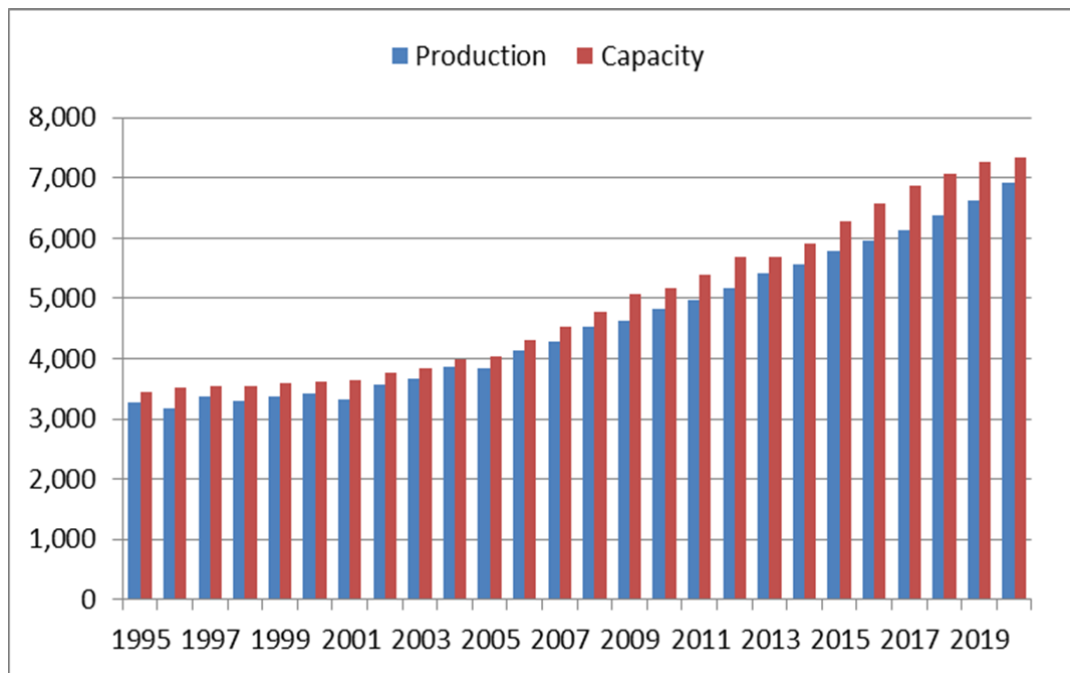


Table 4: evolution of demand and capacity (worldwide) Source: Notifying Party presentation based on RISI data

4.2.1.3. Switching and expansion

- (71) The Commission also notes that the market investigation indicated that customers can easily switch suppliers. Respondents to the market investigation, supporting the Notifying Party's claim, indicated that the largest part of supply contracts is based on short term contracts (generally yearly in duration) and generally concluded following a tender procedure. A customer responding to the market investigation also indicated that multi-sourcing is a common practice, so to mitigate non-performance risk. Therefore every time a contract comes to an end, the customer can appoint one or more new suppliers without incurring a significant cost.
- (72) Finally, the Commission expects that the Transaction will not allow the Parties to hinder the likely expansion of competitors. To the contrary, it is likely that the expected expansion of production capacity will occur on this market, driven by an expected steady grow in demand, making further expansion in competition foreseeable.

4.2.1.4. Incentives to reduce output in order to increase prices

- (73) Against the above background, the Commission takes the view that it is unlikely that the Parties will have the incentive to unilaterally reduce output of fluff pulp by shifting production to market pulp in order to increase prices. Such a strategy would not be economical, as margins realised by the Parties with regard to fluff pulp are higher than the margins realised with regard to market pulp.
- (74) The empirical evidence available shows that the average sale price of fluff pulp has been significantly higher than the average sale price of market pulp. Also, the average gross margin realised on the sales of fluff pulp is higher than the average gross margin realised on the sale of market pulp. More specifically, the Parties achieved the following margins:

	IP			WTB		
	<i>2013</i>	<i>2014</i>	<i>2015</i>	<i>2013</i>	<i>2014</i>	<i>2015</i>
FLUFF PULP	[...]	[...]	[...]	[...]	[...]	[...]
MARKET PULP	[...]	[...]	[...]	[...]	[...]	[...]

Table 5: profit margins of the Parties

(75) Therefore, the Commission takes the view that post-Transaction the merged entity does not have an incentive to unilaterally reduce the output of fluff pulp or increase prices.

4.2.1.5. Conclusion on horizontal non-coordinated effects

(76) For these reasons, the Commission takes the view that the Transaction does not raise serious doubts as to its compatibility with the internal market, with regard to horizontal, non-coordinated effects on the EEA-wide or worldwide market for fluff pulp.

4.2.2. *Horizontal Coordinated effects*

(77) The Notifying Party argues that the Transaction does not create any risk of coordination in the fluff pulp market as prices for fluff pulp are not transparent, fluff pulp sales are generally made to large sophisticated customers and, capacity on the fluff pulp market is increasing.

(78) More specifically the Notifying Party claims that, first, prices for fluff pulp are difficult to monitor as the vast majority of fluff pulp sales are made on the basis of individually negotiated contracts, and information about these contracts is kept confidential. The prices decided upon in these contracts are not basic list prices, but unique negotiated prices that vary per contract. In this respect, the RISI list price is an indication and discounts are then negotiated with the customers. More generally, the Notifying Party submits that the fluff pulp market is not very transparent, as the prices agreed upon in contracts are not reported to RISI.

(79) The Commission takes the view that it is unlikely that the Transaction will lead to any coordinated effect because (i) monitoring deviations in terms of quantities produced and prices is unlikely if not impossible, and (ii) the reaction of customers and competitors will counter any possible negative effects of coordination.

(80) With regard to the difficulties in monitoring deviations the market investigation has indicated that monitoring how the production capacity on each mill is unlikely: given that the swing may be performed in a very short time and that no significant modification to the production assets are required to swing production, competitors will not be able to monitor any swing to producing fluff pulp. The difficulty in monitoring any such deviation is also evidenced by the fact that RISI itself is not able to provide neither estimates nor precise figures on the proportion of fluff pulp

and market pulp produced by each mill, but simply provides for the total theoretical production capacity.

- (81) Secondly, the Commission considers that it would arguably be difficult to identify and compare prices relating to ongoing sale contracts, given that they reflect different individual arrangements between producers and customers concerning product specifications, logistics and supply-chain management.
- (82) Respondents to the market investigation supported this statement and indicated that the RISI list price is an indicative price and that an important part of each negotiation is the discount to apply. Those discounts can vary from one customer to another. Also, it emerged that the final price agreed upon is kept confidential. In this respect, monitoring any price deviation would be difficult.
- (83) Also, the Commission considers that coordination will not be sustainable because of the reaction of both customers and non-coordinating firms.
- (84) With regard to customers, the majority of fluff pulp sales are made to sophisticated large customers, who would be able to detect and deter coordination between their suppliers. In particular, the market investigation and internal documents have highlighted the important relationship between [confidential information related to the Parties' customers]. A reaction from these customers would, on the one hand significantly impact the merged entity's business and, on the other hand, incentivize competitors to deviate from the terms of coordination in order to gain those sales.
- (85) With regard to competitors, the significant overcapacity on the market in the future will incentivise competitors to further increase their share and participate aggressively in tender procedures should other firms coordinate in reducing the output.
- (86) Finally, the analysis of the Parties' average sale price in the last three years of both fluff pulp and market pulp as well as the profit margin realised on such sales provide convincing indications to the Commission that the Parties are unlikely to have an incentive in reducing the sales of fluff pulp. In fact, the average sale price of fluff pulp has been significantly higher than the average sale price of market pulp. Also, the average gross margin realised on the sales of fluff pulp is higher than the average gross margin realised on the sale of market pulp.²²
- (87) Hence, the Commission takes the view that foregoing sales of fluff pulp in an attempt to limit output is unlikely as it will not be economically advantageous given both the above-referred significant differences in prices and margins between fluff and market pulps.
- (88) In light of the foregoing, the Commission takes the view that Transaction does not raise serious doubts as to its compatibility with the internal market with regard to horizontal coordinated effects on the EEA-wide or worldwide market for fluff pulp.

22 Please refer to paragraph 75 above

5. CONCLUSION

- (89) For the above reasons, the European Commission has decided not to oppose the notified operation and to declare it compatible with the internal market and with the EEA Agreement. This decision is adopted in application of Article 6(1)(b) of the Merger Regulation and Article 57 of the EEA Agreement.

For the Commission

(Signed)

*Margrethe VESTAGER
Member of the Commission*