CHAPTER 7

Conclusions

THE MERGER SITUATION

140. Under the terms of the reference and the provisions of sections 69(2) and 75 of the Fair Trading Act 1973, we are required to investigate and report on the question whether arrangements are in progress or in contemplation which, if carried into effect, will result in the creation of a merger situation.

141. We are required to exclude from consideration the condition under section 64(1)(*a*). The condition set out in section 64(1)(*b*) is satisfied by the fact that the value of Century's assets exceeds £5 million.

142. On 9 November 1976 BP announced that it offered to acquire all the ordinary and preference shares of Century. The offer for the ordinary shares was conditional on acceptance being received not later than 30 November 1976 and the offer not being referred to the Monopolies and Mergers Commission. Although the offer by BP has lapsed, BP has told us that it intends, subject to clearance under the Act, to make a new offer. Arrangements are, therefore, in contemplation which, if carried into effect, would result in enterprises carried on in the United Kingdom by or under the control of BP ceasing to be distinct from enterprises carried on by or under the control of Century.

143. We conclude that a merger situation qualifying for investigation will be created if the arrangements in contemplation for the merger of BP and Century are carried into effect. We are required by the Act to proceed in relation to the merger as if it had already taken place. We now consider whether the creation of that situation may be expected to operate against the public interest.

THE PUBLIC INTEREST

144. We first consider the main arguments advanced for and against the merger by each of the parties under the headings set out below.

Prices of base oils

145. Century claimed that it kept down base oil prices in the United Kingdom. First, it was able, as the largest independent purchaser in the United Kingdom across the whole range of base oils, to buy base oils abroad if and when they were available at prices lower than those of domestic supplies. Secondly, Century said that the lower prices that it was able to obtain were used as a marker for the prices at which other independent purchasers bought comparable oils. It claimed that few other independents, owing to their smaller purchases, were able to influence the prices of base oils in this way. In addition, Century said that it helped to keep down prices by supplying both virgin and re-refined base oils to other lubricant producers at prices below those sought by United Kingdom refiners. Century considered that, if it became part of the BP group, it would be likely largely to lose its power of independent buying and to find itself almost entirely reliant on BP for supplies of base oils, as Duckham became after its merger.

146. BP replied that Century's purchasers were too small to have any significant effect on market prices for base oils in the United Kingdom. After the merger, Century would still be entirely free, according to BP, to purchase base oils and other materials outside the BP group if it could thereby obtain supplies more cheaply. Century, however, considered that other suppliers would be unlikely to offer the company such favourable prices if it became part of the BP group.

147. BP gave us details of prices for base oils charged to Duckham. Although precise comparisons are difficult, these appeared to be the same as, or even lower than, the prices paid by Century for similar oils.

148. We consider that Century is an efficient buyer and may occasionally buy and resell base oil at advantageous prices; but the scale of its purchases and resales to third parties is too small to have any persistent or significant effect on the general level of prices. We are not satisfied, therefore, that a merger would have any material effect on the prices Century pays. Still less would it affect the level of base oil prices in the market.

Costs and efficiency

149. BP considered that savings would be possible by eliminating the separate manufacture of certain similar products and pursuit of the same research by Duckham and Century, by setting up common services of accounting and administration and by arranging for one company to undertake packaging and some distribution for the other. It considered also that costs of research could be spread over a larger volume of sales, and that, in general, Century and Duckham would be able to assist and support one another by exchange of know-how in areas where one was more technically advanced than the other, for example, Century in mining engineering and Duckham in public works. BP said that the extent of the cost savings which might be possible would require further study, and it could not quantify them even approximately at present.

150. Century contended that the extent of such savings was unlikely to offset the additional costs which would arise from the assimilation of its wage and salary structure and, in particular, its pension arrangements to the more generous level of Duckham and BP wages, salaries and pensions (see paragraphs 123-125) and from the effect of spreading overheads over a smaller turnover as a result of loss of sales that it expected as a result of the merger (see paragraphs 117-118). Century also considered that there would be a loss of efficiency because cost-saving improvisation, the keenness, individual enterprise, enthusiasm and job satisfaction, which were so conspicuous in the staff of its comparatively small organisation, would be stifled by incorporation within a larger group. It said that some management staff had expressed their determination to leave if the merger went through and that several had already received offers of alternative employment.

151. We accept that there are possible economies from rationalisation, but we have no evidence to show how significant they may be. On the other hand, the effect of any increases in costs such as Century has predicted is difficult to

determine because it depends on uncertain future developments, for example possible loss of sales resulting from the reaction of customers to Century's loss of independence. We acknowledge the efficiency of Century at present and note that BP attached importance to retaining Century's management with its enterprising approach and experience. But here again the effect of the merger is difficult to assess because it depends on the reactions of staff to circumstances which have not yet been experienced.

152. Although Century expects increased wage and salary costs, we have no evidence to show that there is any significant difference between the level of salaries and wages as between Century and Duckham. Assimilation to the more generous BP pension scheme would mean an early increase in costs to Century, but it seems likely that Century could get financial assistance from BP, if needed, as BP has recently helped Duckham to cope with a similar situation. Moreover, we consider that, if the merger did not take place, pressure for better pension terms within Century could be expected and the cost of satisfying this would have to be met from Century's own resources. On balance we do not consider that the merger would significantly affect the aspects of costs and efficiency discussed in this section.

Employment

153. If rationalisation took place on any substantial scale, there would inevitably be some reduction in the labour force. However, BP told us that it would do its utmost to make any such reduction gradually by not filling vacancies. We do not consider that the merger would have any adverse effect on the public interest so far as employment is concerned.

Balance of payments

154. Century argued that several adverse consequences for the balance of payments would flow from the merger. First, oil imports would increase since its re-refining operations would end; secondly, the price of imported base oils would be increased by Century's absence as a buyer; thirdly, Century's exports would be reduced, partly as a result of a reduction in efficiency and an increase in costs, and partly because BP, being a multinational company, would discourage Century from exporting to countries where one of its subsidiaries could manufacture similar products. In Century's view, Duckham's export performance has suffered as a result of its merger with BP and its own would be similarly affected.

155. On the other hand, BP said that Century would have the benefit of Duckham's overseas sales contacts, experience and networks, and its manufacturing sources and services. It agreed that there had been some replacement of Duckham's direct exports by overseas blending in the 1970s but argued that this reflected relative costs of the alternative operations and enabled Duckham's sales in the markets concerned, and therefore also its foreign exchange revenue, to increase. BP also said that the replacement of Century's imports of base oils by BP's supplies of domestically refined base oils would benefit the balance of payments.

156. We find these claims and counter-claims difficult to quantify, but the effect of the merger upon the balance of payments could only be extremely small. We therefore conclude that the merger would have no significant effect upon the balance of payments.

Re-refining

157. The Department of Energy have told us that re-refining of used lubricating oils is desirable because of the environmental advantage in an organised waste oils collection service and because of the growing emphasis on energy conservation (see paragraph 134). We note also that base oils re-refined from waste oils are a substitute for imports of base oils or crude oil. We therefore consider that it is in the public interest that re-refining activities should be continued and expanded, provided that the re-refining of waste oils can be done economically.

158. BP told us that it regarded acquisition of Century's re-refining operation, coupled with BP Oil's used oil reclamation agreement with Midland Oil Refineries and possible future interest of Duckham in reclamation based on current small scale trials, as a basis for potential development in its used oil recycling activity. But it said that plans for expansion of re-refining would need to satisfy BP group financial criteria. Century argued that its approach to re-refining was determined by its view of the operation as a scrap industry, requiring a different approach to capital equipment and staff remuneration from that likely to be adopted by a major oil company. It did not believe that BP would continue to support re-refining, an activity Century believes to be contrary to the interests of a major producer and refiner of crude oil. Century, on the other hand, had a strong incentive to produce re-refined oil as an alternative to supplies of base oil from the major oil companies. It argued also that the costs of re-refining would rise as a result of the merger, and make it less attractive.

159. We consider that, on the whole, the development of re-refining is likely to be pursued more energetically by Century as an independent company than it would be after the merger by a company of the BP group. BP has not as strong an incentive to pursue it as an independent company has, and consequently the merger might lead to restriction of Century's development of re-refining. Several other companies re-refine waste oils and might expand their activities if Century's expansion were not to take place, but this would inevitably involve delay in the expansion of re-refining in the United Kingdom. Further, we were impressed by Century's experience of re-refining and its proven ability to cut costs by improvisation of inexpensive capital equipment. We conclude, therefore, that in this respect the merger would have some adverse effect upon the public interest.

Price competition in the supply of finished products

160. Century maintained that, where its products overlapped and competed with those of Duckham and BP Oil, the active competition which took place at present would be reduced after the merger. Competition with Duckham would disappear, and that with BP Oil would be muted. BP said that Duckham and BP Oil competed actively for business and firmly denied any intention on its part to interfere with Century's day-to-day marketing policy after the merger.

On the other hand, BP said that it would be obliged to intervene if Century was 'indulging in misrepresentation or vicious price cutting'.

161. Century's major activity is in the manufacture and supply of industrial lubricants. On the information given to us, we estimate that in this market the merger would increase the BP group's share of total supply from 8 to 19 per cent. We believe that, in certain types of specialised products within the general category of industrial lubricants, the merger might result in bigger increases in the BP group's market share. Century is also an important producer of hand cleansers, and of engine coolants and anti-freeze. In these products, the merger would increase the BP group's market share from about 12 per cent to 29 per cent and 13 per cent to 25 per cent respectively.

162. The enlarged BP group's market shares for certain specialised lubricants, hand cleansers, and engine coolants and anti-freeze might be big enough, as a result of the merger, to affect competition. It is impossible to say categorically that a diminution of competition would result from the merger, because we are satisfied that competition does go on at present within the BP group. Nevertheless, we do not think the competitive situation between subsidiaries of the same group is the same as that between independent companies. In the former case there is always the possibility that limitation of competition may be imposed by the parent company, and, even if this does not happen, the companies may be less inclined to maintain a competitive attitude between themselves than independent companies would be.

163. If the merger does not proceed, it is perhaps possible that Duckham and BP Oil might increase the volume and range of their production of lubricating oils and thus intensify independent competition with Century. If, on the other hand, the merger proceeds, other producers might increase their output and sales of products comparable with Century's, particularly if some of Century's customers were to seek other sources of supply after the merger as Century fears they would do (see paragraph 118). These possible developments make it difficult to envisage with much clarity the effect of the merger upon competition.

164. On balance, because of the possibilities described in paragraph 162, we consider that the merger would tend to produce some risk of an adverse effect on price competition for certain products manufactured in significant quantities by both Century and the BP group.

Service to customers

165. Century attached great value to the extensive research on which it engages to produce specialised lubricants adapted to meet customers' particular needs, however small the demand for the particular lubricant may be, to the extensive services which it offers in instructing customers as to the application of the lubricants and its constant readiness to provide urgent deliveries and services even at weekends and public holidays, when an emergency arises. These claims were supported by evidence that we received from various customers (see Chapter 6). The response from Century's largest customer, the NCB, was particularly significant (see paragraphs 130–131). Century argued

that its special customer-orientated research would suffer if it became merged within a larger group interested primarily in large volume sales, which would not consider that such specialised business was worthwhile. It also feared that some of the specialised products produced on a small scale would be likely to be eliminated in the process of rationalising its range and that of Duckham and BP Oil, rationalisation which it considered would be financially necessary in view of increased costs which it expected to result from the merger (see paragraph 150).

166. BP emphasised that Century would retain its autonomy and consequently denied that it would interfere with Century's research and service to customers. It said that rationalisation would be confined to elimination of obvious duplication. In particular, it maintained that it would do its utmost to retain the custom of the NCB, which accounts for so large a proportion of Century's sales.

167. We do not doubt that these statements represent BP's present intention. Nevertheless, we have misgivings about what would happen in the longer term. The merger would make Century part of a very large group, the major part of the business of which is conducted in very large volumes. We do not think it possible to avoid the risk that, in such a group, interest in business of small volumes might not be maintained, and consequently attention to the peculiar problems of individual small customers might be diminished. The likelihood of this would be increased as Century's existing staff came to retire (or, as Century fears some would, to leave), and had to be replaced by others with no experience of the conduct of the business by Century as an independent company.

168. There is a more general point to which we attach some importance. The products produced and sold by oil companies are very diverse, as are the needs of the companies' customers. The advance of industrial technology constantly requires new products, often of a highly specialised nature. The volume required of some products is very large, of others very small. It therefore seems to us that efficiency and competition are most likely to be maintained if the market is served by a number of separate concerns varying both in size and in degree of specialisation in activities and products. It would thus be regrettable if Century, which is the largest of the independent specialist lubricant producers in this country, were to disappear as an independent company.

Century's prospect of surviving and expanding as an independent company

169. Finally, it is necessary to consider whether Century can be expected to survive successfully on its own.

170. The future of small or medium sized oil firms without their own crude oil refining capacity is dependent upon ability to finance their development and to survive oil shortages such as that of 1973/74. A merger would give Century the advantage of the much larger financial backing of BP, but we consider that the financial resources at present available to the company are adequate to finance the expansion and developments that it has in mind. So far as a further oil shortage is concerned, Century survived 1973/74 and should be in a somewhat stronger position to survive any similar crisis in the future.

171. We do not, therefore, consider that there is any serious risk of Century being unable to survive as an independent company.

CONCLUSION

172. We consider that the merger would be likely to have the following effects adverse to the public interest:

(a) it might restrict the development by Century of re-refining capacity and so delay, at least, the growth of re-refining in the United Kingdom;

(b) it would tend to produce some risk of a diminution of price competition in the sale of certain products;

(c) it would be likely to lead to a reduction of customer-orientated research and service to individual customers;

(d) it would mean the disappearance as an independent company of the largest independent specialist producer of lubricants in the United Kingdom, with the possible consequences indicated in paragraph 168.

173. We do not consider that there is any advantage to the public interest arising from the merger that would outweigh these disadvantages. We conclude on balance that the merger would operate against the public interest. We are unable to recommend any action that would remedy or prevent these adverse effects. We recommend, therefore, that the contemplated merger should not be permitted.

J G LE QUESNE (*Chairman*)

R L MARSHALL

C T H PLANT

J S SADLER

HARRY STREET

B S YAMEY

Y LOVAT WILLIAMS (*Secretary*)

28 April 1977