CUTS International

SUBMISSION OF COMMENTS ON
PROPOSED COMBINATION OF AGRIUM INC AND POTASH CORPORATION OF SASKATCHEWAN INC

CUTS International (www.cuts-international.org) is an independent, non-profit economic policy research and outreach organisation. It works towards improvement in quality of regulation, competition and governance across sectors with the objective of enhancing consumer welfare.

I. SETTING THE CONTEXT - INDIA'S DEPENDENCY ON POTASH IMPORTS

The backbone of India's economy is agriculture, which contributes to over 22 percent of the gross domestic product (GDP) and provides livelihood to two-thirds of the population.[1] With rapidly increasing population, achieving food security is a constant challenge and dependence on agricultural inputs such as fertilisers has continuously seen an upward trend. The global average demand for total fertilizer nutrients is estimated to grow at 1.8 percent per annum from 2014 to 2018, and the demand for potash is expected to grow at a rate of 2.6 percent per annum.[2] Moreover, the regional demand growth for potash in South Asia is expected to be 4.9 percent (2014-2018), only second to the African region.[3]

In the coming months of 2017-18, market experts predict that consumption of fertilisers in India will increase, raising the demand by 5 percent in FY18.[4] Notably, one of the major crop nutrients utilised entirely for the fertiliser industry in India is Potash. However, Indian reserves of Potash are not commercially exploitable and the entire demand for the mineral is met from other counties making India 100% dependent on imports in case of Potash.[5] Globally, India is the 4th largest importer of potash (See Table 1). The broader dependence on imports of fertilizers has also been recognised by the Indian Ministry of Chemicals and Fertilizers which has noted that it is not possible for India to achieve self-sufficiency in the fertilizer sector.[6]

Table 1. Global Potash Imports

Country	Import Qty (thousand tonnes nutrients)
Brazil	5570.6
United States	5404.3
China	5091.6
India	**2587.0**

Source: International Fertilizer Association (2014)

1 Fertiliser Use by Crop in India, FAO, http://www.fao.org/docrep/009/a0257e/A0257E02.htm
2 Food and Agriculture Organization of the United Nations, *World Fertilizer Trends and Outlook to 2018,* 9 (2016), available at http://www.fao.org/3/a-i4324e.pdf
3 Ibid.
4 Rahul Oberoi, *Did you notice? One of the world's biggest sectors gave us many gems in last 3 years*, available at http://economictimes.indiatimes.com/articleshow/57507823.cms?utm_source=contentofinterest&utm_medium=text&utm_campaign=cppst
5 Indian Bureau of Mines, *Indian Minerals Yearbook,* ed. 54, 2 (2015), available at http://ibm.nic.in/writereaddata/files/11292016104837IMYB2015_Potash_29112016_Adv.pdf
6 Self–sufficiency in fertilizer production, Press release by the GOI, Ministry of Chemicals and Fertilizers, available at http://pib.nic.in/newsite/PrintRelease.aspx?relid=121426

II. POTENTIAL APPRECIABLE ADVERSE EFFECT ON COMPETITION

Canada's pole position as a Potash exporter

Very few regions across the globe have commercially exploitable Potash reserves. These are highly concentrated and the world's largest known deposits are located in Saskatchewan, Canada.[7] In 2014, Canada's global exports accounted for 10978.2 thousand tonnes (see Table 2) and currently, it accounts for 35 percent of the global potash trade.[8] The second and third largest potash exporting countries are Russia and Belarus respectively. Potash Corp. and Agrium (the parties) are both leading Canadian potash producing firms. The Saskatchewan (Canada) government had formed PotashCorp in 1975 as a Crown corporation, which was privatized in 1989. Agrium, a major producer of agricultural products including potash, was founded in 1931.

Table 2. Global Potash Exports	
Country	**Export Qty (thousand tonnes nutrients)**
Canada	10978.2
Russian Federation	6909.5
Belarus	5808.7
Germany	2685.7
Israel	1843.0

Source: International Fertilizer Association (2014)

Current Market Scenario of Potash Production

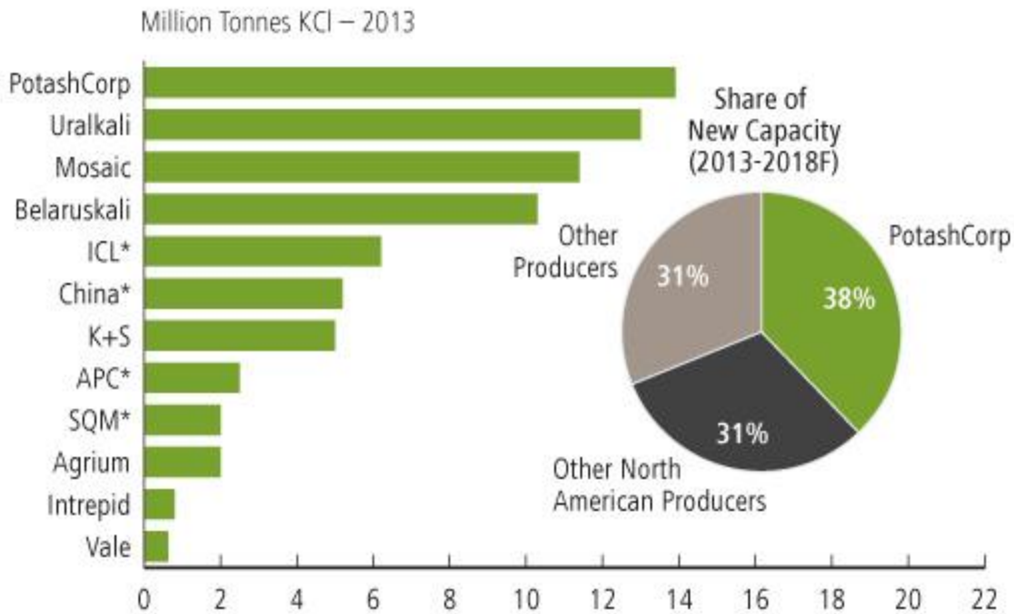
Currently, the market leader in fertiliser production is Potash Corp. (based in Saskatchewan, Canada). It is the world's largest producer of potash by capacity (30 percent of global capacity).[9] Russia's Uralkali as well as Belaruskali are top competitors and are among the world's leading potash suppliers.[10] The market shares in this sector in 2014 were as follows (latest market shares not available in open domain):

[7] Agrium, *Annual Report 2016*, at 24

[8] Michael Wiggins De Oliveira, *Potash Corp. Is Heavily Exposed To The Potash Upturn Expected To Materialize In 2017,* available at https://seekingalpha.com/article/4043420-potash-corp-heavily-exposed-potash-upturn-expected-materialize-2017

[9] Ibid.

[10] Emiko Terazono, *Potash: what's next for one of the world's major fertilisers*, Financial Times, 27 July 2016, available at https://www.ft.com/content/56f782b8-5345-11e6-9664-e0bdc13c3bef



Source: Potash Corp (2014)

It is apparent from the aforementioned statistics that Potash Corp. is the global leader in terms of capacity and production of potash. .

Notably, Form IV - 443 submitted by the parties states that there is significant competition for the supply of potash to customers in India from players such as Uralkali, Belaruskali, APC, ICL, K+S, and SQM, among others. However, Potash Corp. expects to increase its capacity further through brownfield expansion contacts and its investments in competitors such as ICL (14 percent investment), APC (28 percent investment), SQM (32 percent investment) and Sinofert (22 percent investment).[11]

These statistics have to be kept in mind while assessing their impact of the proposed merger.

Potential effect of merger on competition in India

This section seeks to assess whether the proposed combination between Potash Corp. and Agrium would have the effect or is likely to have an appreciable adverse effect on competition in the relevant market in India. As mentioned in Form IV-443, the parties do not have any physical presence or any subsidiary in India, and do not sell potash in India directly. However, both companies distribute potash through Canpotex, which is an export marketing consortium equally owned by Potash Corp., the Mosaic Company and Agrium.[12] A 2013 industry report claims that Canpotex is the world's largest exporter of potash, with sales ranging from 7 to 10 million tonnes every year.[13] Since its beginning of operations in 1972, Canpotex has delivered approximately 185 million tonnes to 135 customers in 60 countries. Out of these, a major chunk of 106 million tonnes went to 5 countries i.e. India, China, Brazil, Indonesia and Malaysia.[14] In 2015, 9 percent of total

[11] Potash Corp. represented the majority of capacity growth in 2016-17E. See Morgan Stanley, *Global Chemicals Potash S&D Update*, 7 (2016)
[12] Agrium Inc. SEC Filing 40-F, *Annual report for the fiscal year ending Thursday, December 31, 2015*, 42 (2016), available at https://www.last10k.com/sec-filings/agu
[13] *Saskatchewan Mining Journal*, Issue 1, 7 (2013)
[14] Supra 12

sales of Canpotex were made to India.[15] The prominence of Canpotex as the leading global supplier of potash, clubbed with the growing capacities of both Potash Corp. and Agrium in the global market make this combination worth looking into. Following are the major points of concern which need further investigation:

Effect on global price competition and Indian markets

Further, a more egregious concern, discussed below in detail is that the proposed merger has the capability of turning into a more concentrated export cartel, which can fix prices and control capacity utilisation thus harming Indian markets in the future. Markedly, Canpotex has earlier been touted as an export cartel.[16]

The Commission may recall that CUTS International had filed a Preliminary Information Report (PIR) regarding "Global Potash Cartel" vide its letter No. C.75(2)/1880, Dated 28.08.2012, along with relevant information. It may further be recalled that the D/o Fertilizers, Ministry of Chemicals & Fertilizers, India had made a Reference before the Commission vide DO No.SF/Misc/2013, dated 27-02-2013 on global potash cartelisation. In the Reference, the D/o Fertilizers had also mentioned about the CUTS' PIR and had requested for appropriate actions under the provisions of the Competition Act, 2002.[17]

The current situation is that the shareholders of Canpotex have committed to use the company as their exclusive offshore export outlet for potash produced in Canada that is exported to destinations outside the United States and Canada (including India).[18] In 2015, 53 percent Potash Corp's total sales were made to Canpotex and Agrium's share in Canpotex's total sales also increased from 7.3 percent in 2015 to 10.3 percent in 2016.[19] This increase was attributed to Agrium's completion of one million tonne capacity expansion project in Vanscoy, Saskatchewan in 2015, which is expected to ramp-up production volumes to full rates in 2017.[20] The project named VAULT (VAnscoy ULTimate Expansion) is expected to move Agrium's position from the 10th largest potash producer to the 8th largest.[21]

It can be inferred from Agrium's increasing sales and interest in investment in the Potash sector, that the company is pro-actively working on capacity expansion and is exploring possibilities of becoming a major exporter of potash globally. However, consolidation between Potash Corp. and Agrium would decrease global competition and eliminate a potential competitor in the potash market. Resultantly, the merger would strengthen Canpotex as an export cartel. It will also result in eliminating the possibility of Agrium exiting the cartel and acting as a global competitor.

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15 Potash Corporation of Saskatchewan Inc. SEC Filing 2015, 12 (2015), available at https://www.sec.gov/Archives/edgar/data/855931/000119312516480730/d137329d10k.htm#toc

16 Paul Waldie, *Canpotex and potash: The monopoly behind the mineral,* The Globe and the Mail, (2010), available at http://www.theglobeandmail.com/globe-investor/canpotex-and-potash-the-monopoly-behind-the-mineral/article1241076/?page=all

17 PIR available at http://www.cuts-ccier.org/pdf/CUTS_Preliminary_Information_Report_Submitted_to_CCI.pdf

18 Supra 12

19 Supra 7

20 Supra 11

21 http://potashworks.com/agrium-wholesale-expands-operations-at-vanscoy-mine/

Agrium has been known to be a company with most diverse business model in the industry of crop inputs and with Agrium's unique and globally competitive business model aimed at "Feeding a Growing World", the likelihood of it becoming a big player in the fertiliser segment (including potash) should not be ruled out.[22] For instance, Agrium acquired AWB, an Australian firm dealing in grain trade in 2010. However, Cargill Australia acquired the same from Agrium in 2011. Further, the retail business of Agrium, the Crop Production Services ("CPS") is on an acquisition spree of numerous locations in North America. All these reflect the diverse business plans of Agrium.

The point is that, Agrium being a potential maverick firm can choose to exit Canpotex export cartel and act independently of other shareholders. This is not a hypothetical scenario as something similar happened in 2013, when the Russian company Uralkali which grew into a major player in the potash market pulled out of the Belarusian Potash Company (BPC), a joint venture with Belarussian partner Belaruskali after reaching "deadlock" over sales.[23] This broke one of the two major potash cartels in the world and rendered Canpotex as the dominant export cartel.

The merger between Agrium and Potash Corp. obliterates the possibility of Agrium acting as an undisciplined member of the cartel and choosing to not partake in it. Concurrently, the merger increases the ability of the subsequent new entity (having only 2 entities) to control production and utilise capacities to the detriment of buyers. Notably, the global potash market is already oligopolistic, has substantial entry-barriers (i.e. economically mineable deposits are rare, capital costs are high and lead times are long), high levels of seller concentration (see statistics above) and has substantial product homogeneity.

Globally, further concentration in potash can reduce competition and make it easier for players (such as the merged entity) to peacefully coexist and unilaterally fix prices way above their production costs (non-coordinated effects) or even coordinate with other players to that end (coordinated effects). With further consolidation, the danger of market allocation (geographic market) amongst the exporters is also a risky possibility. Also, this could eventually result in reduction of the countervailing buyer power of Indian buyers as it makes easy for competitors to coordinate and turn off the supply spigot or levy export quotas if buyers try to gain the upper hand.

The aforementioned possible scenarios can result in being harmful to the Indian companies, the Indian government and most importantly Indian farmers who are the end consumers of fertilisers. Farmer associations abroad have already expressed their discomfort and stated that "When two manufacturers come together, there's less optionality of who to buy from, so the price point will probably be higher for them."[24] Hence, this merger demands scrutiny as it is bound to make price competition on the world market less likely, which can affect Indian markets in the form of coordinated prices, lower countervailing buyer power and increased supply power in the hands of the exporters.

[22] John Lawlor, *Agrium: Feeding The World, And Your Income,* available at https://seekingalpha.com/article/3968079-agrium-feeding-world-income
[23] Reuters, *Potash sector rocked as Russia's Uralkali quits cartel*, available at http://www.reuters.com/article/russia-uralkali-idUSL6N0G013H20130730
[24] Leslie Picker and Ian Austen, *Agrium and Potash Corp. to Merge, Creating Fertilizer Giant*, The New York Times, available at https://www.nytimes.com/2016/09/13/business/dealbook/agrium-and-potash-corp-to-merge-creating-fertilizer-giant.html?_r=0

Some of these arguments have been further elucidated in the points below:

Impact on countervailing buyer power

Competitive pressure on suppliers is not only exercised by competitors but can also come from its customers. It is important to consider to what extent customers will be in a position to counter the increase in market power that the merger would be likely to create. Form IV-443states that large purchasers in India exercise substantial buyer power that constrains prices and contract terms for the sale of potash to Indian customers. However, this statement requires the demonstration that after the merger, buyer power will remain sufficient to undermine attempts by sellers to increase prices.

Potash importers negotiate prices with global suppliers through annual contracts. There are a number of key potash importers in India, in particular Rashtriya Chemicals and Fertilizers Ltd, Indian Potash Ltd (IPL), Indian Farmers Fertilizers Cooperative Ltd (IFFCO), Chambal Fertilizers & Chemicals Ltd (CFCL), Tata Chemicals Ltd (TCL), Coromandel International Ltd (CIL) Zuari industries Ltd.[25] The bargaining strength that these buyers will have vis-à-vis suppliers in negotiations needs to be shown. It has already been pointed out by experts that the merged company would have more negotiating clout and supply discipline.[26]

The threat of curtailing supply is real. Potash companies, in 2016, made moves to cut costs and production, with PotashCorp shutting its recently opened Picadilly mine in New Brunswick and temporarily closing some Saskatchewan mines, while U.S.-based Mosaic Co. has closed its potash mine near Colonsay, Sask., until market conditions improve.[27]

India is one of the world's largest potash importers and is an important market for global Potash suppliers such as Canpotex. Notably, Canada is the largest supplier of Potash for India. In the month of November 2016, India exported $35 million worth of potash in a month from Canada alone, which amounted to 36.37 percent of India's total potash imports.[28] With the country relying on Canadian imports for meeting majority of its annual potash demand, there is a strong possibility that the proposed entity could threaten to increases prices, resulting in harm to the Indian buyers and the end consumers of fertilisers (i.e. the farmers). Hence, the increased commercial significance of the merged entity in the condensed global market, (even more post- than pre-merger) could considerably destabilise Indian companies' power to negotiate.

Furthermore, it needs to be taken into account that the countervailing buyer power may not be as effective in the long run as competition among the sellers in terms of preventing inefficiency and promoting product innovation and cost reduction for the end-consumer. Countervailing buyer power will not increase welfare if it results in negotiation failures and it might reduce incentives to innovate upstream.

[25] http://www.fert.nic.in/sites/default/files/documents/list_06122011.pdf
[26] http://saskatoon.ctvnews.ca/potashcorp-agrium-in-preliminary-merger-talks-to-create-agricultural-giant-1.3050249
[27]http://globalnews.ca/news/2911210/potashcorp-agrium-shares-halted-following-report-on-merger-talks/
[28] http://www.infodriveindia.com/india-import-data/potash-import-data.aspx

Need to weigh proposed efficiencies of the new entity with impact on supply of potash to India

With India's demand for fertiliser inputs (especially potash) on the rise, a steady and reasonably priced supply of potash would be an important consideration for Indian buyers as well as final consumers i.e. the farmer. Currently, the global potash market is working through a large supply overhang and prices are low, which is beneficial for import countries such as India.

However, the merged entity is poised to become one of the biggest providers of potash and it is important to understand and weigh the efficiency effects with the anti-competitive effects. The parties claim that it would create a diversified, low-cost wholesale supplier of fertilizers and retail supplier of agricultural products, services, and solutions to growers.[29]

On the other hand, the merger also poses negative effects, one of which is the grant of power to the entity to control supply at any given point in time.[30] With the strengthening of Canpotex as an export cartel, importing countries such as India are likely to face artificial supply constraints.

In this context, it is important to recognise that in order to justify a merger; the efficiencies must be greater than the potential adverse competitive effects. In addition, it must be determined that the efficiencies are passed through to consumers and that the merger does not have an anticompetitive effect in the relevant market.

In the present case, although it is apparent that the merger will reduce costs and increase margins, but the subsequent effect on export markets and end consumers is likely to be negative.[31] Given this, it is important to weigh this particular merger on an objective scale and test the claim of Agrium that Potash Corp. that the merger will not have an appreciable adverse effect on competition in India.

Question of control over Canpotex

The parties mention in Form IV-443 that post-merger, Canpotex would be controlled by the New Parent Company and Mosaic. But, the parties do not mention if (and how) the merger would affect the shareholding equity of Canpotex between the New Parent and Mosaic. They just vaguely indicate that the proposed combination will not affect Canpotex and contend that the export consortium operates independently of its shareholders/members. The claim of the parties that Canpotex acts independently of its shareholders should be tested. This is primarily because the control of the parties on Canpotex is real as one of the annual reports of Agrium states, "We have significant influence through our ability to appoint directors to the board of Canpotex".[32] This needs to be further investigated as consolidation of the shareholders poses a threat to the Indian fertiliser market.

CUTS Submission

In light of the aforementioned facts and arguments, it is submitted that while reviewing the proposed merger of Potash Corp. and Agrium the Commission should:

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[29] Form IV-443, p.2

[30] Jacob Donnelly, *Making Sense of the Agrium Inc./Potash Corporation of Saskatchewan Inc. Merger,* available at http://www.fool.ca/2016/10/19/making-sense-of-the-agrium-inc-potash-corporation-of-saskatchewan-inc-merger/

[31] India is one of the major markets that Canpotex caters to. See http://www.canpotex.com/who-we-are

[32] Supra 7, at 107

a. Conduct an in-depth competition analysis/merger review taking into account India's import dependence on potash and prevailing global cartels, including the parties to the merger;

b. Conduct the review by taking into account the 'maverick' nature of one party to the merger (i.e. Agrium);

c. Conduct the review keeping in mind above-discussed possible AAEC, particularly adverse effects on 'price' and 'supply' (timely and in adequate quantity) of potash, viewing the increased negotiating clout of the merged entity and its impact on countervailing buying power;

d. Pass any other order(s), that it deems fit in larger public interest, given the circumstances as illustrated in the above-stated facts and information.

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