



Highlands & Islands ENTERPRISE

24 July 2006

Sandy Cumming CBE Chief Executive

Edwin James
Inquiry Secretary (Pan Fish/Marine Harvest inquiry)
Competition Commission
Victoria House
Southampton Row
LONDON
WC1B 4AD

Dear Mr. James

ANTICIPATED ACQUISITION BY PAN FISH ASA OF MARINE HARVEST N.V.

Highlands & Islands Enterprise (HIE) is pleased to respond to the invitation of the Competition Commission to submit views on the above proposed acquisition of Marine Harvest by Pan Fish.

The Highlands & Islands Enterprise Network is the UK government agency responsible for economic and community development, training and environmental renewal throughout the north and west of Scotland – the Scottish Highlands and Islands. HIE and our predecessor organisation the Highlands & Islands Development Board have worked closely with the aquaculture industry in the highlands and islands from its emergence in the late 1960s through to the present day's internationally competitive salmon farming industry supplying high quality produce to UK, European and global markets.

We have previously described aquaculture as the most significant new industry to emerge in the highlands and islands in the last quarter of the 20th century, which conveys something of the importance of this industry in the economic and social fabric of many of our most remote communities – areas where alternative economic opportunities are scarce. In such areas up to 30% of the local working population has been shown to be directly or indirectly dependent on the aquaculture industry for their livelihood. In our view the proposed acquisition would likely have both positive and negative consequences which we outline below.

Positive consequences.

The salmon farming industry continues to rationalise as it has over the past 20 years, with the current high in market prices attracting external investor interest to this global industry as never before. Pan Fish is in the process of building a global business predicted to have some 30% of global production of farmed Atlantic salmon. A producer of this scale will be able to bring a greater degree of market-led discipline to production, reducing the cyclical nature of salmon production and pricing which has helped drive so many small/medium scale operators out of business in Scotland and Ireland. Also, a business of such scale will be better placed to ride out the down turns in such cycles as may continue into the future and to invest in research and market development. It is of strategic importance that the Scottish salmon farming industry includes the world's largest salmon farming business. The business must also be able to operate an appropriate scale in Scotland to secure its continuing presence as part of the global Pan Fish portfolio.



The distribution of production sites in the Scottish salmon farming industry is in large part a matter of historical coincidence and a number of companies are in the process of rationalising the location and scale of their sea cage production sites in order to operate fewer, larger sites more cost effectively. The proposed acquisition would facilitate a number of these rationalisations which would otherwise require lengthy negotiation between the above two firms as separate entities, involving other stakeholders.

Management of sea cage farms is the responsibility of site and company managers however the effectiveness of fish health and parasite control measures increase significantly when neighbouring sites are managed on a co-ordinated "area management" basis. This area management approach would be facilitated and strengthened as a result of neighbouring farm sites falling under single ownership in many coastal areas as would be the case following the proposed acquisition.

The above two companies, and Fjord Seafood already acquired by Pan Fish, have their distinct strengths and this acquisition would provide an opportunity to mine the expertise of each company's workforce to the benefit of the new merged operation.

A major concentration in ownership as proposed may be expected to reduce the parties' interest in tackling the minority and niche markets which the independently owned salmon farms have developed and are targeting as a means of avoiding head on competition against the volume operators. These independent firms produce around 15% of industry output and employ a slightly higher proportion of the total industry workforce.

Negative consequences

The potential negative consequences revolve around the level of concentration of ownership in the farmed salmon production sector in Scotland. Estimates of the share of Scottish farmed salmon tonnage for Pan Fish post acquisition are in the range 45-60%. In addition, independent companies may be contracted to either of the above firms to supply farmed salmon so it is difficult to define their effective industry share with accuracy. This may well prompt concerns as to the operation of the market in the UK for goods and services for the salmon farming industry and possibly the wider aquaculture industry (encompassing trout and other species).

The commercial advantages offered by increased scale of operation in Scotland are not limited to Pan Fish and will be of interest to other salmon farming businesses in Scotland seeking to improve their competitiveness. Consideration should be given to the number of major producers of farmed salmon which would be required for satisfactory operation of the market for goods and services, which may in the process point to a maximum scale for an industry leader.

The impact of the proposed acquisition on the UK and EU markets for farmed salmon would appear to be less problematic, with a substantial proportion of the UK market and the majority of the EU market supplied by Norwegian based producers, supplemented by supplies from Faroe and Chile. If there is a concern for the market it relates to the price premium which farmed salmon from Scotland maintains over its Norwegian equivalent. The image of the Scottish product and its perceived quality, form part of the marketing mix which Scottish independent producers in particular have employed to good effect, and which has helped sustain them in business alongside larger, more cost effective producers. The approach to marketing Scottish farmed salmon by a global operator controlling half the Scottish industry's output might not be unduly concerned to maintain its distinctive image and associated price premium.

Conclusion

The salmon farming industry has been a remarkable success story for the highlands and islands, for Scotland and the UK. The industry has developed to become a key part of an expanding global industry providing high quality seafood products in the face of growing market demand. As a young, growing industry, change must be embraced as inevitable.

As the industry's rate of growth Scotland slows, and feed costs rise as projected, the pressures to improve competitiveness will inevitably focus attention on labour efficiencies. Whatever the outcome of this investigation, we expect jobs will continue to be shed from the industry as one consequence of the globally competitive nature of the industry and its markets. The industry in Scotland cannot be insulated from free and fair market forces.

We fully recognise the importance of the employment provided by an economically and environmentally sustainable salmon farming industry across the Highlands and Islands. We reluctantly accept that some loss of jobs from the industry is a necessary price to be paid for the continuation of the industry and the remaining workforce.

The salmon farming industry in Scotland needs Pan Fish in its midst as the largest global producer of farmed salmon. The proposed acquisition of Marine Harvest would offer a number of benefits through rationalisation which would accrue both to the parties to the merger and to a number of other salmon farming businesses. We are however unsure of the effects an unconditional merger of the two companies in Scotland might have on the market for goods and services to the industry in the UK.

The HIE Network has extensive dealings with salmon farming operators, including Pan Fish and Marine Harvest. As the Commission's findings become known we will work with all parties concerned to assist the future development of the business operations as well as the individuals and communities which may be affected by the future direction of these businesses.

We would be pleased to expand on any of the above points should the Competition Commission wish and look forward to hearing of progress in the Commission's investigation.

Yours sincerely,