



COMPETITION TRIBUNAL OF SOUTH AFRICA

Case No: 09/LM/Feb11

In the matter between:

**Lexshell 826 Investments (Pty) Ltd
Firm**

Acquiring

And

**Umcebo Mining (Pty) Ltd
Firms
Mopani Coal (Pty) Ltd**

Target

Panel : Yasmin Carrim (Presiding Member)
Andreas Wessels (Tribunal Member)
Medi Mokuena (Tribunal Member)
Heard on : 02 June 2011
Order issued on : 02 June 2011
Reasons issued on : 04 August 2011

Reasons for Decision

APPROVAL

- 1] On 02 June 2011 the Competition Tribunal ("Tribunal") unconditionally approved the transaction involving *inter alia* Lexshell 826 Investments (Pty) Ltd, Umcebo Mining (Pty) Ltd and Mopani Coal (Pty) Ltd. The reasons for approval of this transaction follow below.

PARTIES TO THE TRANSACTION

- 2] The primary acquiring firm is Lexshell 826 Investments (Pty) Ltd (“SPV”), a private company incorporated in terms of the company laws of South Africa. SPV is a special purpose vehicle established for purposes of this transaction. The shareholding in SPV is held as follows:

- Lexshell 827 Investments (Pty) Ltd (“BEECo”), an empowerment company incorporated in accordance with the company laws of South Africa, has a 50.1% shareholding interest in SPV;

Dremalo BV (“Dremalo”), a private company incorporated in accordance with the company laws of the Netherlands, has a 29.441% shareholding interest in SPV. Dremalo is a wholly-owned indirect subsidiary of Glencore International AG (“Glencore”). Glencore *inter alia* has a 34.4% shareholding interest in Xstrata Plc (“Xstrata”)¹ and a 70% shareholding interest in Shanduka Coal (Pty) Ltd (“Shanduka”); and Moxitorque Investments (Pty) Ltd (“SmitCo”), a private company incorporated in accordance with the company laws of South Africa, has a 20.459% shareholding interest in SPV.

- 3] BEECo, Glencore and SmitCo are the other acquiring firms (see description of transaction in paragraph 6 below).

The primary target firms in the Umcebo acquisition (see description of transaction in paragraph 6 below) are (i) Umcebo Mining (Pty) Ltd (“Umcebo”); and (ii) Mopani Coal (Pty) Ltd (“Mopani”). Both Umcebo and Mopani are private companies incorporated in terms of the company laws of South Africa. The shareholding in Umcebo is as follows: Umcebo Holdings (Pty) Ltd - 50.1%; Mopani - 44.9%; Scaup Holdings Ltd (BVI) - 2.75%; and AMCIC-AMCI Umcebo JV (Mauritius) Ltd - 2.25%.

The other target firms are Inyanga Trading 35 (Pty) Ltd (“Inyanga”) and Jicama 81 (Pty) Ltd (“Jicama”) (see description of transaction in paragraph 6 below). According to the merging parties Umcebo, Inyanga and Jicama historically have effectively operated as a group. Any reference below to Umcebo will refer collectively to the activities and operations of these three firms.

DESCRIPTION OF THE TRANSACTION

- 4] The proposed transaction involves a number of composite transactions in terms of which a number of firms which pre-merger directly or indirectly holds shares in Umcebo have negotiated sales agreements with the acquiring firms. The merging parties submitted that this composite transaction consists

¹ According to the merging parties it is not clear whether or not Glencore has *de facto* control of Xstrata through its shareholding. The Commission considered the activities of Xstrata in its competition analysis.

of three inter-related and interdependent components:

- i) first, SPV intends to acquire a 55.1% shareholding interest in Umcebo and a 100% shareholding interest in Mopani. Given Mopani's pre-merger interest in Umcebo (see paragraph 4 above), this acquisition therefore will effectively give SPV a 100% shareholding interest in Umcebo ("Umcebo acquisition");

second, Dremalo and SmitCo intend to acquire respective shareholding interests of 29.5% and 20.5% in Inyanga, a subsidiary of Umcebo; and third, Dremalo and SmitCo intend to acquire respective shareholding interests of 20.65% and 14.35% in Jicama, also a subsidiary of Umcebo.

RATIONALE FOR TRANSACTION

- 5] For the acquiring firms the rationale is that the proposed transaction will *inter alia* secure access to resources in the Mpumalanga coal fields, which enjoys an established infrastructure for the transportation of export quality thermal coal. They furthermore submit that the transaction raises the potential for financial and operational synergies.
- 6] Umcebo submitted that this transaction will provide it with financial, operational, balance sheet and administrative flexibility.

BACKGROUND

- 7] We provide some background information below regarding the Richards Bay Coal Terminal (RBCT) in order to contextualise the activities of the merging parties relating to the export of coal from South Africa as well as a complaint that the Competition Commission ("Commission") received from a black-owned junior coal mine, Endulwini Resources Ltd, which relates to *inter alia* limited access to the RBCT for the export of coal (see paragraphs 24 to 35 below).

The majority of coal exports from South Africa are shipped from the RBCT, which is the single largest coal export terminal in the world. It opened in 1976 and has grown with several upgrades into a 24-hour operation with a design capacity of 91 million tons of coal per annum since its "Phase V" expansion of 2010.²

The major international mining companies have export allocation rights in regard to the RBCT. The major shareholders in the RBCT are Anglo Operations Ltd, BHP Billiton Energy Coal South Africa Ltd and Extrata SA (Pty) Ltd. The other shareholders, holding the balance of the export allocations, include

² See www.rbct.co.za.

Optinum Coal Holdings (Pty) Ltd, Total Coal South Africa (Pty) Ltd, Sasol Mining (Pty) Ltd, Kangra Coal (Pty) Ltd, Exxaro Coal (Pty) Ltd and Koorfontein Mines (Pty) Ltd.

Recent expansions of the RBCT's capacity have however resulted in certain junior South African coal mining firms also obtaining export allocations. More specifically, as stated above, the RBCT's Phase V expansion project increased the port's export capacity to 91 million tonnes of coal per annum. As a result of these expansions the following additional export allocations have been granted:

- i) an allocation of four million tonnes per annum of coal export capacity has been made to 18 BEE coal producers for a minimum three-year period ("the Quattro Scheme"). At the end of each year the past performance is reviewed and the next three-year period is considered. The Quattro scheme was agreed to by the RBCT to broaden use of the terminal by non-member, BEE coal producers following criticism that it was restricting access to the coal export markets. These quotas are made available on a commercial basis without any entitlements to shareholding in the RBCT; and

in terms of the Phase V expansion project an allocation of 19 million tonnes of coal per annum have been made to BEE coal mining firms. This scheme is intended to give these firms shareholding in the RBCT.

- 8] Current rail and loading capacity constraints however restrict the ability of these BEE firms to make full use of their allocations at this time. South Africa's national utility, Transnet, provides the railway services linking the coal mines to the port. The merging parties submitted that there at present exists a mismatch between the capacity of the RBCT to load coal onto vessels and the capacity of Transnet Freight Rail (TFR) to transport coal from the coal mines to the port. They submitted that the rail capacity at present is only approximately 63 million tonnes of coal per annum.

ACTIVITIES OF MERGING PARTIES

Acquiring group

- 9] SPV, BEECo and SmitCo do not currently have any business operations. Glencore is a trader in coal in South Africa and, more specifically, purchases thermal coal from a number of South African thermal coal producers.

The other firms within the acquiring group whose activities are relevant for purposes of the competition assessment of this transaction are Shanduka and Xstrata. Xstrata comprises of five major businesses which are housed in various entities, namely a coal, copper, zinc, alloys and nickel business. Of relevance to this transaction is its coal business which is involved in the mining

of thermal and coking coal in South Africa, Australia and Colombia as well as in an exploration project in Canada. Shanduka, through various subsidiaries, operates a number of coal mines. Shanduka also has a coal export allocation at the RBCT under the Quattro allocation (see paragraph 12 above).

Target firms

- 10] Umcebo operates three thermal coal mines, namely Klippan, Middelkraal and Kleinfontein as well as two stand-alone coal beneficiation plants at Strathrae and Doornrug (a coal crushing and wash plant). All these mines are situated in the Mpumalanga province of South Africa.

According to the merging parties' submissions, Umcebo will have a total export allocation of 1.5 million tonnes of coal at the RBCT once the TFR network achieves a capacity of 91 million tonnes per annum (see paragraphs 10 to 13 above). This allocation includes a one million tonne allocation in favour of Umcebo through the RBCT Phase V expansion projection.

COMPETITION ANALYSIS

Horizontal overlap

- 11] The merging parties' activities overlap in respect of the mining and sale of thermal coal. Thermal coal is used in power generation and also has certain industrial uses, for example as an energy input in the cement production process.
- 12] In line with previous Tribunal decisions³ we distinguish several relevant coal markets: first, a delineation of bituminous coal from other types of coal; and second, a delineation between two types of bituminous coal, namely thermal and metallurgical coal.⁴ The broad bituminous thermal coal market can be further divided into three separate relevant product markets, namely:⁵
- (i) the export market i.e. bituminous thermal coal exported by South African producers (mainly to the Atlantic Basin and the Pacific Rim);
 - (ii) the "tied" domestic market i.e. bituminous thermal coal sold to two domestic customers namely Eskom and Sasol; and
 - (iii) the residual domestic market i.e. the sale of bituminous thermal coal to domestic companies other than Eskom and Sasol, for example

³ See the large merger involving *Optimum Coal Holdings (Pty) Ltd, Optimum Koornfontein Investments (Pty) Ltd and Main Street 431 (Pty) Ltd, Twin Cities Trading 39 (Pty) Ltd and Dunrose Trading 191 (Pty) Ltd*, case no. 86/LM/Dec09.

⁴ See, for example, the large merger involving *Anglo South Africa Capital (Pty) Ltd and Arnot North Mining Business and Additional Reserves*, Case no. 44/LM/May05.

⁵ See, for example, the large merger between *Lexshell 668 Investments (Pty) Ltd and Wakefield Investments (Pty) Ltd*, Case no. 82/LM/Oct06.

cement companies and smaller coal mines requiring coal for market blending.

13] Regarding the relevant geographic market, the Commission did not deem it necessary to come to a definite conclusion in respect of the above-mentioned domestic thermal coal product markets, i.e. whether they are national or regional in geographic scope since the merging parties will continue to face competition from significant competitors whose mines are located within relatively close vicinity of the merging parties' thermal coal mines (also see paragraph 22 below). We concur with this approach of the Commission to the delineation of the relevant geographic market.

14] With regard to market shares, the merging parties' combined post merger national market shares in the various relevant product markets are as follows:

i) export market – less than 20%;

“tied” domestic market – less than 10%⁶; and
residual domestic market – less than 20%.

15] The competitors of the merging parties in all three relevant product markets are large well-established companies such as Anglo Coal, Exxaro Coal and BHP Billiton. From a potential regional geographic market perspective, according to the Commission's findings the proposed deal still is unlikely to raise competition concerns since the coal mines owned by Anglo Coal, Exxaro, BHP Billiton and Optimum Coal are located with a 50 to 80 km radius of the merging parties' coal mines in Mpumalanga.

Vertical assessment

16] There is a vertical relationship between the merging parties since Umcebo supplies Glencore and Xstrata with thermal coal. The Commission however found that given the number of other producers of thermal coal in South Africa, including significant players such as BHP Billiton, Exxaro, Anglo Coal and Optimum Coal, the proposed deal raises no significant input foreclosure concerns. The Commission further found that given the relatively low volumes of thermal coal purchases of Glencore and Xstrata in terms of the

⁶ Sasol's coal production is excluded from this market share analysis since it uses the coal internally within Sasol.

overall size of the market(s) in question, the proposed transaction is unlikely to give rise to any significant customer foreclosure concerns. We therefore do not discuss these vertical issues any further in these reasons.

Third party complaint from Endulwini

- 17] The Commission received a complaint in regard to the proposed deal from Endulwini Resources Ltd (“Endulwini”), a black-owned junior mine.⁷ However, no other third party raised any concerns in regard to the proposed merger.

Endulwini’s concerns raised with the Commission include:

- i) that the proposed merger will remove an effective competitor from the market and will also negatively impact Endulwini’s competitiveness as a junior mine as well as that of other junior mines. Endulwini therefore was of the view that it or one of the other junior mines should rather acquire Umcebo or its assets;

allegations of restrictive practices under sections 4 and 5 of the Competition Act, 1998 (Act No. 89 of 1998, as amended) (“the Act”) involving Glencore and a number of complicit participants in various agreements. Endulwini therefore requested the Commission to launch an investigation into various Glencore agreements, including off-take, marketing, financing and joint venture agreements; and very restrictive access to the RBCT, which is problematic for junior coal miners seeking to export their product to the international coal markets.

- 18] Mr S. Nodwele⁸ of Endulwini made further submissions in regard to its concerns at the hearing. Its main concern related to the export of coal.
- 19] On the issue of access Endulwini submitted that junior coal miners producing export coal face difficulties regarding the exportation of their coal at the RBCT since the terminal has generally been controlled by the “*previously white-owned*” large mining entities. We were further informed that in order to allow junior black coal miners to export their coal, the (former) Department of Minerals and Energy set up the Coal Industry Task Team (“CITT”) to oversee the Quattro scheme.⁹ Endulwini submitted that its concerns specifically relate to Glencore acquiring Umcebo’s allocation in the RBCT Quattro

⁷ See letter including annexures at pages 1058 to 1067 of the record.

⁸ The Head of Legal at Endulwini.

⁹ The CITT is chaired by the Department of Mineral Resources and comprises coal industry stakeholders such as TFR, the RBCT, Transnet National Ports Authority (TNPA) and BEE junior coal producers.

scheme. This situation, according to Endulwini, is undesirable as the acquisition will lead to one less black mining firm being able to export its coal which goes against economic transformation in the country. Mr Nodwele argued that it is incumbent on the CITT to consider the issue of a change in ownership of RBCT allocations made specifically to emerging black coal miners in order to enhance their share in the South African coal export market. Mr Nodwele further submitted that Glencore could never be viewed as an “*emerging*” black coal mining firm.

- 20] The Tribunal enquired whether there are any conditions attached to the RBCT export allocations to BEE firms that relate to the transfer to a third party of these allocations. Mr Nodwele stated that to its knowledge the allocations to BEE coal miners cannot be transferred to a third party without the consent of the CITT. Mr Nodwele in this regard stated “... *that allocation belongs to the CITT, they are the custodians of that allocation, so for you to enter into a transaction which sees the passing of that ownership and I put ownership in brackets because it is not ownership, you are merely—because of your profile as a black junior coal miner you are afforded an opportunity to pass coal through the RBCT and you just cannot simply sign it away, it is not yours to sign away hence there is a CITT allocations committee which looks at these types of things.*” Mr Nodwele further informed us that Endulwini will formally take up this issue with the CITT.

Merging parties’ response

- 21] In response to Endulwini, the merging parties submitted that this acquisition is not intended to take out an empowerment shareholder as has been suggested by Endulwini but merely replaces one set of empowerment shareholders with another since the controlling shareholder in the scheme is an empowerment shareholder. They alleged that the deal therefore is not detrimental to the interests of empowerment. The merging parties further alleged that the export coal market is not the only opportunity available for a junior coal miner and suggested that a number of junior coal miners have entered the coal markets over the last few years. In addition the merging parties indicated that in the 2010 RBCT Phase V expansion, empowerment companies, through a competitive bidding process, were given priority in the allocation of export capacity so as to increase their participation in the export market. On the issue of Glencore’s off-take agreements, the merging parties

averred that these agreements are standard supplier/customer arrangements which do not in any way restrict or inhibit the development of junior coal miners.

Commission's response

22] The Commission responded to Endulwini's concerns in its recommendation¹⁰ and at the hearing. In regard to the competition-related issues the Commission concluded that the change in market structure as a result of the transaction under consideration is not significant in any of the affected coal markets and that it is therefore unlikely that the instant merger would significantly alter the competitive landscape of these markets.

23] In regard to the alleged restrictive practices, the Commission found that the off-take agreements in question are not brought to existence as a result of this merger. The Commission further indicated that the issues raised by Endulwini in regard to the alleged anti-competitive off-take agreements as well as limited access to the RBCT will be highlighted to its Enforcement and Exemptions Division. The Commission at the hearing however indicated that it did not contact the CITT in regard to the issues raised by Endulwini.¹¹

24] The Commission further indicated that the proposed deal does not raise any significant public interest issues in terms of the Act.

Conclusion

25] The concerns raised by Endulwini in respect of the alleged contraventions of sections 4 and 5 of the Act do not appear to be merger-specific, i.e. they are not related to the instant transaction. Endulwini may consider lodging a formal complaint with the Commission regarding these concerns in the prescribed format.

26] We note that Endulwini contemplates taking up with the CITT the issue of the possible transfer, following the proposed transaction, of Umcebo's export allocation at the RBCT to the acquiring firms (see paragraph 28 above).

¹⁰ See pages 20 and 21 of the Commission's recommendation.

¹¹ Transcript page 22.

- 27] In regard to the limited coal export capacity at the RBCT and access by BEE firms thereto, we suggest that the Commission in its advocacy role should in a broader competition context engage with the relevant Government department and/or the CITT. The Commission may be able to advise the relevant structures in regard to the potential effects on (future) competition in the coal export market associated with the allocation of RBCT export capacity quotas and relevant conditions placed on such allocations.
- 28] From a horizontal and vertical competition perspective we conclude that the proposed transaction is unlikely to substantially prevent or lessen competition in the relevant markets.
- 29] From a coordinated effects perspective, there is no evidence that this merger would increase the likelihood of coordination in any of the relevant markets or that there is existing coordination in any of these markets. We however find that the pricing analysis performed by the Commission, which considers only limited pricing data relating to the export and spot market coal prices of only Umcebo and Shanduka, is too limited to come to any meaningful conclusions in regard to potential coordinated conduct or the closeness/effectiveness of competition between the merging parties.¹²

PUBLIC INTEREST

- 30] The merging parties submitted to the Commission that this transaction will not have any effect on employment and that no retrenchments will result from it. On the contrary, they submitted that the proposed transaction will generate employment since Umcebo will have the financial and operational support it requires to initiate the projects it intends undertaking.¹³
- 31] The Commission however received a complaint alleging that Shanduka retrenched employees in preparation of the instant transaction. It appears that in the last 24 months some 380 retrenchments took place within the acquiring group at the Lakeside, Springlake and Leeuwfontein mines. The

¹² The Commission suggested that this limited price analysis shows that the merging parties' coal producing firms are not effective competitors. There is however no reliable evidence to support such a conclusion.

¹³ See page 9 of the record.

Commission's investigation however confirmed that these retrenchments were the result of the closure of these mines which were no longer economically viable to operate. The Commission therefore concluded that these retrenchments are not linked to the proposed transaction and therefore are not merger-specific. We have no reason not to accept this conclusion.

32] The proposed deal raises no other significant public interest issues.

CONCLUSION

33] We conclude that there is no evidence that the proposed transaction is likely to result in a substantial lessening or prevention of competition in any of the affected markets. In addition, there are no significant public interest issues arising from this transaction. We accordingly approve the transaction unconditionally.

04 August 2011

Andreas Wessels

DATE

Yasmin Carrim and Medi Mokuena concurring

Tribunal researcher: Ipeleng Selaledi

For the merging parties: Adv D Unterhalter SC instructed by
WerksmansInc.

For the Commission: Thabelo Ravhugoni