Client Alert

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Glencore's Long March to Take Over Xstrata

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At long last, Glencore has overcome the final regulatory hurdle and secured the approval of China's Ministry of Commerce (**MOFCOM**) to acquire the 66 percent of Xstrata that it does not already own. But not before agreeing to part with one of the prized assets in Xstrata's portfolio, the Las Bambas copper project in Peru.

If no suitable buyer for Las Bambas is found by September 2014, Glencore will have to auction off one of its other copper assets of MOFCOM's choosing. To clinch MOFCOM's blessing of the deal Glencore also committed to continue offering long-term supply arrangements to sell copper concentrate to Chinese customers, as well as somewhat less stringent supply commitments on zinc and lead concentrates.

It has been a long road for Glencore and Xstrata who announced their plan to combine in February last year. They have had to navigate the merger review processes in several major jurisdictions, which can frustrate the most patient of company executives. Glencore's acquisition of Xstrata will unite one of the world's largest producers and traders of commodities and one of the largest mining companies globally – but at what price? It was no surprise that competition authorities in those countries and regions most affected would closely scrutinize the deal.

The transaction had to be approved by merger control authorities in Australia, China, the EU, South Africa and the US before the parties could close the deal. Australia was the first to give the green light. Having begun its review in April 2012, the Australian Competition and Consumer Commission (**ACCC**) approved the transaction in early July 2012. The ACCC cited the merged company's "relatively low share of global production" and the existence of several "remaining substantial competitors" post-transaction in concluding that any effect the deal may have on global markets would pose "minimal impact on Australian users of those products or end-consumers."

A few days after receiving the ACCC's blessing, the deal got antitrust clearance in the US, when the Department of Justice allowed the Hart-Scott-Rodino waiting period to expire without taking any action or seeking any type of remedy.

South Africa's review looked at the potential impact the deal has on the coal market, but the concessions required of the parties grew out of public interest considerations. While the Competition Commission of South Africa (**CCSA**) found the transaction raised no competition related concerns, it took issue with the companies' proposed dismissal of almost 200 employees post-merger. To win over the CCSA, the companies agreed to limit the dismissals to certain managerial and specialist roles and offer re-skilling training to certain employees subsequently laid off. Adopting the CCSA's recommendation, the Competition Tribunal approved the transaction in late January 2013.

If you have questions or comments about this Client Alert, please contact:

John Tivey
Global Head of Mining and Metals Industry Group
Partner, Hong Kong
T: + 852 2822 8779
M: + 852 6050 0225
jtivey@whitecase.com

Rebecca Campbell
Partner, London
T: + 44 20 7532 2315
M: + 44 79 1259 6131
rcampbell@whitecase.com

Patrick Ma
Counsel, Beijing
T: + 86 10 5912 9615
M: + 86 1590 119 7821
pma@whitecase.com

Beijing
White & Case LLP, Beijing Office
19th Floor, Tower 1 of China Central Place
81 Jianguo Lu, Chaoyang District
Beijing 100025
China
+ 86 10 5912 9600

Hong Kong
White & Case
9th Floor, Central Tower
28 Queen's Road Central
Hong Kong
+ 852 2822 8700

London
White & Case LLP
5 Old Broad Street
London EC2N 1DW
United Kingdom
+ 44 20 7532 1000

From the outset of pre-filing negotiations with the parties, which began shortly after the deal was announced, the European Commission focused its attention on the combined entity's power in the production and trading of zinc. Ultimately, the Commission required the divestment of Glencore's minority stake (7.8 percent) in and termination of its recently renewed exclusive off-take agreement with the world's largest zinc smelter, Nyrstar, originally due to run until 2018, as conditions to approving the transaction. As part of the deal with the Commission, struck in late November 2012, Glencore also committed not to enter into any other commercial arrangements with Nyrstar for ten years. The clearance came despite the concerns expressed by the European Steel Association (**EUROFER**), whose members purchase much of the commodity grade zinc traded in Europe for use as corrosion-resistant coatings (galvanizing) in steel products.

MOFCOM took its time in reviewing the transaction- almost twice the normal maximum statutory period allowed for merger reviews under China's Anti-Monopoly Law, which can last up to 180 days. As MOFCOM noted in its published decision, the parties withdrew their filing towards the end of the statutory review period, and then re-submitted the filing. This "pull and refile" effectively reset the clock on the review time line and provided MOFCOM with extra time to review the transaction.

It's to be expected and entirely legitimate for a country's competition authority to thoroughly examine a transaction that has potentially anticompetitive impacts on its industries and consumers, and to focus on such aspects of the transaction that pose the most threat to competition. Review of a complicated transaction takes time, and established merger review authorities do not rush to accommodate an overly aggressive closing schedule. However, reviews by MOFCOM have become so protracted that it routinely takes three months or longer, which often include a multi-week pre-acceptance period, for MOFCOM to reach an unconditional clearance decision even in straightforward cases with no substantive antitrust concerns. In cross-border deals where merger filings are required in multiple jurisdictions including China, MOFCOM is often the last antitrust regulator to reach a decision before the deal can close.

The conditions MOFCOM imposed in clearing the Glencore-Xstrata transaction confirm that the influence the merged entity could wield over the supply of copper concentrate to Chinese buyers is MOFCOM's overriding concern. Given that China is the world's leading consumer of copper concentrate, and that almost 70 percent of China's consumption in 2011 was imported, it is unsurprising that China is somewhat fixated on securing a stable and affordable supply of copper concentrate.

This is not the first time China has acted in response to activities of the major mining houses. In 2010, when BHP Billiton, Rio Tinto and Vale announced – all around the same time – their plans to change their iron ore pricing model from long-term contracts to shorter-term arrangements, MOFCOM promptly announced it would review the legality of the move. There were also accusations of state secret theft, which were subsequently downgraded to charges of industrial espionage and bribery, against Rio Tinto executives when they allegedly obtained certain internal information about Chinese steelmakers and their negotiation tactics for iron ore price negotiations. Such a backdrop naturally leads to observations that MOFCOM's mission as China's merger control enforcer is not driven by conventional antitrust principles, but rather anti-monopoly precepts with Chinese characteristics.

It will be interesting to watch how China's nascent merger control regime continues to evolve, and how MOFCOM asserts itself as an antitrust enforcer on the world stage.