

COMPETITION TRIBUNAL OF SOUTH AFRICA

Case No.: 74/LM/Sep06

In the matter between:

KWV LTD

Acquiring Firm

and

NMK SCHULZ FINE WINE AND SPIRITS (PTY) LTD

Target Firm

Panel : N Manoim (Presiding Member), Y Carrim (Tribunal Member), and U Bhoola (Tribunal Member)

Heard on : 13 September 2006

Order Issued on : 13 September 2006

Reasons Issued on : 14 September 2006

REASONS FOR DECISION

Approval

- [1] The Competition Tribunal issued a Merger Clearance Certificate on 13 September 2006 approving without conditions the proposed merger between KWV Ltd ("KWV") and NMK Schulz Fine Wine and Spirits (Pty) Ltd ("NMK").

The parties and the merger transaction

- [2] KWV will acquire 51% of the entire ordinary issued share capital of NMK together with 51% of all the claims on loan account which NMK Global

may have against NMK.¹ KWV is a JSE listed company and is not controlled (either directly or indirectly) by any of its shareholders.² KWV does control a number of firms.³ NMK is a South African firm controlled by NMK Global,⁴ which in turn wholly owns two (2) subsidiaries, viz., Tuscanbeam Trading (Pty) Ltd and Schultz Wagner (Pty) Ltd.

- [3] Pursuant to the entering into the sale of shares agreement, the ordinary shareholding in NMK will be as follows: KWV (51%) and Newco (also known as NMK Global) (49%). It is recorded that the individual shareholders in NMK Global have combined their indirect interest in NMK through means of Newco.⁵ Post-acquisition, KWV will exercise control over NMK by virtue of its 51% shareholding in NMK.⁶

Rationale for the transaction

- [4] KWV wants to broaden the distribution base of the alcoholic beverages it manufactures.⁷
- [5] NMK submitted that the proposed deal would allow for a substantial re-investment to provide for the destined future growth and expansion which would improve NMK's position as a competitive distributor of alcoholic beverages. NMK asserted that it would benefit from KWV's international presence in sourcing new international brands for distribution by NMK in South Africa.

1 Refer to page 69 of the merger record. That is, paragraph 4 of the sale of shares agreement concluded between KWV, NMK, Greg Holtman, Peter Hoyer, Rob Bender, Andre Homann, Hendrik van Nieuwenhuizen and NMK Global Beverage Brands (Pty) Ltd ("NMK Global"). See also paragraph 4 of the shareholders agreement, that is page 118 of the merger record.

2 KWV's largest shareholders are Phetogo Investments (Pty) Ltd 18.3; KWV Employee Empowerment Trust (6.7%) (these two together are the BEE partners with a combined share of 25.1%); Titan Nominees (Pty) Ltd (11.016%); and Vinpro Kooperatief Bpk (7.26%). See page 496 of the merger record as well as page 1 of the transcript dated 13 September 2006.

3 With the exception of only one entity (being KWV Investments Ltd (as to 55,6%) KWV's only interest here is a 50,0% holding in Remgro-KWV Investments Ltd), KWV wholly owns the rest of the subsidiaries, which are: KWV International (Pty) Ltd; KWV South Africa (Pty) Ltd; KWV Finance (Pty) Ltd; KWV Intellectual Properties (Pty) Ltd; and KWV Projects (Pty) Ltd. KWV International (Pty) Ltd, a subsidiary of KWV, controls four (4) non-South African firms which are unnecessary to mention here for purposes of the proposed transaction. See in this regard, page 495 of the merger record.

4 NMK Global is jointly controlled by four (4) individuals each holding 24% in NMK Global. They are Rob A Bender; the Greg Holtman Trust; Andre Homann; and Peter J Hoyer. Hendrik van Nieuwenhuizen holds the remaining 4% of the issued shares in NMK Global.

5 See clauses 4.1 and 4.2 of the merging parties' shareholders' agreement. Page 118 of the merger record.

6 See para. 4, page 214 as well as para. 6, page 492 of the merger record.

7 See a document titled "*Project Delta*" – pages 204-207 of the merger record.

The relevant market

- [6] KWV manufactures, distributes, markets and sells a number of brands of alcoholic beverages, viz., wines; and spirits. KWV also distributes (but does not produce) the Groenland wine brand for and on behalf of its manufacturer. There are as mentioned above other KWV subsidiaries whose activities are not too significant for purposes of analysing this transaction. Our focus here will be only those subsidiaries that are involved in the manufacturing, distribution, marketing and sale of alcoholic beverages.
- [7] NMK distributes, sells, markets and administers (for and on behalf of various manufacturers either as an agent or as a distributor) a variety of brands of alcoholic beverages, viz., wines; spirits; and beer. The merging parties submit that NMK does not produce any of the above alcoholic beverages, and also that NMK does not distribute brandy at all. NMK provides the foregoing services to “on-consumption” customers (e.g., to hotels, bars, and the like, where alcoholic beverages are purchased by end consumers and consumed on the premises) and to “off consumption” customers (e.g., largest retail stores, where end consumers purchase such beverages for consumption outside of the premises on which they were bought).⁸
- [8] There is a difference of opinion with regard to the relevant product market between the Commission⁹ and the merging parties.¹⁰ From a

8 KWV deals with wine brands such as KWV Classic, KWV Reserve, KWV Cathedral, Roodeberg, Laborie, Roberts Rock, Pearly Bay, and Golden Kaan whilst NMK is involved in wine brands such as Warwick, Simonsig, Clos Malverne, Groot Constantia, De Krans, Simonsvlei, De Waal, Laibach, and Kaapzicht. KWV’s spirits brands are KWV Brandy – 20, 10, 5 and 3 Year, and Groenewald whereas NMK’s spirits brands are Stroh Rum, Sierra Tequila, Dalmore Whisky, Bruichladdich, Stortebeker, Wild Africa Cream, Glavya and Boutari Ouzo. Beer brands, which NMK is involved with, are Stella Artois, Fostert’s, Grolsch, and Erdinger. See pages 193-198 of the merger record.

9 The Commission submits that the proposed transaction entails both a horizontal overlap and a vertical integration. It argued that the horizontal overlap is in respect of distribution of alcoholic beverages, mainly wines and spirits throughout South Africa whereas a vertical integration arise in that KWV is a producer of alcoholic beverages whilst NMK is a distributor of alcoholic beverages. The Commission’s view is that the proposed acquisition affects two markets, viz., (1) the upstream market for manufacturing of wines and spirits; and (2) the downstream market for distribution of wines and spirits.

10 The merging parties argued that save for the fact that KWV distributes wine for one independent wine label therefore the products sold and services rendered by KWV and NMK are not substitutable or interchangeable with one another. Their view is that KWV and NMK operate at different levels of the value chain because KWV is a producer of alcoholic beverages whereas NMK is a distributor thereof. In light of the above, the merging parties submit that the relevant product market in which NMK operates can be defined broadly as the distribution services market, which market includes services such as sales; distribution; marketing; and administration. Their argument is that as there is no specialised logistical procedure (other than

geographical point of view, both the Commission and the merging parties submit that both the merging parties and their competitors operate nationally and thus rendering the geographic market to be national. We need not consider these differences as in our view it appears unlikely that the proposed transaction may lead to anticompetitive concerns. That is, no matter how the market is defined.

Competition analysis

[9] A number of factors support our conclusion below which is that the proposed merger ought to be unconditionally approved.

[10] Firstly, there will be virtually no substantial accretion of market shares pursuant to the implementation of the proposed transaction. With regards to market shares the Commission's investigation revealed that KWV has a 5% market share for the distribution of alcoholic beverages whilst NMK has 1%. If this figures are indeed correct, this would result in the merged entity having a 6% combined market share post-acquisition. The merging parties further submit that as KWV distributes only one brand of wine which is not its own, therefore one can only assume that its market shares as an independent distributor is so small as to be *de minimis*.

[11] Secondly, the distribution services market appears to be competitive and fragmented and comprises of a substantial number of competitors. Apart from the merging parties, there are other distributors, viz., Douglas Green

obtaining a liquor licence, which has no substantial onerous requirements) and based on the functional characteristics of the services rendered, therefore the market should be construed as a broad market for distribution services. They further contend that should the above product market definition not viewed as the correct one, alternatively the market may be more narrowly defined as the market for the distribution of alcoholic beverages, which market includes the sales, distribution, marketing and administration of alcoholic beverages.

Bellingham; NUCED; E Snell; Meridian; Smollan Liquor Division; and Parnod Ricard. With regards to the upstream market for the production of alcoholic beverages, the Commission's investigation revealed that KWV has a 5% market share.¹¹ The Commission further indicated that KWV is not considered as a big player in the upstream market because it did not even feature on the top five list of manufacturers.¹²

[12] According to the Commission, NMK does not distribute alcohol beverages for and/or on behalf of KWV, but currently distributes these products for Western Wines (Pty) (Ltd) and Wine Cape Liquors (Pty) Ltd. The Commission indicate that other manufacturers (including KWV) who are competitors of the merging parties distribute their own products. We are advised that NMK has just entered into a distribution agreement with KWV in terms of which it will distribute the latter company's products. We are convinced that KWV may not be able to foreclose other manufacturers of alcoholic beverages from utilising NMK as a distributor given that most of these manufacturers conduct their own distribution.¹³ We further agree with the Commission's view

11 During the Commission's investigation, the merging parties indicated that KWV's market shares in respect of the markets for production of spirits and wines is actually less than the above estimated figures. Their market share for 2006 is estimated to be approximately 3,44% and 0,40% respectively. See paras. 7.2.2 and 7.3.2, pages 492-493 of the merger record.

12 This is in accordance with the BMI Foodpack Report of 2004, pages 431-432, and 472-474 of the merger record.

13 In fact, the merging parties submitted that NMK would continue to supply the brands of the alcoholic beverages that it is currently sourcing from approximately 60 "principles" and supplying to its customers. Post-acquisition, NMK will simply extend its product range by adding to its basket the KWV brands. They further submit that there is little reality to KWV requiring at any future point in time that NMK solely distributes its products for reasons, amongst others, that the commercial viability of an independent distributor is dependent on the diverse product range of alcoholic beverages on offer to purchases. We are told that KWV currently distributes its own products and also supplies third party distributors, which it will continue to do post-acquisition.

which is that should KWV attempts to foreclose the current manufacturers that use NMK as a distributor, those manufacturers may conduct their own distribution or they may contract other distributors available.

[13] Lastly, barriers to entry into the market appear to be low. Insofar as the distribution of alcoholic beverages, the merging parties submit that any potential distributor is required to obtain a wholesaler liquor licence prior to being able to commence such business, and that such licence is not difficult to obtain – usually it takes between six months and a year.¹⁴

Public Interest

[14] The merging parties submitted that proposed transaction would not have an impact on any public interest aspects. In addition, the merging parties anticipate no job losses post merger, but foresee a potential increase in employment to cope with the distribution of the additional volumes of KWV's alcoholic beverages.¹⁵ Although the Food and Allied Workers Union (Fawu) wrote a letter to the Commission subsequent to its recommendation in which it sought the imposition of a moratorium on retrenchments for a period of 48 months subsequent to the merger, it failed to lay a basis for why such a condition should be imposed.

Conclusion

See page 53 of the merger record.

14 According to the merging parties the capital required for a party to enter the distribution services market is low as all that a potential entrant requires is to have stock and a vehicle (either owned or leased) with which to deliver such stock. Where a new entrant wishes to distribute on a large scale, then that distributor would require a warehouse (either owned or leased) in which to store stock. The merging parties also submit that because there are numerous distributors of alcoholic beverages, retailers can easily negotiate trade terms, and play distributors off one another in such negotiations. According to the merging parties, there is little or no cost involved in switching distributors.

15 See in this regard, pages 54, 212 and 420 of the merger record. In addition, an employee representative of the target firm wrote to the Commission informing the latter that "the employees of NMK have no objection to the proposed merger". See also page 2 of the transcript.

[15] We are satisfied that the proposed transaction is unlikely to result in a substantial lessening or prevention of competition in the relevant markets. There are no public interest grounds that justify prohibiting or imposing any conditions on the merger. We accordingly approve the proposed transaction unconditionally.

N Manoim

Y Carrim and U Bhoola concurring.

Tribunal Researcher: T Masithulela

For the merging parties : N Lopes (*Edward Nathan Corporate Law Advisers*)

For the Commission : M Mohlala assisted by G Mudzanani (Mergers and Acquisitions) and A Kalla (Legal Services)