ECONOMIC DEVELOPMENT DEPARTMENT

NOTICE 150 OF 2017

COMPETITION COMMISSION

NOTIFICATION TO PROHIBIT THE TRANSACTION INVOLVING:

ITALTILE LIMITED

AND

CERAMICS INDUSTRIES PROPRIETARY LIMITED

2016APR0207

The Competition Commission hereby gives notice, in terms of Rule 38 (3)(c) of the 'Rules for the Conduct of Proceedings' in the Competition Commission, that it has prohibited the transaction involving the above-mentioned firms:

Background

1. On 29 April 2016, the Competition Commission (Commission) received notice of an intermediate merger in terms of which Italtile Limited (Italtile) intends to acquire control of Ceramic Industries (Pty) Ltd (CIL) and Ezee Tile Adhesive Manufacturers (Pty) Ltd (Ezee Tile). On completion of the proposed transaction, Italtile will control CIL and Ezee Tile in terms of section 12(2)(a) of the Competition Act no. 89 of 1998, as amended (the Act).

The parties and their activities

2. The primary acquiring firm is Italtile, a public company listed on the Johannesburg Securities Exchange (JSE) in South Africa. Italtile is controlled by Rallen (Pty) Ltd (Rallen). Rallen currently has shareholding in CIL. Italtile indirectly, through its wholly-owned subsidiary Italtile Ceramics, currently owns shares in CIL.

3. In South Africa, Italtile does not manufacture any products. It is a retailer of imported ceramic and porcelain tiles, laminated boards, sanitaryware, brassware and bathroom accessories, décor, baths, showers and grout and adhesives to consumers. It owns and operates its own retail outlets comprising Italtile Retail, CTM and Top T, each targeting a specific market segment and located throughout South Africa. Italtile imports and distributes the products to its Italtile-owned retail outlets. All products imported by Italtile are A Grade products and are sold by the Italtile Group's retail outlets or are supplied to and sold by its franchise outlets. Italtile franchise outlets are located throughout South Africa.

4. The primary target firm is CIL. CIL is currently controlled by Rallen. The second target firm is Ezee Tile. Rallen indirectly controls Ezee Tile since it ultimately controls both CIL and Italtile Ceramics, who also hold shares in Ezee Tile.

5. CIL manufactures and supplies tiles, sanitaryware and baths to retailers including the Italtile Group. It is the largest manufacturer of ceramic tiles and glazed porcelain sanitaryware in South Africa, comprising of seven (7) manufacturing facilities in South Africa and one (1) in Australia. The tile factories (Samca Floor, Samca Wall, Vitro, Pegasus, Gryphon and Centaurus) manufacture a combination of pressed and extruded tiles in various sizes, textures and finishes, while the sanitaryware factory (Betta) manufactures a wide range of vitreous china sanitaryware, the main focus being on water closets, basins, cisterns and pedestals. CIL also owns three (3) factory shops that sell some of its B-grade produced tiles, sanitaryware and baths, grout and adhesives directly to consumers. The factory shops are located in Hammanskraal, Vereeniging and Krugersdorp (CIL factory shops). CIL also owns its own clay quarries situated in Vereeniging and Limpopo. Clay is an input material for the production of Tiles and Sanitaryware. Ezee Tile manufactures and supplies grout, adhesives and related products to retailers of these products, including the Italtile Group. Ezee Tile does not own or operate any retail outlets.

The transaction

6. The Commission considered whether the proposed transaction results in a change in control over the CIL and Ezee Tile businesses and whether this change results in a change in incentives in how the merged entity would behave post-merger.

7. The Commission finds that there will be a change in control and a change in incentives. The Commission finds that the proposed merger will strengthen the ability of the merging parties to self-supply and unilaterally increase prices post-merger.

8. Given the above, the Commission considered how the transaction would impact on competition post-merger by assessing the various factors described below.

Areas of overlap

9. The proposed transaction results in a vertical integration in the activities of the merging parties in relation to the upstream markets for the manufacture and supply of (i) tiles (ceramic and porcelain floor and wall tiles), (ii) sanitaryware, (iii) baths and (iv) grout and adhesives and related products and the downstream market for the retail sale of the products in South Africa.

Market shares

10. The Commission found that in relation to the national upstream market for the manufacture and supply of ceramic and porcelain floor and wall tiles, the pre-merger and post-merger market share of CIL is between 60% and 70%, with no market share accretion. As regards the national upstream market for the manufacture and supply of sanitaryware, the pre-merger and post-merger market share of CIL is between 60% and 70%, with no market share accretion. The remainder of the market shares are held by Vaal Sanitaryware (between 20% and 30%) and imports (between 20% and 30%).

11. In relation to the national upstream market for the manufacture and supply of baths, the pre-merger and post-merger market share of CIL is between 70% and 75%, with no market share accretion. The remainder of the market shares are held by Libra Bathrooms (between 20% and 30%) and imports (less than 5%). In the national upstream market for the manufacture and supply of grout, adhesives and related products the Commission found that the pre-merger and post-merger market share of Ezee Tile is between 30% and 40%, with no market share accretion. The remainder of the market shares are held by competitors such as Webber Tylon, Stick a Tile, TAL, Tile Magic and Multi Construction that will continue to constrain Ezee Tile post-

merger. There are numerous suppliers of the products such as Kwiktile, Titan Tiles, ETM, Icon and Tin Pro.

12. In relation to the national downstream market for the retail sale of the products, the pre-merger and post-merger combined market share of the merged entity is between 40% and 50%, with no market share accretion. The remainder of the market shares are held by Tile Africa, Cashbuild, Bathroom Bizarre, Massbuild and Iliad.

Vertical assessment

13. The Commission identified vertical relationships between CIL and Ezee Tile, producers and suppliers of Tiles, Sanitaryware, Baths, Grout and Adhesives operating in the upstream markets and the Italtile Group, a retailer of Tiles, Sanitaryware, Baths, Grout, Adhesives and related products operating in the downstream market in South Africa. CIL Group has made significant sales of Tiles, Sanitaryware and Baths to the Italtile Group in the preceding financial year and continues to supply these products to Italtile Group. In addition, Ezee Tile has made sales of adhesive, paint and related products to the Italtile Group in the preceding financial year and continues to supply the products to the Italtile Group. Ezee Tile also supplies the CIL Group's factory shops with grout, tile adhesive and related products.

14. The Commission found that the merging parties has the ability to foreclose downstream rivals in relation to the supply of the tiles as they have high market shares in the upstream markets for the manufacture and supply of tiles and an incentive to foreclose rivals and self-supply due to the significant volumes of sales supplied to Italtile and other customers post-merger.

15. Further, the investigation revealed that there are no competitive constraints on the merged entity to self-supply or increase prices of tiles as there are no alternative suppliers of tiles besides two (2) other local manufacturers and there is a lack of spare capacity to manufacture more tiles by all market participants.

16. The Commission is concerned that the merged entity will self-supply tiles or raise the price of these products to the detriment of its rivals which is likely to harm consumers

post-merger. There were third party concerns relating to foreclosure by the merged entity post-merger.

Barriers to Entry

17. The Commission found that CIL is the largest producer of tiles with the largest operations in South Africa. Whilst barriers to entry are relatively low for small operations, they are high for large scale operations such as the merging parties. No new entry in the production of these products is indicative that entry barriers at a large scale are substantial. Thus, there is unlikely to be new entrants with sufficient scale to place a competitive constraint on CIL post-merger.

Imports

18. The Commission finds that imports are not a constraint as retailers have not imported any tiles in the past three years due to higher import prices.

Countervailing Power

19. The Commission found that the degree of countervailing power post-merger is not sufficient to offset any adverse effects of the proposed merger given that there are no alternatives for customers in the affected markets. The proposed transaction is therefore likely to substantially prevent or lessen competition in the affected markets.

Remedies

20. In order to address the harm identified, the Commission considered a supply condition in respect to the affected products but found that this was not sufficient to address the harm post-merger. The Commission invited the merging parties to propose possible remedies on the harm and found that the condition proposed by the merging parties was not sufficient to address the harm.

21. Although significant competition concerns arises from the upstream market for the manufacture and supply of tiles, the business models of the target firm, CIL, is integrated with all the operations of tiles, sanitary ware, baths and grouts and hence a structural divestiture of CIL's tiles operation as a remedy is implausible. The Commission found that a remedy to divest from CIL would render the proposed merger ineffective as the merged entities' businesses are intertwined. The

Commission is of the view that there are no remedies to address the substantial competition concerns likely to arise.

Public interest consideration

22. There are no merger-specific retrenchments or redundancies that are expected to occur by virtue of the implementation of the proposed transaction. The transaction does not raise any other public interest concerns. The Commission finds that the transaction does not raise any substantial positive public interest issues that would outweigh the negative competition effects likely to arise from the merger.

Conclusion

The Commission therefore prohibits the proposed transaction.

Enquiries in this regard may be addressed to Manager: Mergers and Acquisitions Division at Private Bag X23, Lynnwood Ridge, 0040. Telephone: (012) 394 3298, or Facsimile: (012) 394 4298.