NEWS ANALYSIS

# Underperforming COC business on the ropes

Cyclic olefin copolymers have been around for 15 years but have still only carved themselves niche markets. Steven Pacitti finds out why Ticona has decided that Topas is not the jewel in its crown

Ticona has delivered another blow to the engineering polymers market by announcing its decision to quit the cyclic olefin copolymer (COC) business as a result of unsatisfactory sales. The company's COC business (marketed under the Topas brand) reported a $35 million loss in 2003, and is on course to make similar losses for the last financial year.

Although demand for COC is growing, commercialisation has been slower than Ticona expected. Two years ago the company predicted it would break even by 2006 but was evaluating options to reduce its load as pricing levels, about three times higher than other optical resins such as acrylic and polycarbonate, had limited them to niche markets in the packaging and medical sectors.

Now, Celanese Corporation (of which Ticona is the engineering plastics subsidiary) believes that the business will have a more successful future in the portfolio of another owner that can realise additional synergies. According to Henning Kuell, media relations manager for Ticona Europe, discussions are under way with a number of possible investors.

The news comes just over a year after The Blackstone Group acquired Celanese and took it private for $3 billion, which included Blackstone putting up $650m in equity. This loaded Celanese down with $3.2bn in debt.

Blackstone, along with a strategic partner (believed to be GE), had originally targeted the acquisition of Ticona, but late in the negotiations the latter jilted Blackstone at the altar. Blackstone subsequently decided to go it alone and purchase the entire business for $3.8bn.

The largest public-to-private buyout in German history, the deal was not without its critics. This year an initial public offering (IPO) saw Celanese become a public stock company, although Celanese did not use any of the money raised to pay debt, which indicated that Blackstone was looking out for itself.

However, the deal gave the company more financial flexibility to pursue its growth strategy in the acetic acid chain, emulsions and other downstream chemicals, and its Ticona technical polymers business. But another bad financial return in the Ticona COC business – with the company's 30,000 tonnes per year COC plant in Oberhausen, Germany, once again running below capacity – has resulted in this decision. This is despite Ticona president Lyndon Cole saying last year that a second production site for COC was being planned.

Ticona is one of only four producers of COCs worldwide. Another, Mitsui Chemicals of Japan, is expanding COC capacity to 3,400 tonnes a year by the end of 2005 to meet growing demand in high-performance packaging. Applications for the company's COC include pharmaceutical barrier packaging and shrink films. JSR Corporation, also in Japan, produces COC and has been linked with a move for Ticona's business.

Topas COC from Ticona offers high transparency, rigidity, purity and heat-resistance coupled with strong moisture barrier properties and dimensional stability, and since the market launch four years ago applications have included pharmaceutical blister packs, flexible packaging for food and medical products, pre-filled syringes, vials, diagnostic parts and optical components.

# ECJ delivers stinging rebuke in Tetra/Sidel case

The European Court of Justice says the European Commission was wrong to block the Tetra/Sidel merger. International law firm Hogan & Hartson highlights the relevance of this landmark case for private equity firms and venture capitalists

The European Court of Justice (ECJ) delivered two judgments in Cases C-12/03 P and C-13/03 P Commission of the European Communities v Tetra Laval BV on 15 February, confirming an October 2002 judgment of the Court of First Instance (CFI) that annulled the European Commission's decision to block the Tetra Laval/Sidel merger. The ECJ's decision marks the epilogue of a legal epic that began nearly four years ago.

In 2001, Tetra Laval BV's French subsidiary Tetra Laval SA (Tetra Laval) acquired Sidel SA (Sidel), a French company, as a result of a successful public bid. Tetra Laval is active in the market for equipment and consumables used in the production of carton packaging for liquid food, while Sidel is a leading producer of stretch blow moulding (SBM) machines that are used to produce liquid food packaging made of plastics material PET (polyethylene terephthalate.)

The Commission prohibited the merger on the grounds that Tetra Laval could leverage its dominant position on the market for carton packaging equipment/consumables into the neighbouring market for SBM machines, by persuading its customers who were switching to PET to choose Sidel's SBM machines. The Commission also considered that the elimination of Sidel as a significant potential competitor in the packaging market would deprive Tetra Laval of any incentive to lower prices and innovate in that market. Tetra Laval successfully appealed the Commission's decision to the CFI. The Commission, in turn, appealed the CFI judgment to the ECJ but was unsuccessful on virtually every ground of appeal.

The Commission's first ground of appeal was that the CFI wrongfully ignored the Commission's margin of discretion in the appraisal of complex economic matters in merger cases. For the Commission, the CFI unduly raised the Commission's standard of proof by requiring the pulling together of "convincing evidence" of the merger's anti-competitive effects. In its contested decision the Commission had concluded that the markets for carton and PET packaging systems were closely related and encompassed a growing number of common customers. It had also taken the view that PET would displace HDPE as the main material competing with carton by 2005. But on appeal, the CFI questioned the Commission's growth forecasts for the PET market. The CFI therefore faulted the Commission for failing to prove the factual basis of its contention that the acquisition of the leading PET player would make Tetra dominant on the market for SBM machines. The ECJ considered that, although the Commission had some discretion in its economic appraisal of mergers, it had been appropriate for the CFI to determine whether the evidence relied on contained all the information necessary to substantiate the Commission's conclusions.

The Commission's second ground of appeal was that the CFI incorrectly concluded that the Commission should have considered whether the illegality of the conduct resulting in leveraging could have acted as a disincentive on Tetra Laval adopting such conduct. The ECJ only endorsed part of the CFI's findings. It agreed with the CFI that the Commission had to assess the likelihood that Tetra Laval would engage in such leveraging. However, the ECJ found that the Commission was not required under this analysis to undertake an exhaustive examination of the legal orders and enforcement rules applicable in the various Member States since this would be too complex a task and would run counter to the purpose of the Merger Control Regulation.

Nonetheless, Tetra Laval had offered commitments not to engage in illegal conduct that would result in leveraging. The ECJ accepted the CFI's findings that the Commission had wrongfully dismissed these commitments as inadequate, as a matter of principle. The Commission ought to have made an assessment of whether or not these remedies could have effectively removed the competition concerns.

Lastly, the Commission argued that the CFI had failed to recognise the fact that potential competition to carton packaging systems from PET packaging systems would be eliminated by the disappearance of Sidel, the leader in the market for PET packaging systems, as a potential competitor. As a result, Tetra would lose an essential incentive to lower its prices and innovate on the carton packaging market. The ECJ rejected this argument, considering that the Commission had failed to take into account the reaction of Tetra Laval's competitors in that case and, in particular, whether they could have cancelled out the elimination of Sidel as a potential competitor by taking advantage of any failure on Tetra's part to price competitively and innovate.

The ECJ judgment will force the Commission to adopt a more rigorous approach when reviewing mergers by raising the standard of proof that the Commission can rely on. This will be particularly relevant in the case of conglomerate mergers. These are mergers involving companies which, essentially, do not have a pre-existing competitive relationship, either as direct competitors or as suppliers and customers. For instance, while Tetra Laval and Sidel were both providing solutions for liquid food packaging, they were, for the most part, not offering their products to the same customers nor were they in a supplier-customer relationship. This illustrates the relevance of this judgment to potential mergers in the packaging industry, an industry so diverse that merger candidates are as likely to encounter conglomerate concerns as horizontal or vertical concerns.

The analysis of conglomerate mergers is extremely likely since the Commission cannot rely on existing overlaps or vertical relationships. As a result of the ECJ judgment, the Commission will be required to produce particularly convincing evidence in order to establish the anti-competitive effects of such mergers. This case is also important as it sends a direct message to buyers who are willing to offer commitments with respect to their future behaviour in order to alleviate competition law concerns arising from the deal. The judgment confirmed that the Commission cannot dismiss behavioural commitments as a matter of principle without having made a bona fide attempt to analyse whether or not such commitments are adequate to address competition concerns.

All attention will now focus on the Court's anticipated judgment in the GE/Honeywell case where conglomerate effects were also an issue.

• Jean-Michel Coumes, counsel, and Aymeric Dumas-Eymard, associate, can be contacted at Hogan & Hartson at the following locations: jmcoumes@hhlaw.com (33 1 557 32300) and adumas-eymard@hhlaw.com (33 2 2505 0911).

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