

7 Conclusions

7.1. Under the reference dated 21 December 1989 (see Appendix 1.1), made under the provisions of sections 69(2) and 75(1) of the Fair Trading Act 1973 (the Act), we are required to investigate and report whether arrangements are in progress or contemplation which, if carried into effect, will result in a merger situation qualifying for investigation, as defined in sections 64(8) and 64(1)(b) of the Act.

7.2. We describe in paragraph 2.1 the agreement under which British Steel plc has undertaken to acquire the business interests of C Walker & Sons (Holdings) Ltd (Walker), other than its aviation interests, subject to the acquisition receiving clearance from the appropriate regulatory authorities. Walker is the largest steel stockholder in the United Kingdom, with almost one-fifth of total stockholder sales.

7.3. The reference prescribes the test in section 64(1)(b) of the Act (the assets test) and provides that, if we find this test, or the alternative test prescribed in section 64(1)(a) (the market share test), satisfied, we shall exclude the other from our consideration. As is shown in Appendix 4.7, the value of the assets to be taken over exceeds £30 million.

7.4. We accordingly conclude that arrangements are in contemplation which, if carried into effect, will result in the creation of a merger situation qualifying for investigation. We have, therefore, to investigate and report whether the creation of the situation may be expected to operate against the public interest.

The scope of the investigation

7.5. Our investigation throughout has had to be mindful of the jurisdiction of the European Commission in relation to the merger. As stockholders, both British Steel and Walker sell a wide range of steel products. We have established that the majority of products sold by each firm, probably in the region of 80 per cent, are Paris products, ie they are subject to the provisions of the Treaty establishing the European Coal and Steel Community (ECSC) (the Treaty of Paris). The remainder are Rome products, ie subject to the Treaty of Rome. Under Article 66 of the Treaty of Paris mergers involving Paris products require authorisation by the European Commission. We considered submissions put to us during the course of the inquiry, described more fully in paragraphs 2.3 and 2.4, that since the great majority of steel products covered by the merger were Paris products, it was not open to us to reach public interest findings on the merger.

7.6. We have consulted leading Counsel on the matter. We are advised, and we accept (see paragraph 2.7), that the Treaty of Paris is part of United Kingdom law and that the Fair Trading Act must be applied in conformity with it. The Treaty of Paris gives the European Commission exclusive jurisdiction over the merger in respect of Paris products, and the Fair Trading Act could not be applied inconsistently or in conflict with the Treaty of Paris. Therefore, this Commission is precluded from investigating and reporting on whether, as regards Paris products, the merger may be expected to operate against the public interest. We retain jurisdiction, however, to investigate and report on the proposed merger in so far as Rome products (ie products not covered by the Treaty of Paris) are concerned and to consider the effect of the merger on the United Kingdom public interest in relation to these products. We have been advised that, in so doing, we may comment on the position regarding Paris products only to the extent necessary for a proper understanding of our conclusions. We accept this advice and have conducted the reference accordingly.

The steel stockholding market and the firms concerned

7.7. Some 60 per cent of steel products supplied in the United Kingdom reach the consumer through stockholders. The large number of products supplied by stockholders (stockholder products) can be classified in a number of broad groups:

- plates and sections;
- strip mill products;
- merchant bar;
- stainless products;
- tubes; and
- bright bar.

Steel reinforcements are not generally regarded as stockholder products but are sold by a few stockholders, including Walker. The importance of Rome products within these groupings is discussed below. While many of these stockholder products can be bought direct from the mill, particularly by larger customers, the stockholders' proportion of sales of 'stockholder products' has risen steadily from 39 per cent in 1973 to 60 per cent in 1989. Major factors have been the moves by consumers to reduce their own stocks and the ability of stockholders to provide a 'just in time' (JIT) service. There has also been a tendency for stockholders to add value by carrying out, on an increasing scale, fabrication and processing, particularly in producing blanks and profiles, of a type earlier undertaken by the eventual purchaser as part of his manufacturing operation.

7.8. There are estimated to be some 400 to 500 stockholders in the United Kingdom. These range from large stockholders, usually with a number of depots, and with nation-wide coverage supplying a complete range of stockholding products, to large numbers of small firms with a turnover of perhaps no more than 5,000 tonnes per annum.

7.9. The merger in contemplation would bring together the two largest stockholders in the United Kingdom. We estimate that in 1989 Walker held about 19 per cent of the United Kingdom stockholding market and British Steel, through its stockholding division, British Steel Distribution (BSD), held 15 per cent. The third largest supplier in the market, ASD Plc, held about 8 per cent and there were about 20 other large stockholders with shares ranging from 1 to 4 per cent.

7.10. British Steel is the main supplier of steel products within the United Kingdom. In 1989 it supplied 7.3 million tonnes of finished products to the United Kingdom market, 62 per cent of the total United Kingdom market for products within British Steel's range. It is also the major supplier to the stockholder industry. With its associates it supplies 58 per cent of stockholders' total purchases of products within its range, including around 85 per cent of the products bought by both Walker and BSD.

The position of Rome products in the merger

7.11. There are difficulties in establishing the precise proportions of Paris and Rome products in some categories. Broadly speaking, the Treaty of Paris covers the core activities of the steel industry in the early 1950s, ie basic steel products emerging from the larger mills, including heavy sections, plate, sheet and hot-rolled strip. Further processing tends to remove products from the Treaty's ambit. However, there have been developments in techniques of production and processing, particularly of strip products, since the Treaty was signed in 1951 and the definitions then adopted are not always easy to apply today. Within some categories, only the European Court of Justice could establish definitively whether a particular product is subject to the provisions of the Treaty of Paris. We have, however, consulted the European Commission and industry sources on where the line

should be drawn in 'grey areas', and have established that some Rome products now occur in most of the main stockholder product groupings.

7.12. We have identified the main Rome products sold by stockholders as tubes, bright bar, some narrow strip products including stainless narrow strip, some blanks, some profiles produced from plates, and some reinforcements. Tubes are the most important group, about half the total in terms of tonnage. All tubes are Rome products and are often dealt with by specialist stockholders. The tube group also includes structural hollow sections (SHS), the greater proportion of which are for use in the construction industry and are handled by stockholders as part of their general steels business. All bright bar, used primarily for fastenings (including nuts and bolts), is classified as a Rome product. The position on strip products, which tend to be handled separately by stockholders, is more complex. We understand that, within the sector, cold-rolled narrow strip (ie less than 500 mm in width), wider strip slit to 500 mm width or less by stockholders and simple rectangular blanks produced by guillotining such narrow strip are all Rome products. It also appears that blanks made from any type or size of sheet or strip also become Rome products where their fabrication involves more than shearing into rectangles, for example bending or notching. Plates and simple rectangular profiles cut from them are Paris products but more complex flame-cut profiles are Rome products. Within reinforcements, bars and rods are classified as Rome products if they have been bent, twisted or manufactured into mesh; otherwise they remain Paris.

7.13. For most stockholders, and particularly for those handling strip products, it is of no practical significance whether a product they handle is classified as Paris or Rome and the distinction is not noted in their records. Neither do available statistics make this distinction. Table 7.1 summarises our estimates, based on information from the firms, of the proportion of BSD and Walker sales of Rome products within the main product groups and, since estimates of the total sales of Rome products are not available, of their share of the total stockholder market in each of the main product groups. Fuller details, together with information on the stockholder share of the total market, are given in paragraphs 3.55 to 3.65 and associated tables.

7.14. The Rome products occur within most of the main stockholder product groupings listed in paragraph 7.7. Taken as a group they do not form a coherent sector of the market and have little in common. In attempting to categorise them in a way which reflected the nature of competition in the stockholder market, we started from the proposition that every Rome steel product sold by a stockholder has started life as a Paris product and then undergone some form of processing, either before it reaches him or while in his hands, that has changed its nature.

7.15. First there are products, of which tubes are the most important but also including bright bar, which have undergone the relevant processing before they reach the stockholder. For these he carries out the traditional stockholding function of breaking bulk and supplying to order with no processing except for perhaps simple sawing to length.

7.16. Secondly, there are those Rome products to which the stockholder adds some significant value through processing. These generally come to him as Paris products. For some products this processing is fairly straightforward, most importantly the decoiling and slitting of strip and cutting narrow strip to length. But there is also a group of products, in particular specialised profiles and fabricated blanks, where the stockholder himself is effectively carrying out a fabricating process significantly different from the normal stockholding role.

7.17. We have considered the public interest issues that arise in relation to these groupings. Some of these products can only be considered against the wider Paris groupings to which they relate. Even then the various categories of steel product cannot realistically be considered as if they occupied separate markets. We have, therefore, had to take account of their position within the wider stockholder market.

TABLE 7.1 Walker and BSD sales of Rome stockholder products, 1989

	<i>Walker sales</i>				<i>BSD* sales</i>				<i>Combined BSD/Walker % share of total stockholder sales within product group**</i>
	<i>Total KT</i>	<i>of which Rome products KT</i>	<i>Rome products as % of total</i>	<i>Walker % share of total stockholder sales within product group**</i>	<i>Total KT</i>	<i>of which Rome products KT</i>	<i>Rome products as % of total</i>	<i>BSD % share of of total stockholder sales within product group**</i>	
Tubes:									
SHS	71.6	71.6	100	22	68.2	68.2	100	21	43
Other welded	16.5	16.5	100	6	15.5	15.5	100	6	12
Seamless	14.2	14.2	100	10	10.5	10.5	100	7	17
Stainless	2.6	2.6	100	N/A	-	-	-	-	-
Total	104.9	104.9	100	14	94.2	94.2	100	13	27
Bright bar*	5.2	5.2	100	3	15	15	100	10	13
Plates and sections	390	25.4	6.5	25	219	22	10	14	39
Merchant bar	122	-	-	19	68	-	-	11	30
Strip mill	513	39.9	7.8	17	549.7	67	12.2	18	35
Stainless	28.9	4.6	15.9	25	15.1	2	13.2	13	38
Total all products	1,164.0	180.0	15.5	19	961	200.2	20.8	15	34

Source: MMC.

*Including British Steel associates.

**These percentages are rounded.

The public interest

7.18. Two broad groups of public interest issues arise in relation to these Rome products. First, competition issues arising from the horizontal effects of the merger in bringing together the market shares of BSD and Walker. Secondly, issues of vertical integration arising from the role of British Steel as the major supplier of steel products to the United Kingdom stockholder market. We discuss these as they relate to the wider market situation and as background to our detailed examination of the Rome products.

7.19. The main issues under the first head are the extent to which consumer choice in Rome products will be restricted, and the enlarged group perhaps able to charge higher prices. Alternatively, whether the group will be able to use its enhanced market position to attack competitors' market share. In this context we note that, while the combined BSD/Walker share of the stockholder market as a whole would be some 34 per cent, the share of the market for those Rome products alone which can be separately identified, ie tubes and bright bar, would be about 25 per cent see Table 7.1.

7.20. We have been told, not only by the main parties, that competition between stockholders in the United Kingdom is keen. There are several large stockholders with nation-wide chains of depots providing a complete range of products, other large single-site stockholders, some of whom specialise in a group of products, and large numbers of smaller stockholders, often geared to providing personal service to a limited range of customers and purchasing non-standard items from larger stockholders. Walker and BSD are the two largest of a limited number of full-range national chains. If they merge, consumer choice among independent stockholders of this type will be lessened. However, the distinction between stockholders by size of operation is not clear-cut and in general they do not appear to serve different classes of customer. There are some types of processing that the smaller man may not be equipped to handle, but he can usually turn to hire processors to carry out this work on his behalf. Multi-depot firms have the advantage of being able to provide a wider range of products 'in-house', but this is to some extent offset by the single depot's ability to buy at trade prices from other stockholders. Price and reliability are key factors from the buyer's point of view and the majority 'shop around' for competitive quotations and are prepared if necessary to split orders among different stockholders.

7.21. There are few barriers to entry to the industry on a small scale: little more is required than warehouse capacity, some working capital and perhaps simple craneage. Large-scale entry requires considerable resources, but some substantial new ventures have taken place, for example by ASD and, more recently, by Hall Engineering (Holdings) Plc. There have also been numerous examples of stockholder acquisitions over recent years involving both United Kingdom and foreign interests.

7.22. For all the main Rome product categories there are significant numbers of other stockholding depots of various sizes, including depots of other national chains, within the range of 25 to 50 miles which appears to be a typical supply area for most customers. We received no complaints about particular areas and have not identified any parts of the country which stand out from the general pattern.

7.23. There seem to be few operational advantages of scale, although there are likely to be some administrative economies. Walker has operated its last and most substantial acquisition, GKN Steelstock, as an independent operation and we have been told by others in the industry that the two continue to compete vigorously on price. Although British Steel has stated that it proposes to retain BSD and Walker as separate entities, Walker has co-ordinated buying and investment decisions for Walker and Steelstock, and at least the same degree of integration can be expected if the present merger takes place. Walker at present receives rebates from British Steel which take account not only of its volume of purchases within individual product groups but also of its total purchasing power. The size of Walker and BSD taken together compared with the group's nearest competitors may, however, justify additional rebates in return for the stability and regularity of purchases.

7.24. The evidence we received showed that some stockholders were worried by this possibility and considered that the level of rebates given by British Steel after the merger should be controlled. Most evidence from steel users related to the effects of the merger as a whole as it affected all products and could not be taken into account. However, the British Iron and Steel Consumers' Council (BRISCC) was able to give evidence relating to Rome products. BRISCC thought the merger was unlikely to have a significant effect on competition in cold-rolled narrow strip, bright bar or reinforcements. Some members, particularly smaller firms, were worried about competition in the tubes market, given British Steel's dominant position as a United Kingdom producer, but many believed the merger would not in practice result in any significant changes.

7.25. Vertical issues arise since British Steel is the major supplier to United Kingdom stockholders who take nearly 60 per cent of their supplies of products within the British Steel range from them. British Steel supplies both BSD and Walker with about 85 per cent of their total purchases of products within British Steel's range and other stockholders with nearly half of their supplies. One of the main concerns voiced to us by other stockholders during the inquiry was that, as suppliers, British Steel would be able to favour BSD/Walker by manipulating prices, with adverse consequences for other producers, stockholders and consumers. Offering BSD/Walker favourable terms could enable them to increase their share of the market by undercutting others. Concern was also expressed that British Steel would be able to favour its own stockholders in times of shortage and the possibility of this would tend to encourage other stockholders to 'keep in' with British Steel by placing a larger proportion of orders with them.

7.26. British Steel has argued that none of these courses would be in its interest, either as producer or distributor. The existing relationship between British Steel and Walker is so close that it would already be possible for British Steel to favour Walker as suggested; in itself the merger does not strengthen this possibility or weaken the position of other stockholders. Moreover, if British Steel ceased to supply other stockholders on reasonable terms they would be bound to turn to other suppliers, particularly imports. There are some disadvantages to importing, in particular the need for larger orders and longer delivery times, with the increased risks these involve, which give a built-in advantage to home supplies. However, other United Kingdom stockholders already draw 35 per cent of their supplies from non-United Kingdom sources, and competition to supply the United Kingdom market is keen.

7.27. Imports are already a significant source of supply for the stockholder market. Total imports of products within the British Steel range have increased by 64 per cent over the last five years and in 1989 accounted for 36 per cent of sales by United Kingdom stockholders. In some sectors of interest to the inquiry the proportion is higher; for example about half for bright bar, over 40 per cent for all strip mill products and about 25 per cent for SHS. Four-fifths of imports come from ECSC countries and ECSC producers have shown increasing interest in establishing themselves in the United Kingdom market, in particular by acquiring United Kingdom stockholder interests. There appear to be virtually no parts of the British Steel range where imports are not an alternative source of supply.

The competitive situation in the Rome products

7.28. Against this general background we looked at the main groups of Rome products identified in paragraph 7.7.

Reinforcement steels

7.29. Reinforcements are not part of stockholders' normal business and are fabricated and sold direct to buyers by specialist firms. BSD does not handle reinforcements and Walker, which has 4 per cent of the market, sells them only through three specialist depots, one in Grantham and two in Northern Ireland. British Steel does not manufacture the bars and rods used in fabrication, its business having been transferred some years ago to ASW Holdings Plc in which it has a 20 per cent equity interest. Subsidiaries of ASW hold less than 20 per cent of the fabricated market, the remainder being held by independent specialist fabricators. Against this background we concluded that the effects of the merger on reinforcements need not be further considered.

Bright bar

7.30. Bright bar is a product used primarily for fastenings, couplings and other engineering components, particularly for the automotive industries. British Steel does not itself manufacture bright bar but has a 50 per cent holding in United Engineering Steels Ltd (UES) which has well under a fifth of the United Kingdom market as a whole. More than half the United Kingdom deliveries go directly to the end user and the remainder is handled by a wide range of stockholders both by specialists and as part of general steels business. According to British Steel's estimates, the leading stockholders are Glynwed International Plc, Arthur Lee & Sons Plc and ASD, each with between 15 and 20 per cent of the market. BSD and Walker, together with UES, have in total less than 15 per cent of stockholders' sales. We concluded that the proposed merger would not lessen competition in this market.

Specialist profiles

7.31. Profiles, usually flame-cut from steel plate, are classified as Rome products when cut to irregular shapes. By tonnage, all types of profile account for about 10 per cent and 6.5 per cent respectively of BSD and Walker sales of all plate and sections, where their market share as a whole is some 40 per cent.

7.32. British Steel made available to us some results of an independent survey carried out for it in 1988 which suggested that BSD and Walker together carry out perhaps two-thirds of the profiling done by stockholders. This is, however, only a small part of the total market; the survey suggested that two-thirds of plate profiling is done by steel users themselves and two-thirds of the remainder by specialised profilers. Taking this as the total market, BSD/Walker's share is under 10 per cent. The equipment for flame cutting is relatively low cost and we have been told that some 150 firms in the United Kingdom provide a profiling service, including stockholders and profiling specialists, in competition with the alternative of in-house profiling by the steel user. The amalgamation of British Steel and Walker activities is unlikely to affect the competitive situation in this market.

Rome strip mill products

7.33. We described in paragraph 7.12 the difficulty of applying the Rome definitions in this area. British Steel was unable to provide us with estimates of the Rome proportion within BSD's sales of strip mill products. Walker, however, conducted for us a review of its sales over a recent period from which it estimated that just under 8 per cent of its sales of strip products were of slit strip and blanks which might be classified as Rome products. Given that the distinctions have little meaning in the market and are not followed in stockholders' records, it became clear from our contacts with the industry that it was not possible to establish precise market shares in this area. Informal contacts with other stockholders suggested some difference of opinion on how far their sales were to be classified as Rome products. The Rome element of the strip market does not, however, appear to be of major importance.

7.34. It was suggested that British Steel and Walker were leaders in developing the blanking side of stockholders' activities. However, entry to the strip product sector of the industry is comparatively easy at different levels. Basic decoiling and slitting equipment can be bought fairly cheaply; or capacity can be hired from specialist processors. A large modern development on a greenfield site could cost several million pounds, but a number of such developments have taken place in recent years, sometimes with foreign involvement. Overall there appears to be considerable surplus capacity for processing strip products.

7.35. Walker has invested heavily in modern processing equipment and sees this as a growth area for stockholders, particularly in fabricated blanks, where they hope to take over some part of the process currently carried out by manufacturers, particularly of domestic equipment, by providing JIT supplies of components for assembly. One other stockholder of strip products has announced a major new joint venture on these lines to supply components to the new Nissan factory at Sunderland. This is, however, a developing market which is very small at present and stockholders wishing to break into it will be competing as much with the end users as with other stockholders. Against this background we see no reason to assume that the Rome products are of more than minor importance within the strip product sector in relation to the merger situation, or that a merger by British Steel and Walker will have any significant effect in this area of increasing competition.

Tubes

7.36. Tubes are the most important group of products covered by our inquiry, accounting for over half of BSD/Walker's estimated sales of Rome products. The market shares of the merged group would be substantial. Together BSD/Walker would hold 27 per cent of stockholder sales of all tubes; within this total, however, they would account for 43 per cent of sales of SHS, as against 12 per cent of other welded tubes and 17 per cent of seamless.

7.37. Tubes are used for a wide range of purposes and are sold by a range of stockholders, including large specialist firms and general purpose stockholders. British Steel is a major producer and in 1989 supplied about 52 per cent of all tubes delivered to the United Kingdom market. However, the three categories of tube to a large extent supply different markets. SHS are sold by British Steel mainly through stockholders as part of their general steel business for use in the construction industry but more than half of other types of tube are sold direct to end users, particularly seamless tube for use in specialist applications, eg by the oil industry. In total British Steel supplied 55 per cent of stockholder requirements of tube in 1989, about 35 per cent being supplied by foreign producers and the remaining 10 per cent by a range of United Kingdom specialist producers. Walker took about three-quarters of its total tubes from British Steel, while stockholders other than BSD/Walker took 48 per cent of their tubes from them.

7.38. A number of tube producers and stockholders gave us views on the effect of the merger on the tube market. Among producers two expressed anxiety about the power of British Steel to discriminate on price after the merger. Two other producers, however, expected to continue to compete successfully. Some stockholders selling tube expressed concern about the effects of the merger; Brown & Tawse Plc, however, whom we believe to be the stockholder with the largest share of the tube market after Walker and BSD, felt able to compete successfully with the merged group and indeed expected to win business from it.

7.39. The share of the merged BSD/Walker group in sales through stockholders of other welded tubes would, at 12 per cent, be less than that of either Brown & Tawse or Murray International Holdings Ltd, and there are several other firms with significant shares of about 5 per cent. In seamless tubes the merged group's market share of 17 per cent would be higher but again there are three specialist suppliers with significant shares of the market, at least one of whom is foreign owned. Given the potential competition from imports and other United Kingdom tube-makers and the ability of large purchasers in particular to 'shop around' for their requirements, we do not think that the merger will adversely affect competition in these two sectors of the tube market.

7.40. SHS are the most important type of tube involved in the merger both in terms of tonnage handled by BSD/Walker and their share of the market. British Steel supplies 65 per cent of all United Kingdom purchases of SHS and about 85 per cent of both Walker's and BSD's purchases. SHS were an innovation developed by British Steel as an alternative to sections in the construction industry and some two-thirds of them is sold by general steel stockists alongside plates and sections. The remainder is sold through dedicated tube stockholding depots. With their growing popularity, particularly in the construction market, other competition has developed, both in the United Kingdom and from abroad, producing a cheaper cold-rolled version to challenge British Steel's hot-rolled product. Over the four years 1986 to 1989, British Steel estimates that the total market for SHS has nearly doubled from about 170 KT to 325 KT, but within this total British Steel increased sales by

only about 50 per cent compared with almost a threefold increase by other suppliers. As a result, British Steel's share of the United Kingdom stockholder market in SHS fell from 82 per cent to 65 per cent. Over the same period sales of SHS by other stockholders increased significantly faster than those of BSD and Walker. As a result BSD/Walker's combined share of SHS sales by stockholders fell from 58 per cent to 43 per cent. About 8 per cent of this 43 per cent share of the SHS market consists of sales to other stockholders, giving BSD/Walker about 35 per cent of sales direct to end users.

7.41. The SHS market is, therefore, an expanding one within which British Steel's share as a producer has been falling and BSD and Walker, with their heavy dependence on supplies from British Steel, have also lost ground. Given the very high proportion of its SHS supplies that Walker already takes from British Steel there seems little scope for British Steel to increase its share of the market through the acquisition, although it might be freed from any anxiety that Walker would at some stage in the future reconsider its purchasing policy. There are other suppliers and their deliveries to the market have been rising rapidly. At the stockholding level the greater part of SHS is sold alongside general steels, where BSD and Walker also have significant market shares. However, there are depots of competing stockholders selling SHS throughout the country, and competition comes both from larger chains and from smaller stockholders who are able to purchase within the trade to supplement their own supplies. Consumers also 'shop around' and are prepared to split orders among stockholders. The costs of entry to tube stockholding are very low, since no significant processing is required. Against this background it seems unlikely that the consolidation of BSD/Walker's market shares will lead to any significant diminution of competition.

Conclusion

7.42. Accordingly, we conclude that the merger may not be expected to operate against the public interest in respect of the groups of Rome products which we have identified.

Further observations

7.43. Our inquiry has shown that for some types of product, particularly strip products, the distinction between Rome and Paris in classification no longer reflects the structure and practice of the industry. It fails to take account of the changed nature of the industry and, in particular, the developments in processing technology now widely adopted by steel stockholders. This can lead to arbitrary and confusing classifications and anomalies in the consideration of competition issues.

M S LIPWORTH (Chairman)

R O DAVIES

M R HOFFMAN

G C S MATHER

C A UNWIN

S N BURBRIDGE (Secretary)

16 March 1990