PHILIPPINE COMPETITION COMMISSION
Ensuring businesses compete and consumers benefit

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In the Matter of the Proposed Acquisition by Universal Robina Corporation of Assets of Central Azucarera Don Pedro, Inc. and Roxas Holdings, Inc.

PCC Case No. M-2018-006

Universal Robina Corporation, Central Azucarera Don Pedro, Inc. and Roxas Holdings, Inc.

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COMMISSION DECISION NO. 03-M-021/2019

I. STATEMENT OF THE CASE

1. This case refers to the proposed acquisition by Universal Robina Corporation ("URC") of the assets of Central Azucarera Don Pedro, Inc. ("CADPI") and, Roxas Holdings, Inc. ("RHI"). (RHI, together with URC and CADPI, shall be collectively referred to as the Parties.)

2. Upon review of the proposed acquisition, the Mergers and Acquisitions Office raised competition concerns on the proposed acquisition, finding that the proposed acquisition will likely substantially prevent, restrict, or lessen competition in the relevant market.

A. The Acquiring Parties

3. URC is a Philippine corporation engaged in a wide range of food-related businesses which it operates through divisions, subsidiaries, and affiliates. URC is organized into three (3) core business segments: (1) branded consumer foods, (2) agro-industrial products, and (3) commodity food products. The commodity food products segment includes the Sugar Division.[1]

4. URC's ultimate parent entity ("UPE"), JG Summit Holdings, Inc. ("JG Summit"), is a Philippine holding company that has business interests in food, agro-industrial and commodities, real estate and hotel, air transportation, banking, and other supplementary services.[2]

B. The Owner of the Assets Sought to be Acquired

5. CADPI is a Philippine corporation engaged in the business of producing and trading raw and refined sugars, molasses, and other related products or by-products. It owns and operates an integrated sugar cane milling and refining

[1] SOC, par. 6 citing Appendix 7.4, JG Summit Holdings, Inc. Annual Report as at 31 December 2017.
[2] SOC, par. 14, pp. 4-5.

facility located in Nasugbu, Batangas, with a total milling capacity of [confidential] of cane per day and a total refining capacity of [confidential] .[3]

6. CADPI's UPE, RHI, is a publicly-listed Philippine holding company with investments in entities that are engaged in the manufacturing of sugar and allied products, such as bioethanol fuel. RHI owns 100% of CADPI's issued and outstanding capital stock. Moreover, CADPI's sugar milling and refining assets are located in approximately 2,364,520 sqm. of land owned by RHI.[4]

C. The Transaction

7. The Transaction involves URC's proposed acquisition of (1) all the assets of CADPI used for the operations of its milling and refinery plant,[5] and (2) the parcel of land owned by RHI where CADPI's facilities are situated (the "Transaction"). The total consideration for the Transaction is approximately PhP [confidential].[6]

   7.1 RHI and CADPI are selling their respective assets allegedly in order to improve the overall financial performance of the RHI Group, while at the same time significantly reducing RHI's debt level. RHI will use the proceeds of the Transaction to prepay its existing loans with several financing institutions.[7]

   7.2 URC aims to expand its sugar milling and refining operations[8] and expects the Transaction to enhance its capability to produce and store good quality refined sugar and complement its existing network which will maximize the synergies and scale of economies that will result from the integration.[9]

D. Procedural Antecedents

8. On 1 June 2018, the Philippine Competition Commission (the "Commission"), through the Mergers and Acquisitions Office ("MAO"), was notified by the Parties of the Transaction.[10]

9. On 30 October 2018, MAO issued its Statement of Concerns ("SOC") pertaining to the Transaction.[11] Accordingly, the Commission, on the same date, issued to

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[3] SOC, par. 16, p. 5.

[4] SOC, par. 18, p. 5 *citing* Appendix 2.4, Notification Form of Roxas Holdings, Inc.

[5] The assets to be acquired are composed of all buildings, improvements, machineries & equipment, laboratory equipment, and transportation equipment that are necessary for the continuing operations of its milling and refinery plant located at Brgy. Lumbangan, Nasugbu, Batangas at a milling capacity of [confidential] and refining capacity of [confidential] . The Transaction likewise include the following assets: all spare parts inventory available for the operations of Don Pedro's milling and refinery plant.

[6] SOC, par. 11, p. 6 *citing* Appendix 7.1, Asset Purchase Agreement between URC (as purchaser) and CADPI and Roxas Holdings (as seller).

[7] *Id.*

[8] *Id*.

[9] SOC, par. 11.2, p. 6.

[10] SOC, par. 1.

[11] Notice dated 31 October 2018.

the Parties a Notice directing them to submit, within ten (10) days from receipt of the said Notice, their respective Verified Comments on the SOC.[12]

10. After requesting[13] and being granted an extension of fifteen (15) days[14] RHI filed its Verified Comment on 20 November 2018.[15] URC, on the other hand, requested for another extension and was thereafter granted by the Commission until 29 November 2018 within which to file its Verified Comment.[16]

11. On 22 November 2018 however, URC submitted a proposal for commitments accompanied by a request for the suspension of the Phase 2 review period for sixty (60) days in order for the Commission to evaluate its proposed commitments ("Commitment Review Period"). [17]

12. On 21 January 2019, upon the expiration of the Commitment Review Period, the Commission found the proposed commitments insufficient to completely address or remedy the harms identified in the SOC and rejected the same. Thus, pursuant to Section 12.5 of the PCC Rules of Merger Procedure, the Phase 2 review of the Transaction resumed.

13. On 25 January 2019, URC, for the third time, requested,[18] and was granted, an extension of ten (10) days, or until 7 February 2019, within which to file its Verified Comment on the SOC.[19]

14. However, the Commission did not receive URC's Verified Comment on 7 February 2019. The Commission thus makes the following findings upon consideration of MAO's SOC and RHI's Verified Comment.

II. ISSUE

15. The issue before the Commission is whether or not the Transaction will substantially prevent, restrict, or lessen competition in the relevant market.

16. In their SOC, MAO alleges that the Transaction will likely result in a substantial lessening of competition in the market for provision of sugar cane services in the four (4) provinces of Batangas, Cavite, Laguna, and Quezon for the following reasons:

    16.1. The Transaction is a merger-to-monopoly and will eliminate the only competitor of URC in the relevant market;

    16.2. The Transaction will create market power for URC and allow it to unilaterally reduce the planter's share in the planter-miller sharing

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12 Notice dated 31 October 2018.
13 URC's Letter-Request dated 9 November 2018; RHI's Letter-Request dated 9 November 2018.
14 Notice dated 9 November 2018.
15 RHI's Comment dated 19 November 2018.
16 Notice dated 20 November 2018.
17 URC's Proposed Undertaking; URC's Request and Waiver dated 22 November 2018.
18 URC's Letter-Request dated 25 January 2019.
19 Notice dated 25 January 2019.

agreement, the theoretical recovery rates quoted to planters, and the incentives provided to planters;

16.3. Potential substitution outside of the relevant market, to other sugar mills outside Batangas or other revenue-generating activities, is not sufficient to constrain URC from exercising market power; and

16.4. Barriers to entry are high and the possibility of a new entrant seems remote and, if at all possible, may not be immediate to constrain URC from exercising market power post-Transaction.

17. In its Verified Comment, RHI alleges the following:

17.1. The laws governing the sugar industry and the unique symbiotic and interdependent relationship between sugar planters and millers do not allow for an independent and unilateral exercise by URC of alleged "market power" in the relevant product and geographic market;

17.2. The farmers in Southern Luzon have market power. Substitution outside the market remains as a sufficient competitive constraint;

17.3. The gains in efficiencies far-outweigh any alleged finding of substantial lessening of competition; and

17.4. The counterfactual adopted by the MAO does not constitute a logical projection given the prevailing financial constraints suffered by RHI and CADPI and the current under-supply of sugar cane.

III. ANALYTICAL FRAMEWORK

18. In resolving the issue, the Commission adopts an analytical framework wherein the Commission shall:

18.1. Assess whether a proposed merger or acquisition is likely to substantially prevent, restrict, or lessen competition in the relevant market or in the market for goods and services as may be determined by the Commission;[20]

18.1.1. A merger gives rise to a substantial lessening of competition when it has a significant effect on competition, and consequently, on the competitive pressure on firms to reduce prices, improve quality, become more efficient or innovative.[21]

18.1.2. A relevant market refers to a market in which a particular good or service is sold, and which is a combination of the relevant

[20] Rules and Regulations to Implement the Provisions of Republic Act. 10667 (Philippine Competition Act [PCC IRR], Rule 4, Sec. 1 (a) (1).

[21] PCC Merger Guidelines, Sec. 4.2.

product market and the relevant geographic market,[22] which is defined as follows:

18.1.2.1. The ***relevant product market*** comprises all those goods and/or services that are regarded as interchangeable or substitutable by the consumer or the customer, by reason of the goods and/or services' characteristics, their prices, and their intended use;[23] and

18.1.2.2. The ***relevant geographic market*** comprises the area in which the entity concerned is involved in the supply and demand of good and services, in which the conditions of competition are sufficiently homogeneous and which can be distinguished from neighboring areas because the conditions of competition are different in those areas.[24]

18.2. Take into account any substantiated efficiencies put forward by the parties to the proposed merger or acquisition, which are likely to arise from the transaction.[25]

19. In evaluating the competitive effects of a merger or acquisition, the Commission shall endeavor to compare the *competitive conditions that would likely result from the merger or acquisition* with the *conditions that would likely have prevailed without the merger or acquisition* ("counterfactual").[26]

19.1. In adopting a counterfactual, the Commission observes the prevailing conditions of competition pre-Transaction and considers the foreseeable events or circumstances.[27]

19.2. The Commission generally adopts the pre-Transaction situation as counterfactual, unless contrary evidence suggest that such condition is not realistic.[28]

20. In its evaluation, the Commission may consider, on a case-by-case basis, the broad range of possible factual contexts and the specific competitive effects that may arise in different transactions, such as:

a. the structure of the relevant markets concerned;
b. the market position of the entities concerned;
c. the actual or potential competition from entities within or outside of the relevant market;

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22 Philippine Competition Act, Chap. 1, Sec. 4(k).
23 Philippine Competition Act, Chap. 1, Sec. 4(k)(1).
24 Philippine Competition Act, Chap. 1, Sec. 4(k)(2).
25 PCC IRR, Sec. 1 (a) (2).
26 PCC Merger Review Guidelines, Sec. 4.12.
27 *Id.*
28 *Id.*

d. the alternatives available to suppliers and users, and their access to supplies or markets; and
e. any legal or other barriers to entry.[29]

IV. RELEVANT MARKETS AND COMPETITIVE ASSESSMENT

A. Relevant Product Markets

21. In its SOC, MAO identified the following as markets where the Parties have overlapping lines of businesses in the sugar manufacturing process and the products produced therein:

    a. Provision of sugar cane milling services
    b. Raw sugar
    c. Provision of refining or tolling services
    d. Refined sugar
    e. Molasses[30]

22. RHI interposed no objections to the product markets as defined by MAO.

23. As in this case, some mergers may have potential effects in more than one (1) relevant product or geographic market as to require an independent competitive assessment of each market in which a potential competitive concern arises.[31] The Commission, thus, considered all the relevant markets that may be impacted by the Transaction to determine whether significant harm to competition is likely to occur in any of them.[32]

24. The provision of sugar cane milling services was identified as a distinct product market based on the following considerations:

    24.1. First, both Parties are engaged in the provision of sugar cane milling services for the purpose of producing raw sugar, with URC and RHI operating six (6) and two (2) sugar cane mills, respectively. The provision for sugar cane milling services is thus an overlapping line of business between the Parties.[33]

    24.2. Second, sugar cane milling is a unique service that can only be used for extracting and processing sugar cane juice and producing raw sugar as well as its by-products. It is not possible for the facilities of the Parties to be used to mill other crops or manufacture other products and there is no alternative service that can be used to extract sugar cane juice in order to produce raw sugar. The provision for sugar cane milling services, therefore, is non-substitutable.[34]

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[29] PCC IRR, Sec. 1 (c).
[30] SOC, par. 83.
[31] Merger Review Guidelines, Sec. 5.9.
[32] *Id.*
[33] SOC, par. 84.
[34] SOC, par. 84.

25. MAO considered the possibility of expanding the relevant market to include milling of sugar cane by distilleries for bioethanol production on the premise that the planters, who are the customers of the Parties' sugar cane milling services, can sell their sugar canes instead to these distilleries. However, it was found that bioethanol distillation cannot be considered as a substitute for the sugar cane milling services due to the following reasons:

    25.1. There are fundamental differences between the relationships of the planters with the millers, and the planters with the distillers, due to the difference in method of obtaining sugar cane supply and its corresponding compensation scheme. Millers provide their milling services to the planters and are compensated through a share in the raw sugar output, the product of the milled sugar canes.[35]

    25.2. Distillers, on the other hand, purchase the sugar canes that are delivered to them by the planters.[36]

26. Thus, considering the Parties' overlap in this business and the non-substitutability of sugar milling services, the Commission finds the *provision of sugar milling services* as a relevant product market subject to analysis.

27. With respect to the market for raw sugar, the Commission affirms MAO's determination that raw sugar is a separate relevant product market. This is primarily because CADPI and URC-Balayan have an overlap in the trading of standard raw sugar sold to industrial users and traders.[37]

28. With respect to the market for the provision of refining or tolling services, the Commission agrees with MAO's finding that it is a separate relevant product market. Apart from CADPI and URC-Balayan's overlap in this market, tolling or refining of raw sugar is a process unique to the production of refined sugar and therefore cannot be substituted with other similar manufacturing process. Furthermore, the equipment, facilities, and technical know-how required to operate a refinery is specific to the sugar industry.[38]

29. With respect to the market for refined sugar, the Commission accepts MAO's findings that refined sugar constitutes a relevant product market of its own. Apart from CADPI and URC-Balayan's overlap in this market, refined sugar and its market have specific characteristics that distinguishes it from other sweeteners, thereby constituting a separate product market.[39]

30. With respect to the market for molasses, the Commission affirms MAO's findings that molasses has its own relevant product market. Apart from CADPI and URC-Balayan's inevitable overlap in the market—molasses being a by-product of sugar production, MAO was correct in identifying molasses as a relevant product

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[35] SOC, par. 86.1.
[36] *Id.*
[37] SOC, Annex "K".
[38] SOC, Annex "L".
[39] SOC, Annex "M".

market because of its specific quality and purpose which will not allow its customers to easily shift to other alternatives.[40]

B. Relevant Geographic Markets

31. In the SOC, the identified relevant geographic market for sugar cane milling services are the provinces of Batangas, Laguna, Cavite, and Quezon (the "Provinces"), in which the assessment of competitive effects of the Transaction is to be conducted.

    31.1. The geographic scope of competition for sugar cane milling is circumscribed by the perishable nature of harvested sugar cane. Customer interviews and customer lists provided by URC-Balayan and CADPI facilities indicate that the relevant geographic market is limited to Batangas, Laguna, Cavite and Quezon.[41]

    31.2. MAO likewise considered the possibility of expanding the geographic market to include the nearest sugar cane mills located in adjacent provinces, i.e. (1) Sweet Crystals Integrated Sugar Mill Corporation ("Sweet Crystals") in Porac, Pampanga, (2) Central Azucarera de Tarlac ("CADT"), in Tarlac City, Tarlac, and (3) Peñafrancia Sugar Refining Mill ("Pensumil") in Pili, Camarines Sur.[42] However, considering the distance of these mills from the plantations in Cavite, Laguna, Batangas and Quezon Province,[43] the considerable travel time of transporting sugar,[44] transport costs,[45] the inelasticity of demand of majority of the planters in the identified geographic market,[46] and the strong customer testimonies obtained by the Commission,[47] these mills in adjacent provinces were not considered part of the relevant geographic market.

32. Considering the foregoing observations by MAO, the Commission affirms the relevant geographic market definition for the provision of sugar milling services—the provinces of Batangas, Laguna, Cavite, and Quezon.

33. As to the other four (4) relevant product markets that were initially identified, the Commission concurs with MAO's findings that a substantial lessening of competition ("SLC"), as a result of the Transaction, is not likely to occur within these markets.

    33.1. With respect to the *raw sugar market*, the Parties, through their respective sugar cane milling facilities, are both engaged in the production of raw sugar which are thereafter sold to industrial users and traders.[48] Notwithstanding this overlap, the Commission finds that URC

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[40] SOC, Annex "N".
[41] SOC, par. 88.
[42] SOC, par. 90.
[43] SOC, par. 93-95.
[44] SOC, par. 96-97.
[45] SOC, par. 98-99.
[46] SOC, par. 100-101.
[47] SOC, par. 93-95.
[48] SOC, par. 108.

will not have the ability nor the incentive to prevent, lessen, or restrict competition in the raw sugar market, which is national in scope, considering the number of players in the market for raw sugar and the small combined shares of the Parties post-Transaction.[49]

33.2. With respect to the *provision of refining or tolling services* market, the Commission finds that URC does not have the incentive, post-Transaction, to increase the tolling rates of CADPI or any of its refineries in Luzon and Visayas.[50] The existence of other large competitors will limit the amount of sales that will be diverted to URC following an increase in the price of CADPI. The same is true for the amount of sales expected to be diverted to CADPI following an increase in the price of URC.[51]

33.3. With respect to the *refined sugar* market, the Parties are both engaged in the trading of refined sugar to industrial users and traders.[52] Notwithstanding this overlap, the market investigation conducted by the Commission showed that due to the existence of other players in the geographic market, which is national in scope, an increase in the price of refined sugar sold by CADPI will not result to an increase in URC's refined sugar sales. Conversely, an increase in the price of refined sugar sold by URC will not translate to an increase in CADPI's sales of refined sugar. Thus, the Commission finds that URC will not have the ability nor the incentive to prevent, lessen, or restrict competition in the refined sugar market.[53]

33.4. With respect to the *molasses* market, the Commission finds that the geographic market for the trading of molasses is nationwide in scope.[54] Thus, the Commission concludes that the trading of molasses will continue to be an unconcentrated market post-Transaction, and will not likely result to SLC in the molasses market.[55]

C. Competitive Situation Pre-Transaction

34. As noted by MAO in the SOC, the sugar industry is one of the oldest and most important industries in the Philippines.[56] Its crucial role in the economy, in fact, prompted the creation of government agencies that are primarily tasked to protect, promote, and regulate the sugar industry. Today, the Sugar Regulatory Administration ("SRA") is the foremost government authority tasked to oversee the development of the industry.[57]

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49 SOC, par. 101.
50 SOC, par. 111.
51 SOC, par. 112-113.
52 SOC, par. 114.
53 SOC, par. 118-119.
54 SOC, par. 120.
55 SOC, par. 121-122.
56 SOC, par. 13, p. 7 *citing* Philippine Institute for Development Studies, Industry Structure and Competitiveness - Refined Cane Sugar. 1999.
57 SOC, par. 15 *citing* Executive Order No. 18, issued by then President Corazon C. Aquino on 28 May 1986, established the Sugar Regulatory Authority. It is mandated to carry out the following functions: (a) To institute an orderly system in sugarcane production for the stable, sufficient and

35. The production of sugar from sugar cane involves several stages starting from the cultivation of sugar cane to trading of processed sugar.[58]

    35.1. Sugar cane planters ("planters") deliver cut sugar canes to their mill of choice where the sugar cane millers ("millers") extract cane juice and process it in order to produce raw sugar.

    35.2. Raw sugar produced from milling is shared between the miller and the planters.

    35.3. Raw sugar is then stored in SRA-registered warehouses, while negotiable warehouse receipts or "*quedans*" representing the share of the miller and the planters are issued by the mills. These *quedans* may then be traded or sold to industrial users or traders.

36. Planters consider several factors when deciding which mill to deliver or supply their sugar cane such as sugar recovery, mill capacity and efficiency, manner of hauling canes, speed of milling, and distance from the plantation, among others.[59]

37. In view of these considerations and to attract the planters located in Southern Luzon to mill in their facilities, URC-Balayan mill and CADPI mill have been competing in three (3) aspects: sharing agreement, sugar recovery rates, and incentives.

D.1. Planter-Miller Sharing Agreement

38. Raw sugar produced after milling is divided or shared between the sugar cane planters and millers, otherwise referred to as the "planter's share" and "miller's share," respectively. The miller's share is the compensation for services of the mill in processing the sugar cane. The planter's share is the portion planters receive.[60]

39. The planters, usually through the sugar cane planters' associations, and the sugar cane mills negotiate and execute a sharing agreement for the raw sugar and by-products produced out of the sugar cane delivered.[61]

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balanced production of sugar for local consumption, exportation and strategic reserve; (b) To establish and maintain such balanced relation between production and requirement of sugar and such marketing conditions as will insure stabilized prices at a level reasonably profitable to producer and fair to consumers; (c) to promote the effective merchandising of sugar and its products in the domestic and foreign markets so that those engaged in the sugar industry will be placed on a basis of economic viability; (d) To undertake such relevant studies as may be needed in the formulation of policies and in the planning and implementation of action program.

[58] Information on sugar production were gathered and verified through market investigation by MAO employing tools such as interviews, site visits, supply chain research, among others.

[59] SOC, par. 97.1 *citing* Summary of Statements of Sugar Cane Planters Regarding Considerations in Selecting Sugar Cane Mills.

[60] SOC, par. 142 *citing* Appendix 2.4, Notification Form of Roxas Holdings, Inc., IR-021-2018-002.

[61] *Id.*

40. In the absence of a formal written agreement between the sugar cane mill and the planter, Republic Act No. 809[62] mandates a graduated sharing agreement.

41. According to the results of MAO's market investigation, the ability of planters to bargain for a higher sharing agreement in one mill is contingent on the presence and actions of a competitor mill.[63]

    41.1. In 2017, URC increased the planters' share from 65% (which was the rate for the past two crop years) to 67% [confidential] to protect URC-Balayan's sugar cane supply in response to an anticipated adjustment [confidential] in CADPI's sharing agreement [confidential] failure to adjust the sharing agreement would result in the loss of delivery from its largest sugar cane supplier, [confidential]

42. These show that prior to the Transaction, the Parties competed based on adjustments in the planter-miller sharing agreement and are constrained by each other's behavior when setting and negotiating sharing agreements.

D.2. Sugar Recovery Rates

43. The sugar recovery rate represents the amount of raw sugar derived from sugar cane. Millers and planters monitor two (2) kinds of recovery rates:

    43.1. Theoretical or *quoted recovery rate* is determined at the start of the milling process by extracting samples from sugar cane delivered to the mill. Based on the readings of equipment used to sample the cane, quoted recovery rates are provided to planters per truckload of delivery.

    43.2. *Actual recovery rate* is determined by simply dividing the actual raw sugar output in number of 50-Kg bags by the amount of sugar cane milled in metric tons. Actual recovery rates can be calculated and monitored as frequent as on a daily or weekly basis.[67]

44. Actual recovery rates may be viewed as a measure of the mill's efficiency. Plant shutdowns, poor juice extraction, longer truck turnaround time, and other plant inefficiencies that lead to lower actual recovery rates discourage planters from delivering sugar cane to a particular mill. The current competitive conditions

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[62] SOC, par. 143 *citing* Republic Act No. 809, otherwise known as, An Act to Regulate the Relations Among Persons Engaged in The Sugar Industry, 1952.

[63] SOC, par. 143

[64] SOC, par. 144.1 *citing* [confidential]

[65] *Id.*

[66] *Id.*

[67] SOC, par. 162.

between URC-Balayan and CADPI compel both mills to continue improving their respective plants in order to yield higher recovery rates.[68]

45. Planters are issued *pesadas* based on quoted recovery rates instead of actual recovery rates. Thus, they are more inclined to deliver sugar canes to both mills which gives them higher quoted rates.[69] It is common practice among planters to deliver to both mills in order to compare recovery rates. If the quote in one mill is lower than what a planter expects, such planter would likely shift his next delivery to the competitor mill.[70]

46. While the millers guarantee efficient operations through actual recovery rates, it is the quoted recovery rate that eventually becomes the basis for the amount of raw sugar provided to planters.[71]

47. For this reason, a closer look into the quoted recovery rates is necessary to determine how it is being utilized by the Parties to compete with each other on sugar cane supply.

48. MAO presented empirical evidence that the Parties compete on the basis of quoted recovery rates. In its analysis, MAO examined the movement of quoted sugar recovery rates of both mills for the past three (3) crop years (2015-2016 to 2017-2018).[72]

    48.1. The analysis sought to observe a scenario where there is a loss of a competitor in the relevant market and how this would affect the quoted sugar recovery rates offered by the remaining miller.

    48.2. In this instance, MAO considered CADPI's factory stoppages or plant shutdowns for more than six (6) hours as a case where there is a loss of competitor and observed how URC-Balayan's quoted recovery rates responded to CADPI's absence in the relevant market.[73]

    48.3. Statistical analyses were conducted to confirm the hypothesis that CADPI shutdowns correspond to lower recovery rates in URC-Balayan. This is because URC-Balayan would have less incentive to quote high recovery rates when the planters have no option for a particular day or week within a milling season.[74]

    48.4. Using data from the Daily Factory Statements of the Parties, a comparison of the average daily quoted recovery rates in URC-Balayan

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68 SOC, par. 162.
69 SOC, par. 163 *citing* Excerpt from the Position Paper of Luzon Federation of Sugarcane Growers Association Inc. dated 26 July 2018 states that: "A sugarcane farmer would naturally send his sugarcane to the mill which registers the higher yield as measured in LKGTC/PSTC. Often times, the choice is made per truckload as the results of the two existing mills in Batangas may vary even if the sugar cane sent separately to the two (2) mills came from the same field."
70 *Id.*
71 SOC, par. 165
72 SOC, par. 166.
73 SOC, par. 166.
74 SOC, par. 168.

when CADPI was experiencing shutdowns and *when the latter's operations are continuous*, revealed that URC-Balayan's average daily quoted recovery rates are in fact lower on days when CADPI is experiencing plant shutdowns. The same observation holds true for the average actual recovery rates.[75]

Comparison of Average Daily Quoted Recovery Rates

Period	***Quoted Recovery Rate***
Without CADPI shutdown	[confidential]
With CADPI shutdown	[confidential]
Difference	0.11
t-statistic (p-value)	4.6267 (0.0000)

48.5. On the basis of the same daily production data, MAO constructed a time series Error Correction Model (ECM) to examine the relationship between quoted recovery rates in CADPI and URC-Balayan.[76]

48.5.1. Results of the said regression analysis showed a significant and negative relationship between CADPI shutdowns and the average daily quoted recovery rate in URC-Balayan. URC-Balayan quoted recovery rates were approximately 0.01 unit or 1% lower when CADPI was experiencing factory stoppages of more than six (6) hours.[77]

48.5.2. Moreover, a unit increase in CADPI's average quoted recovery rate from the previous day corresponded to a 4% increase in the quoted recovery rate in URC-Balayan for the succeeding day.[78]

49. These indicate that the market conditions prior to the Transaction were such that the Parties competed based on sugar recovery rates and were constrained by each other's behavior when setting the said rates. This competition allowed the planters to choose between the Parties in terms of better sugar recovery rate.

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75 SOC, par. 168.

76 SOC, par. 169.1 and 169.2. The main objectives of the regression analysis are:
a. Isolate the effect of Don Pedro plant shut downs and determine whether the difference in the quoted recovery rate of URC-Balayan as described above can be attributed to constraints from the operations of Don Pedro, controlling for other factors that might affect average daily recovery rates
b. Characterize the effect of Don Pedro and URC-Balayan's recovery rates on each other and determine whether the average quoted recovery rate in Don Pedro from the previous day affects the average quoted recovery rate in URC-Balayan for the succeeding day.

77 SOC, par. 170.

78 SOC, par. 171.

D.3. Incentives for Planters

50. Planter incentives range from monetary incentives, such as trucking subsidies, early and late milling incentive, and green cane incentive, and non-monetary incentives such as hauling services.[79]

51. Similar to the sharing agreement, incentives are negotiated between planters and millers at the beginning of a crop season. Among the incentives available to planters, only trucking subsidies are regularly provided at fixed rates. The availability of other incentives may vary per milling season. The presence or absence of some incentives provided by a mill depends largely on the strategy of the competing mill in attracting sugar cane planters.[80]

52. Competition between the Parties resulted in improving incentives extended to planters.

    52.1. URC had previously offered incentives to maintain and grow its planter base despite CADPI offering a higher sharing agreement. [confidential] [81]

53. As the market conditions prior to the Transaction show, the Parties competed based on incentives to planters and were constrained by each other's behavior when deciding which incentives to offer and the corresponding extent of these incentives.[82]

    53.1. As may be concluded from the foregoing observations and the evidence on record, no standard set of incentives is being offered by Parties per milling season. Millers may choose to introduce new incentives in the middle of a crop year to secure cane supply and increased share in the market.[83]

54. Consequently, such competition allowed the planters to bargain for better incentives by leveraging their ability to switch to the competitor miller for more compelling set of incentives.

D.4. Conclusion on the Pre-Transaction Competitive Situation

55. The Commission finds that based on the evidence on record, the prevailing competitive situation in the relevant market without or prior to the Transaction is one where the Parties are engaged in a head-to-head competition to secure

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[79] SOC, par. 181.
[80] SOC, par. 182.
[81] SOC, par. 183.1 *citing* [confidential]
[82] SOC, par. 184.
[83] *Id.*

sufficient or even bigger share in the supply of sugar cane from the planters. The general parameters of competition pre-Transaction are: (1) planter-miller sharing agreement; (2) sugar recovery rate; and (3) incentives for planters.

56. Accordingly, the Commission assessed whether competition in the relevant market would be substantially lessened by virtue of the Parties' merger to monopoly. To fully understand the resulting monopoly and its implications in the relevant market, the likely effects of the Transaction were examined.

E. Competitive Situation Post-Transaction

57. As earlier discussed, the analytical framework implemented by the Commission requires a careful comparison between the counterfactual and the anticipated state of competition that would result from the merger.

58. In this case, the counterfactual is the scenario wherein URC-Balayan and Don Pedro will continue to operate independently and compete with each other for the supply of sugar cane from Batangas, Cavite, Laguna and Quezon.[84]

59. Based on its market investigation, MAO identified the following theories of harm: (1) unilateral decrease in planter's share; (2) unilateral decrease in sugar recovery rates; and (3) unilateral decrease in incentives for planters.

F. Theories of Harm

60. A horizontal merger like this case, might substantially lessen competition in two (2) ways: unilateral effects and coordinated effects. It is likewise possible that a merger will result in both types of concern. Analysis of these effects gives rise to theories of harm.

61. In analyzing the potential for coordinated effects, the Commission assesses whether the merger increases the likelihood that firms in the market will successfully coordinate their behavior or strengthen existing coordination in a manner that harms competition.[85]

    61.1. In this case, it is unnecessary to conduct an analysis on the potential coordinated effects as the Transaction would clearly lead to a monopoly. Thus, there will be no coordination between different firms in the relevant market post-Transaction.

62. On the other hand, the Transaction may bear unilateral effects because it may create or enhance URC's ability or incentives to independently exercise market power.[86] Certain mergers may increase the likelihood of the exercise of unilateral market power in a variety of settings, including but not limited to a merger to monopoly. A merger to monopoly combines the only two (2) rivals in a properly defined market, thus raising a high risk of significant anti-competitive unilateral

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[84] SOC, par. 111.

[85] PCC Merger Review Guidelines, Sec. 7.10

[86] PCC Merger Review Guidelines, Sec. 7.5

effects. Review of such merger entails an assessment of whether any competitive constraints exist, such as ease of entry, that would preclude the unilateral exercise of market power by the merged firm.[87]

63. The Commission finds that the Transaction is a *merger to monopoly*, which means that it would combine the only two (2) rivals, CADPI and URC-Balayan, in the relevant market—the provision of sugar milling services in the provinces of Batangas, Laguna, Cavite, and Quezon. It is clear that the Transaction would translate not only to a lessening of competition but a **total elimination of competition** in the relevant market. URC, being the sole owner of the mills in the geographic market post-Transaction, would therefore have consolidated market power which it can utilize for its own benefit without any constraints that could mitigate its exercise of the said market power.

64. Thus, under the theory of unilateral effects, the Commission examines whether URC will have the ability and incentive to unilaterally decrease planter's share, sugar recovery rates, and planter's incentives post-Transaction, to maximize its profits, without fear of losing sugar cane supply and incurring losses in its sugar cane milling services.

F.1. Unilateral Decrease in Planter's Share

65. Under this theory, it is assessed whether the Transaction enhances the market power of URC as the sole owner of the mills in the relevant market, such that it has the ability and incentive to unilaterally decrease the planters' share in the sharing arrangement, ultimately increasing CADPI and Balayan's ("URC-controlled" mills) respective shares in the sugar output.

66. In the SOC, MAO observed that even pre-Transaction, CADPI planters have historically been unsuccessful in mirroring the 70-30 sharing stipulated in R.A. 809 when negotiating their sharing agreements.[88]

67. The Commission notes that while R.A. 809 applies only in the absence of a written sharing agreement, the 70-30 sharing ratio provided therein at the very least indicates a fair sharing agreement for both the planter and the miller. The fact that pre-Transaction, the Parties were able to command planters' share lower than the rate of 70% shows the Parties have always had the ability to decrease planters' share. This ability will be further enhanced once a monopoly is created post-Transaction.

68. MAO likewise considered whether URC would find it profitable post-Transaction to unilaterally adjust and skew the planter-miller sharing agreement to its favor.[89]

    68.1. The profitability strategy is dependent on two counteracting factors – (1) the benefit gained from additional revenue as a result of the increase in

[87] PCC Merger Review Guidelines, Sec. 7.7
[88] SOC, par. 149.
[89] SOC, par. 152.

the miller's share, and (2) the reduction in volume and equivalent foregone revenues that would have been earned absent the adjustment.

69. In assessing the profitability to unilaterally adjust the sharing agreement, MAO used the Gross Upward Pricing Pressure Test to quantify the firm's incentive to increase the miller's share, and correspondingly reduce the planter's share.[90]

69.1. The Gross Upward Pricing Pressure Index (GUPPI) typically measures how much the merged entity stands to gain from an increase in price by considering the lost sales (due to diverted customers) that are re-captured by the other merging party. The more profitable the price increase is for the merged entity, compared to pre-Transaction profits, the more incentive there is to impose an adjustment in price post-Transaction.[91]

69.2. In this case, the price is the planter-miller sharing ratio where the increase in price is represented by the increase in miller's share (and correspondingly decrease in planter's share).

69.3. The GUPPI is used to measure the potential gains of either Party from increasing the miller's share. It considers two factors which affect a firm's incentive: (1) the margins or profit from the services provided, and (2) the diversion ratio, which measures the proportion of lost sales, following the decrease in planters' share, that is diverted to the other merging party.[92]

69.4. A merger is expected to raise significant unilateral effects and lead to substantial lessening of competition if the GUPPI is proportionately high, or in practice, more than 10%.[93]

70. The tests resulted to a GUPPI of more than 10% when miller's share, which represents the *price* in this test, is increased to 33-35% and correspondingly the planter's share is reduced to 65-67% in either the URC-Balayan or CADPI sharing agreements.[94]

71. The results likewise indicate that the merged entity will find it profitable post-Transaction to increase the miller's share and correspondingly decrease the planter's share. The merged entity will prejudice planters' interests to the extent that:

71.1. A reduction of 1% in the planter's share will correspond to a Php320.00 decrease in planter's revenue per ton of cane delivered.[95]

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[90] SOC, par. 154.
[91] SOC, par. 155.
[92] *Id.*
[93] SOC, par. 156.
[94] SOC, par. 158.
[95] SOC, par. 161.

71.2. This will result in a Php2,210.68 loss in revenue for an average planter from AAROB, an association of planters, and as high as Php17,189.23 for a planter from BISPMPC.[96]

72. Based on the merger investigation, the Commission finds that the Parties have the ability and incentive to unilaterally decrease the planters' share in the sugar output sharing agreement.

73. RHI, in its Verified Comment on the SOC, generally argued the following:

73.1. The laws governing the sugar industry and the unique symbiotic and interdependent relationship between sugar planters and millers do not allow for an independent and unilateral exercise of market power in the relevant market;[97] and that in fact sugar cane planters may easily reject an unfair sharing ratio that may be demanded by a miller and seek recourse to the default sharing ratio provided under R.A. 809;

73.2. The farmers in Southern Luzon have market power. Substitution outside the market remains as a sufficient competitive constraint and that in fact sugar cane planters have bargaining power because of their freedom to accept or reject contracts with the sugar mills.[98]

74. The Commission finds RHI's arguments unconvincing.

75. R.A. 809 or *The Sugar Act of 1952* only provides default sharing ratios in the absence of any sugar output sharing agreement between the planters and the miller. To be clear, the provision on default sharing ratios in R.A. 809 presupposes that the miller agreed to take the supply of sugar cane from a planter and that the matter unresolved is the sharing agreement between such miller and the planter. However, R.A. 809 does not apply in instances where a miller entirely refuses to provide sugar milling services. Thus, it does not protect the planters from a scenario where a sole miller postures a *take it or leave it* stance with the view to compelling planters to yield to an unfair sharing agreement.

76. In this case, when URC becomes the sole miller post-Transaction, it could decide to entirely reject the supply of sugar cane from planters who refuse to accede to a sharing agreement favorable to its mills. Considering that there are no other sugar mills in the relevant market, the planters will not be "free to accept or reject contracts with the sugar mills" as RHI would have this Commission believe. In such a situation, planters have no leverage or bargaining power, not to mention the fact that R.A. 809 will not apply as to give protection to the planters.

77. To further support its argument that planters have market power, RHI contended that the sugar milling industry has "unique characteristics" that allegedly deny a sugar miller monopoly the extent of control that a monopoly in other industries would otherwise have. This is allegedly shown by the fact that the planters are

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96 SOC, par. 161.
97 RHI Comment, pages 7-15.
98 RHI Comment, pages 16-18.

organized[99] and that the millers, which are allegedly under-capacitated, have no alternative ventures other than milling of sugar cane.

78. The Commission is not persuaded.

79. First, RHI does not even explain what these unique characteristics are.

80. Second, the fact that the planters have similarly worded resolutions in itself is insufficient proof that the planters are "organized and have very strong lobbying power." Moreover, there is no proof that these translate to market power, as shown by the experience of planters described in the preceeding paragraphs.

81. Further, the argument that CADPI and URC-Balayan were under-capacitated does not negate the resulting market power of URC-controlled mills post-Transaction. Even assuming that the claim of under-capacity is true, data submitted by RHI showed that the supposed under-capacity had been existing pre-Transaction. But even in such case, the Parties were able to command a sharing agreement favorable to them—lower than the sharing ratios provided in R.A. 809.

82. Clearly, URC will gain further ability to command better sharing agreements for its mills post-Transaction when it will control both mills. This enhanced ability is likely to result in prejudice to planters who will have to bear a lower share of the output.

83. Apart from this ability, the Commission is convinced by the results of MAO's investigation showing that URC has an incentive to facilitate the unilateral decrease of planters' share post-Transaction because of the profitability of such unilateral measure.

84. Considering the foregoing and the Parties' failure to address the identified harm, the Commission finds that the Transaction will likely enhance the ability and incentive of URC unilateral decrease of planters' share, thus resulting in SLC.

F.2. Unilateral Decrease in Sugar Recovery Rates

85. In the SOC, MAO alleged that in the absence of a competitor, there is no more incentive for URC to ensure the accuracy and competitiveness of the quoted recovery rates considering that there is a lack of transparency in how quoted recovery rates are computed by millers,[100] and that it is in the interest of millers to decrease the quoted recovery rates given to planters in order not to forego its share of the final output.[101]

86. In its Verified Comment, RHI alleged that under the existing rules and regulations of the SRA, any excess sugar resulting from an intentional decrease in the

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[99] Some of the resolutions submitted by municipalities, cooperatives and are similarly worded.
[100] SOC, par. 174.3.
[101] SOC, par. 177.

recovery rate by the miller will be undeclared and hence, will not be issued a *quedan*, and any sugar without *quedan* cannot be sold to the market.[102]

87. RHI did not contest MAO's finding that there is a lack of transparency in the exact method of calculating quoted recovery rates.

88. The Commission finds that the lack of transparency in the process of computing for the quoted sugar recovery rates, particularly, the information asymmetry between planters and millers relating to the millers quoted recovery rate formulas, provided the Parties the ability to influence and manipulate the quoted sugar recovery rates.[103]

    88.1. To illustrate, in computing for the quoted sugar recovery rates, the Parties conduct chemical tests to measure certain parameters of the cane sample.[104] The results of these tests are used as an input in the formula that determines the quoted recovery rate provided to planters.[105] Although the planters are allowed to send their representatives to monitor the chemical tests conducted by the Parties, there was no sufficient visibility as to how the chemical test results were used to arrive at the quoted recovery rates.[106]

89. The ability of the Parties to manipulate the quoted sugar recovery rates was highlighted even more through the data and reports received by the Commission that the sugar recovery rates quoted by a commissioned third party, including the SRA, on the same cane sample delivered by the planters to the Parties, are often higher than the sugar recovery rates quoted by the Parties.[107]

90. The Commission notes that while the ability to unilaterally decrease the recovery rates as observed by MAO already exists pre-Transaction, they had limited incentive to unilaterally decrease such rates because of the presence of another competitor which could offer planters better quoted recovery rates.

91. Post-Transaction, the observed incentive to unilaterally decrease the recovery rates would be enhanced as a consequence of the total elimination of competition, which could compel planters to accept URC's rates.

92. With respect to MAO's finding that it is in the miller's interest to decrease the recovery rates given to planters, RHI argued that such finding cannot be possible by virtue of SRA's rules and regulations which, allegedly, penalizes a miller's intentional reduction of the quoted recovery rate given to planters with a non-issuance of a *quedan*.

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102 RHI's Comment, par. 5.13.
103 SOC, par. 174.3.
104 SOC, par. 174.2.
105 SOC, par. 174.1.
106 SOC, par. 174.2.
107 *Id.*; *also* Interviews with planters.

93. The Commission finds RHI's argument to be unconvincing.

94. When a planter delivers sugar canes to a miller, the planter is issued a *pesada* by the miller.[108] The *pesada* contains the name of the planter, the date of delivery, the volume of the sugar canes delivered, and the quoted sugar recovery.[109]

95. As soon as these sugar canes are milled, transformed into raw sugar, and stored in SRA-registered warehouses, the planter is issued a *quedan* by the miller[110] which contains, among others, the name of the planter and the sugar produced in fifty (50) kilogram bags.[111]

96. The recovery rate referred to in *quedans* is the actual recovery rate whereas the recovery rate referred to by MAO in its findings is the quoted recovery rate. Hence, assuming RHI's argument to be true, a miller's attempt to decrease the recovery rate that it quoted to planters in the *pesada* will not prevent the miller from issuing a *quedan,* which relies on actual sugar recovery, later on. RHI's argument, evidently, did not address the harm identified by MAO.

97. The Commission, thus, agrees with MAO's conclusion that URC has the enhanced ability and incentive to unilaterally decrease the quoted sugar recovery rates post-Transaction.

F.3. Unilateral Decrease in Incentives for Planters

98. In the SOC, MAO identified URC's increased ability post-Transaction to reduce or eliminate incentives employed by millers to entice planters to their mills as a potential harm. Pre-Transaction, planters have the ability to bargain for better incentives due to the existence of competition between the two (2) mills. However, with the elimination of CADPI as URC's only competitor, these incentives will likely be eliminated as the URC-Balayan and the CADPI mills, both owned and operated by URC post-Transaction, no longer need to compete with each other for cane supply.

99. Moreover, MAO alleges that the profitability of reducing the incentives provided to planters, by reducing URC's operational costs, incentivizes URC further to unilaterally decrease the planters' incentives.[112]

100. In its Verified Comment, RHI argued that the Commission misappreciated the nature of the amounts that the Parties give to the planters.[113] RHI claimed that the only existing "incentive" provided by CADPI to planters is the amount for the transportation subsidy.[114] Such transportation subsidy, however, is a

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[108] SOC, par. 176.
[109] SOC, note 129.
[110] SOC, par. 18.
[111] A Primer on PEF's Priority Commodities: Industry Study on Cane Sugar, *available at* http://pef.ph/wp-content/uploads/2016/03/Industry-Study_Cane-Sugar.pdf
[112] SOC, par. 193.
[113] RHI Comment, p. 13.
[114] *Id.*

reimbursement for the transportation and hauling costs incurred by the planters.[115]

100.1. RHI explained that pursuant to the mandate of R.A. 809, "the share of the planters shall not be diminished directly or indirectly by any deductions for transportation costs, among others." Thus, the hauling subsidy was designed as a reimbursement mechanism rather than an additional source of income for the planters.[116]

101. The Commission is not persuaded.

102. The Commission finds that RHI's argument does not address the harm identified by MAO, that is, URC's ability and incentive to reduce the amount or eliminate some of the incentives currently provided to planters.

102.1. URC [confidential] offered planters a special milling incentive [confidential] in order to effectively compete with CADPI [confidential].[117]

102.2. Clearly then, if CADPI would leave the market, URC has no other reason to offer incentives to the planters as there is no longer any competitor which could lure the planters away from URC.

102.3. RHI did not, in its Verified Comment, offer any argument to refute this conclusion of MAO.

103. The Commission, hence, agrees with MAO's findings that URC, post-Transaction, has the ability and incentive to unilaterally decrease, if not eliminate, the incentives currently provided to planters.

G. Entry and Expansion

104. Firm entry and/or expansion by existing competitors is an integral part of the analysis of whether the Transaction is likely to harm competition significantly and allow the Parties to raise prices or reduce output, quality or innovation.[118]

105. Entry, or the threat of entry from potential competitors or from customers turning to in-house supply, can be a significant competitive constraint on the conduct of the Parties. If URC is subject to significant competitive constraints from the threat of market entry, the Transaction is unlikely to have meaningful anticompetitive effects.[119]

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115 *Id.*
116 RHI Comment, p. 14.
117 SOC, par. 183.1.
118 Merger Guidelines, Sec. 8.1.
119 Merger Guidelines, Sec. 8.2.

106. In assessing whether entry and/or expansion would effectively constrain URC, the Commission considered whether entry and/or expansion would be: (a) likely, (b) timely, and, (c) sufficient in nature, scale, and scope.[120]

106.1. For entry and/or expansion to be likely, it should be profitable for URC's competitors to expand output and/or for potential entrants to enter the market in response to an attempt by URC to profit from the potential reduction in competition brought about by the merger.[121]

106.1.1. In assessing the likelihood of entry, the Commission considered the history of entry into and/or exit from the relevant market using available evidence, including information on firms that have recently entered or exited the market, information about past and expected market growth, evidence of planned entry and/or expansion, direct observation of the costs, risks and benefits associated with entry and information from firms identified as potential entrants.[122]

106.2. In assessing whether entry and/or expansion is timely, the Commission considered whether entry and/or expansion would take place within a reasonable period of time after the Transaction. This often means that entry must have a competitive impact within two (2) years to have a sufficiently disciplining effect. The appropriate time horizon may vary according to the characteristics of the relevant market.[123]

106.3. For entry and/or expansion to be sufficient, the Commission considered whether entry and/or expansion would be:

a. Sufficient in scale to compete effectively with the merged entity;

b. Able to counteract any specific anti-competitive effects resulting from the merger; and

c. Able to counteract any localized effects of the merger.[124]

107. The Transaction being a case of merger to monopoly, other sources of competitive constraint, such as ease of entry or exit, was assessed by the Commission to consider whether these options are likely to preclude URC from exercising market power.

108. In the SOC, MAO found that there is little evidence to show the possibility of a new entrant, given the high barriers to entry in the relevant market.[125]

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[120] Merger Guidelines, Sec. 8.4.
[121] Merger Guidelines, Sec. 8.5.
[122] Merger Guidelines, Sec. 8.6.
[123] Merger Guidelines, Sec. 8.7.
[124] Merger Guidelines, Sec. 8.8.
[125] SOC, par. 240.

109. Moreover, MAO found that the proportion of sugar cane planters that have the choice to substitute to outside market options is not significant enough to provide any real constraint on the Parties' behavior, particularly: (1) shift to alternative revenue generating activities;[126] (2) shift to alternative crops,[127] and (3) shift to other mills outside Batangas.

110. In its Verified Comment, RHI argued that MAO failed to take into consideration another viable outside market option available to planters—selling their sugar canes to bioethanol distilleries.

111. The Commission finds sufficient evidence to support MAO's findings.

G.1. Likelihood of Entry

112. There is little evidence that support the possibility of a new entrant that can be considered as sufficient competitor post-Transaction.[128] This was also unrebutted by RHI.

113. The barrier to entry identified by MAO are indeed high as to dissuade another entity from entering the relevant market:

    113.1. Building a sugar cane plant would cost approximately Php5 Billion while its maintenance and operations may cost Php 60-100 Million annually;[129]

    113.2. The current supply of sugar cane is already insufficient for both URC-Balayan and CADPI mills to fully utilize their respective rated capacity;[130] and

114. Moreover, the Commission noted that Cavite Biofuels Producers, Inc., is developing a bioethanol plant that uses both molasses and sugar cane juice as feedstock and may be a potential entrant that can compete with URC post-Transaction for the supply of sugar cane. This potential entrant however, may not be incentivized to enter the market considering that there is a significant difference in the projected income of planters between sugar distilling and sugar milling and current regulatory restrictions by the SRA.[131] Thus, the possibilities of new entrant appear to be remote, and may not be immediate to actually constrain URC from exercising market power.

G.2. Timeliness of Entry

115. Market participants have consistently stated that setting up a new facility requires long-term planning and preparation. On top of the pre-development stage which includes the procurement of the location on which the mill will be built, the securing of permits and licenses from the regulators, and the procurement of the

[126] SOC, par. 201.
[127] SOC, par. 208.
[128] Interview with representatives of SRA.
[129] SOC, par. 235.
[130] SOC, par. 236.
[131] SOC, par. 237.

mill's equipments and machineries, construction and development of a milling facility could already take three (3) to five (5) years.[132] Additional period would be required for the mill to be fully operational. Considering the potential effects of the Transaction in the relevant market, even a period of three (3) years would not be considered timely entry.

G.3. Sufficiency of Entry

116. The Commission notes that the current supply of sugar cane of URC-Balayan and CADPI is not sufficient for both mills to fully utilize their respective rated capacity. It can therefore be deduced that a new entrant would face the same limitations on supply of input.[133] As the supply of sugar cane could not sufficiently utilize URC-Balayan and CADPI's capacity pre-Transaction, it could not be expected that a new competitor can enter with such scale as to effectively compete with URC.

G.4. Substitution Outside the Market

117. The Commission assessed the likelihood of planters shifting to outside market options—outside the product market to other alternative crops and revenue generating activities, or outside the geographic market to mills outside Batangas.

118. In a survey commissioned by MAO, respondent planters were asked whether they would consider shifting to other revenue generating activities in response to the changes in the current competition conditions. The Commission noted that the results of the planter survey show that the Parties are in fact the only viable alternatives for the respondent planters.[134]

    118.1. 59% and 63% of URC-Balayan and CADPI planters, respectively, will still choose to mill with either party even if the sharing agreement decreases to as low as 65-35. In fact, even if the sharing agreement was reduced to 61-39, majority of the planters in Batangas would still not likely consider outside market options.[135]

119. MAO also evaluated the viability of shifting to other identified crops from the perspective of affected sugar cane planters. However, other alternatives such as rice, corn, and coffee farming, are not as practical as sugar cane farming and would unlikely be a real and immediate option for planters.[136]

    119.1. Rice fields are heavily dependent on a well-functioning irrigation system. The agricultural lands, particularly the sugar cane plantations, in Batangas, Cavite, Laguna, and Quezon, do not have a reliable irrigation system and are heavily dependent on rainfall for water supply.[137]

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[132] SOC, par. 239.
[133] SOC, par. 236.
[134] SOC, par. 197.
[135] SOC, par. 199.1.
[136] SOC, par. 202.
[137] SOC, par. 203. *citing* Interview with Small Scale Farmers [confidential] .

119.2. Market investigation showed that on-farm labor intensity of fruit and vegetable farming is nearly twice than that required in rice and corn production. Ambient storage and sizeable logistics to minimize losses are not readily available in their areas and acquiring these resources require capital which they do not have.[138]

119.3. Batangas, Cavite, Laguna, and Quezon do not have comparative advantage relative to other regions in terms of coffee and corn production based on its yield per hectare, typically affected by external factors such as soil quality and climactic conditions.[139]

120. With respect to RHI's argument that MAO incorrectly excluded ethanol from the possible viable substitutes to sugar cane milling, the Commission found that MAO, contrary to RHI's allegation, did not exclude ethanol from the scope of the market study. As a matter of fact, MAO considered ethanol when it conducted the exercise of market definition for the sugar milling service product market.[140]

121. The Commission in defining the relevant market considered to include bioethanol production because planters, who are the customers of the sugar mills for milling services, may instead sell their sugar cane to these distilleries. The Commission found that milling for bioethanol, however, cannot be considered as a substitute for the services offered by the Parties from both a demand and supply-side perspective.

121.1. The method of obtaining sugar cane supply and compensation for the sugar cane is different for sugar mills and distilleries resulting in fundamental differences in the relationship between planters and sugar millers on the one hand and planters and distilleries on the other.

121.2. Majority of planters would rather bring their cane to a sugar mill and get a share of raw sugar than sell sugar cane to a distillery.

121.3. The intended purpose and primary output of the milling process are also different for sugar mills and distilleries.

H. Efficiencies

122. In its Verified Comment, RHI claimed that the Transaction will promote cost efficiency as it will necessarily result in economies of scale. With URC's acquisition of CADPI Assets and CADPI Land, RHI projected a reduction in operational costs and production shortfalls post-Transaction.[141]

123. In addition to economies of scale, RHI also claimed that the Transaction would result in greater yield of sugar production. [142] At present, URC's and CADPI's

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138 SOC, par. 202.

139 SOC, par. 141. *citing* Statement of [confidential]

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140 SOC, par. 86.1.

141 RHI's Comment, par. 7.04.

142 RHI's Comment, par. 7.04.

mills are under-utilized due to the scarcity of sugar cane supply. The Transaction, however, will supposedly allow URC to devote capital resources to machineries or equipment which, according to URC, will benefit not only URC, but the planters as well.[143]

124. Moreover, RHI claimed that the Transaction will also benefit the Southern Luzon sugar industry in terms of bringing back the close coordination and partnership between the millers and the planters.[144] URC further claimed that it will have the ability to improve the scheduling of harvests as a result of the mill consolidation, prompting ideal processes to be followed, which in turn will lead to the maximization of sugar recovery.[145]

125. Under Chapter IV, Section 21(a) of the PCA and Rule IV, Section 10 of the PCA's Implementing Rules and Regulations ("IRR"), the Commission may exempt an otherwise anti-competitive merger from prohibition when the Parties establish that the Transaction is likely to bring about gains in efficiencies that are greater than the effects of any limitation on competition that will likely result from the Transaction.

126. The gains in efficiency that the Commission may consider include lower prices, improved quality, enhanced service, and new products.[146] The Commission may also consider efficiencies that increase competition in the market.[147]

127. Efficiencies, by their nature, are difficult to verify and possibly, may never be realized.[148] Thus, in order for the Commission to consider the supposed efficiencies that the Transaction will likely bring about, the Parties, should they rely on an efficiencies justification, must demonstrate that if the Transaction was implemented, significant efficiency gains would be realized.[149] The Parties' demonstration of the gains in efficiency, in order to be taken into account by the Commission, must be accompanied by detailed and verifiable evidence of anticipated price reductions or other benefits.[150]

128. In addition to the above, the Parties' claimed gains in efficiencies should be substantial, timely, and will benefit the consumers in the relevant market where it is likely that competition concerns would occur.[151] Hence, the Parties must demonstrate before the Commission that:

    128.1. The efficiency gains are merger specific,[152] that is, they are likely to be accomplished with the Transaction, and unlikely to be accomplished in

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143 RHI's Comment, par. 7.04.
144 RHI's Comment, par. 7.09.
145 RHI's Comment, par. 7.04.
146 Merger Review Guidelines, Sec. 9.2.
147 Merger Review Guidelines, Sec. 9.3.
148 Merger Review Guidelines, Sec. 9.4.
149 *Id*.
150 Merger Review Guidelines, Sec. 9.6.
151 *Id*.
152 *Id*.

the absence of either the Transaction or another means having comparable anti-competitive effects;[153] and

128.2. The consumers will not be worse off as a result of the Transaction.[154]

129. RHI failed to provide *detailed and verifiable* evidence of the supposed benefits that the Transaction is projected to bring about. Moreover, RHI failed to demonstrate to the Commission that its claimed efficiencies are merger specific. The Commission thus finds RHI's efficiency claims to be unsubstantiated and without basis.

V. DISPOSITIVE PORTION

Considering the foregoing, the Commission finds that the Transaction will create or enhance URC's ability or incentives to independently exercise market power because of the total elimination of competition.

Accordingly, the Transaction will substantially prevent, restrict or lessen competition in the market for the provision of sugar milling services in the provinces of Batangas, Laguna, Cavite, and Quezon.

As there is no basis for exemption, the Transaction is **prohibited** in accordance with Section 18(a) of the Philippine Competition Act.

SO ORDERED.

12 February 2019, Quezon City, Philippines

[153] Merger Review Guidelines, Sec. 9.7.
[154] Merger Review Guidelines, Sec. 9.6.

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