

Completed acquisition by Bunzl Retail Supplies Limited of Southern Syringe Services Limited and Universal Hospital Supplies Limited

The OFT's decision on reference under section 22(1) given on 21 November 2006. Full text of decision published 5 December 2006.

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**Please note that square brackets indicate figures or texts which have been deleted at the request of the parties for reasons of commercial confidentiality.**

**PARTIES**

1. **Bunzl plc (Bunzl)** supplies a range of consumables into several customer sectors, including cleaning and hygiene products, through its UK subsidiary Bunzl Retail Supplies Limited.<sup>1</sup> Bunzl's trading division, Shermond, imports and supplies medical consumables<sup>2</sup> direct to the NHS and to distributors in the UK.
2. **Southern Syringe Services Limited (SSS)** is a distributor for medical and surgical products.<sup>3</sup> It supplies both hospital and non-hospital customers (such as nursing homes) throughout the UK. It also supplies some non-food consumables (predominantly cleaning and hygiene products) to the healthcare sector. SSS was, prior to the merger, ultimately controlled by John Denman and his family. They also controlled Universal Hospital Supplies Limited (UHS), which has also been acquired by Bunzl as part of this transaction. UHS exclusively sells a number of surgical and medical consumables to SSS.

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<sup>1</sup> Bunzl plc has requested that it is noted it also sells cleaning and hygiene products through a number of other subsidiaries.

<sup>2</sup> Including examination gloves, swabs, dressing packs, face masks, overshoes, tongue depressors.

<sup>3</sup> Such as those named in footnote 1 together with many others including mid-stream urine connection kits, oxygen and suction bubble tubing, sterile connecting tubing, kylls, bile bags.

3. The combined UK turnover of SSS in the financial year to 31 December 2005 was some £182 million.

## **TRANSACTION**

4. Bunzl completed the acquisition of SSS on 4 July 2006. The statutory deadline, as extended, expires on 21 November 2006, which is prior to the administrative deadline.

## **JURISDICTION**

5. As a result of this transaction, Bunzl and SSS have ceased to be distinct. The UK turnover of SSS exceeds £70 million, so the turnover test in section 23(1)(b) of the Enterprise Act 2002 (the Act) is satisfied. The OFT therefore believes that it is or may be the case that one or more relevant merger situations have been created.

## **FRAME OF REFERENCE**

6. The merging parties overlap in two areas. The first is the supply of cleaning and hygiene products to the healthcare sector, where both offer the same products and services. The second is the supply of medical consumables to the healthcare sector. In this area Bunzl's activities are limited to importing and selling medical consumables both direct to the NHS and to third party wholesalers/distributors, who resell to the healthcare sector. SSS manufactures, imports and wholesale/distributes its own and third party medical consumables direct to the healthcare sector. It also offers a logistics service that consists of storing and delivering medical consumables that healthcare customers have bought directly from the manufacturer or importer.

### **Supply of cleaning and hygiene products to the healthcare sector**

7. The merging parties both supply cleaning and hygiene products<sup>4</sup> to the healthcare sector. These products are not exclusive to this sector; Bunzl and its competitors also supply them to other customer sectors such as facilities management companies and catering providers.

8. Bunzl submits that due to supply side substitution, the frame of reference should include cleaning and hygiene product suppliers serving other sectors and companies supplying non-food consumables other than cleaning and hygiene products, as they could easily switch to start supplying such products to the healthcare sector. Third parties confirmed that post-merger they have a wide range of alternatives, including buying direct from the manufacturer or from suppliers not currently focused on the healthcare sector.
9. We also considered whether it was necessary to segment the supply of cleaning and hygiene products by product type. However, responses from third parties support the view that it is relatively easy for wholesale suppliers to add to their product range any of the cleaning and hygiene products supplied by the merging parties and/or for customers to source these products from alternative manufacturers or distributors.
10. Adopting a cautious approach, we then looked at the parties' estimate of their sales of cleaning and hygiene products to the healthcare sector in the UK; this gives them a post-merger share of [less than 15] per cent, with an increment of about one per cent.
11. Given the share of supply of the parties post-merger, the negligible increment, the number of remaining alternative suppliers and lack of concern by customers, we concluded that the merger does not give rise to any competition concerns with regard to this segment and have not considered it further.

## Supply of medical consumables to the healthcare sector

### By route to customer

12. Customers in the healthcare sector may obtain medical consumables through two basic routes: (i) directly from manufacturers or importers of these products, (ii) from wholesaler/distributors. As noted the parties only overlap in relation to the importer route. It was therefore necessary to consider whether the different routes constrain each other.

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<sup>4</sup> The products include refuse sacks, washroom cleaners, wipers and surface cleaners, industrial skin care and many other janitorial items.

13. The question of whether direct purchase from manufacturers or importers and distribution by wholesalers should be considered to be in the same product scope was considered by the OFT in the SSS/HMS merger decision of January 2005.<sup>5</sup>
14. In that case, the OFT acknowledged that there may be advantages for customers in obtaining their supplies through a wholesaler/distributor, such as having a single source for a range of products or, for customers with limited storage facilities, not having to store bulk purchases. However, the availability of logistics providers meant that direct purchase routes could still constrain the ability of wholesaler/distributors to raise prices as direct purchase was an option for at least some customers.
15. We have not obtained any evidence in the current case that would lead us to deviate from this conclusion. A number of the manufacturers and customers (including nationwide private hospital chains) we consulted in this case told us that they already obtain a significant proportion of their medical supplies directly from manufacturers and would be able to increase this. Moreover, while a minority of customers were concerned that they lacked adequate storage facilities or an in-house distribution system, several customers and manufacturers confirmed that there are several logistic providers able to meet these customers' needs. Furthermore, as the products in question are not perishable, on the face of the evidence before it, the OFT believes that end-consumers could improve their stocking system in order to switch to contract distribution in the event of a price rise by the merged entity. Some private hospitals have already done this in order to reduce their procurement costs.
16. In this case, although the overlap is only as an importer, we have considered a wider frame of reference to assess the horizontal impact of this merger under the assumption that Bunzl was constrained pre-merger by the ability of SSS to supply the healthcare sector as a manufacturer, importer and wholesaler/distributor. As such the product scope includes both direct supply by importers and/or manufacturers and wholesale supply.

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<sup>5</sup> OFT decision of 24 January 2005 on the completed acquisition by Southern Syringe Services Limited of Hospital Management and Supplies Limited. See at: [www.offt.gov.uk/Business/Mergers+EA02/Decisions/Clearances+and+referrals/Southern+Syringe.htm](http://www.offt.gov.uk/Business/Mergers+EA02/Decisions/Clearances+and+referrals/Southern+Syringe.htm)

## By customer segmentation

17. In the SSS/HMS merger decision,<sup>6</sup> the OFT segmented the market by customer groups given the different needs and competitive constraints faced by suppliers to each group. The customers were considered to fall into three groups: (i) NHS hospitals; (ii) private hospitals; and (iii) non-hospital customers.
18. Since the OFT cleared the SSS/HMS merger in January 2005, there have been material changes which may have altered the relevance of this segmentation by customer groups. Most significantly the volume restriction on NHS Supply Chain (formerly NHS Logistic) supplying non-NHS customers has been removed,<sup>7</sup> thus allowing them to exercise at least a potential constraint on the merged entity.
19. In the SSS/HMS merger decision, the main reason for having a separate segment for private hospital customers was their ability to procure products direct from manufacturers. It was argued that direct supply was not an option for private hospitals given that some private hospitals procure smaller volumes than those delivered directly by manufacturers (which would normally meet the regular bigger demand of an NHS hospital) . This issue was also raised by a third party on this case and is discussed above at paragraph 15.
20. It is not necessary to reach a definitive conclusion on this customer segmentation in this case due to the lack of substantive competition issues arising even in these narrow frames of reference. The OFT has nevertheless assessed the competitive situation in the segments for NHS hospital customers, private hospitals and non-hospital customers for completeness.

## Geographic scope

21. In the supply of medical consumable products to NHS hospitals, there may be separate geographic frames of reference for England, Wales, Scotland and Northern Ireland. The provision of logistic services as part of the centralised procurement process is a distinctive characteristic traditionally

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<sup>6</sup> Ibid, paragraph 15.

<sup>7</sup> Under its former Framework Agreement, NHS Chain Supply was restricted to supply 5 per cent at most of its total turnover to non-NHS customers.

only existing in England and Wales (through NHS Supply Chain). Now, Central Services Agency Regional Supplies Service provides similar logistic services in Northern Ireland, and Scottish Healthcare Supplies has announced that it will be implementing a new Scotland-wide logistic strategy. As this merger does not raise competition concerns regarding supply to NHS-hospital customers, no conclusion on this issue is necessary in this case.

22. The private hospital (such as BUPA and Nuffield Healthcare) and non-hospital customers (such as BUPA nursing homes) that operate nationally and have centralised procurement require suppliers with national coverage. While customers that operate in a particular region require only regional supply, this is not considered by the OFT to be sufficient in itself to conclude that the geographic market is regional. We have therefore assessed the effect of the merger in the UK taking into account sub-national considerations where relevant.

## **HORIZONTAL ISSUES**

23. The merger does not substantially alter the current position of the parties in the supply of medical consumables at the horizontal level. The OFT obtained the parties' estimates for the supply of each individual product line separately to NHS hospitals, private hospital and non-hospital customers where this exceeded 25 per cent. Where the parties overlapped in any of these products<sup>8</sup>, the increment was less than five per cent and there remain various other sizeable manufacturers, importers and distributors.
24. Customers did not raise horizontal competition concerns. Responses from NHS contracting agencies in England, Wales, Scotland and Northern Ireland, who are Bunzl's main customers, confirmed the lack of competition concerns in this segment. In addition, non-hospital customers confirmed that there are more alternatives for this group than others as they require fewer products and can also use regional and local distributors. We do not therefore expect this merger to affect competition on horizontal level in the supply of medical consumables to the healthcare sector in the UK.

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<sup>8</sup> Out of a range of hundreds of products, these overlaps relate only to four products: examination gloves, overshoes, face masks and tongue depressors.

## VERTICAL ISSUES

25. Some third parties expressed concerns that Bunzl, as an importer, would foreclose distribution via SSS to rival manufacturers and importers and that, as a result, rivals would face increased distribution costs and end customers would have to multi-source to obtain the full range of products they required. This concern arises as a result of SSS's strong position in the supply of medical consumables to the healthcare sector. It is notable, however, that the majority of manufacturers and customers contacted were not concerned by this merger.
26. The OFT Substantive Assessment Guidance provides that vertical mergers are often efficiency-enhancing. Nevertheless, they may give rise to competition concerns in certain cases where market power exists or is created in at least one market in the supply chain. Even if market power exists, a proper analysis of both the ability and incentive of the merged firm to engage in the strategy described above must be conducted. Both must be present for such a strategy to be profitable (successful) and to establish vertical concerns as well-founded.<sup>9</sup>
27. As discussed under Horizontal Issues, the merger does not substantially increase SSS's market power downstream in the supply of medical consumables. Thus, we do not expect this merger to increase SSS's ability to foreclose rivals.
28. A consequence of the merger is that SSS's range of own-brand products will increase so that if it already had the ability and incentive to foreclose rivals manufacturers and/or importers, this would be extended to any new product line added to this range as a result of the merger. We note, however, that Bunzl supplies only approximately two per cent of the product lines SSS distributes. Therefore, any prospect of vertical foreclosure would not increase materially and would not be extended for the significant majority of the medical consumables the merged entity supplies. In any event, we do not consider that SSS does have the ability to foreclose access by other manufacturers to end-customers. This is explained further below.

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<sup>9</sup> Substantive Assessment Guidance, May 2003 at paragraphs 5.1 and 5.4.

29. SSS's ability to foreclose is constrained by the availability of several other routes to market to wholesalers of medical consumables for manufacturers, importers and end-customers, including the new possibility of the NHS Supply Chain for private hospital and non-hospital customers.
30. The fact that customers can, and a number already do, obtain their supplies through other means suggests that it would not be in the merged entity's interest to stop supplying competing brands or to discriminate against these brands. If enough customers can switch to these other sources of supply, rather than be forced to buy the merged entity's own-brand products. Bunzl would simply forgo the margins it could have made from the distribution of these rival products without any significant gains in terms of sales of its own-brand products. In addition, we noted that [ ].
31. In conclusion, we do not expect that this merger will result in the merging parties having the ability or incentive to foreclose competitors in the supply of medical consumables and access to end-customers.

### **THIRD PARTY COMMENTS**

32. We contacted a large number of third parties in the assessment of this case. The vast majority either did not respond or raise concerns. A small number of competition concerns were raised and these are addressed in the above assessment.

### **ASSESSMENT**

33. The merging parties overlap in supply of cleaning and hygiene products into the healthcare sector. Post merger they supply [less than 15] per cent<sup>10</sup> (increment one per cent) nationally, they face sizeable alternative suppliers and the merger has not generated third party concern. Therefore the merger does not give rise to any competition concerns with regard to this segment.
34. The parties also overlap in the supply of medical consumables to the healthcare sector. This has been considered in relation to several routes to the end customer (direct from the importer or manufacturer and via wholesaler/distributor) and types of end-customer (NHS hospitals, private

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<sup>10</sup> Bunzl has requested that it is noted this share of supply is estimated. See paragraph 10 above.



hospitals and non-hospital customers). On this basis, the merger represents only minimal increments (below 5 per cent) to the parties' existing shares of supply in a small number of products. Customers contacted by us in this inquiry had no horizontal competition concerns. Thus, we do not expect this merger to reduce competition on horizontal level in the supply of medical consumables to the healthcare sector in the UK.

35. Three third parties were concerned about the vertical effects of the merger between Bunzl and SSS. On the available evidence, the OFT has concluded that the merged entity will not have the ability or incentive to foreclose the route to market to other manufacturers or importers of medical consumables. This is because: (i) there are alternative routes to market; (ii) Bunzl's range of products is such a small proportion of that distributed by SSS that any increase in incentive is immaterial; and (iii) the fact that customers can, and some already do, obtain their supplies through routes other than SSS suggests that it would not be in the merged entity's interests to cease supplying rival products.
36. 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**

37. This merger will therefore not be referred to the Competition Commission under section 22(1) of the Act.