Anticipated acquisition by Danone Holdings (UK) of Complan Foods Limited

ME/4950/11

The OFT's decision on reference under section 33(1) given on 8 June. Full text of decision published 21 June 2011.

Please note that the square brackets indicate figures or text which have been deleted or replaced in ranges at the request of the parties or third parties for reasons of commercial confidentiality.

PARTIES

1. **Danone Holdings (UK)** is part of Group Danone (jointly 'Danone'). Danone is an international manufacturer of food and beverage products. In the UK, Danone's subsidiary Nutricia manufactures and supplies medical nutrition products on prescription.

2. **Complan Foods Limited** (Complan) manufactures and supplies medical nutrition products. The majority of Complan's sales are made 'over the counter', but Complan also makes a limited quantity of sales through the supply of its prescription product Complan Shake. In the year to 31 July 2010, Complan's turnover in the UK was around £[ ] million.

TRANSACTION

3. Danone has agreed to acquire 100 per cent of the issued shares in Complan from its existing shareholders.

JURISDICTION

4. As a result of this transaction Danone and Complan will cease to be distinct. The parties overlap in the supply of enteral prescription medical nutrition products with a combined share of supply of around [45-55] per

cent. The share of supply test in section 23 of the Enterprise Act 2002 (the Act) is therefore met. The OFT therefore believes that it is or may be the case that arrangements are in progress or in contemplation which, if carried into effect, will result in the creation of a relevant merger situation.

5. The OFT's administrative deadline for a decision is 8 June 2011.

MARKET DEFINITION

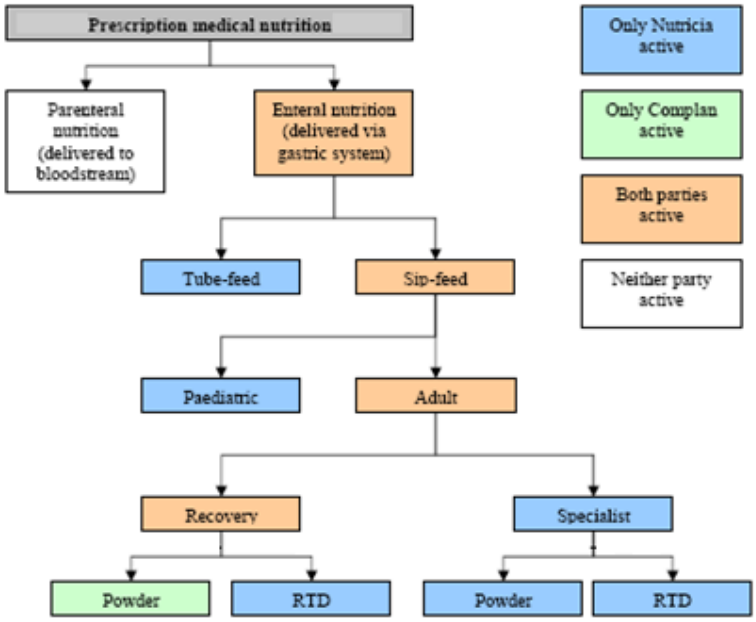
Product market

6. The parties are both active in the provision of enteral medical nutrition products. Enteral medical nutrition products are foods that are delivered via the gastric system (as opposed to parenteral products, which are delivered to the bloodstream) and are adapted to specific healthcare needs; for example, to prevent malnutrition, aid disease recovery for patients in hospitals or in the community, and to address the nutritional needs of consumers with particular medical conditions that preclude an ordinary diet. Complan supplies enteral medical nutrition products both 'over the counter' (OTC) and on prescription through the NHS, while Nutricia supplies only prescription products.

7. When selecting a candidate market, the OFT will include at least the substitute products (narrowly defined) of the merging parties.[1] Put differently, the starting point for market definition is the narrowest plausible market in which the parties' products overlap. In this case, the parties submitted that enteral prescription medical nutrition products should be further segmented based on product characteristics and other factors that affect a clinician's prescribing decision. These distinctions are between (i) tube-feed and sip-feed products, (ii) adult and paediatric products, (iii) powder based and ready-to-drink (RTD) products, and (iv) recovery-oriented and specialist products.

8. Nutricia supplies a recovery-oriented product in an RTD format (Fortisip) and specialist products in both powder based format (Scandishake) and RTD format (Calogen). The only prescription product supplied by Complan is a recovery-oriented product in a powder based format (Complan Shake). The diagram below shows the extent to which the parties' products overlap within these segments.

[1] *Merger Assessment Guidelines* (CC2 and OFT1254, September 2010), paragraph 5.2.11.



9. On the narrowest possible markets – the supply of recovery-oriented products in powder format, recovery-oriented products in RTD format, specialist products in powder format and specialist products in RTD format – the parties' products do not overlap. However, if the market is defined more widely, the parties' products do overlap. At its narrowest, their products overlap if the market includes specialist products in powder format and/or recovery-oriented products in RTD format, but overlap also exists if the market is defined more widely to include OTC products, parenteral products, tube-feed and paediatric products. The OFT has set out below whether it would be appropriate to consider any of these wider markets. The OFT has further set out below whether it would be appropriate to segment the market by distribution channel, in addition to a segmentation by product type.

Prescription and OTC products

10. The parties submitted that distinct product markets exist in the UK for enteral products sold under prescription and products sold OTC, based on two key differences between prescription and OTC products:

    i. products offered under prescription are subject to NHS approval and price regulation whereas products available OTC are not, and

    ii. the manner in which purchasing decisions are made differs significantly between prescription and OTC products.

11. The OFT's market testing confirmed the distinction between OTC and prescription markets for enteral medical nutrition products.[2] As there is no overlap between the parties' activities in the supply of OTC products, the OFT has not further considered OTC products.

Parenteral and enteral products

12. The European Commission (EC) concluded in its *Nestlé/Novartis* merger decision in 2007 that parenteral products are not in the same market as enteral products[3] and the OFT did not receive any evidence in its current investigation to suggest that this had changed. The OFT has therefore not further considered parenteral products.

Tube-feed and paediatric enteral prescription products

13. As noted above, two possible distinctions of enteral prescription products are between (i) tube-feed and sip-feed products and (ii) paediatric and adult nutrition products. The parties' activities only overlap in sip-feed products for adults. As neither the parties nor third parties suggested that it was appropriate to include tube-feed products and paediatric products in the relevant market and there was no indication that such inclusion would impact on the competitive assessment, the OFT has not further considered tube-feed products and paediatric products.

Powder based and RTD enteral prescription products

14. The parties submitted that it was appropriate to distinguish between powder based and RTD products because of functional differences in the preparation of the product by customers and substantial price differentials between the products, as well as differences in the manufacturing process. Third parties did note the difference in preparation for the two product types and the influence of this on their purchasing decisions. However, the majority of third parties considered that, for patients who could use either product, powder based and RTD products are close substitutes which they would consider switching between following a SSNIP.[4] In addition, an internal document submitted by the parties provides evidence of [ ].[5] The evidence therefore suggests that powder based products may be in

[2] See also the EC's decision in Case COMP/M.5476 *Pfizer/Wyeth*, 17 July 2009 (paragraph 18).
[3] Case COMP/M.4540 *Nestlé/Novartis*, 29 June 2007 (paragraph 23).
[4] A small but significant non-transitory increase in price (SSNIP), usually defined as 5 per cent – see *Merger Assessment Guidelines*, paragraphs 5.2.11-12.
[5] [ ].

sufficiently close competition to RTD products to put both in the same relevant market.

15. On this basis, the OFT considers that a market consisting of only powder based or RTD products would be too narrow and that it is appropriate to include both powder based and RTD enteral prescription products in the relevant market for the purposes of calculating market shares.[6]

Recovery-oriented and specialist enteral prescription products

16. The parties submitted that recovery-oriented and specialist products differ in their nutritional content, with recovery-oriented products containing a standard combination of nutrients for supplemental nutrition and recovery, and specialist products aimed at those with specific clinical needs or diseases such as cancer or diabetes. The parties submitted that this difference means it is appropriate to define separate markets. Third party responses were mixed on the substitutability of the two types of products. Some customers highlighted the price and nutritional differences between the products as evidence of separate markets, while others suggested that recovery-based and specialist products were to a significant extent interchangeable for many patients, with patient preference an important factor in the prescription.

17. In its *Nestlé/Novartis* merger decision, the EC found that although recovery-oriented and specialist products appeared to be substitutable for a majority of patients, the growing awareness of practitioners and the dynamics of innovation in specialist products spoke in favour of segmentation. However, the EC left the market definition in this respect open.[7]

18. Taking a cautious approach, the OFT has considered the parties' position in separate recovery-oriented and specialist product segments. Since the merger does not give rise to competition concerns on either basis, it was not necessary for the OFT to reach a conclusion on the exact scope of the relevant product market in this respect.

[6] See *Merger Assessment Guidelines*, paragraph 5.2.3: the OFT will not normally have regard to market share and concentration thresholds calculated on anything other than the narrowest market that satisfies the hypothetical monopolist test.
[7] Case COMP/M.4540 *Nestlé/Novartis*, 29 June 2007 (paragraph 34; the EC referred to the relevant products as 'standard' and 'speciality' products).

Different distribution channels

19. The parties submitted that prescription medical nutrition products are distributed through three channels, which differ in procurement process and prescribing methods:

    - hospital (acute) care, in which prescriptions are written by hospital clinicians and dispensed by the hospital pharmacy at a price determined in contracts between hospitals and suppliers
    - community care, in which prescriptions are written by patients' GPs and dispensed by pharmacies at a price ultimately set by government, and
    - home care, in which prescriptions are first written by hospital clinicians, then renewed by GPs and dispensed by suppliers at a price determined in contracts between hospitals and suppliers.

20. The parties submitted that segmentation of the market by channel is not necessary, because competition occurs across all three channels. In particular, they submitted that sales in the community care channel are linked to sales in the hospital care channel, as GPs often prescribe products that were prescribed to patients in hospital. The parties highlighted that there is cross-subsidisation between the hospital care and community care channels, as suppliers recognise the importance of hospitals prescribing their products in gaining follow-on community care sales. Third parties confirmed this cross-subsidisation, giving examples of identical products supplied to both channels at price differentials of over 100 per cent. Third parties did, however, suggest separate markets based on different distribution channels, although the majority of third parties only identified two channels: hospital care and community care, with home care included within one of these two channels. This segmentation by distribution channel is consistent with the market definition adopted by the EC in its *Nestlé/Novartis* merger decision.[8]

21. Taking a cautious approach, the OFT has considered the parties' position in the hospital care channel and the community care channel separately. However, since the merger does not give rise to competition concerns on any basis, it was not necessary for the OFT to reach a conclusion on the exact scope of the relevant product market in this respect.

[8] Case COMP/M.4540 *Nestlé/Novartis*, 29 June 2007 (paragraph 39; the EC referred to the hospital channel and the outpatient channel). The OFT notes that the EC's conclusion in this respect was primarily based on the national markets of France and Spain which were the focus of its assessment.

Geographic market

22. The parties submitted that the relevant geographic market in which to assess the transaction is national. This is consistent with the conclusions of the EC on the geographic market for the provision of medical nutrition products in its *Nestlé/Novartis* merger decision.[9] The OFT has received no evidence that the market is narrower or wider than national, and as such has examined the market for enteral prescription medical nutrition products on a national basis.

HORIZONTAL ISSUES

Hospital/acute care channel

23. With respect to the supply of enteral prescription medical nutrition products to acute care providers (hospitals), the parties submitted, and third parties confirmed, that competition takes place in the form of bidding for tenders for new contracts. The contracts to supply medical nutrition products to acute care providers were characterised by third parties as 'full service' and require the supply of a variety of types of medical nutrition products and various additional services such as the provision and servicing of pumps for tube-feed supply and the sponsorship of certain posts (for example, dieticians).

24. The parties submitted that Complan does not compete in the hospital care channel because it does not supply the full range of products typically requested in a tender.[10] This was broadly confirmed by third parties and there is no evidence of Complan competing on its own, or as part of a consortium, for contracts to supply medical nutrition products to acute care providers. As such the inclusion of this segment of the market for enteral medical nutrition products on prescription could not increase the prospect of a substantial lessening of competition (SLC) beyond that discussed below for the supply in the community care channel.

[9] Case COMP/M.4540 *Nestlé/Novartis*, 29 June 2007 (paragraph 54). As noted above, the EC's conclusion in this respect was primarily based on the national markets of France and Spain.
[10] The parties noted that Complan does submit single product tenders [ ].

Shares of supply in the community care channel

25. The parties provided share of supply data for the supply of medical nutrition products to community care providers based on multiple segmentations of the market. Consistent with its approach to market definition (see paragraph 7), the OFT first considered the segment in which the parties' overlap appears the most problematic: the supply of all powder based enteral medical nutrition products on prescription.[11] The shares of supply of the main suppliers are set out at Table 1.

Table 1: Shares of supply of all powder based enteral medical nutrition products on prescription to community care providers

Supplier	Value	Share
Nutricia	£[ ]	[30-40]%
Complan	£[ ]	[20-30]%
Merged entity	**£[ ]**	**[55-65]%**
Abbott	£[ ]	[5-15]%
Fresenius	£[ ]	[10-20]%
Nestlé	£[ ]	[0-10]%
Other	£[ ]	[5-15]%
Total	£[ ]	100%

Source: Parties' estimate based on IMS data on invoice sales value of community prescriptions.

26. The OFT notes that a share of [55-65] per cent with an increment of [20-30] per cent, as identified for the parties in Table 1, would normally give rise to cause for concern. However, as detailed above (see paragraph 15), the evidence indicates that RTD products should be included within any analysis of market shares.

27. The OFT therefore next considered the supply of all enteral medical nutrition products on prescription, consisting of both powder based and RTD products. The shares of supply of the main suppliers on this basis are set out at Table 2.

[11] The OFT notes that the parties do not overlap if the supply of powder based products is further segmented by standard and speciality products (see at paragraph 8 above).

Table 2: Shares of supply of all enteral medical nutrition products on prescription to community care providers

Supplier	Value	Share
Nutricia	£[ ]	[45-55]%
Complan	£[ ]	[0-10]%
Merged entity	**£[ ]**	**[45-55]%**
Abbott	£[ ]	[25-35]%
Fresenius	£[ ]	[0-10]%
Nestlé	£[ ]	[0-10]%
Other	£[ ]	[5-15]%
Total	£[ ]	100%

Source: Parties' estimate based on IMS data on invoice sales value of community prescriptions.

28. The OFT notes that, on this measure, Nutricia is the largest supplier of enteral medical nutrition products on prescription with a [45-55] per cent share, with Abbot the second largest at [25-35] per cent and Fresenius the third largest with [0-10] per cent share. Complan has only a very small share at [0-10] per cent. Therefore, while Nutricia is the largest supplier, the merger does not give rise to a significant increment in its share.

29. On a cautious basis, the OFT has also considered the parties' position in separate segments for recovery-oriented and specialist prescription medical nutrition products (see paragraph 18 above). While there would be no overlap between the parties in the supply of specialist products (see paragraph 8), for recovery-oriented products (in both powder based and RTD format), the shares of supply of the main suppliers are set out at Table 3.

Table 3: Shares of supply of recovery-oriented enteral medical nutrition products on prescription to community care providers

Supplier	Value	Share
Nutricia	£[ ]	[45-55]%
Complan	£[ ]	[0-10]%
Merged entity	**£[ ]**	**[45-55]%**
Abbott	£[ ]	[35-45]%
Fresenius	£[ ]	[0-10]%
Nestlé	£[ ]	[0-10]%
Total	£[ ]	100%

Source: Parties' estimate based on IMS data on invoice sales value of community prescriptions.

30. Table 3 shows that when recovery-oriented products are considered separately, there will be no significant increment in Nutricia's share of supply as a result of the merger, as applies also to the consideration of all products at Table 2 above.

Counterfactual

31. The above analysis is based on a comparison of the prospects for competition after the merger against the current conditions of competition. However, the OFT will assess a merger against an alternative counterfactual where, based on the evidence available to it, there is a realistic prospect of a counterfactual that is more competitive than the prevailing conditions.[12]

32. In this case, the parties noted that Complan is planning to launch a recovery-oriented medical nutrition product on prescription in RTD format (Complan Complete) to complement its existing powder based product in [ ]. This launch could increase the competitive constraint Complan imposes on Nutricia and as such forms the appropriate counterfactual.[13] One third party also highlighted Complan's planned launch of an RTD product.

33. The OFT reviewed internal documents from Complan on the planned launch of Complan Complete and found that Complan's targeted market share over the next four years is [ ] per cent. However, this is based on a market

[12] *Merger Assessment Guidelines*, paragraph 4.3.1ff.
[13] *Merger Assessment Guidelines*, paragraph 4.3.19.

size far below that shown above and [ ]. Therefore, while the OFT considers that the proposed entry of Complan Complete provides a realistic prospect of a counterfactual that is more competitive than the prevailing conditions, the OFT does not believe that the increase in competitive constraint placed on Nutricia by Complan is sufficient to give rise to concerns with respect to a realistic prospect of an SLC.

BARRIERS TO ENTRY AND EXPANSION

34. The parties submitted that barriers to entry into the provision of medical nutrition products are low. Third parties were mixed in their responses, highlighting the need to provide a range of medical nutrition products to compete for acute care contracts, while suggesting that adding an single product for a current competitor could be achieved at relatively low cost and within a short time frame.

35. The evidence from the parties on the planned entry of a Complan RTD medical nutrition product points towards low barriers to entry for a single product, with estimated costs of approximately £[ ] and entry within [ ] years.

36. However, it has not been necessary for the OFT to conclude on barriers to entry and expansion because the merger does not give rise to competition concerns.

THIRD PARTY VIEWS

37. Third party comments have been discussed above where relevant. The OFT received one complaint from a customer, but it placed only limited weight on this complaint as it was not substantiated by evidence and contained only a broad indication of the identity of the customer without including any contact details.

38. Other third parties raised no material competition concerns with respect to the merger. Third parties were mixed in their views as to whether the merging parties were close competitors, with one customer commenting that 'Complan is a 'one trick pony' and Nutricia is a provider of a wide range of products'. Third parties also highlighted the benefit of Complan Shake being available to acute care providers through incorporation in to the Nutricia range.

ASSESSMENT

39. The parties overlap in the supply of enteral medical nutrition products on prescription, with both parties supplying recovery-oriented products (Nutricia in RTD format and Complan in powder based format) and Nutricia also supplying specialist products (in both RTD and powder based formats). If the supply of powder based products is considered separately, the parties' combined share is high with a significant increment. However, the evidence obtained by the OFT indicates that this is too narrow a market segment and the merger is best considered on a wider basis that includes RTD products. On this basis, Nutricia is the largest supplier with a significant share of supply, but the increment from the merger is very small. This applies whether all enteral medical nutrition products on prescription are considered together or recovery-oriented products are considered separately.

40. The OFT notes that the appropriate counterfactual against which to assess the proposed transaction should include the proposed entry of a new RTD medical nutrition product by Complan [ ]. However, based on the evidence presented to the OFT, there appears to be no significant increase in competitive constraint from Complan on Nutricia in the counterfactual in comparison to the current conditions of competition.

41. No material third party concerns were raised with respect to the merger.

42. Consequently, the OFT does not believe that it is or may be the case that the merger may be expected to result in a substantial lessening of competition within a market or markets in the United Kingdom.

DECISION

43. This merger will therefore **not be referred** to the Competition Commission under section 33(1) of the Act.