

## Glencore and Marubeni: Chinese merger policy in practice

2 May 2013

### Summary

April was a month for both theory and practice in Chinese international merger clearance. After a long delay, Chinese authorities approved the mergers of Glencore and Xstrata and Gaviion and Marubeni. In both cases Beijing imposed strict conditions on the mergers. In the same week the Chinese Ministry of Commerce (MOFCOM) also closed a public consultation on its new regulations on Restrictive Conditions for mergers. The gap between theory and practice was notable and instructive. With Glencore and Marubeni Beijing has used the merger clearance process less to address competition concerns and more to leverage favourable terms for the supply of what it sees as strategic commodities.

April was a month for both theory and practice in Chinese international merger clearance. On April 17, after a long delay, Chinese authorities approved the merger of commodities trader Glencore and mining company Xstrata. A week later it cleared the acquisition of US grain trader Gaviion by Japanese commodity trader Marubeni. In both cases Beijing imposed strict conditions on the mergers. On April 26, the Chinese Ministry of Commerce (MOFCOM) closed a public consultation on its new regulations on Restrictive Conditions for mergers. The gap between theory and practice was notable and instructive.

On paper, the proposed Chinese remedies system will work much like the EU or US equivalents. The competition authorities in Beijing can impose a range of remedies on merging companies that can include structural changes and, or behavioural remedies that oblige companies to conduct themselves in a certain way for up to 10 years. However, the draft gives little or no guidance with respect to how Beijing might determine what form of remedy is appropriate for what scenario, which will make predicting Beijing's likely decisions no easier.

There are, however, also some important differences. The Chinese rules impose no timeframe on authorities for defining remedies, something that is potentially important, as the Chinese merger clearance process for complex cases is already typically more protracted than the US or EU one. MOFCOM's opaque

and slow process - no doubt further delayed by departmental caution through the leadership transition from November - pushed Glencore uncomfortably close to its deadline to close the merger to meet UK Takeover Panel rules. Beijing also pushed Gaviion's timetable back by seven months with delays. The law also gives MOFCOM scope for subsequently revising its remedy requirements after clearance, without prior consultation with the parties.

How Beijing approaches remedies in clearing mergers of non-Chinese companies is a question that reveals a lot about the instincts of the Chinese system. The US and EU systems both contain for scope for securing behavioural commitments from merging companies, but have a strong and explicit bias towards cleaner and simpler structural commitments. The US Department of Justice explicitly states in its own regulations that it will avoid conduct remedies that imply on-going government intervention in market behaviour. Beijing has already demonstrated no such compunction - if anything, it has demonstrated the opposite.

Of the six mergers cleared in 2012 by Beijing all involved a mix of structural and behavioural remedies. Western Digital was required to hold the Hitachi Viviti Hard Disk Drive business it proposed to acquire separate from Western Digital itself, to sustain R&D spending, to report production levels for

both companies to Beijing annually and to agree not to require customers to use their own HDD technology . As the price for acquiring Motorola’s Mobile telephony division, Google was required to continue licensing Android for free and to guarantee to treat original equipment manufacturers dependent on the android operating system in a non-discriminatory way. Back in 2009, GM’s purchase of auto parts manufacturer Delphi was made conditional on explicit commitments to sell to Chinese car manufacturers in a non-discriminatory way.

### The soybean angle

Glencore and Marubeni have taken this tendency to approve with conduct conditions in a new and overtly political direction. The price of MOFCOM’s approval for Glencore’s acquisition of Xstrata was again a hybrid remedies package. Glencore was required to divest the large Las Bambas copper mining operation in Peru. It would seem likely that Beijing’s preference will be for the Peruvian operations to be sold to a Chinese miner. Glencore has also been required to guarantee copper ore supplies to China at annual contract prices for the next eight years.

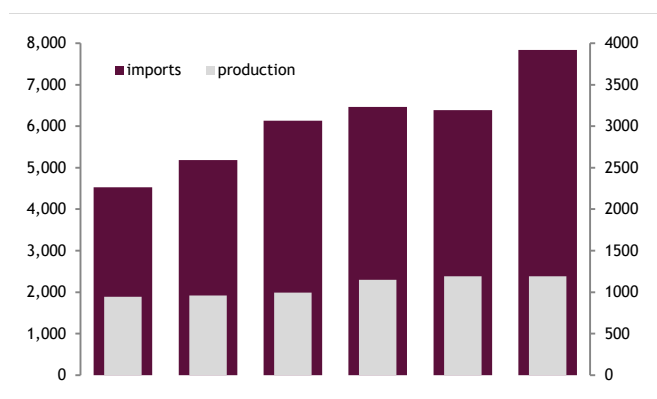


Fig 1: Chinese copper ore and concentrate imports ((LH) and production (RH) 2007-2012 (000 tons)  
Source: USGS, Comtrade

On April 23, MOFCOM announced that it would approve the takeover of US grain trader Gavilon by Japanese commodity trader Marubeni only subject to an agreement by Marubeni to hold the two companies’ soya businesses apart and ensure that they continued to sell to China as independent

competing businesses. This will prevent Gavilon’s US soybean operations servicing China through Marubeni, which supplied about 16% of China’s soybean imports.

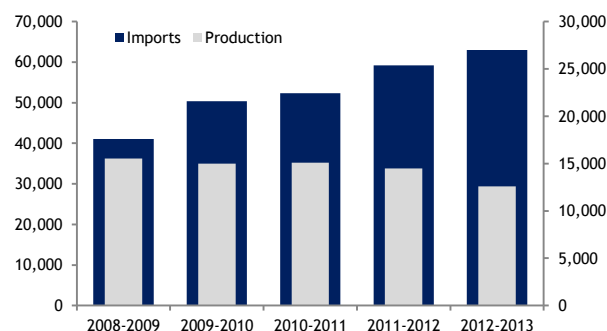


Fig 2: Chinese soybean production (RH) and imports (LH) 2008-2013 (000 tons)  
Source: USDA/Chinese Ministry of Agriculture

Article 29 of the Chinese Anti-Monopoly Law commits the Chinese authorities to not taking into account non-competition issues in their judgments on mergers. Both of these cases make this look a little thin. Brussels and Washington cleared both mergers without conditions (excluding concentration remedies in Glencore’s zinc operations), as they had Google/Motorola and GM/Delphi. In the Western Digital/Hitachi case, MOFCOM went considerably further than both the European Commission and the Department of Justice by imposing a ‘hold separate’ arrangement on Viviti.

This of course does not mean that the mergers in question might not have raised particular concern in the Chinese market. To be sure, both merged companies are significant players in China. But they are well below the threshold of 35-40% market share that would normally trigger concern from European and American regulators. Glencore/Xstrata accounts for just under 20% of the Chinese market in copper ore. Even globally, the new merged Glencore-Xstrata company will only just have around a third of global markets for copper ore.

The rationale behind these remedy packages clearly has more to do with securing access to commodity imports than competition policy. Both the Chinese

copper ore (Fig 1) and soya (Fig 2) markets are characterised by stalling or falling domestic production and rising imports. China's people, industry, pigs, and poultry have a growing appetite for both, and both are regarded as strategic.

There are a number of important points to draw from these cases and the codification of the Chinese approach to remedies. They are a reminder that the Chinese merger clearance process is likely to remain long and opaque. Planning a merger timetable around a quick and uncomplicated clearance in Beijing, especially in a sector where Beijing has strategic supply issues, looks like something of a gamble. Both Glencore and Marubeni were seriously inconvenienced by Beijing, and others should expect the same.

As more and more cross-border mergers will require Chinese clearance these cases also suggest that Beijing may be tempted to see this as a form of leverage. Since the Chinese Anti-Merger Law came into force in 2008 China has only rejected one merger outright - Coca Cola's attempt to buy juice maker Huiyuan in 2009. This again suggests a political instinct for extracting industrial policy advantage from merger clearance process - even when the mergers involve only non-Chinese parties. Indeed, the

merger clearance process provides Beijing with a unique moment of leverage over non-Chinese companies active in the Chinese market.

Many multinationals will simply see this as the cost of doing business in, or with, China. Guaranteed supply arrangements for the Chinese market may seem a low enough price to pay for a consolidation on the scale of Glencore/Xstrata. Nevertheless, it will probably encourage those in Europe and the US who continue to politicise the 'going out' of Chinese companies. The next time a Lenovo seeks a smooth path to an acquisition of an IBM, how many American or European politicians will be tempted to cite precedents like Glencore and Marubeni?

info@global-counsel.co.uk  
+44 (0)203 667 6500

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