

2 The companies involved and the merger situation

The merger

2.1. Monsanto Company of St Louis, Missouri, has reached provisional agreement with Rhône-Poulenc SA of Courbevoie, Paris, to sell to Rhône-Poulenc the whole of Monsanto's world-wide business in the production and supply of bulk analgesics (including bulk aspirin, bulk paracetamol and the chemicals salicylic acid and methyl salicylate).

2.2. The proposed transaction is described in this chapter (paragraphs 2.27 to 2.31) following descriptions of the companies concerned.

Monsanto Company

2.3. Monsanto Company is based in St Louis, Missouri, and incorporated in the State of Delaware, USA. It is the successor to Monsanto Chemical Works, the original company set up in 1901 in St Louis to manufacture saccharin.

2.4. The activities of Monsanto world-wide are organised into six main operating units as follows:

- Agricultural Products
- Chemicals
- Electronic Materials
- Fisher Controls
- Low-calorie sweeteners ('Nutrasweet')
- Pharmaceuticals

2.5. The analgesics business is part of the Specialities Division of Monsanto Chemical Company. In 1988 Specialities, with net sales of US\$424 million, accounted for 5 per cent of total Monsanto sales revenue. Analgesics accounted for about 20 per cent of Specialities Division sales about 1 per cent of total Monsanto sales world-wide.

2.6. Monsanto has a long association with analgesics having first entered the business in 1917 when the expiry in the United States of Bayer's patent on aspirin allowed it to set up in aspirin manufacture and sale. Monsanto's first site was the J F Queeny plant in St Louis, still making bulk aspirin today. In 1923, aspirin production was commenced at the Ruabon site, in North Wales (then the Graesser works, Monsanto having a 50 per cent share in the business until it bought out Graesser in 1928). Monsanto was also involved in the manufacture of two other analgesics (phenacetin and salicylamide) at Ruabon between the 1930s and 1970s but ceased production when these products were no longer profitable.

2.7. Monsanto entered the paracetamol market in 1952 with the commissioning of a pilot plant at the J F Queeny site; this venture was discontinued in 1956 due to lack of customers. However, in 1974 Johnson & Johnson (the manufacturer of a major US brand, Tylenol) requested Monsanto to

recommence production and a paracetamol unit was set up at the Luling plant in Louisiana. Luling is still Monsanto's only paracetamol production unit.

2.8. Monsanto's most recent analgesics venture is a 1,000 tonnes per annum paracetamol plant which will utilise part of the existing 1,500 tonnes per annum aspirin facility established in 1987 in Bangkok as a joint venture with a local tableter, Osothsapha (Teck Heng Yoo) Co Ltd. The paracetamol plant is under construction and is expected to start production in the second quarter of 1990.

2.9. Monsanto Chemical Company now operates four bulk analgesics manufacturing plants:

<i>Site</i>	<i>Products made</i>
Luling, Louisiana	Paracetamol
J F Queeny, St Louis, Missouri	Aspirin, salicylic acid, methyl salicylate
Ruabon, North Wales	Aspirin, salicylic acid, methyl salicylate
Bangkok (joint venture)	Aspirin, paracetamol (in 1990)

Over the five years 1984 to 1988, the Ruabon plant accounted for about 20 per cent of Monsanto's world-wide revenue from the sale of bulk analgesics and associated chemicals. Salicylates account for about one-quarter of Ruabon's production, the rest consisting mainly of rubber chemicals. The principal products are manufactured in separate plants at the site but all operations benefit by sharing the fixed costs of common utilities and services. A total of 483 employees are based full-time at Ruabon, of which approximately 110 are dependent on the salicylates business.

Financial information

2.10. In 1988 Monsanto Company had an operating profit of \$955 million and a net profit before income taxes of \$893 million on net sales of \$8,293 million. Total assets at 31 December 1988 were \$8,461 million and shareholders' equity was \$3,800 million. A segmental analysis of its assets, net sales and operating profit is shown in Appendix 2.1.

2.11. In 1988 Monsanto plc, the United Kingdom holding company in the Monsanto group, made a profit on ordinary activities before taxation of £44 million on a turnover of £314 million. Shareholders' funds at 31 December 1988 were £215 million. Its 1988 Annual Report gave a geographical analysis of turnover (see Appendix 2.2) but no analysis of turnover and profit by class of business.

2.12. Monsanto told us that it did not normally prepare separate accounts for its United Kingdom analgesics or salicylates businesses, or for its Ruabon plant as an entity. At our request, however, it provided us with specially-prepared statements derived from its management accounts, which it believed showed a fair view of the profitability of its Ruabon salicylates business for the past five years. These are summarised in Table 2.1.

TABLE 2.1 **Monsanto: profitability of Ruabon salicylates business**

	<i>£'000</i>				
	<i>1984</i>	<i>1985</i>	<i>1986</i>	<i>1987</i>	<i>1988</i>
External sales	9,786	9,737	8,892	8,409	10,749
Costs	(8,471)	(9,479)	(8,355)	(8,957)	(10,458)
Profit/(loss) before tax	<u>1,315</u>	<u>258</u>	<u>537</u>	<u>(548)</u>	<u>291</u>
Capital employed	5,668	9,522	8,950	9,820	7,709
Return on sales (%)	13.4	2.6	6.0	(6.5)	2.7
Return on capital employed (%)	23.2	2.7	6.0	(5.6)	3.8

Source: Monsanto.

2.13. Monsanto commented on these statements as follows:

- (a) The Ruabon salicylates business shared certain facilities with other activities at Ruabon, the costs of which were allocated between those activities in accordance with Monsanto's cost accounting rules.
- (b) The business benefited from group services, including Head Office services provided by the Group's European Headquarters in Brussels and its offices in Basingstoke. An appropriate allocation of the cost of these services had been made to the Ruabon salicylates business.
- (c) The returns on capital employed were well below that of the group as a whole, and far short of the return of 20 per cent after tax that Monsanto would normally expect. Performance in 1988 was particularly disappointing, as bulk aspirin sales were almost 40 per cent higher in volume than in 1987, salicylic acid and methyl salicylate sales had achieved record levels and, following the modernisation of its production facilities in 1986/87, Ruabon had the most efficient salicylic acid plant in the group.

Rhône-Poulenc SA

2.14. The origins of Rhône-Poulenc can be traced back to 1858 when a young Parisian pharmacist, Etienne Poulenc, acquired a small pharmaceutical supply business. The business began to produce its own chemical specialities and developed from there. By the early 1920s, Etablissements Poulenc Frères had expanded to the point of acquiring an English company, May & Baker, and establishing two subsidiaries, Specia (a speciality chemicals company) and Rhodiaceta (a manufacturer of artificial textiles). In 1928 Poulenc Frères merged with Société Chimiques des Usines du Rhône to form Société des Usines Chimiques Rhône-Poulenc. In 1961 a holding company, Rhône-Poulenc SA, was formed to direct the long-term strategy of the group, and Rhône-Poulenc gradually moved away from fertilisers and bulk chemicals towards speciality chemicals. The Rhône-Poulenc group was nationalised in 1982.

2.15. Rhône-Poulenc's activities are organised into four sectors: Chemicals, Fibres, Agro-chemicals and Health.

2.16. The activities of the Chemicals sector are spread through four divisions: Basic Chemicals, Speciality Chemicals, Fine Inorganics and Films. The sector is at the heart of the group's strategy and accounts for over 40 per cent of Rhône-Poulenc's turnover. In recent years it has received substantial investment aimed at improving production capacity and at upgrading and automating production processes, and investment in research has risen by more than 25 per cent in the last three years.

2.17. The activities of the Basic Chemicals sector are concentrated mainly on major organic and inorganic intermediates such as phenol, used in the production of resins, pharmaceuticals and agro-chemicals.

2.18. The Health sector, which accounts for about 24 per cent of total group turnover, develops and markets ethical pharmaceuticals, vaccines and a range of active ingredients (including bulk analgesics) and other products in the fields of human and animal health.

2.19. Under the Treaty of Versailles France was accorded the right to use the aspirin name, which until the First World War had been the monopoly of Bayer. Production of bulk aspirin began in 1920 in Rhône-Poulenc's St Fons plant in France. The plant was replaced in 1971 by a new plant on the same site, with a capacity of 8,000 tonnes per annum; it produced 5,300 tonnes in 1988.

Rhône-Poulenc has been producing paracetamol in France since 1959 (at St Fons until 1987 and subsequently at Roussillon). The group began selling aspirin and paracetamol in the United Kingdom in the early 1970s.

2.20. Salicylic acid production was begun by Rhône-Poulenc at the beginning of the century. In 1970 the group invented a new process at its Roussillon site. The site had a production of 12,000 tonnes in 1988. Rhône-Poulenc opened a new plant in Brazil in 1987 which had a production of 2,000 tonnes in 1988.

2.21. Thus, the current position is that aspirin and methyl salicylate are manufactured in France at St Fons, and salicylic acid and paracetamol at Roussillon; and salicylic acid is also manufactured in Brazil.

2.22. Both of the French plants are owned and operated by Rhône-Poulenc Chimie (ie they fall within the Chemicals sector): Rhône-Poulenc Chimie is itself responsible for production and sales strategy for salicylic acid and methyl salicylate; but production and sales strategy for aspirin and paracetamol are the responsibility of Rhône-Poulenc Santé (ie they fall within the Health sector). The position with regard to sales in the United Kingdom is described below.

2.23. Rhône-Poulenc's United Kingdom holding company is Rhône-Poulenc Ltd. Together with its subsidiaries, that company employs 6,000 people around the world, of whom over 3,000 work in the United Kingdom. Its annual turnover is over £500 million per annum, of which about 50 per cent is earned abroad. The headquarters of the Chemical and Health Care Divisions, the research institute, and the production facilities of many of the major product lines sold world-wide are based at Dagenham in Essex. The headquarters of the Agricultural Division and its research station are at Ongar, also in Essex.

2.24. Salicylates and paracetamol are supplied to the United Kingdom market through Rhône-Poulenc Chemicals Ltd, a subsidiary of Rhône-Poulenc Ltd.

Financial information

2.25. In 1988 Rhône-Poulenc had an operating profit of FF5,880 million and a net profit from continuing operations, before taxes and minority interest, of FF4,576 million on net sales of FF65,334 million. Total assets at 31 December 1988 were FF67,688 million and stockholders' equity FF18,807 million.¹ A segmental analysis of its assets (to the extent that they are identifiable to business sectors), net sales and operating profits is shown in Appendix 2.3.

2.26. Rhône-Poulenc told us that it did not prepare separate accounts for its European salicylates business, which includes supplies in the United Kingdom. However, in response to our request, it provided us with the specially-prepared statements that are summarised in Table 2.2. They show profitability in terms of return on sales only, not return on capital employed, as Rhône-Poulenc told us that it would not be practicable to allocate capital to products which formed such a small part of its chemical plants' output.

¹Rhône-Poulenc's capital stock is divided into common stock class A and preferred stock class B. Preferred shares B are split into non-voting preferred shares and voting certificates. The French state holds directly 91.2 per cent of voting rights.

TABLE 2.2 Rhône-Poulenc: profitability of European salicylates business

	<i>FF '000</i>				
	<i>1984</i>	<i>1985</i>	<i>1986</i>	<i>1987</i>	<i>1988</i>
<i>Salicylic acid</i>					
Turnover	162,811	152,223	126,294	104,368	124,808
Costs	<u>(123,416)</u>	<u>(115,558)</u>	<u>(94,930)</u>	<u>(93,753)</u>	<u>(109,846)</u>
Profit before tax	39,395	36,665	31,364	10,615	14,962
Return on sales (%)	24.2	24.1	24.8	10.2	12.0
<i>Methyl salicylate</i>					
Turnover	N/A	N/A	N/A	12,338	14,463
Costs	N/A	N/A	N/A	<u>(14,325)</u>	<u>(16,554)</u>
(Loss) before tax	N/A	N/A	N/A	<u>(1,987)</u>	<u>(2,091)</u>
Return on sales (%)	N/A	N/A	N/A	(16.1)	(14.5)
<i>Aspirin</i>					
Turnover	121,300	120,300	93,500	103,500	103,200
Costs	N/A	N/A	<u>(93,700)</u>	<u>(118,000)</u>	<u>(122,200)</u>
(Loss) before tax	N/A	N/A	<u>(200)</u>	<u>(14,500)</u>	<u>(19,000)</u>
Return on sales (%)	N/A	N/A	(0.2)	(14.0)	(18.4)

Source: Rhône-Poulenc.

The proposed transaction

2.27. Although no binding agreement between the parties for the sale and purchase of any part of the Monsanto analgesics business has yet been signed, the Memorandum of Understanding between the parties contemplates that the transaction will be effected in the following way:

- the transfer to Rhône-Poulenc of the 74 per cent shareholding in Monsanto Chemicals (Thailand) Ltd held by Monsanto;
- the acquisition by Rhône-Poulenc of the tangible and intangible assets of such part of the Ruabon facility as manufactures analgesics;
- the acquisition by Rhône-Poulenc of the tangible and intangible assets of the relevant part of the Queeny site at St Louis;
- the acquisition by Rhône-Poulenc of the tangible and intangible assets of the Luling paracetamol plant, excluding title to the freehold of the land on which the plant is situated: as with Ruabon, the Luling plant forms part of a larger Monsanto manufacturing facility and it is proposed that Rhône-Poulenc will be granted a licence of that part of the plant producing paracetamol and that the plant will be operated on behalf of Rhône-Poulenc by Monsanto under the terms of an operating agreement to be concluded between the parties.

2.28. Monsanto's complex at Ruabon produces a number of chemical products. There are separate plants on the site for the production of salicylic acid, methyl salicylate and aspirin. Each of these plants, although dedicated to the production of a specific salicylate product, is dependent upon other parts of the complex for the supply of various services.

2.29. Accordingly, it is proposed that the freehold title to the land and buildings should remain vested in Monsanto but that a 25-year lease of the relevant parts of the site should be granted to Rhône-Poulenc. Rhône-Poulenc will purchase the plant, machinery, inventory and other tangible assets of the analgesics facilities. Rhône-Poulenc will also purchase customer and supplier lists, and all Monsanto's intellectual property rights in the production of salicylates will be assigned to Rhône-Poulenc or provided to Rhône-Poulenc under the terms of a perpetual royalty-free licence.

2.30. An operating agreement will be entered into between the parties, pursuant to which Monsanto will operate the plants on behalf of Rhône-Poulenc for the production of salicylates and possibly for other carboxylated aromatic products. The operating agreement would, subject to the rights of prior termination referred to below, be for an initial period of 25 years and would be subject to termination by either party at the end of that 25-year period, or at any time thereafter on three years' notice. Apart from the usual default provisions, each party would also be able to terminate the agreement earlier in the following circumstances:

- (a) If Rhône-Poulenc were to discontinue either all its operations or its salicylic acid operations at Ruabon, it could at any time after the first three years terminate the agreement (or so much of it as related to salicylic acid, as the case may be) on giving not less than 18 months' notice. The minimum duration under these arrangements would therefore be four and a half years.
- (b) Rhône-Poulenc could shut down an entire production unit, other than the salicylic acid production unit, at any time on giving not less than 12 months' notice.
- (c) After five years Monsanto could give three years' notice to Rhône-Poulenc to terminate the agreement (so that it would have run for at least eight years) if Monsanto decided to discontinue all, or substantially all, its manufacturing operations at Ruabon, or to sell all, or substantially all, the adjoining land to a third party. (Monsanto would then use its good offices to see that the purchaser of the land provided similar services to Rhône-Poulenc, failing which the relevant facilities and assets would, if Rhône-Poulenc wished, be bought by it at their book value.)

2.31. The intention of the parties is further reflected in a draft Ruabon Operation Agreement, some clauses of which we have seen. These show that the provisions concerning Rhône-Poulenc's rights of termination are based directly on the Memorandum of Understanding. Rhône-Poulenc told us that they had remained substantially the same throughout the drafting and negotiating process and that they were not expected to change materially in the course of further negotiations.

2.32. The agreement between Monsanto and Rhône-Poulenc will contain a restrictive covenant restraining Monsanto from competing with Rhône-Poulenc in the manufacture or sale of salicylic acid, methyl salicylate, aspirin or paracetamol for a period of five years. The transaction will have no effect on competition between Monsanto and Rhône-Poulenc in other areas of activity, where they will remain fully independent competitors.

The responses of other regulatory authorities

2.33. The European Commission was informed of the proposed transaction in February 1989 and in July 1989 informed the companies that it had decided not to object to the merger.

2.34. A formal notification of the proposed transaction was also made to the US Federal Trade Commission on 28 February 1989. No response had been received by 30 March 1989 which was the last date by which objection could be raised by the Federal Trade Commission. The transaction had accordingly effectively been cleared by the US authority.