

## Other competitive constraints

1. This appendix considers competitive constraints other than that imposed by Schütz Group's new facility in Moerdijk. We consider, in turn, the likelihood of further new entry or expansion by competitors, and whether buyers would be able to act to constrain market power.

### Entry

2. In addition to the entry by Schütz Group through its new plant at Moerdijk, we considered the likelihood of further new entry in response to the merger.
3. Third parties estimated that a new large steel drum factory would cost between £2 million and £4 million, with a lead time of 8 to 15 months. Greif accepted that these estimates might be appropriate for a greenfield site with new equipment, but submitted that entry costs could be drastically reduced by purchasing second-hand equipment, stating that a second-hand production line with a lower speed would cost approximately £1 million. Ramsden and Whale entered the new steel drum market by acquiring second-hand equipment. The production line was purchased about ten years ago for £[REDACTED], but Ramsden and Whale stated that [REDACTED]. There have been no new entrants to the manufacturing of new large steel drums in Great Britain in the past five years. There were two exits: T&D exited the market in 2003 following acquisition by Greif, and Economic Drums exited the market because of insolvency.
4. Greif said that the most likely new entry would be for a current UK supplier of alternative industrial packaging to begin supply of new large steel drums alongside existing production processes. It suggested that Mauser and Schütz could transfer a steel drum production line to their UK operations at low cost because they had underutilized steel drum capacity elsewhere in the world.
5. Mauser said that the investment needed for a new steel drum operation was considerable. It would not expect a sizeable entry in the UK market, and told us that [REDACTED]. Schütz also told us that entry was expensive and as the market was diminishing year on year it did not believe that anyone would set up a new steel drum plant in the UK.
6. Additional factors that might deter entry include economies of scale, and overcapacity in the market. Further, third parties pointed to continuing exits (by both acquisition and liquidation) from the industry, significant examples being Economic Drums and T&D. The potential for Greif's capacity to be utilized aggressively in response to a new entrant might also increase perceived entry risk.

### Expansion

7. We considered that expansion by an existing supplier of new large steel drums in Great Britain could occur with relatively low investment and within a short timescale, by increasing the number of working shifts and/or removing bottlenecks in the production process. Information on the ability of existing Great Britain manufacturers to expand their capacity in this way is set out in paragraphs 20 to 35 of Appendix F. Our assessment suggests that capacity of around 830,000 drums could be added relatively easily.

8. However, as discussed in paragraphs 36 to 39 of Appendix F, we believe that existing Great Britain suppliers operated at higher variable costs than Greif and Blagden, due in particular to their higher material cost arising from their smaller size. Any quick and relatively inexpensive expansion would be unlikely to change this pattern; the variable cost incurred by these suppliers would remain higher than Greif's and Blagden's.
9. We found that existing importers incurred significant transport costs because of the distance between their plants and customers in Great Britain, and this would constitute a significant element of their variable costs. This would be unaffected by any transformations of their capacity or production facilities.
10. We do not consider that additional higher-cost excess capacity in the hands of the smaller suppliers in Great Britain or existing importers would exert as strong a constraint on Greif's prices as Blagden's capacity pre-merger or Schütz Group's planned new capacity in the Netherlands.
11. Expansion could be a stronger constraint on Greif's pricing if the expansion resulted in economies of scale. We considered this possibility in relation to the existing Great Britain manufacturers. If one of the smaller suppliers wished to transform its capacity to manufacture new large steel drums in similar volumes at a similar variable cost to Blagden or Greif, it could purchase an entire new production line. This step would be similar to new entry in terms of investment and timing.
12. Metal Drum estimated that a new large drum line would cost £[redacted] and take 12 months to set up. Ramsden and Whale said that [redacted]. Greif provided evidence that a second-hand production line could be purchased for approximately £[redacted] (excluding transport, installation and training costs). It was not clear what level of investment would be needed to achieve a similar level of automation to that operated by Greif or Blagden. However, even an investment at the lower end of these estimates would still be a considerable step for a small company and would involve a substantial financial commitment.
13. We considered whether any of the smaller suppliers would be likely to undertake such a transformational change to its production capacity. The smaller suppliers are long-established, owner-managed businesses. One told us that its strategy was to 'stay under the radar'. Another said that it tried to avoid low-margin, high-volume business. Any significant capacity expansion and increase in volumes would therefore represent a radical change in strategy. However, we recognized that the merger alters the market significantly.
14. In taking a decision whether to expand capacity, suppliers must be sure that they will gain sufficient new customers beyond the short term. If these new customers were liable to switch away, or if the price at which the customer could be supplied was unprofitable, then small suppliers would be less willing to undertake the risks associated with expansion. We noted that the smaller suppliers feared retaliation from Greif if they won business from it.
15. In addition, finance for an investment of around £1 million could prove difficult to obtain for a company the size of the three smaller suppliers. Even if it were available, such a debt would increase the smaller suppliers' financial risk substantially. Although newer machinery could be bought and introduced in stages, this would significantly increase the timescales. There could also be disruption to supplies as the newer machinery was brought on-stream.

## Sponsored entry or expansion

16. To the extent that there are barriers associated with entry or expansion, a customer could, in principle, facilitate any necessary new investment by giving assurances over prices or volumes of business and thereby provide sufficient security for this new investment to be undertaken. Whether this would represent a sufficient constraint would depend upon the costs, and the credibility, of such a strategy. The credibility would depend, in part, on the proportion of customers' costs accounted for by steel drums, which was unlikely to be high. It would also depend on the size of customers' orders relative to business required in order to make an investment profitable; this is discussed below.
17. Greif cited Ramsden and Whale as an example of entry being sponsored by BP. However, Ramsden and Whale told us that it entered the market approximately ten years ago and received BP's order in 2004. [REDACTED] Although we acknowledged that the BP contract might have helped Ramsden and Whale to increase its market share, we did not consider this to be an example of past sponsored entry into the new large steel drum sector.
18. Greif also told us that several other large customers were of a sufficient scale to guarantee the financial viability of a new entrant, or to encourage expansion by a smaller competitor. It noted that [REDACTED] had had its own in-house drum manufacturing operations. Table 1 shows the volume of drums purchased in 2006 by Greif's top five customers.

TABLE 1 Drum purchases for top five Greif customers, 2006

Customer	Drum purchase 2006
[REDACTED]	[REDACTED]

Source: Greif.

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Note: These are purchases from Greif alone and so do not include purchases from Blagden or other steel drum suppliers.

19. As discussed in paragraphs 2 to 15, entry or expansion that would constrain the merged entity's pricing would require significant investment and large volumes. Very few customers in this market purchased more than 100,000 drums a year and would therefore have had sufficient size to sponsor entry. And no customer suggested that this was a strategy that they would consider implementing. In the future, a customer would have the option of sourcing drums from Schütz Group as an alternative to Greif, without having to incur the costs of sponsoring another supplier.

## Countervailing buyer power

20. Countervailing buyer power refers to a situation where 'buyers, either because of their size or commercial significance to their suppliers, may have the ability to prevent the exercise of market power by suppliers'.<sup>1</sup> Buyer power can arise only if buyers have an alternative supply option. This alternative option or threat must be credible in the sense that it would be available to customers should agreement with a

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<sup>1</sup>Merger References: Competition Commission Guidelines, CC2, paragraph 3.58.

supplier fail to be reached. The more powerful the buyer's threat, the closer the price will be to marginal cost.

21. Whereas we anticipated that the new capacity coming on-stream from Schütz Group would offer the merged parties' customers a credible alternative in future negotiations, we also considered whether there were further sources of buyer power that could constrain the merged parties.
22. We have already discussed the possibility of customers sponsoring entry or expansion. Greif also suggested that buyer power could act as a constraint because many large customers had the option to take steel drum manufacture in-house. Customers did not mention this as an option.
23. For the customer, a threat would be credible only if it imposed substantial costs on the supplier. Blagden suggested that customers with multinational accounts could threaten business in other countries. Greif told us of an instance in which Greif had given a price reduction to a customer in the UK and in the Netherlands in order to safeguard its global contract with it. However, it was not apparent to us that the merged entity would necessarily and consistently sacrifice profits in Great Britain to protect global business. In addition, Greif noted that a Continental European or international presence was not a determining factor in choice of supplier. This was supported by evidence from Ramsden and Whale that although larger customers tendered on a Europe-wide basis, it had been invited to tender for Great-Britain-only business and it had been successful on more than one occasion.
24. The evidence was unclear whether larger customers could exert sufficient countervailing buyer power to obtain more competitive prices than those that would be available because of the constraint imposed by Schütz Group.