

6 Views of the main parties

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Introduction

6.1. In this chapter we summarize the views of the main parties to the inquiry. These were presented in written submissions and at hearings, of which two were held with each main party.

Views of Rockwool

Jurisdiction

6.2. Rockwool accepted that arrangements were in contemplation which, if carried into effect, would result in the creation of a merger situation qualifying for investigation within the meaning of section 64(8) of the Act in that Rockwool's share of the supply of stone wool in the UK, already well above one-quarter, would be increased.

Market definition

6.3. Rockwool considered that the relevant product market was that constituted by all products used for thermal insulation.

6.4. The thermal insulation market, in Rockwool's view, contained the following principal products:

- mineral wool, including stone wool and glass wool;
- EPS and XPS;
- polyurethane foam;
- phenolic foam;
- perlite;
- microporous silica;
- PIR;
- cellular glass;
- calcium silicate;
- ceramic fibre; and
- flexible materials, for example ENR and polyethylene foam.

6.5. In addition to these principal insulation materials, there were other materials that could be used for insulation purposes. These were PVC foam, cellulose fibre, cork, expanded synthetic rubber, vermiculite, fibreboard and melamine foam.

6.6. Rockwool based its views on the premise that, although insulation materials had different properties and some were more suited to certain applications than were others, it was very often the case that a manufacturer (such as Rockwool) did not know at the point of sale which segment of the total market the product would be used in. The almost universal presence of the distributors (who distributed a wide range of thermal insulation products) in the supply chain between manufacturers and end-users made it even more natural that manufacturers should regard the thermal insulation market as a whole.

6.7. We put it to Rockwool that it was appropriate for the purposes of the inquiry for us to examine separately a number of market areas, without implying at that stage that they formed separate markets, namely:

- (a) the supply of insulation materials for use by the building industry;

- (b) the supply of insulation materials for industrial applications in the following temperature ranges:
- up to 150°C;
 - from 150°C to 230°C;
 - from 230° to 540°C; and
 - from 540° to around 850°C;
- (c) the supply of fire protection materials; and
- (d) the supply of materials for acoustic insulation.

6.8. Rockwool broadly accepted this approach but suggested that on the whole it made more sense to combine the first two industrial application bands into one, ie up to 230°C. Rockwool noted that the categorization of fire protection and acoustic insulation as separate market areas—an approach it agreed with, since it believed they were separate markets—was based on the fact that the insulation materials were used expressly for these purposes in particular contexts separate from any thermal insulation objectives, even though some of the materials from which the products were manufactured were used mainly in the thermal insulation market.

6.9. With respect to the geographic definition of the market, we put it to Rockwool that in view of the relatively low levels of imports of insulation materials, due to transport costs being high in relation to the value of the products, and the similarity of market conditions (price and product availability) in different parts of the UK, the market or markets in insulation materials were UK-wide but largely separate from the markets in other countries. Rockwool agreed that the geographic market was the UK but did not believe that imports (or exports) were thereby precluded.

The effects of the merger

Availability of products competing with stone wool

6.10. In Rockwool's view, it would increase its share of the insulation market by at most 4.7 per cent—from 16.3 to 21 per cent—through the merger. Moreover, that maximum increase took no account of OCBP's plans to continue to supply stone wool products to certain specified customers and therefore overstated the size of the increase in Rockwool's share to a certain extent.

6.11. OCBP, which would retain approximately 18 per cent (or more) of the insulation market, would, therefore, continue as Rockwool's main competitor. In fact, Rockwool and OCBP would have more evenly distributed shares of the insulation market than before the acquisition. The only difference would be that OCBP would compete mainly, and even more vigorously, through glass wool and foam-based products (although not to the complete exclusion of stone wool products), leaving Rockwool as the predominant supplier of stone wool. However, glass wool and stone wool were direct competitors in all applications except the segment for high-temperature applications over 540°C, in which stone wool competed with ceramic fibre and calcium silicate (and which represented, on Rockwool's estimates, 0.35 per cent of the overall insulation market, or £1.2 million by value).

6.12. In addition, OCBP would remain capable of supplying customers which purchased stone wool products destined for both structural and industrial uses (including high-temperature applications up to 800°C) and which wished to single-source their purchases, as it would continue to supply a certain quantity and range of stone wool products through its Partek and Icerock distributorships (see paragraph 6.15) and its Supply Agreement with Rockwool.

Other manufacturers

6.13. Other major manufacturers in the insulation market were Kingspan (an Irish-owned company specializing in polyurethane and phenolic foams), Celotex Limited (dedicated to the manufacture of polyurethane), Vencel Resil (part of the Dutch Synbra group and principally dedicated to EPS), BGI (which marketed glass wool from its plant in Runcorn jointly owned by BPB and the St-Gobain group, the world's largest insulation manufacturer), Superglass (a UK glass wool manufacturer owned by Encon, the second largest UK distributor of insulation products), Armstrong World Industries (a UK company manufacturing nitrile rubber and focusing on the H&V sector) and Cape (an international group of companies specializing in calcium silicate insulation products).

6.14. We put it to Rockwool that the reduction in OCBP's stone wool product range as a result of the merger could be seen as diminishing its credibility as a competitor with Rockwool. However, Rockwool argued that market strength should be viewed more broadly. In mineral wool products alone the merger would raise Rockwool's share from approximately 30 to 40 per cent (by value) and OCBP's share would fall from approximately 49 to 40 per cent. The number of players in the market would not be reduced as a result of the transaction. OCBP would remain a major player in the market, with glass wool, foam and stone wool. The transaction would simply result in a shifting of market share between the two existing major suppliers. Moreover, Rockwool's plans for cost reduction at the Queensferry plant, and OCBP's increased focus on glass wool, would add greater impetus to competition in the market.

Imports

6.15. We asked Rockwool about the importance of imports as a source of competing products, in view of high transport costs in relation to the value of the product. Rockwool argued that insulation materials were traded throughout Europe. In the case of stone wool, for example, St-Gobain, with manufacturing facilities in Germany, France, Spain and Sweden, actively marketed its products in all those countries as well as in Belgium, the Netherlands and Portugal. Likewise, Partek, based in Finland and Sweden, sold its products throughout Northern Europe. In the UK, where there were no restrictions on imports of insulation materials, OCBP had the exclusive distributorship for imported Partek and Icerock products. Together these products represented approximately £4.5 million of sales a year (or over 25 per cent of total OCBP stone wool sales), a not insignificant proportion of the UK market. Heraklith (Austria) and Fujairah (UAE) had also exported products into the UK.

6.16. Moreover, although imports were low relative to the overall size of the insulation market, they formed a significant percentage at the higher end (by value) of the insulation market, where transport costs were proportionately lower. For example, whereas intra-UK transport costs (expressed as a percentage of invoiced sales by Rockwool for 1998) for cavity wall batt were as much as [30] per cent, these costs in the case of wired mat or process pipe sections were reduced to [10] per cent and [10] per cent respectively. Furthermore, stone wool was manufactured in Eastern Europe at substantially reduced costs which compensated for the higher transport costs.

Buyer power

6.17. Rockwool put considerable emphasis on the countervailing power of its customers, particularly the major distributors. Overall, approximately 74 per cent by value of Rockwool products were sold to distributors, and in the industrial process and industrial H&V sectors 100 per cent of Rockwool's sales were made in that way. Two distributors predominated—SIG and Encon. Their combined purchases accounted for about 61 per cent of total Rockwool sales, with 10 to 12 smaller distributors accounting for a further 13 per cent. The distributors resold to all sectors of the insulation market (ie both the general building and the industrial sectors). Of Rockwool's remaining sales, 5 per cent went to builders' merchants and DIY chains (with almost all of that being taken by Wickes Building Supplies), 6 per cent to specialist insulation contractors (who purchased mainly for external wall insulation and blown wool cavity wall applications) and the balance of 15 per cent to a large number of small customers spread throughout the insulation industry.

6.18. Supply patterns varied slightly depending on whether the products were ultimately used in industrial or general building applications. However, with regard to certain products, the best example of which was slabs, the manufacturer, when selling to the distributor, did not know what end-application they would be put to. Consequently, although Rockwool split slab sales 50:50 between its general building and industrial businesses, it did so purely for internal accounting purposes.

6.19. We put it to Rockwool that the distributors appeared to be as dependent on the manufacturers as the other way round, in view of the doubts that were expressed to us by distributors about the practicality of significantly increasing their imports. Rockwool maintained that the large distributors, with their significant percentage of Rockwool's entire sales in the insulation market, wielded enormous purchasing power over Rockwool. They exerted serious pressure on Rockwool with regard to prices, delivery terms, quality, etc. Rockwool was heavily dependent on these distributors and had to be responsive to their demands to retain their business.

The industrial process sector

6.20. We put to Rockwool the concerns expressed by distributors in respect of the industrial process market. One concern was that the greater flexibility shown by OCBP in being willing to fill small and mixed orders would be lost. Some customers also considered OCBP to be more accommodating over payment terms. Most important, there was a fear that a sole supplier for a large part of the stone wool product range, as Rockwool would be if the merger proceeded, would be able to raise prices for applications where there were few substitute products available.

6.21. Rockwool argued that there was a significant overlap of products used in both the structural and industrial sectors. The distributors which purchased a particular product (for example, stone wool slabs) for structural sector applications also purchased the same product for industrial sector applications. The price was the same, regardless of use. There were certain applications in the industrial sector requiring high-temperature properties which would primarily be served by Rockwool products (for example, stone wool slabs) after the acquisition. However, Rockwool would be prevented by market forces from unduly raising its prices in respect of such products since it was unable in advance to distinguish between: (a) industrial process contractors (ie the distributors' customers) requiring the products for high-temperature applications which, alone, would have no choice but to pay more for such products; and (b) the other industrial process customers who could, and doubtless would, switch to other (ie non-stone-wool) products if the prices of these stone wool products were to rise unduly. Consequently, any attempt to raise prices for such products without regard to competitors would leave Rockwool with a much lower volume of sales of the stone wool products concerned and, consequently, overall lower profitability, for which it would be unlikely to be able to compensate by a price increase affecting its remaining sales.

6.22. Rockwool argued, further, that it was necessary to consider the different segments, in the industrial market, as classified by temperature ranges, as follows.

Temperature range up to 150°C

6.23. Rockwool believed it was generally acknowledged that in the temperature range up to approximately 150°C (which represented the vast majority of applications, including all of the general building sector) there were numerous substitutes for mineral wools, including the foam-based products which were in many cases cheaper.

Temperature range 150°C to 540°C

6.24. Both stone wool and glass wool competed directly in the temperature range between 150°C and 540°C. Although above 230°C the binder used in mineral wool began to oxidize, that process was controllable and did not affect the relative merits of glass wool or stone wool as competing products.

Rockwool contended, therefore, that glass wool could compete with stone wool in the temperature range up to 540°C.

6.25. Rockwool accepted that certain industry sectors showed a preference for stone wool products. That could well be due to successful marketing and technical product support by Rockwool. However, the fact remained that technically glass wool was just as effective as stone wool in that temperature range. OCBP currently marketed its glass wool products for applications up to 230°C but that should be seen in light of its decision to promote its competing stone wool business. If the merger proceeded, Rockwool would expect Owens Corning to reconsider its marketing strategy in that respect. The extra marketing strength which could be derived from OCBP focusing more of its efforts on glass wool could make it an even more effective competitor across the market. Furthermore, Superglass, one of the other two main UK glass wool competitors, marketed and sold its products as capable of operating up to 540°C.

6.26. The insulation market in the USA was, in Rockwool's view, a useful illustration that glass wool could be used over a wide range of temperatures. In the USA, stone wool hardly had a presence and glass wool and calcium silicate tended to predominate in higher-temperature applications, ie glass up to 540°C and calcium silicate above 540°C. There were numerous examples of glass wool manufacturers selling into the 230°C to 540°C range such as, in the USA, Knauf with its glass wool pipe insulation for all applications up to 537°C, and in Continental Europe G+ H Isover, which offered glass wool pipe sections and glass wool wired mats for use up to 500°C.

Temperature range 540°C to 800°C

6.27. Rockwool acknowledged that within the temperature range 540°C to 800°C glass wool ceased to be a substitute for stone wool. Stone wool was not, however, the only material in the market. Other insulating materials (for example, ceramic fibre, calcium silicate or microporous silica) could all operate within the temperature range and indeed beyond, where stone wool could no longer compete. Even within that temperature range, there might be other specific requirements, such as pack volume or compressive strength, that were better satisfied by other materials. Calcium silicate and ceramic fibre, for example, were particularly used in the chemical and petroleum industries, the first for its compressive strength, the second because of its thermal conductivity at high temperatures.

6.28. In any event, Rockwool argued, applications in that temperature range represented a tiny proportion of the market—only 0.35 per cent for insulation products as a whole or 0.8 per cent of mineral wool sales.

6.29. Stone wool products capable of use in that temperature range included process pipe sections and slabs. Rockwool had no doubt, in respect of both those products, that manufacturers were incapable of distinguishing products destined for applications in this temperature range from those in other applications, whether by reference to the supply chain which they followed, as they all flowed through specialized distributors, or by reference to the physical characteristics of the product, given that the product had an inherent quality of being able to operate up to 800°C with no special processing necessary. Hence, Rockwool pipe sections or slabs found themselves competing with foam-based products at the lower end of the temperature range and with glass wool, calcium silicate, ceramic fibre and others at the higher temperatures, without Rockwool being able to determine how that competition took place.

6.30. Rockwool argued, therefore, that it would be prevented from raising prices of process pipe sections or slabs for applications in the temperature range 540°C to 800°C because it could not target those sales alone. It would have to raise the prices of all its slab or process pipe products, with the following consequences:

- (a) It would lose business in relation to products used in applications below 540°C. Many materials, notably glass wool, competed directly up to that temperature. It was extremely difficult to calculate the precise proportion which high-temperature applications represented of the total insulation market. An independent analysis made for Rockwool suggested that over 95 per cent of all process pipe sections sold in the UK, measured by length, were used for temperatures below 540°C. Rockwool's knowledge of the market led it to believe that that

proportion also held true for slabs. Therefore, it would not be economically viable for Rockwool to sacrifice its low-temperature business for higher prices in the high-temperature sector.

- (b) In a highly transparent industry, such price increases were unlikely to be condoned by direct customers (ie industrial distributors, representing up to 93 per cent of Rockwool industrial process sales), which could threaten credibly to switch purchases of a whole range of products, or by the end-users themselves, who could easily seek out alternative suppliers.

Wired mat

6.31. Rockwool referred to the importance of wired mat and the fact that it would continue to face competition in respect of the applications served by wired mat from slabs and stone wool wired mat made by LGF in the UK. Wired mat was a form of insulation that possessed great flexibility and was particularly useful for wrapping around tanks and other vessels with awkward shapes and which could not easily be insulated with slabs, although slabs could be and were also used. Glass wool wired mat (which could be used up to 540°C) was rare although that product was being marketed in Europe.

6.32. Rockwool added that the potential for imports of that product was also great. It was a higher-value product with good pack volume, which made transport costs proportionately lower. Imports of wired mat into the UK had come particularly from Heraklith in Germany and Austria.

Fire resistance and protection

6.33. Rockwool stressed that the fire safety properties inherent in certain insulation materials should be clearly distinguished from their thermal qualities, such as temperature range or thermal conductivity (ie their ability to insulate at different temperatures and how effective they were at achieving that). An inherent property of certain insulation materials was that they were not combustible. That could, in certain circumstances, be a valuable property for an insulation material, in guaranteeing that the insulation products would not ignite, spread or otherwise contribute to a fire. In that regard, both stone wool and glass wool offered fire-safe properties. In addition to mineral wools, other insulation materials (with the notable exception of foam-based materials) were also non-combustible.

6.34. The question of fire safety in insulation products was a different matter from that of products whose prime purpose was for fire protection. Fire protection applications could include: protection of ducts, etc, to prevent the spread of fire through a system, structure or building; protection of structural supports to prevent collapse of buildings; and filling of voids to restrict spread of fire and smoke within buildings. Rockwool added that in most situations where fire protection was required there was not an insulation requirement, and the fact that materials such as stone wool or calcium silicate were suited to fire protection did not have a bearing on their acceptability as an insulation product. In fact, Rockwool products designed for fire protection tended to be specially formulated (including variation in density, binder content, thickness, facing, etc) and fire tested and certified by reference to the intended construction. Thus Rockwool had a separate and differently named range of stone wool products dedicated exclusively to fire protection applications.

6.35. As for sales of fire protection products and their distribution between competing products, Rockwool considered that total sales amounted to some £70 million of which stone wool's share was about 14.5 per cent, half of which was due to Rockwool and OCBP combined. Building boards (for example, calcium silicate, vermiculite) had the highest share—around 32 per cent. The high value of the products made imports economic and significant quantities were entering the market (for example, from Scandinavia) at very competitive prices. In addition, there was sharp competition from UK fabricators with low overheads who bought stone wool slabs and produced the fire protection materials from them. For these reasons, and given the small market share of stone wool-based products, Rockwool would not be able to raise prices as a result of the merger.

Flexibility of supply

6.36. We asked Rockwool what policy it intended to follow in the event of the merger proceeding in respect of flexibility of supply, ie minimum order quantities, mixed loads and provision of non-standard products: concerns had been expressed that OCBP was easier to deal with for smaller and non-standard customers and that that advantage would be lost. Rockwool did not envisage basic changes to its supply policies. It considered that it was already flexible, for example with a new customer it was ready to let it build up business over a year or so even if that customer's orders were smaller than Rockwool's standard quantities. In addition, Rockwool was prepared to supply a mix of up to nine different slab products in a single full load. Even if some OCBP standard Rocksil ranges would no longer be available, these would be replaced by Rockwool equivalents. Rockwool would also stick to its requirement for payment within 30 days, although it had phased this in over a number of months when it had won customers from OCBP (which allowed payment in 60 days). Rockwool added that its policy was that end-users, and other customers which wanted to buy occasional loads, should buy through distributors.

Prices

6.37. We asked Rockwool whether it expected to increase prices for particular applications or products in the event of the merger proceeding. Rockwool said that the insulation market was a very competitive one, as could be seen in the general stagnation of prices for both stone and glass wool. Its own experience was one of seeing discounts (particularly, but not only, for the larger distributors) from its list prices ratched upwards. The fact that in recent years the annual increases to list prices which it had announced were, in practice, nowhere near realized was specific evidence of the strength of competition. A particular example was the roofing market where Rockwool's prices were around twice those of the major competing products such as polyurethane foam. Rockwool had just launched a new product, imported from Denmark and based on new technology, which would be priced at only some [§<] per cent more than foam substitutes.

6.38. We asked Rockwool how it reconciled these statements with the figures in its business plan which projected for the next three years a 1 per cent increase in average realized prices over the total business without the merger and an additional 1 per cent with the merger. Rockwool said that its projections assumed all of the additional 1 per cent average price rise would come from increases in market prices for roofing products and slabs, increases achieved through a reduction in special discounts. It had assumed that the acquisition would enable an additional 5 per cent price increase to be achieved on roofing products and common slab products. These had accounted for 23 per cent of Rockwool's sales in 1997, so the effect of these 5 per cent increases would be to add some £600,000 to sales value, representing 1.2 per cent of Rockwool's overall 1997 sales value.

6.39. In roofing, for which prices were generally set for each contract, most customers were not prepared to pay a large premium for stone wool's better fire resistance properties, compared with foam. However, Rockwool sought to persuade architects and other specifiers to specify its premium Hardrock product for customers willing to pay a high price for a fully fire-resistant roof. When it succeeded, however, the specification would usually allow an alternative to be chosen and OCBP took advantage of the situation to undercut Rockwool's price. It was for this reason that Rockwool had assumed that the merger would enable it to raise prices for this application. That assumption had been overtaken, however, by Rockwool's introduction of the new, much cheaper, product as a result of which its average roofing price might fall. Rockwool said that it would continue to sell its Hardrock product—sales of which had been nearly £4 million in 1998—but expected to see an increasing amount of sales transfer to the new product over the coming years.

6.40. Rockwool's assumptions for slab pricing after the merger were very similar. It expected to achieve a small general rise in slab prices and a somewhat larger rise in a few cases where OCBP had been driving prices down in bidding for large projects, particularly in the structural sector. The general increase would be possible because of Rockwool's superior after-sales service, together with its normal specification activity and its expectation that glass wool would take a few years to compete effectively. Slabs accounted for some £8 million of Rockwool's sales in 1998.

6.41. Rockwool's current estimate was that the extra revenue from these increases would be no more than £400,000 to £500,000 a year for three years, compounded but not rising further thereafter—and perhaps even falling as glass wool became a stronger competitor through, for example, the development of the OCBP product range.

6.42. In addition, Rockwool explained that it had not intended to imply that in the project area almost all prices were negotiated contract by contract. Its system of setting company-wide discounts with distributors for each of the largest contractors was supplemented from time to time by special discounts for specific projects. But only one such contract-specific set of discounts had been agreed in 1998 in the industrial sector, although there were several agreed in the structural sector. The discount-setting system applied case by case, ie for each large contractor, but not for each and every contract.

6.43. Rockwool added that, in referring to OCBP's realized prices being in some cases apparently 5 to 10 per cent lower than Rockwool's, the emphasis was on that applying to a strictly limited number of cases and on an equivalent product-for-product basis. In the event of the merger proceeding, the general assumption was that all sales would be made at Rockwool's prices whether or not the products were made at the Queensferry plant or were sold to former OCBP customers. The overall effect on prices of the unified Rockwool prices applying would depend on the mix of Rockwool's total sales post-merger: despite prices for equivalent products being in some cases lower than Rockwool's, OCBP appeared to be realizing a higher average price per tonne than Rockwool because it sold a higher-value mix of products.

6.44. In any event, even without the planning assumption of an additional 1 per cent increase in average realized prices, Rockwool's analysis showed that the IRR from the merger would still be considerably above Rockwool's general target rate.

Entry to the market

6.45. We asked Rockwool how likely it was, in the event of the merger proceeding, that another producer would contemplate establishing new productive capacity for stone wool in the UK, in view of the high costs of doing so—approximately £1,000 for every tonne of annual capacity. Rockwool did not consider it was out of the question that a competitor would wish to set up a UK plant: the most likely company to do so would be St-Gobain, given its existing know-how in stone wool production in Continental Europe and the fact that its joint venture with BPB in the manufacture of glass wool would ensure that it had a wide and attractive product range in the event of its developing stone wool capacity in the UK.

Benefits of the merger

6.46. We put it to Rockwool that, whilst there appeared to be financial advantages to Rockwool from the acquisition of Queensferry, it was much less clear what the benefits, if any, would be to others. Rockwool considered that over a three-year period it would, by dint of additional investment and other operating efficiencies, be able to secure a reduction in variable production costs at Queensferry of around £[] per tonne. In addition, there should be savings in transport costs (of up to £[] a year) due to the ability that a two-centre operation would provide for supplying each customer from the optimal location. Whilst Rockwool had not earmarked any of the anticipated cost savings for customers in its business plan in the form of lower prices, the very competitive nature of the UK insulation market would be a factor which would be taken into account by Rockwool as soon as it had realized the anticipated operating cost benefits.

6.47. Rockwool believed that the acquisition of Queensferry would lead to a net increase in employment. The existing 125 jobs at Queensferry would be safeguarded (both in the short and long term, as Rockwool's efficiencies resulting in a certain amount of labour saving would be counter-balanced by its increasing capacity at Queensferry). Some additional jobs might also be created at Queensferry, for example through Rockwool's investment in [*Details omitted. See note on page iv.*]. If the acquisition were blocked and if Rockwool built a third line, that would create further jobs at Bridgend when it came on stream two to three years later. Rockwool

believed that if the acquisition did not proceed Queensferry would be likely to close down, creating a shortage of supply in the UK. In that event, were Rockwool to build a third line it would immediately operate at full capacity to meet demand thus creating around [≈] new jobs two to three years after the decision to go ahead. In the unlikely event of Queensferry still being operational in two to three years' time, a third line, if built, might not operate at full capacity, reducing the new jobs at Bridgend to around [≈]. On the above hypotheses, prohibiting the merger would result in the immediate loss of 125 or more jobs at Queensferry offset by the possible creation of up to [≈] new jobs at Bridgend in two to three years' time (assuming a third line at Bridgend were built and operated to capacity).

6.48. Rockwool also believed that the wider community in the Queensferry area could benefit from the acquisition in that Rockwool would undertake significant environmental investment, of up to £4.5 million, in the plant, for example in a modern afterburner to improve significantly the smoke emission. No doubt OCBP would also invest in environmental improvements in the event of the acquisition not being permitted. However, since it would not put in new capacity, the scale and scope of the benefits to the environment from continuing investment by OCBP might well be less extensive than would be the case if Rockwool were upgrading Queensferry.

Remedies

6.49. We asked Rockwool to comment on a number of possible steps which we might recommend in the event of our concluding that the merger might be expected to operate against the public interest because of its effect on competition in the supply of stone wool.

6.50. Rockwool, whilst not opposed to the idea in principle, could not envisage any watertight method of controlling its average realized prices for particular products in order to ensure, for example, that they could not be increased faster than the general rate of inflation or an index of building material prices. The wide variety of discounts, quantity rebates and individually negotiated prices in the market would make such a measure very hard to operate and monitor.

6.51. Rockwool had no objection to a requirement to supply all would-be customers who met specified criteria such as a minimum order quantity, provided that there was proper allowance for customer creditworthiness and customer status. Any problems that arose, for example of definition, could probably be dealt with. Thus some partial arrangement might be capable of being worked out. In the final analysis, Rockwool wanted more customers.

6.52. A requirement to give equivalent terms for equivalent orders was not objected to by Rockwool, provided some allowance could be made for the size of a customer's total business. Again, as in relation to a requirement to supply provision, it might be possible to find some areas where an arrangement was feasible.

6.53. With respect to the possibility of an undertaking to continue to supply a specified range of products (unless it could be demonstrated that termination of a particular line was economically justified), Rockwool said that it had no plans to make reductions so far as the standard range of OCBP products was concerned. It could not, however, enter into any commitment in respect of non-standard products which might be made by OCBP which Rockwool was not aware of.

6.54. While starting from the premise that the very competitive insulation market made remedies unnecessary, Rockwool was ready to contemplate a number of other possibilities. One could be an amendment to the proposed Supply Agreement (see paragraph 3.5 and Appendix 3.1) to permit OCBP to supply a wider range of products, including some industrial products such as process pipes and wired mattress. In addition, small customers currently in the 'non-compete' list in the Business Sale Agreement (see paragraph 3.5 and Appendix 3.1) could be moved to the 'compete' list, giving them an additional source of supply through OCBP. The widening of the product range under the Supply Agreement would be beneficial to OCBP in that it would interact with the provisions whereby Rockwool had to meet prices offered to OCBP by other suppliers or release OCBP to purchase from any other source of stone wool supply.

6.55. Since there appeared to be some concern that smaller customers might face higher prices as a result of the merger, Rockwool was also ready to enter into an undertaking to provide audited accounts of the average prices of an agreed list of products (principally process pipes and wired mattress) by customer type. Such an arrangement would be similar to a recommendation made by the MMC, in respect of milk prices, in their report on the Wiseman Dairies/Scottish Pride merger inquiry:¹ a reporting system of that kind would put the OFT in a good position to deal with any complaints.

Consequences of the merger being prohibited

6.56. We asked Rockwool what steps it would be likely to take in the event of the merger being prohibited. Rockwool said that an option would be to proceed to install a third line at Bridgend, for which it had received planning permission in July 1997. It was uncertain whether Rockwool would build a third line and any decision might be delayed for several years. Another option would be to undertake the 'debottlenecking' of one of the existing two lines: that could well be a viable choice in its own right and not necessarily as part of a programme to build a third line.

Views of Owens Corning

Jurisdiction

6.57. Owens Corning accepted that arrangements were in contemplation (ie the proposed acquisition of OCBP's stone wool manufacturing business by Rockwool) which, if carried into effect, would result in the creation of a merger situation qualifying for investigation within the meaning of section 64(8) of the Act in that Rockwool's share of the supply of stone wool in the UK, already well over one-quarter, would be increased. Owens Corning commented, however, that for economic purposes, the supply of stone wool was too narrow to represent a market (see paragraph 6.58.)

Market definition

6.58. Owens Corning believed that it was very difficult to define markets for insulation materials as many products could be used for different purposes and in different market segments. That factor was also important for market definition as, outside the short run, significant shifts between products in a market could take place. For many purposes a market definition based on stone wool alone, or even all mineral wool, would be too narrow, though the latter was clearly the more appropriate of the two.

6.59. We put it to Owens Corning that for the purposes of the inquiry it was appropriate to examine separately a number of market areas, namely:

- (a) the supply of insulation materials for use by the building industry;
- (b) the supply of insulation materials for industrial applications in the following temperature ranges:
 - up to 150°C;
 - from 150°C to 230°C;
 - from 230°C to 540°C; and
 - from 540°C to around 850°C;

¹*Robert Wiseman Dairies plc and Scottish Pride Holdings plc: a report on the proposed merger*, The Stationery Office, Cm 359, December 1996.

- (c) the supply of fire protection materials; and
- (d) the supply of materials for acoustic insulation.

6.60. Owens Corning agreed that this grouping of market areas was an acceptable basis for analysing the questions likely to arise in the inquiry.

The effects of the merger

Availability of products competing with stone wool

6.61. Owens Corning thought that the acquisition would have very little effect on the structure of the market and the availability of substitute products for a wide range of applications.

6.62. In the UK mineral wool sector, to take a convenient if, in Owens Corning's view, too narrow a product market definition, OCBP would retain the highest market share at 36 per cent compared with Rockwool's 34 per cent, against pre-acquisition shares of 43 and 27 per cent respectively (using OCBP estimates for 1998, by value). For the vast majority of applications in which stone or glass wool was used, the two were, in the technical and marketing senses, entirely substitutable. While the prices per tonne of the two products differed, that was mainly because stone wool's higher density meant that a greater weight of stone wool would usually be needed to achieve the same thermal performance in any given application. Prices per square metre and installation costs for the two materials were similar so that overall costs would also be very similar for any given application.

6.63. We asked if the reduction in OCBP's capacity to supply stone wool products would not damage its credibility in the market as a competitor to Rockwool. Owens Corning believed that would not be the case, for a number of reasons.

6.64. First, the Supply Agreement with Rockwool and OCBP's continuing arrangements to import products from Partek and Icerock would enable OCBP to offer a competitive and wide range of products to those customers which wished to receive comprehensive product offers for both stone wool and glass wool. OCBP expected to continue sales of Icerock and Partek products at about the same level as in recent years, that is about 5,000 tonnes worth £3 million. Although restrictions would be placed on OCBP by the terms of the Supply Agreement, the quantity of 3,000 tonnes to be purchased each year from Rockwool was set as a minimum, not a ceiling. In practice, as OCBP sought to switch customers from stone to glass wool, OCBP estimated that it might buy around 4,000 tonnes. That compared to estimates (annualized on the basis of actual sales in the first half of 1998) of 4,600 tonnes, worth some £4.5 million, supplied to 'compete' customers in 1998. Though the overall quantity of stone wool likely to be sold by OCBP following the merger was no more than about 35 per cent of its current sales, OCBP would be free to market vigorously the supplies available to it and could certainly provide significant competition for Rockwool in the stone wool market.

6.65. Second, OCBP would after the acquisition be an even tougher competitor for stone wool and other products in the market by virtue of its enhanced focus on glass wool. Although neither Pilkington (between 1991 and 1994) nor OCBP (since 1994) had produced glass wool capable of competing for industrial applications in the 230°C to 540°C range, that was due to decisions taken for strategic marketing reasons. In particular, they reflected the wish to run Queensferry at a high throughput, rather than any view that glass wool was not a viable competitor in that range. Stone wool was used extensively in the 230°C to 540°C range and it had been natural for OCBP (and Pilkington before it) to take maximum advantage of stone wool's particular qualities. Given that OCBP and Pilkington had both glass and stone wool manufacturing facilities in the UK, it had not been necessary to promote glass wool in the 230°C to 540°C temperature range.

6.66. Owens Corning said that the Owens Corning group marketed and sold glass wool products in the USA capable of meeting operating temperatures well above 230°C and up to 540°C in some cases. Both independent research and Owens Corning's own operating experience in the USA showed that glass wool in some cases had advantages over stone wool for industrial applications in that temperature

range, through better weight-for-weight thermal conductivity and higher resistance to vibration, for example in power station applications. Owens Corning also provided recent examples of US glass wool sales for use in temperature applications of up to 350°C.

6.67. Owens Corning also emphasized the success which the group had achieved since 1997 selling glass wool for use in major projects in China, a market where stone wool had been widely used and in which there had not previously been any domestic glass wool manufacturing facilities. The projects included 16 power plants, 4 chemical plants, 2 steel plants and 2 power supply lines for a utility plant and a paper plant. Owens Corning had sold nearly 2,000 tonnes of glass wool for these projects: the maximum operating temperatures ranged between 400°C and 450°C. In competing for the business Owens Corning had emphasized as benefits from glass wool its light weight, high resistance to vibration and thermal insulation performance.

6.68. We asked Owens Corning if it was confident that there would be no problems from exothermic reactions ('pinking') in insulation material made from glass wool and used in the higher 230°C to 540°C range. Owens Corning believed that there would be no difficulty. It could now buy binder resins with the necessary anti-pinking additive already included: these would provide effective control over pinking and would add less than [§<] per cent to manufacturing costs. It cited the Mott MacDonald report (see Appendix 4.3) in support of its contention that pinking was not a problem (see also paragraph 6.83).

6.69. Owens Corning informed us that OCBP was in the process of drawing up a marketing plan (details of which were given to us) for its proposed initiative to displace stone wool with glass wool in industrial process applications. It had just appointed, through internal promotion, a marketing manager to carry the plan forward. That showed the importance it attached to repositioning its glass wool products in the UK as an effective insulation in the 230°C to 540°C temperature range.

Other manufacturers

6.70. Owens Corning stated that if the merger proceeded that would not in itself reduce the availability of substitute materials from competitors of Rockwool other than OCBP. Other suppliers of mineral wool included the following:

- (a) BGI, a joint venture between BPB and Isover St-Gobain, the insulation business of the St-Gobain group (the world's largest insulation manufacturer), producing glass wool;
- (b) Superglass, the glass wool manufacturing subsidiary of Encon, the UK's second largest distributor of insulation materials; and
- (c) LGF, a manufacturer of stone wool which, though small overall, produced both wired mat and slabs.

6.71. Outside mineral wool, significant producers of other insulating materials included:

- (a) Cape, which apart from its large contracting business also produced calcium silicate and phenolic foam;
- (b) Kingspan, an Irish company specializing in the manufacture of EPS, polyurethane products and phenolic foam;
- (c) Celotex, the major manufacturer of PIR rigid foam boards for the structural market;
- (d) Vencel Resin, a part of the Dutch Synbra group and mainly dedicated to the production of EPS; and
- (e) Dow Construction Products Ltd, the largest UK and worldwide producer of XPS.

Imports

6.72. We asked Owens Corning about the importance of imports of stone wool as a source of competition, in view of high transport costs in relation to the value of the products.

6.73. Owens Corning said that imports of stone wool tended to be of high-value products such as the fire protection slabs imported by Cafco from Partek. In earlier years, imports of stone wool had been higher than in the recent past and could become so again. Companies such as Pfleiderer in Germany and Heraklith in Austria were selling into the UK. Manufacturing capacity was also growing in Eastern Europe. Though transport costs were higher from that region, they would be offset by the lower production costs. Owens Corning was of the view that imports should not be underestimated as a check on stone wool prices if there were any tendency for these to rise in the UK after the acquisition. Imports of other insulation materials, such as calcium silicate and ceramic fibre, both high-value and sophisticated products, also took place.

Buyer power

6.74. Owens Corning emphasized two points about the channels of distribution for insulation products. First, the great majority of products were supplied via specialist distributors and merchants. Second, the principal purchasers of insulation materials, whether specialist distributors or builders' merchants, were becoming increasingly concentrated and exerted considerable buying power, which was reflected in declining prices.

6.75. Of OCBP sales in 1998, around 68 per cent were made through distributors, builders' merchants and large DIY stores. The leading ten customers accounted for 55 per cent of OCBP sales, though the percentage was even higher in the industrial process sector. The importance of the distributors was greatest in that sector, where they accounted for all of OCBP's mineral wool sales.

6.76. Owens Corning stressed, therefore, that the specialist insulation distributors exercised considerable and increasing buying power. The larger distributors were also well placed to seek supplies from overseas: for example, the IIDA had already begun to import stone wool slab and wired mat from Central Europe. It might be the case that some distributors (or the contractors ordering from them) had a customary preference for the use of stone wool in particular applications. However, where glass wool or other substitutes met the necessary technical requirements and were competitive in price terms, any attempt by Rockwool to raise stone wool prices after the acquisition would swiftly erode any such preference.

6.77. We asked Owens Corning why it had sold Kitson's, an insulation distributor, to SIG in mid-1998, since that had the apparent effect of concentrating the distributor market even more. Owens Corning replied that it had decided to sell Kitson's for the same reasons it wished to divest the Queensferry business, ie it was an under-performing and non-core asset; out of a number of bidders it had received the highest price from SIG.

Flexibility in supply terms and conditions

6.78. We put to Owens Corning the concern expressed by some distributors and end-users that if the merger proceeded it would be to their disadvantage because OCBP was more flexible than Rockwool in, for example, supplying smaller loads or offering better payment terms. Owens Corning said that it could not speak for Rockwool on such matters. For its part OCBP, as number two among stone wool suppliers, had something of an 'Avis mentality': it tried harder by offering a more flexible service package from Queensferry to distributors—for example, by sometimes agreeing to supply half-loads—and which particularly favoured smaller distributors.

6.79. OCBP did not intend to change its commercial practices in respect of terms on such matters. Owens Corning also thought that there would be logistical advantages to those customers which purchased both stone wool and glass wool after the merger in that imports from Partek and Icerock would be distributed from OCBP's St Helens glass wool plant; this would be the first time that OCBP would

be able to supply both stone wool and glass wool from one place, giving it greater flexibility in being able to mix loads as between glass wool and stone wool.

The industrial process sector

6.80. We put to Owens Corning the concerns expressed by some distributors and end-users about the supply of stone wool in the industrial process section. One such concern was that a sole supplier for a very large part of the stone wool range, as Rockwool would be if the merger proceeded, would be able to raise prices for applications where there were few substitute products available.

6.81. Owens Corning argued that it was necessary to limit the discussion to those applications where stone wool appeared to be the only mineral wool which was competitive on price and which met any technical requirements in those applications. Owens Corning suggested that two areas of those applications should be distinguished, as follows.

Temperature range up to 540°C

6.82. Owens Corning considered that the two main issues to determine were:

- (a) at what temperatures glass wool ceased to be a satisfactory substitute for stone wool; and
- (b) what temperatures stone wool itself could not withstand.

6.83. On (a), OCBP put the temperature limit for glass wool at 540°C, the temperature at which it would devitrify. Above 230°C the binder used in glass wool (and stone wool) began to oxidize, leading to the possibility that punking could be caused with consequent deterioration in the effectiveness of the insulation material. However, punking could be prevented by the addition of an agent to the binder and where that was carried out (as by Owens Corning in the USA or by St-Gobain in France) punking was prevented.

6.84. To support their arguments, Owens Corning submitted a paper by an independent expert, Eur Ing Derek Morgan, which analysed the technical characteristics of glass wool and stone wool and concluded that glass wool products were directly substitutable for stone wool up to temperatures of 540°C. In addition Owens Corning provided empirical evidence of glass wool being used in high-temperature applications (see paragraphs 6.66 and 6.67). Furthermore, Owens Corning drew attention to the MMC's Morgan Crucible/Manville report¹ in which glass fibre was referred to as used for insulation at temperatures up to 500°C.

6.85. We asked Owens Corning about the commonly held view that many process plant contractors and end-users had a traditional and firm preference for using one insulating material so far as possible and that that material tended to be stone wool. Owens Corning thought that such preference might have arisen in part from a belief that stone wool's higher density gave better compressive resistance to the outer metal cladding required in many process plant applications. Owens Corning believed it had shown by test work that glass wool had the necessary compressive strength and was more resistant to vibration than stone wool because (unlike stone wool) it contained no shot. If the merger proceeded, OCBP, as part of its intensified marketing programme for glass wool and its manufacture of a product capable of operating up to 540°C, would wish to highlight increasingly those characteristics of glass wool.

6.86. As for (b), Owens Corning stated that stone wool could be used up to temperatures of between 750°C and 900°C; that was confirmed by Mott MacDonald's report which put the temperature at which stone wool began to devitrify at around 850°C and found that the maximum operational temperature for stone wool was usually quoted in the region of 700°C to 850°C.

¹The Morgan Crucible Company plc and Manville Corporation: a report on the merger situation, The Stationery Office, Cm 1551, May 1991.

Temperature range 540°C to 850°C

6.87. Owens Corning stated that it was for operating temperatures within this range that glass wool did not provide a substitute for stone wool. There were, in fact, very few process applications within that temperature range (or, indeed, above 150°C). Applications within the range were limited essentially to specialized processes such as catalytic crackers in petrochemical plants, certain flues on power plants and highly specialized kilns, for example for sugar production. Owens Corning estimated that the size of the industrial process segment where operating temperatures were between 540°C and 850°C was small, with total annual sales amounting to only £600,000.

6.88. For certain high-temperature applications within the 540°C to 850°C range end-users had other specific requirements which made stone wool unsuitable as a solution. For example, in the nuclear power generation industry there was a need to be able to inspect the metal pipework at regular intervals, and for underground pipework high stress resistance was important. In those applications calcium silicate pipe sections would almost invariably be used because they could be much more easily removed for inspection purposes and because of their compressive strength. That category of end-user would therefore be unaffected by the merger.

6.89. Even in the very small sub-segment where stone wool products represented the only cost-effective solution for a given industrial application, Owens Corning argued that the acquisition would not confer any market power. There were essentially three reasons for that:

- (a) stone wool products for applications in the temperature range 540°C to 850°C were incapable of differentiation from stone wool products used in other applications;
- (b) ample competition from glass wool and a variety of non-mineral wool substitutes existed in those other applications (which accounted for a much higher proportion of the total market for insulating materials) and there was price transparency for those products; and
- (c) it would be impossible for Rockwool to increase its profits by raising prices for stone wool products in high-temperature applications because either the end-use would not be known when it took orders from specialist distributors (which were thought to account for around 90 per cent of purchases in the industrial sector) or because a direct customer (such as a contractor) would ensure that it paid no more than for the same product used in low-temperature applications.

Owens Corning considered that Rockwool's inability to raise prices for these limited high temperature applications, post-merger, could be demonstrated by looking at the two main stone wool products used in high-temperature applications, namely slabs and pipe sections.

6.90. First, it was important to note that uncured stone wool was not made in differentiated grades. The batch composition of the melt was not altered depending on the end-use of the stone wool. So finished products were not differentiated in terms of the physical characteristics of the semi-finished product. There was no special grade of stone wool for high-temperature applications.

6.91. In the case of slabs, the only differences were in density and thickness. But those were not differences which enabled a manufacturer to single out stone wool slabs for high-temperature applications. For high-temperature applications a contractor might well opt for a denser, thinner stone wool slab, because it would have good insulation properties and would be a cheaper solution than a thicker, less dense slab. But the same density slab (for example, OCBP's Rocksil 200) would be used in both high-temperature applications and for flat roofs (where there was vigorous competition from EPS, XPS and PUR). Another slab (for example, Rocksil 100) could be used in high-temperature applications as well as for factory flooring (where there was ample competition from glass wool, EPS and PUR). Those building applications accounted for a much larger proportion of sales than did the high-temperature process applications for mineral wool.

6.92. In the case of pipe sections, the situation as to price and specifications was even more transparent and unpropitious for price discrimination according to end-use because stone wool pipe sections were made only in one density, albeit in a variety of thicknesses and inner diameters. Pipe sections for the H&V sector differed slightly from pipe sections for process applications by usually having a foil

facing applied at the factory. However, some unfaced pipe sections were also used in H&V applications and some faced sections were used in process applications. Furthermore, a pipe section used for high-temperature process applications would also be used in much larger volume applications at lower temperatures where it was subject to competition from glass wool, phenolic foam, ENR and PUR. For example, OCBP pipe insulation could be used in a catalytic cracking plant but could also be sold (via the same specialist distributors) for use on chilled liquid pipes in industrial processes where it competed with phenolic foam, ENR and glass wool. Glass wool, PUR and phenolic foam in particular provided vigorous price competition to stone wool products used in non-high-temperature applications. Owens Corning told us that it was unable to see how a manufacturer could achieve dual pricing of the same stone wool product for different applications.

6.93. Eur Ing Morgan's report examined the characteristics of stone wool products in those applications and concluded that the products were equally suitable for other applications, where they were also subject to competition from other insulation materials substitutes. He had also noted that there were a variety of substitutes for high-temperature applications.

Wired mat

6.94. In addition to considering the effects of the merger on the supply of stone wool slabs and pipe sections, Owens Corning also considered its effects on the supply of wired mat. Owens Corning said that the merger would cause no adverse effects in supply of wired mat. Wired stone wool mat was a flexible product used for cladding tanks and vessels with awkward shapes which could not easily be clad with rigid slabs. Its usage in the UK, however, was extremely limited: for example, in a petrochemical plant a minute percentage of the plant would be clad with wired mat. Within that small segment, the principal insulant at temperatures above 540°C was Capoplastic, a form of calcium silicate plastic mix spread over the vessel and cured. Capoplastic was cheaper than stone wool mat and easier to apply. There were other mixes similar to Capoplastic using perlite and vermiculite. The cost of installation of wired mat was considerable because it had to have a protective coating applied after the mat was fixed to the vessel. Indeed, it was only recently that wired stone wool mat had begun to make limited inroads into this segment. Moreover LFG, another UK stone wool manufacturer, produced wired stone wool mat. Although its total stone wool capacity was thought to be very small compared with that of Queensferry, most of that capacity was devoted to wired mat. Also, given that mat was a higher-value product, there were also considerably more imports of it than of lower-value products, particularly from Germany and from Austria (Heraklith). For use below 540°C glass wool wire mat was also produced by St-Gobain.

Fire resistance and fire protection

6.95. Finally, Owens Corning considered the effects of the merger on the supply of fire resistance and fire protection products. Owens Corning did not believe there was any material risk of insufficient competition in the supply of these products. The fire protection sector fell under three main headings: cladding of structural steel beams in buildings; sealing of continuous cavities in buildings, for example to prevent the spread of fire; and barriers to prevent spread of fire and smoke in large concealed spaces in buildings (for example, roof spaces above ceilings).

6.96. In those applications, the primary requirements were that the product be non-combustible, that it did not burn through within the minimum time prescribed for a given application and that it produced no toxic fumes and little smoke. Glass wool was non-combustible and produced little smoke, but it burnt through in around 15 to 30 minutes, whereas some other products would withstand four hours or more.

6.97. For structural steel cladding, the main products were various forms of boards and sprays treated with calcium silicate or vermiculite. Although most of these boards were more expensive than stone wool slabs, they tended to be specified by architects (who were extremely influential in this sector). The major board manufacturers were Cape Insulation Products and Promat. Mandoval, which

also specialized in fire protection, manufactured mainly sprayed vermiculite products. In addition, Cafco, the largest fire protection mineral wool board distributor, imported stone wool fire protection slabs from Partek. Owens Corning believed that Cafco's sales of such slabs in the UK were probably larger than Rockwool's. Finally, increasing use was being made of intumescent, particularly where the beams were required to have a pleasing appearance, for example in supermarkets. Those were sprayed or brushed on to the steel structure: with fire they expanded and charred, leaving a protective layer.

6.98. In the fire-sealing application the protective product was a mastic, usually based on calcium silicate, rather than a board or slab. Coated stone wool slab competed with many other boards coated with an appropriate mastic. OCBP did not itself produce mastic-coated products but supplied manufacturers with slab for coating. Other substitutes included granular materials made in small packages and coated with intumescent material. These were slightly more expensive than the various types of boards and slabs, but had the long-term cost advantage of being easier to remove and re-use (for example, if pipework had to be repaired in the cavity).

6.99. For smoke and fire barriers in larger concealed spaces, wired stone wool mat could be used. This product was manufactured by Rockwool, OCBP (in very small quantities) and LFG. However, fire curtains were also widely used and had a much lower installed cost than wired stone wool mat. They were made of woven glass cloth covered with a fire-resistant mastic similar to those used in fire-sealing products. The principal manufacturers of fire curtains were TBA Textiles and LFG. There was consequently no risk of insufficient competition in the fire protection sector if the acquisition proceeded.

Prices

6.100. Owens Corning did not believe that if the merger proceeded it would lead to price rises for either stone wool or glass wool. As regards stone wool, the availability of a wide range of substitute products and the inability in the vast majority of cases of even a sole manufacturer, as Rockwool would be for some products, to identify orders destined for a high-temperature application in the industrial process market meant that the scope for differential price increases in that market would be very limited and short lived. In addition, stone wool prices had been static or declining in recent years and any attempt to raise them materially would be resisted strongly by buyers. The competition from all the other substitute products would be important in such resistance by buyers, as would the latter's considerable purchasing and bargaining power (see paragraphs 6.74 to 6.76).

6.101. We asked Owens Corning whether it thought that OCBP's stone wool prices were lower than Rockwool's. Owens Corning believed they were as OCBP was number two among stone wool suppliers in the UK. We therefore asked Owens Corning whether the fact that OCBP's stone wool prices appeared on the whole to be lower than Rockwool's would not give Rockwool a ready opportunity to raise prices. OCBP did not accept that that necessarily followed. Owens Corning itself would provide a competitive check to such pricing behaviour through its continued presence in stone wool sales and the more extensive product range which it would have from being able to offer glass wool suitable for applications above 230°C. At present OCBP often subverted Rockwool's specifications and set its prices competitively against Rockwool to win business—though Rockwool, too, was very price competitive in what was a very aggressive market.

6.102. We put it to Owens Corning that Rockwool envisaged being able to increase prices for some of its stone wool products in the event of the merger proceeding and asked Owens Corning in which part of the market it thought such price increases might be targeted. Owens Corning said it would be very difficult for Rockwool to raise prices, particularly given the power of the distributors which were its main customers. The industrial sector was perhaps the most likely but Rockwool would face the difficulty of determining when a pipe section order, for example, was destined for a high-temperature application rather than, say, to cover a chilled pipe in which case other materials, including glass wool, could be used. Moreover, if Rockwool did try to raise prices in this sector it would assist OCBP's strategy of increasing glass wool's share of sales. Therefore, Owens Corning did not believe that prices were likely to rise as a result of the merger.

6.103. We asked Owens Corning if it disputed the suggestion put to us that OCBP was a weak competitor in the industrial process sector and would become even more so if the merger proceeded. Owens Corning acknowledged that OCBP could be viewed as a minor competitor in the sector. There might be a perception in the market that the stone wool technology used by OCBP was less up to date than Rockwool's. However, Owens Corning was a large company with large resources. OCBP's agreement with Partek to import, *inter alia*, stone wool pipe sections, and the high-quality glass wool pipe sections now available from Owens Corning plants in China (which were being test marketed in the UK) would enable OCBP to offer a significant challenge in what was not, after all, in the higher-temperature applications, a very large market.

Entry to the market

6.104. We asked Owens Corning whether it had offered to sell Queensferry to anybody other than Rockwool.

6.105. Owens Corning said that it had very much left the search for a buyer to its merchant bank, Flemings. [

Details omitted. See note on page iv.

] were not considered as being in a position to achieve the same synergies and operating efficiencies from owning Queensferry as would Rockwool and were thus not approached. [*Details omitted. See note on page iv.*] Rockwool was thus viewed as the only credible and acceptable bidder for Queensferry. Subsequently, [✕] approached Flemings to indicate a preliminary interest in Queensferry but by then Owens Corning was anxious to complete the negotiations with Rockwool and not risk delaying them by opening new discussions with another potential purchaser.

6.106. We asked Owens Corning why it was depriving itself of the competitive capability to manufacture both stone wool and glass wool in the UK [*Details omitted. See note on page iv.*]. Owens Corning said that as stone wool manufacture was not within its core competence and it did not control the technology used (which was Partek's), its prospects of earning a satisfactory rate of return from Queensferry were poor even after a programme of restructuring. Hence its firm intention to withdraw from stone wool manufacture in the UK. Owens Corning explained that OCBP would maintain its competitive position by continuing to supply both stone wool and glass wool in the UK. Therefore, whilst it remained strongly committed to the manufacture of glass wool for the UK market, its plans to develop its market position would continue in conjunction with the supply of stone wool purchased from other producers thereby enabling it to supply customers with a range of insulation materials (stone wool, glass wool and XPS).

Benefits of the merger

6.107. Owens Corning thought that customers in the market would benefit from the greater competitive pressure which OCBP's ability to offer glass wool products for the 230°C to 540°C range would provide. There would not only be sharper marketing focus by OCBP: it would also invest more in what was its core glass wool competence. If the merger were to proceed, Owens Corning believed that Rockwool would be likely to invest in capacity expansion, which would be beneficial to job security at Queensferry.

Remedies

6.108. We asked Owens Corning to comment on a number of possible remedies which we might recommend be undertaken by Rockwool in the event of our concluding that the merger might be

expected to operate against the public interest because of its effect on competition in the supply of stone wool.

6.109. Owens Corning found it very difficult to envisage the type of control over Rockwool's realized prices for particular products which would ensure, for example, that they could not be increased faster than the general rate of inflation or an index of building material prices. The large numbers of customers and the wide variety of discounts, rebates and individually negotiated prices would make such a measure hard to implement and monitor. Moreover, competition in the market might as a result be distorted, to the detriment of customers.

6.110. Owens Corning thought that a requirement to supply all would-be customers which met specified criteria, such as in terms of minimum order quantities, subject only to creditworthiness, could be difficult to fit into Rockwool's current practices. Rockwool's insistence on full loads reflected the production orientation of its Bridgend plant, which might or might not be adaptable to the different customer base of the Queensferry location. However, Owens Corning said that it believed it might be feasible for Rockwool to offer less than full lorry loads, although it could not say whether Rockwool would want to do so. As for OCBP, when supplying less than full lorry loads it tried to recoup the extra cost from the customer, although it did not always succeed.

6.111. A requirement to offer equivalent terms for equivalent orders appeared on the surface more straightforward but could be subject to real difficulties of interpretation, definition and monitoring. The same applied to the fourth hypothetical remedy, that Rockwool undertake to continue to supply a specified range of products unless it could demonstrate to the OFT in any particular case that the termination of a product line was economically justified. In any event, Owens Corning believed Rockwool would only wish to terminate a product line if it was no longer economically justified to keep it going.

6.112. Owens Corning thought that some form of price reporting by Rockwool might help to allay concerns of smaller customers (possibly converters or fabricators). Owen Corning did not believe that Rockwool would be able to raise prices as a result of the merger, in particular to large customers, or discriminate in prices for products sold for higher-temperature applications. However, price reporting might be useful in enabling a check to be made on prices charged to smaller customers.

6.113. Owens Corning believed that, in addition to price reporting, the interest of fabricators and converters could be safeguarded by moving the [3.1] fabricator/converter and OEM customers in the 'non-compete' customer list in Part B of Schedule 13 to the Business Sale Agreement to the 'compete' list (see paragraph 3.5 and Appendix 3.1). OCBP could then continue to supply them. Provided the sales were not major, such a remedy might be acceptable to Rockwool. A variant would be to move from the 'non-compete' customers list to the 'compete' list all customers whose purchases of stone wool from OCBP were below, say, £[3.1] a year: that would move [3.1] customers from the one list to the other. In addition, since the non-compete covenant applied to customers listed in Schedule 13 as having purchased stone wool from OCBP in the first half of 1998, OCBP would be free to sell to any other customer not listed in the schedule. For example, any dissatisfied Rockwool customer which was not an OCBP customer in the first half of 1998 for stone wool would be free to purchase from OCBP.

6.114. Owens Corning also suggested that if there were concerns about additional types of products not included among the five product ranges listed in the Supply Agreement which it could purchase from Rockwool at specified discount rates (see paragraph 3.5 and Appendix 3.1), those additional products could be included in the agreement, provided that OCBP would be able to purchase them from Rockwool at discounts no more disadvantageous than those offered by Rockwool to distributors buying similar volumes of them. (Rockwool would necessarily have to agree to such amendment of the agreement.)

Consequences of the merger being prohibited

6.115. At our first hearing with Owens Corning we asked about the likely consequences of any decision to prohibit the merger, including the strategy which it would be likely to pursue in that event.

Owens Corning said that it would have to review how it might be able to improve the profitability of Queensferry. It would neither expand future capacity nor make any commitment to support stone wool manufacture. The result would be a restructuring and rationalization programme as a means of improving plant profitability. Similar restructuring and rationalization reviews had taken place at Owens Corning's Visé plant in Belgium and at plants in the USA: at Visé in 1998 it was decided to reduce staff levels and the number of product lines offered in order to reduce costs and focus on the most profitable lines. Sale of Queensferry to another purchaser was also an option, but not immediately.

6.116. We enquired in more detail about these aspects at our second hearing with Owens Corning towards the end of the inquiry. The company said that, although no restructuring and rationalization had so far been carried out at Queensferry while the sale was still pending, the first step would be to adjust the plant loading and workforce levels to the reduced demand which had resulted from the uncertainty over Queensferry's future. Sales were estimated to be down by as much as [30] per cent compared with the previous year. Reduction in the number of shifts was likely, with a reduction in output to about [30] tonnes. The product range would be rationalized by eliminating a number of products being sold at a loss or at low margins, [*Details omitted. See note on page iv.*]. The more profitable stone wool lines would be promoted and working capital reduced. An example was [30] which were currently unprofitable, whereas a positive margin could be earned on imported sections. These changes to product range and staffing levels would be made quickly. [*Details omitted. See note on page iv.*].

6.117. At the same time, Owens Corning would quickly look for another buyer, though it doubted the feasibility of that. It had approached [30] a second time but that company had not changed its position. [

Details omitted. See note on page iv.

the price were acceptable but [].

]. It was hard to rule out anything if *Details omitted. See note on page iv.*

6.118. Owens Corning added that it had not so far carried out extensive research for the purpose of finding a potential purchaser. If it were to do so, it would probably look first at other stone wool manufacturers such as [30]. Owens Corning would be prepared to spend [30] looking for an alternative buyer to Rockwool. At that point in the inquiry, however (that is, at the second hearing), Owens Corning said it thought that apart from Rockwool there was unlikely to be any viable purchaser for Queensferry.

6.119. If no other acceptable buyer were found another major decision would be necessary. Options would be limited: the plant could be closed or mothballed or even, which was another option under consideration, shipped to South Africa where Owens Corning had a stone wool plant in need of modernization. Owens Corning accepted that a programme of rationalization and restructuring might be perceived unfavourably. However, customers were already well aware of Owens Corning's intention to take the necessary steps to try to return Queensferry to adequate profitability. It would be difficult to achieve that object but there would be no alternative to it. The rationalization programme would have no effect on the measures (such as the Partek and Icerock agreements) being taken by OCBP to retain a significant place in the market for the supply of stone wool in the UK.

6.120. How long Queensferry might be kept going by Owens Corning if another buyer could not be found was uncertain—[~~£~~]. If Queensferry were to be closed the cash costs of doing so were estimated to be some ~~£~~ million to ~~£~~ million.

D P B KINGSMILL (*Chairman*)

P MACKAY

K M H MORTIMER

T S RICHMOND

J D S STARK

P A BOYS (*Secretary*)

1 April 1999