

7 Conclusions

The merger situation

7.1. Under the reference made on 19 September 1990 under the Fair Trading Act 1973 (the Act) (see Appendix 1.1) we are required to investigate and report whether arrangements are in progress or in contemplation which, if carried into effect, would result in the creation of a merger situation qualifying for investigation, as defined in section 64(8) of the Act, in that enterprises carried on by or under the control of British Sugar plc (British Sugar) would cease to be distinct from enterprises carried on by or under the control of Tate & Lyle PLC (Tate & Lyle).

7.2. The reference prescribes the test in section 64(1)(b) of the Act (the assets test) and provides that if we find either 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. The assets of British Sugar exceed £30 million (see Appendix 3.4, Table 2). The assets test is therefore satisfied and in accordance with our terms of reference we have excluded from consideration the test prescribed in section 64(1)(a) of the Act.

7.3. On 7 September 1990 Tate & Lyle announced its intention to make an offer for British Sugar which had been put up for sale by the parent company, Berisford International plc (Berisford). Tate & Lyle was included by Berisford in the short list of potential purchasers of British Sugar and submitted an offer by the deadline of 28 November 1990. It has since been announced that Berisford has entered into a provisional agreement for the sale of British Sugar to Associated British Foods plc (ABF). The Secretary of State for Trade and Industry had already announced that the bid by ABF for British Sugar would not be referred to us. Completion of the transaction is, however, dependent on a number of conditions being met. Since the announcement Tate & Lyle has told us that its offer for British Sugar has not been withdrawn and that it would still wish to proceed with the offer if the transaction with ABF were not completed.

7.4. We therefore conclude that arrangements are in contemplation by Tate & Lyle for the acquisition of British Sugar which, if carried into effect, would result in the creation of a merger situation qualifying for investigation.

7.5. Consequently we have to consider whether the creation of the merger situation we have identified may be expected to operate against the public interest.

The market for sugar and related products

7.6. The United Kingdom market for sugar is governed by a system of production quotas and price support within the EC sugar regime that severely limits the scope for, and the extent of, competition between suppliers and generally keeps the price of sugar well above the world market level. The system is described in paragraphs 4.6 to 4.15 and in Appendix 4.1. Total demand in the Community is below current production of sugar produced from beet and there is a large surplus, about 3 million tonnes per annum, of quota sugar available for export. The United Kingdom is, however, very much in deficit on beet sugar, with output roughly one half of total consumption. The deficit is made good by sugar refined from raw

cane sugar imported almost entirely from ACP¹ sources of supply. After account is taken of this, United Kingdom production and consumption are roughly in balance at about 2.25 million tonnes per annum WSE,² with imports and exports of the finished product in recent years at about 200,000 tonnes in each direction.

7.7. Over 90 per cent of United Kingdom consumption of sugar is supplied by British Sugar and Tate & Lyle Sugars (TLS), either directly or through merchants; the remainder is imported from the Continent. British Sugar is the sole processor of domestically-produced sugar beet, with United Kingdom sales in 1988/89 of about 1.2 million tonnes, and TLS the sole refiner of imported raw cane sugar, with total sales last year of a little over 1 million tonnes. The United Kingdom joined the European Community (EC) after the regime for beet sugar was well established, and the arrangements for imported cane sugar provide TLS with lower processing margins than those enjoyed by British Sugar and other beet sugar producers; although, as explained more fully below, the amount of processing required by TLS to produce white sugar is rather less. The effect of this difference in margins on the competitive situation of Tate & Lyle is discussed further in paragraph 7.18.

7.8. Merchants play an important role, particularly for the smaller customer, handling sugar from both United Kingdom producers and from imports, with sales of over 1 million tonnes almost equally divided between sales on own account and 'nominally merchanted' sales (see paragraph 4.40). Since our 1987 report,³ the total amount of merchanting has remained broadly the same but the number of merchants has declined; there are now only three principal merchants who have tended over the last few years to some extent to specialise in particular aspects of the market.

7.9. In addition to sugar (sucrose) there are other sweeteners in the market (see paragraph 4.33). Isoglucose, made from corn but directly competitive with sucrose, has been brought within the EC sugar regime and Tate & Lyle holds all the United Kingdom quota of some 27,000 tonnes. Although isoglucose is effectively interchangeable with liquid sugar the EC quotas are small and the regime is unlikely to change in the foreseeable future in a way which would allow effective competition. Tate & Lyle also supplies some 20 per cent of the United Kingdom glucose market of some 520,000 tonnes. Glucose has different characteristics from sucrose and for many purposes is not an effective substitute.

7.10. Molasses is a by-product of both beet sugar production and the cane refining processes. Total United Kingdom consumption of molasses in 1988/89 amounted to over 1 million tonnes, 76 per cent of which was used for animal feeds, 20 per cent for yeast production and fermentation and 4 per cent in other ways. Both beet and cane molasses, blended together in different proportions, are used in the production of yeast. Beet and cane molasses both go into animal feed production but not for the same purpose or type of animal feed. Beet molasses is the main product used for the production of citric acid.

7.11. United Molasses, owned by Tate & Lyle, supplied about 37 per cent of the United Kingdom market for molasses in 1988/89 and British Sugar about 35 per cent of the market, including molasses used in animal feed production by its own animal feed company (constituting about two-thirds of its total production of molasses). The merged company would therefore supply about 72 per cent of the total of molasses used in the United Kingdom.

Recent developments

7.12. Since the mid-1980s there have been a number of important developments in the United Kingdom market.

¹ African, Caribbean and Pacific countries.

² White sugar equivalent.

³ *Tate & Lyle PLC and Ferruzzi Finanziaria SpA and S & W Berisford PLC: a report on the existing and proposed mergers.* Cm 89, February 1987.

7.13. First, British Sugar has abandoned its aggressive pricing strategy towards TLS and has told us that it now prices its sugars as high as it considers the market will bear without drawing in imports. TLS's prices have also risen and the profitability of both companies has improved considerably.

7.14. In addition, in 1988 the EC Commission reached a decision on the complaint against British Sugar brought by Napier Brown & Company Ltd (Napier Brown), one of the leading merchants, alleging abuse of a dominant position in relation to that company's entry in 1985 into the market for packet sugar. British Sugar was fined 3 million ECU (about £2 million). Soon after the Commission's decision in 1986 to initiate proceedings, British Sugar introduced an EC Competition Law Compliance Programme (see paragraph 2.11), gave specific undertakings to the Commission on its behaviour to Napier Brown and on pricing practices generally to merchants, and laid down general principles governing supply and pricing practices to customers.

7.15. Another major development concerned the cane refining margin. Our 1987 report had drawn attention to structural problems of the Common Agricultural Policy (CAP) which put Tate & Lyle at a serious disadvantage and recommended that the Government should make efforts to ensure that the cane refining margin be increased to allow TLS to compete effectively. Following negotiations within the EC, additional Community aid has been paid from 1987/88 to cane sugar refining in the EC, with Tate & Lyle the main beneficiary, and the United Kingdom Government was itself authorised to provide national aid. Both have contributed to the company's increased profitability (see paragraph 3.25). The EC Commission proposals for arrangements after July 1991 provide for the continuation of EC aid but for the withdrawal of the national aid.

7.16. The movement within the EC towards a single market after 1992 and the GATT (general agreement on tariffs and trade), taken with other pressures for freer trade between the EC and the outside world, may lead to major changes in the EC sugar regime. In particular, both the levels and system of institutional prices and the allocation of quotas might be affected. Such developments towards freer trade could have important consequences not only for the position of both parties to the proposed merger but also for the competitive situation in the EC sugar market.

The public interest issues

7.17. Against this background, we have considered the effects of the proposed merger on the competitive situation in the market for sugar and related products, including effects on prices and service, on the role of imports, and on the position of the merchants; and the consequences of the merger for employment and efficiency, the interests of farmers and the future of cane refining in the United Kingdom.

Effects on competition: prices

7.18. As described in Chapter 4, competition in the United Kingdom sugar market is markedly affected by the unusual features of the sugar regime. First, neither of the two dominant producers can profitably increase production beyond permitted limits and this reduces the incentive for either company to cut prices in order to gain market share; no other producer can enter the market. Secondly, as noted in paragraph 7.7, cane refining receives lower institutional margins than beet processing. The extent of TLS's disadvantage under the EC sugar regime cannot be exactly measured. It is clearly less than the differential between the beet processing and cane refining margins would suggest, since the former has to cover the whole extraction process from the reception of the raw beet while cane refining makes use of a semi-processed product. As the 1987 report explained, in principle the question could be approached by means of a comparison of the return on capital in the two types of manufacture. For the last four years such a comparison would in fact show TLS earning a higher return on capital than British Sugar (see Tables 3.5 and 3.8). However, when the aid is excluded from TLS's profits British Sugar's returns are now better than those of TLS. Other factors, such as problems over the valuation of fixed assets, mean that too much emphasis should not be attached to comparisons of return on capital achieved by the companies. However, we accept that there is a disadvantage to Tate & Lyle, although it is the stronger in some products. Overall Tate & Lyle is likely to be a price follower and British Sugar the dominant influence in determining the price level-as indeed emerged in the mid-1980s price war.

7.19. The proposed merger would result in over 90 per cent of the United Kingdom market being supplied directly or indirectly by a single company. TLS has nonetheless argued that a merger with British Sugar would have only minor effects on competition. The company has stated that there is at present no real competition in the market, that British Sugar is the price leader, and that the level of United Kingdom prices is primarily set by British Sugar in relation to the price of imports.

7.20. Retail sales are highly concentrated; for each company ten customers accounted for 95 per cent of retail sales. The industrial sector is less concentrated with 75 per cent of Tate & Lyle's industrial sales going to its 12 largest customers, and British Sugar's ten largest customers taking about 60 per cent of its sales. Most of the customers giving evidence to us, including the bodies representing most of the larger industrial users and retailers, have opposed the merger on the grounds that it would reduce competition and lead to higher prices; almost all those who did not oppose the merger sought wide-ranging safeguards against the misuse of the merged company's position. More particularly, industrial users and retailers value the opportunity to seek competing quotations and consider that this enables them to secure reductions which, while small in percentage terms, can be significant in total. For most customers the list price is a starting point for negotiation and discounts vary widely. British Sugar gave us figures which showed significant switches in sourcing by some major customers from one year to another and said that it often competed strongly, on both price and service, to secure accounts from TLS in strategically attractive sectors of the market, particularly in the valued area of retail sales; it had found that TLS for its part defended its sales of liquid sugar particularly fiercely.

7.21. It is not easy to assess the effect on market prices since 1986 of the contacts between the two companies on pricing and discounts described in Appendix 2.1 which were discontinued last summer. British Sugar has argued that the initial contacts simply informed TLS of the change in British Sugar pricing strategy and Tate & Lyle told us that later exchanges only speeded up the dissemination of information which would have become quickly available in the market. However, the fact that the two companies thought it worthwhile to exchange information and discuss the poaching of customers suggests some concern on each side about the competitive potential of the other; the discussions can thus reasonably be expected to have had at least some effect on competition and prices in the market.

7.22. In our view the merger would remove a significant element of day-to-day price competition which we have been told is valued by customers. Moreover, the merger would remove any possibility of future competition between United Kingdom sugar producers, were the constraints imposed by the sugar regime to be modified. The effect of the merger on the general level of United Kingdom prices is considered further in paragraphs 7.25 to 7.29.

Effects on competition: service

7.23. Concern was expressed to us by users that the merger would lead to diminution in the service and in the range of products offered. The service offered by suppliers is of considerable importance to customers, particularly industrial users. Many have no significant storage facilities and rely on frequent deliveries, sometimes out of hours and at short notice. British Sugar told us, for example, that it was delivering round the clock at two- to three-hour intervals to one customer.

7.24. British Sugar and Tate & Lyle told us that the merger would not lead to any narrowing of their range of sugars and that maintenance of high levels of service would be a major weapon in discouraging increased imports. On the other hand a good deal of the service offered by the two United Kingdom companies could not be readily duplicated by foreign suppliers or by merchants without the expectation of a substantial and continuing market in the United Kingdom. While we accept that TLS intends to maintain existing levels of service and range of products as long as they remain commercially viable, we think there is a serious risk that over time a monopoly supplier would be less inclined to put itself out to meet the special service requirements of individual customers and more likely to levy a full charge for such requirements.

Effects on competition: imports

7.25. Both Tate & Lyle and British Sugar laid stress on the availability of imports from other EC countries as the main safeguard against any attempt by the merged company to raise prices. British Sugar stated that it had already raised prices to near the ceiling at which it would expect imports to be drawn in and would avoid any price increase which might lead merchants or others to establish facilities for handling a continuing higher level of imports. Tate & Lyle expected the merger to lead to some increase in imports, irrespective of price levels, to meet customers' wishes for secure alternative sources of supply. Tate & Lyle stated that if the merger were allowed it would, as a matter of policy, reduce prices by a small amount per tonne to reassure customers and to keep 'second sourcing' of imports as low as possible. Even so, it thought that initially imports would rise by some 200,000 tonnes per annum but that with continued restraint on its part imports might fall back to about 100,000 tonnes above present levels. A number of sugar users told us in response to a questionnaire (see paragraphs 6.131 to 6.133) that they would seek alternative supplies, including imports, if the merger went ahead and a substantial minority envisaged seeking a significant proportion of supplies from alternative sources, even though the majority thought that import prices would be higher and that there would be barriers to importing.

7.26. British Sugar argued that while United Kingdom prices remained in their present relationship to the restitution price, it was not worthwhile for an EC exporter to seek to compete in the United Kingdom market; but, if United Kingdom market prices were to increase by even a small amount, then imports would be drawn into the United Kingdom. Tate & Lyle argued that sugar would be readily available for export to the United Kingdom in response to comparatively modest increases in prices. Both Tate & Lyle and British Sugar produced figures to support their view that prices were already pitched at the level just below the point at which EC sugar would be diverted from restitution. Broadly similar figures were put to us by one of the merchants. The comparisons put to us related to average prices and ignored quality differences. For the individual customer the extent to which imports provide a competitive alternative will depend on a number of factors including the discounts from list price he is already receiving, the type of sugar required, the importance he attaches to second sourcing and his scale of operation.

7.27. The ready availability of sugar for export to the United Kingdom was disputed by several of those giving evidence and a number of general difficulties were drawn to our attention. Suppliers in other EC countries tended to sell to established home market customers and the restitution system meant that supplies were often earmarked for export some time ahead. Buyers usually had to take on the uncertainties and delays of securing payment of monetary compensatory amounts (MCAs). Sugar available was not always of the quality required by United Kingdom users. Any appreciable increase in demand for imports would require substantial investment in handling facilities by merchants or suppliers. All these factors, together with the levels of service required by many users, suggested to us that imports would only become a major force in the market if foreign suppliers saw the opportunity of significant continuing demand. We also noted that in spite of apparently substantial differences in the price levels among some other EC markets, and the absence in their case of obstacles such as MCAs, there appears at present to be little trade between them. On the other hand, Tate & Lyle argued that the role of the merchant was more developed in the United Kingdom and that the merchants could be expected to take advantage of comparatively smaller differences in price.

7.28. Several witnesses had found it extremely difficult to get supplies from EC sources earlier in 1990 to meet a shortfall and some linked this with Tate & Lyle's admitted discouragement of imports. Tate & Lyle's account of the matter (see Appendix 2.1) explained that as a result of indications of Tate & Lyle's attitude to imports the merchants 'recognise where their best interests lie'. Tate & Lyle had, however, found it necessary to warn Ferruzzi Finanziaria SpA, De Danske Sukkerfabrikker, and Irish Sugar plc (the three main sources of EC sugar sold to the United Kingdom) that if acceptable levels of shipments to the United Kingdom market were exceeded TLS would retaliate in their own markets. Acceptable levels do not appear to have been exceeded. We would expect the merged company to be in an even stronger position to act in this way to deter imports.

7.29. Taking all these factors into account we do not accept the arguments of the main parties that imports, or the threat of imports, would provide sufficient safeguards on prices and consider that a merger would be likely to lead in due course to prices for sugar in the United Kingdom higher than would otherwise exist.

Position of merchants

7.30. Some merchants and users were anxious that without safeguards the merged company, either by withholding supplies or through its pricing policies, would be able to weaken the position of the merchants and undermine their ability to compete. On the other hand, it was argued that after a merger many customers would be anxious to secure their access to alternative sources of supply, even at higher cost, and would turn to the merchants for this. British Sugar drew attention to the undertakings on its behaviour to merchants contained in its Compliance Programme (referred to in paragraph 7.14). Tate & Lyle has stated that it would be prepared to abide by these undertakings. We therefore do not expect the position of the merchants to be greatly affected by the merger.

Markets for related products

7.31. Tate & Lyle's interest in other sweeteners and molasses has been noted in paragraphs 7.9 to 7.11. There are some advantages to a producer in being able to offer a full range of sweeteners. The small isoglucose market is tightly controlled by quota and although glucose is to a limited extent substitutable for sucrose, neither are products in which British Sugar has an interest. The prospective merger seems unlikely to lead to any significant reduction in current levels of competition in these markets and we do not see TLS's interests as more than a marginal detriment.

7.32. British Sugar and United Molasses (owned by Tate & Lyle) each provide about one-third of total United Kingdom supplies of molasses of about 1 million tonnes, but over two-thirds of British Sugar's production is consumed in its own animal food operation. Beet and cane molasses have different properties and although there is some overlap in their use, for the majority of purposes one is preferred. We have received no evidence of concern from consumers. The merger can be expected to result in some reduction of competition in the sector of the market where cane and beet molasses are substitutable but not of itself sufficient to create a public interest detriment.

Effects on employment

7.33. The immediate consequences of the merger for employment would not be large. Tate & Lyle estimates that efficiency gains from combining the two companies' head office functions of central finance, planning systems, sales and marketing could lead to a loss of about 150 jobs. In addition, the rationalisation of speciality sugar production might lead to loss of about 100 jobs. In the longer term it seems likely that the process of rationalising British Sugar factories will continue and might be accelerated as a consequence of the merger. On the other hand, this programme might be affected by any shift of cane refining to beet factories, discussed further in paragraph 7.49, which would also have employment consequences for the two cane refineries.

7.34. The main employment implications would arise, however, if it were thought that the proposed merger would safeguard the future of cane refining in the United Kingdom or to avert closure of the TLS refineries at Thames and Greenock. TLS employs in total just over 2,000 people and of these about 1,200 and over 200 respectively are employed at these two refineries. The effect of the proposed merger on the security of cane refining in the United Kingdom and on the future of the cane refineries is discussed in paragraphs 7.40 to 7.51.

Benefits to efficiency

7.35. Tate & Lyle has told us that were the merger to take place it would expect the programmes for improving efficiency already established by both companies to continue broadly unchanged. In addition, it would see some scope for modest rationalisation of production between the Thames refinery and British Sugar factories, bringing with it some reduction in the capital expenditure needed to refurbish Thames.

There would also be significant savings in central overheads and distribution. Tate & Lyle estimated that in total these savings would come to approximately £10 per tonne, and would support the reduction in prices which the merged company would wish to make, described in paragraph 7.25. While their precise amount is difficult to assess, we accept that the merger would bring with it some efficiency savings. However, the structure of the market and the role of imports in determining the general price level provide little incentive for such savings to be passed on to the customer.

7.36. Tate & Lyle has also suggested that the merged company-which we note would be, by a short head, the single largest sugar company in the EC-would be in a more effective position to compete with the large companies that have been formed within the continental EC. With the development of the single market, companies are more likely to develop an EC-wide strategy and there have been a number of mergers in the continental sugar industry over recent years; in particular two large French/Italian and Belgian/German groups have been formed. Even so, British Sugar on its own remains the third largest enterprise within the EC sugar market and both it and TLS are large enough to benefit from available economies of scale. We agree that other things being equal the relative position of a single United Kingdom sugar producer in the EC market would be strengthened. Effective competition between the new larger companies seems unlikely, however, without major changes in the sugar regime, for example by allowing quotas to be transferred between member states. This would be strenuously opposed by beet growers and seems unlikely in the near future.

Interests of farmers

7.37. The National Farmers Union (NFU) expressed concern to us about a number of issues affecting farmers' interests, on which it considered undertakings should be sought from Tate & Lyle if the merger were to be allowed (see paragraphs 6.101 to 6.105). A number of these undertakings, and particularly those relating to the sugar beet contract and the working of the inter-professional agreement, arise from concern about the NFU's existing need to bargain with a monopoly buyer of beet and not directly from any changes and possible adverse effects arising from the merger.

7.38. Two points raised by the NFU are, however, directly connected with the acquisition. First, the NFU was concerned whether Tate & Lyle, as a cane sugar refiner, would fully defend the interests of United Kingdom beet producers, in particular maximum beet quotas for United Kingdom growers under the EC regime and the retention of the quota within the United Kingdom. Given the relative profitability of beet processing we find it difficult to see why, unless there were a marked fall in United Kingdom consumption, Tate & Lyle should wish either to cut back on its activity in the United Kingdom or to transfer quota away from the United Kingdom if that were at some stage allowed under the EC regime. Tate & Lyle, the NFU and the Ministry of Agriculture, Fisheries and Food have all suggested to us that the merger should make it easier to establish a United Kingdom negotiating position in such matters as quotas.

7.39. The second concern was that farmers' representatives should still be able after the merger to secure the information about the costs and profitability of beet processing needed for effective negotiations over the annual beet contract. At the time of the 1981 merger, Berisford undertook to maintain British Sugar as a separate subsidiary and to continue to publish accounts in a form which gave information comparable with that provided until then in the British Sugar Corporation's own accounts. While it would probably not be practicable to continue to maintain separate accounts for the two sugar businesses after the merger, if the rationalisation outlined in paragraph 7.35 took place, we consider that it would be desirable for the beet growers to continue to have access to the information they need. Tate & Lyle has indicated it would be its intention to provide the necessary information on costs of beet processing if the merger were to take place.

Future of cane refining

7.40. Tate & Lyle has put to us as a major justification for the merger that it is the best way to safeguard the continued refining of cane sugar in the United Kingdom and thus the fulfilment of the EC obligations under the Lomé Convention; on the other hand acquisition by any other party, and particularly by another

EC beet processor, would put the future of cane refining in the United Kingdom at risk. Tate & Lyle drew to our attention the finding of the 1987 report that there was a public interest in maintaining United Kingdom facilities to refine cane sugar.

7.41. There are two separate but linked aspects of the proposed merger to be considered in this context. First, there is uncertainty caused by the arrangements for cane sugar refining under the EC sugar regime; secondly, there is more immediate uncertainty created by the forthcoming sale of British Sugar and the consequences of a sale either to TLS or to another bidder. In addition, were the merger to proceed, the future of cane refining in the United Kingdom would not necessarily equate with that of the two cane refineries operated by TLS-Thames and Greenock.

7.42. The treatment of cane refining and in particular the future of the margin aids is uncertain; it seems likely that EC approval of the national aid will shortly be withdrawn and that adjustment aid, if continued, will be guaranteed only for comparatively short periods ahead. It has been suggested that a merger might make it easier for the United Kingdom Government to develop a stronger position in future EC discussions about the sugar regime. It seems equally likely, however, that other EC members will see the improved security of TLS's position as an argument for cutting back or withdrawing the cane refining aids.

7.43. Tate & Lyle has argued that without the merger it would face a continual threat of price competition from British Sugar supported by the differential margin. An acquisition of British Sugar by another EC beet processor would in Tate & Lyle's view make it likely that the new owner would adopt an aggressive price strategy, and Tate & Lyle would see a risk even with a non-sugar acquirer. Only if this risk were to be removed by a merger of Tate & Lyle and British Sugar would Tate & Lyle feel able to make the investment required to keep the cane refineries in operation. Indeed Tate & Lyle has told us that, regardless of the future of the national and adjustment aids, if the merger took place it would feel sufficient confidence to go ahead with the substantial investment programme needed to refurbish the Thames refinery, and that it would undertake to continue to operate the port refineries, provided that there were no other major changes in the EC treatment of cane refining which made it unprofitable.

7.44. While an EC beet processor with surplus quota sugar might see the United Kingdom as an attractive market and British Sugar as an advantageous purchase, a pricing strategy designed to force TLS out of the market would be high-risk and costly in the short term. Not only would profits from British Sugar be cut substantially in the short term but it is likely that British Sugar would need to import sugar at clearly unprofitable prices. Such action would be open to immediate challenge under Article 86 of the Rome Treaty as abuse of a dominant position.

7.45. While it would be possible for buyers without existing sugar interests to follow a similar pricing strategy, it seems improbable that they would do so, given the fixed United Kingdom quota available to them. At present British Sugar, as price leader, is able to maintain prices in the United Kingdom at levels which give a very satisfactory return without drawing in imports. We do not consider it likely that the new owner of British Sugar would find it worth taking substantial losses from a new price war to drive out Tate & Lyle, in order to seek subsequent benefits from a higher price level. Moreover this would then allow room for substantial imports from EC beet processors, a development which might later stimulate them to mount a further attack on the United Kingdom market.

7.46. In short, we do not think that failure to approve the merger will put the TLS refineries at immediate risk or that a new owner of British Sugar would follow a strategy which attacked TLS's profitability. Even when margin aids are left out of account, this level of profitability is not unsatisfactory for a commodity business. Tate & Lyle has argued that, even if no immediate hostile action were taken, the continuing uncertainty would make it unlikely that the Tate & Lyle Board would approve substantial investment needed to update the Thames refinery, which, without a merger, it estimated over the next ten years at [*]. Tate & Lyle would continue on a hand-to-mouth basis to manage the refineries for cash, as long as they remained profitable. Therefore, if the merger were not allowed to proceed, Tate & Lyle foresaw the gradual run-down and closure of the refineries as a real possibility and, were margin aid then withdrawn, it regarded the refineries as having no future.

*Figure omitted. See note on page iv.

7.47. We note, however, that in spite of the uncertainties of the last five years, Tate & Lyle has invested some £57 million in the two refineries and other facilities, eg a substantial upgrading of the packing operation. For the current financial year, ending in September 1991, the Tate & Lyle Board has authorised capital expenditure by TLS of some [*], a rate well above the average for the preceding five years. As explained above, we do not foresee that the acquisition of British Sugar by another buyer would in itself change market conditions in the United Kingdom in such a way that it would no longer be in Tate & Lyle's interests to invest sufficient to keep the refineries operational. We accept that the approval of the merger would give Tate & Lyle increased confidence in the immediate future and that this could lead to either greater or more rapid investment at Thames than might otherwise take place, as is illustrated by Tate & Lyle's offer of an undertaking to carry out a substantial investment programme over the next four years if the merger is approved. However, we note that extra confidence for Tate & Lyle is the obverse of loss of potential for competition in the market.

7.48. In any event it remains possible in the longer term that, even with the merger and the proposed investment programme, Tate & Lyle would withdraw from the port refineries. Tate & Lyle has made it clear to us that it would not continue to operate the port refineries if this became unprofitable. Against a background of continued pressure for cuts in EC agriculture support there may be changes in the beet sugar regime which adversely affect sugar producers' margins and which are then carried through into the cane sector. Tate & Lyle's cane operations would remain vulnerable to such changes and Tate & Lyle has many other interests which require finance; management and shareholders might well decide that funds are better invested elsewhere. At such a point the EC would be faced with the need to ensure that its commitment to the ACP countries continued to be met.

7.49. In considering the effect of the merger on the future of cane refining in the United Kingdom there is also the question of whether it would be feasible and economically desirable to transfer cane refining to the beet processing factories. British Sugar has suggested that it would be possible, out of season, to refine all the cane which is currently processed at the port refineries in five of its factories. It provisionally estimated a direct investment requirement of some £70 million. Tate & Lyle has not yet been able to look into the British Sugar calculations in any detail but its first examination suggested that in addition to the logistic difficulties of storing the raw cane sugar which is currently delivered all the year round and transporting it to the factories there would be other additional costs which would make the process uneconomic. The effects of transferring part only of the present cane sugar refining would have to be balanced against the effects on the port refineries of working at less than their present capacity. In the longer term, however, the possibility of partial or complete transfer cannot be ruled out, taking into account such actions as the option (already considered by TLS) of turning Thames into a bulk refinery with some reduced output levels, the value of the Thames site, and the chances of the merged company deliberately cutting back on cane refining to pursue a higher price strategy.

7.50. Tate & Lyle's position is stronger than at the time of our last report as a result both of the margin aid provided through the EC and of the continued absence of a price war with British Sugar. There are clearly a large number of uncertainties hanging over the future of cane refining and of the refineries, whether or not the merger takes place. In our view, however, the blocking of the merger would not materially worsen their prospects. As we have explained, we doubt that new owners of British Sugar would see it in their interest to renew the kind of price war that might threaten the existence of TLS; at the same time only a merger between TLS and British Sugar could make certain of avoiding this possibility and give Tate & Lyle the confidence it seeks to underpin its investment programme. A merger may bring some synergy benefits which would also help improve prospects for cane refining; on the other hand, were Tate & Lyle to buy British Sugar the chances of continuing EC aid for the cane refining industry would deteriorate. Tate & Lyle has made it clear that it will only continue to operate the refineries as long as they remain profitable. In the longer term other developments, including possible changes to the sugar regime, are likely to be of more importance in determining the future of the United Kingdom cane refining industry than whether the merger goes ahead or not.

7.51. Taking all these factors into account we consider that a merger might improve the outlook for cane refining and the port refineries over the next few years, but that it would not in itself necessarily ensure the survival of the refineries beyond that period. We therefore conclude that the merger would not safeguard the longer-term future of cane refining or of the port refineries.

*Figure omitted. See note on page iv.

Acquisition of other businesses

7.52. Berisford is putting up for sale with British Sugar three related businesses, a joint venture in beet processing in Poland and two seed pelleting firms. Tate & Lyle has indicated that it is bidding for the whole package. We do not consider that their acquisition will raise competition issues.

Conclusions

7.53. We have indicated above that competition in the United Kingdom sugar market is severely constrained by the EC sugar regime. Production and refining quotas limit the extent to which the two suppliers can take market share from one another and, because of the difference in cane and beet margins, Tate & Lyle sees itself as a price follower. Nevertheless, within these constraints there is competition, both on price and service, to secure particular accounts-competition to which customers attach importance. A considerable number of users opposed the merger for fear of loss of this competition and most of those who supported it did so subject to various undertakings being sought. TLS has told us that it expects to make an initial price cut if the merger takes place, but has made clear that this will be designed to reassure customers and no more than is needed to keep 'second sourcing' from imports to an acceptable level. At current price levels such imported supplies would be likely in any event to involve the users concerned in extra expense.

7.54. Although Tate & Lyle and British Sugar have both argued that imports will act as an effective check on prices, we have received other evidence, discussed in paragraph 7.27, which suggests a number of institutional and practical barriers to the importation of EC sugar. We are bound also to take into account the evidence from Tate & Lyle that steps have been taken to discourage other European suppliers from exporting to the United Kingdom market. We do not therefore see imports, or the threat of imports, as an effective check on the ability of the merged company to raise prices. We consider that over time average market prices in the United Kingdom will tend to be higher as a result of the merger, both directly, and indirectly by full charging for services provided.

7.55. We think therefore that, even within the present constraints, the merger carries the danger of a loss of competition leading to increased prices. It would also rule out for the future any prospect of greater competition between the two companies in the United Kingdom market if changes in the present EC regime opened the way for it.

7.56. Against these perceived detriments Tate & Lyle has argued that the merger would secure the future of cane refining and of the port refineries in the United Kingdom, which otherwise would be at serious risk. There are, however, a large number of uncertainties hanging over the future of cane refining and of the port refineries. While a merger might increase the security of both for the next few years, we do not think it would by itself have a significant effect on their longer-term future. We also noted the prospect of efficiency gains from the merger, although the structure of the market and the role of imports in determining prices provide little incentive for such savings to be passed on to the consumer. Overall we do not think that any advantages arising from the merger would offset the perceived detriments to competition identified above.

7.57. Accordingly we conclude that the merger situation may be expected to operate against the public interest.

Remedies

7.58. Under the provisions of the Act, we are required to consider what action (if any) should be taken for the purpose of remedying or preventing the adverse effects of the merger we have identified above.

7.59. A number of suggestions for safeguards and undertakings have been put to us. We discuss here only those related to the detriments we have identified as arising if the merger takes place. In particular we have examined safeguards designed to remedy the expected loss of competition and adverse effects on prices and to ensure that consumers share any benefits arising from the merger.

7.60. First, we considered the possibility of divestment by Tate & Lyle of a part of the merged business to provide two United Kingdom businesses of viable size. If both held a substantial share of the beet processing operations such a divestment might give a reasonable prospect of remedying some of the detriments to competition we have identified. However, the parties drew a number of practical difficulties to our attention, including the problem of deciding on an appropriate split in the British Sugar activities until its current 'de-bottlenecking' and efficiency programme is complete. Not only would some synergy benefits of the merger be lost but the divested business would have to create its own distribution and customer network. Moreover, although not directly related to the effects of the remedy, Tate & Lyle made clear to us that, with such a constraint hanging over it, it would be in no position to mount an effective bid for British Sugar. Therefore, although we saw attractions for preserving competition in the longer term in adopting a course which would split up the present beet monopoly, we did not think that, in the context of the present inquiry, it would provide an effective remedy.

7.61. A number of suggestions were made to us that if the merger went ahead customer interests might be safeguarded by guarantees on continued availability, at reasonable prices, of the existing range of products and services, and by undertakings on price levels and relativities between prices, for example between industrial and retail sugars or between white granulated and liquid sugars. In examining these proposed remedies we also considered whether such measures could be used to ensure that efficiency gains from the proposed merger would be passed on to customers. However, such safeguards would be extremely difficult to frame initially and to monitor as circumstances change. We do not think that the amount of regulation involved would be either desirable or effective.

7.62. We considered suggestions that guarantees should be given to the merchants on prices and availability of sugar, in order to safeguard the merchanting function. As explained above, we do not think the existing merchanting role will be put at risk by the proposed merger but the British Sugar Compliance Programme, to which TLS has indicated it would adhere, would remain as a protection against abuse of a dominant position.

7.63. We are therefore unable to recommend any effective safeguards that would remove the detriments to the public interest that would arise if the merger were allowed to proceed. We accordingly recommend that the merger should not be permitted to proceed.

7.64. As explained in paragraph 7.3, at a late stage in our inquiry an agreement was announced for the acquisition of British Sugar from Berisford by ABF. Completion of the acquisition is dependent on a number of conditions at this moment still to be fulfilled. Tate & Lyle has told us that its bid for British Sugar has not been withdrawn and that it would still wish to proceed with its offer if the transaction with ABF were not completed. Nor does the agreement with ABF affect our consideration of the issues before us. Accordingly we have completed our inquiry in accordance with our terms of reference.

H H LIESNER (*Chairman*)

S EILON

A FERRY

D P THOMSON

S N BURBRIDGE (*Secretary*)

21 December 1990