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MOFCOM Conditionally Approves Marubeni/Gavilon: Competition Law and Industrial Policy in the Agricultural Sector

On 22 April 2013, China's Ministry of Commerce (MOFCOM) published its conditional approval of Marubeni's acquisition of Gavilon Holdings – hot on the heels of the regulator's conditional clearance of the Glencore/Xstrata merger which also concerned strategically-sensitive global markets where China is heavily dependent on imports. The key issues arising in Marubeni/Gavilon include the following:

- MOFCOM's finding of separate relevant markets for *imports*.
- MOFCOM's apparent willingness to find market power notwithstanding relatively low market share levels.
- MOFCOM's requirement, as a condition of its approval, that Marubeni and Gavilon continue to operate as separate economic entities with respect to exports of soybeans to China.

These aspects of the decision appear driven by industrial policy considerations and indicate that any transaction that involves key industries – food and agriculture in Marubeni/Gavilon – will be scrutinised closely and regulated with an eye toward broader strategic interests.

MOFCOM's review

The US$5.6 billion grain deal between one of Japan's largest trading companies and the third-largest North American grain company took just under a year for MOFCOM to clear. First notified by the parties in June 2012, the notification was withdrawn and re-submitted in January of this year at the end of a Phase III review and after an initial remedies proposal had been rejected by the regulator as insufficient to address its concerns.

The transaction was ultimately cleared several days after the parties agreed to operate Marubeni's and Gavilon's China soybean export businesses through separate and independent legal entities backed up by firewall mechanisms to safeguard against the exchange of competitively sensitive information. The final remedies scheme includes the following elements:

- Within six months, Marubeni and Gavilon will set up two independent legal entities for the purpose of exporting and selling soybeans on the China market.
- Marubeni's soybean subsidiary and Gavilon's soybean subsidiary will maintain structural and operational independence with respect to personnel, sourcing, marketing, sales and pricing functions.
- Post-completion, Marubeni's soybean subsidiary will not source soybeans from Gavilon's US assets except on an arm's-length basis.

The decision is silent on how long these conduct remedies must remain in place though the parties may make a reasoned submission to MOFCOM to have them withdrawn two years after MOFCOM's conditional clearance takes effect. At that time, MOFCOM may decide to release Marubeni/Gavilon from their obligations where market conditions might justify doing so.

Extensive hold-separate remedies of this kind are not unusual in the China context and MOFCOM imposed similar arrangements in Western Digital/Hitachi in 2012. What is telling in this case, is not so much the remedies scheme as such – burdensome as it will likely be for the companies concerned – but more the basis for seeking the remedies in the first place. MOFCOM's decision rehearses the key considerations:

- China is the world's largest importer of soybeans. In 2012, China's imported volume of soybeans accounted for 60% by volume of total worldwide soybean trade, and 80% of China's domestic supply.
- China imported 58.38 million tons of soybeans in 2012 implying a total domestic market of 72.975 million tons (MOFCOM makes no reference however to total market size as it defines the relevant market as a market for imports).
- Marubeni shipped 10.5 million tons of soybeans to China in 2012 – implying a market share of 14% or 18% approximately if the relevant market is defined by reference to imports alone as in the MOFCOM decision.[1] Marubeni ranked first among suppliers of imported soybeans in China.
- Gavilon's global soybean sales in 2012 amounted to 5.1 million tons. This seems to translate into a global market share of approximately 5%.[2] MOFCOM does not provide any market share for Gavilon in China but the figures provided in the decision allow one to determine that its share would be less than 1%.[3] The concern then would appear to have been more about the loss of potential competition.
- While noting that the supply of soybeans in China was highly dependent on imports (80% of all supplies were imported in 2012 as mentioned above), MOFCOM explained that the downstream domestic China market for soybean crushing was highly fragmented and characterised by small scale production with weak countervailing bargaining power. MOFCOM expressed a concern that the notified concentration would further erode the bargaining power of these downstream domestic soybean crushing companies.
- In addition to the market for soybean imports, MOFCOM also considered possible competition issues on China's import markets for corn, soy meal and distiller's dried grains but concluded that the transaction would not give rise to adverse effects on any of these markets.

Commentary

Overall, the key consideration appears to have been that the deal would significantly boost Marubeni's access to global soybean resources through the acquisition of Gavilon's capacity for soybean origination, storage and logistics in North America thus enhancing Marubeni's ability to import soybeans into China. This would result in what MOFCOM terms a "materially strengthening" of Marubeni's "control" over the import market for soybeans. The remedies imposed seek to address this.

That said, taking a more orthodox approach to an assessment of the facts might lead one to question whether the parties have any particular level of market power on the relevant market for soybeans. In this respect it is notable that MOFCOM appears not to have considered in depth the degree of competitive constraint provided by Marubeni's rivals or the ability of competitors to expand in response to attempts by the merged firm to increase prices and/or lower output. And, as indicated above, it is striking that MOFCOM chose to define the relevant market as a market for *imports* into China, thus by implication taking the view that domestic supplies were somehow not relevant to the assessment. Whatever the rationale for such an approach – the decision is silent on the point – the effect of it would be to overstate the parties' market position, albeit that on the facts of the case, not by very much (a 4% increase in market share in the case of Marubeni, it would seem). Interestingly too, MOFCOM makes a point of noting the extent to which China specifically is a key market for Marubeni which, according to the decision, sells some 99% of all of its traded soybeans on the Chinese market. Similarly, in Glencore/Xstrata, MOFCOM made reference to the parties' extensive operations on the China market, although

1. MOFCOM does not in fact give any market share percentages for soybeans in its decision. It explains however that China imported 58.38 million tons of soybeans in 2012 and that this accounted for 80% of China's domestic supply. Accordingly China's total market size would be in the region of 72.975 million tons. Assuming Marubeni shipped 10.5 million tons of soybeans to China in 2012 (MOFCOM's figure), this implies a market share of 14% of all domestic supply or 18% if the relevant market is defined by reference to imports alone as MOFCOM does.

2. MOFCOM advises that in 2012, China's imported volume of soybeans accounted for 60% by volume of total worldwide soybean trade. As China imported 58.38 million tons of soybeans in 2012, this would suggest the global market amounted to 97.3 million tons. If Gavilon's global soybean sales in 2012 amounted to 5.1 million tons (MOFCOM's figure), this translates into a global market share of approximately 5%.

3. MOFCOM advises that in China Gavilon is active in the trading of "bulk agricultural produce such as yellow corn, soybeans, soy meal, and feed and food ingredients". MOFCOM further notes that in 2012, Gavilon exported to China a total quantity of about 400,000 tons of bulk agricultural produce. Even assuming this entire volume was constituted by soybeans (which it would not be), this translates into a market share of less than 1% even where the relevant market is defined solely by reference to imports.

in neither Glencore/Xstrata nor Marubeni/Gavilon did MOFCOM clarify why this fact was particularly significant.

These uncertainties aside, what the decision clearly appears to indicate – and in this respect it is again consistent with Glencore/Xstrata – is that MOFCOM is prepared to find market power at rather low market share levels where strategic imports are at issue (whether these be agricultural or key raw materials), in circumstances where China is heavily dependent on overseas supplies and where downstream Chinese purchasing power is comparatively weak.

In Marubeni/Gavilon, MOFCOM demonstrates once more its confidence in seeking remedies in circumstances where other regulators have concluded there are no competition concerns. The US Federal Trade Commission gave the go ahead to Marubeni/Gavilon in November 2012 with an early termination of its review, while the European Commission cleared the deal under its simplified procedure back in August 2012. MOFCOM of course might counter that the position on the China market is different and certainly the fact that Chinese consumption accounts for 60% by volume of total worldwide soybean trade makes for a compelling argument. Be that as it may, an analysis of MOFCOM's decision suggests that competition considerations were not the only considerations at play in the decision to seek remedies in this case.

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