

**COMPETITION TRIBUNAL
REPUBLIC OF SOUTH AFRICA**

Case no.: 57/LM/Aug04

In the large merger between:

Astral Operations Ltd

and

Earlybird Farm (Pty) Ltd

Reasons

Introduction

On 8 September 2004 the Tribunal approved the merger between Astral Operations Limited and Earlybird Farm (Pty) Ltd without conditions. The reasons are set out below.

The transaction

Astral Operations Limited ("Astral") and Afgri Operations Limited ("Afgri") jointly controlled Earlybird Farm (Pty) Ltd ("Earlybird") in which each held 50% of the issued share capital. Astral Operations is now acquiring Afgri's 50% shareholding after which it will have sole control of Earlybird.

Astral is a vertically integrated company in the broiler industry; it is the sole distributor and supplier of both Ross 788 and 308 breeding parent stock to the broiler industry; it supplies day-old chicks to non-integrated independent broilers as well as parent stock to its own integrated businesses. In addition it also mills and supplies various types of animal feed, supplies animal feed pre-mixes that contain vitamin and minerals and is involved in animal healthcare. The Astral Foods Group controls, in addition to its Earlybird joint venture, Meadow Feeds (Pty) Ltd, Nutec SA (Pty) Ltd, County Fair Foods (Pty) Ltd, Central Analytical Labs, National Chicks Limited, Ross Poultry Breeders (Pty) Ltd, National Veterinary Supplies (Pty) Ltd and Elite Breeding Farms.

Earlybird is a fully integrated broiler producer, which markets a full range of frozen, fresh and value-added chicken products.

Rationale for the transaction

In terms of their Shareholders agreement, Astral Foods and Afgri could not start any new business that competed with the Earlybird joint venture.¹ This agreement did not cover County Fair Foods. Tension between the shareholders arose, as Afgri perceived that Astral had a conflict of interest as it could expand its broiler production through Country Fair, which it owned 100% of, while Afgri was bound to only expand its broiler business through Earlybird. The parties eventually resolved their dispute by Astral making an offer to purchase Afgri's shareholding in Earlybird.

The acquisition enables Astral to transfer the expertise, which County Fair has acquired in supplying fresh chicken products to the Western Cape region, to Earlybird.

One of the conditions to the transaction being concluded successfully is a supply agreement concluded between Earlybird and Afgri in terms of which Afgri will continue to supply Earlybird with a specified quantity of feed for 9 years. Both Astral and Afgri supplied feed to Earlybird in the past. The reason for this is that Astral's mill doesn't currently have the capacity to supply all of Earlybird's needs. The period is seen as the time needed to adjust its milling capacity.

Afgri has indicated that, in future, it intends to enter the broiler market on its own and would thereby create its own feed customer.²

The relevant market

This is a horizontal merger. Astral's subsidiaries, County Fair and Earlybird, are both fully integrated broiler producers and operators, which produce day-old chicks and broilers, as well as process, pack, distribute and sell chicken products. Accordingly, both compete in the same product markets.

The parties claim that the relevant product market is the very broad market for animal protein products, which includes beef, pork and mutton. However, if the Tribunal requires a more narrow delineation of the relevant market they would be prepared to accept an international market for poultry products, which could be split into a international market for frozen poultry products and a regional market

¹ See clause 6.19 of the Shareholders Agreement on page 551 of the record.

² See transcript on page 8.

for fresh poultry products.

The Competition Commission is of the view that the relevant product market should be defined more narrowly as the market for the producing and processing of poultry products consisting of frozen and fresh poultry products, value added or processed poultry products and poultry offal. The geographic market is national for all the various products except for fresh poultry products, which falls within a regional geographic market due to its limited shelf life.

Whether we define the relevant market broadly or more narrowly, for purposes of this evaluation, is not important. Since, as we show below the merged entity would not gain market power as a result of the transaction.

Effect on competition

Rainbow, which owns the Rainbow, Bonny Bird and Farmer Brown brands, is the only other vertically integrated poultry producer in South Africa. It sells the Cobb breed and is the largest broiler producer in South Africa. Other competitors in the market are Tydstroom Pluimveeplaas, which belongs to Pioneer Foods and owns the Tydstroom brand, Country Bird, which owns the Supreme brand, Daybreak farms, which owns the Superior brand and Chubby Chicks.

The following table represents the market shares of some of the largest competitors in the broiler market before the merger:

Broiler producers	Market share %
Rainbow Farms	28
Earlybird farms	17
County Fair Foods	8
Tydstroom Pluimveeplaas	8
Country Bird	6
Medium sized farmers	5

Daybreak farms	3
Chubby Chicks	2

Post the transaction Astral will have a market share of 25%, closely matching that of its biggest rival Rainbow Farms, which has 28%.

Barriers to entry in this industry are high insofar as capital and sunk costs are concerned, specifically if a new entrant wants to establish a grass roots integrated meat production business such as Astral Foods or Rainbow. Moreover, such an entrant would need substantial lead-time, close to 86 weeks, in order to begin producing and selling broilers to its customers. There are also regulatory requirements to ensure meat safety etc.³

However, entry barriers into the non-integrated broiler market, in which Earlybird and County Bird compete, are lower, in that players in this market are regional and concentrate on specific niche products such as fresh or live birds in order to avoid incurring capital outlay in the form of processing plants and equipment. The lead-time to enter in this segment is 24 weeks.⁴

Although Earlybird management from internal documents appears to have regarded County Fair as a competitor it seems that this competition was limited to frozen poultry as given the geographic locations of the plants, Gauteng and Western Cape respectively they were not competitors in respect of the fresh poultry product. The frozen poultry market because of the ease of entry is more contestable than the fresh one.

Major retailers have the ability to import poultry directly from Brazil and Canada at prices that are competitive with those offered locally.

In light of the above we found that the transaction would not substantially lessen or prevent competition. In fact the dismantling of the joint venture enables Afgri, which has the knowledge and experience to compete in the broiler market, to enter as an effective competitor to Early Bird and County Fair, something it could not have done while it was party to the joint venture.

Public interest issues

³ Meat Safety Act No 40 of 2000.

⁴ As indicated earlier in the decision Afgri informed the Tribunal that it would be entering the broiler market sometime in the future.

The transaction does not raise any public interest concerns.

N Manoim

20 September 2004
Date

Concurring: L Reyburn, M Mokuena

For the parties: Lee Mendelsohn from Edward Nathan
For the Competition Commission: M van Hoven