

Mr. Martin Coleman  
Competition and Markets Authority

20<sup>th</sup> May 2025

Dear Mr. Coleman,

I fear the inquiry into the functioning of the pet-care industry in the United Kingdom, while obviously noble in its main objective of consumer protection, is based on a fragile premise whose logical implications not only impede individual enterprise, but also undermine this Government's ambition to foster an environment which attracts business investment and global capital. Some of the CMA's mooted interventions are likely to dis-improve some consumer outcomes and sufficient weight should be applied to these potential negative consequences in the final analysis.

One can only conclude, upon reading the May 1<sup>st</sup> 2025 working paper, the CMA is conducting its investigation based largely on its original<sup>i</sup> premise that businesses (across an industry) earning returns above the cost of capital is indicative of competitive dysfunction which is unfair to consumers. There is a major problem with intervening in markets according to that philosophy: the law of economic gravity - that fair competition will inevitably lead to returns on invested capital declining to levels which just, and no more, satisfy its cost - is *absolutely not* universal. This is amply demonstrated by empirical evidence over reasonable time-frames.<sup>ii</sup>

I believe there is 'something' associated with pet-care that manifests in industry profitability *persistently* above the cost of its required real capital. The 'law' of economic gravity is a law in the sense of Newton, rather than Einstein. It applies less well the further the economic output provided is from a commodity good or service. After all, the definition of a commodity is that its price will equilibrate to its marginal cost at the marginal level of demand. When prices of goods or services do not reflect the marginal cost to provide them there is something else going on (assuming we can exclude price fixing, etc.).

Consider, as contrasting examples, the property & casualty insurance industry and the skincare product industry. Profitability for the insurance industry just about satisfies the costs of its necessary capital over-time, whereas the skin-care industry earns profits far above those commensurate with the capital investment required to generate them. One could not, and should not, conclude from this that the insurance industry is fairer on consumers than the skin-care industry, or that the skin-care industry was competitively dysfunctional. Each industry simply has different intrinsic characteristics which manifest in different return-on-capital profiles.

Another illustrative comparison might be (private) dental-care and landscaping services. The price the consumer pays for dental-care is well above, after deducting the pay of the dentist and nurse, the capital cost of the equipment utilized. The price a consumer would pay for landscaping services would much more closely reflect the cost of the equipment and the charges for labour. In the case of dental care, and indeed skincare, and many other industries<sup>iii</sup> the consumer is implicitly paying for something for which no accounting cost is apparent. As Einstein reportedly quipped, not everything that counts can be

counted. A thorough exposition of what exactly that 'something' is, is beyond the scope of this letter, but it is undeniably there.

Returning the argument to the world of pets in the UK: ask the vets who have started their own practice, and perhaps expanded to several practices, what exactly was required to build up a customer list of pet-owners who trust the health of the non-human members of their family to those vets and his/her colleagues. I daresay the requirement was a sustained period of ingenuity, business acumen, long hours and sweat, tears and perhaps even some blood - drawn by the errant paw or two - on top of the necessary investment capital. This build-up of intangible capital has been quantified by the prices buyers have been willing to pay these entrepreneurs for their businesses. It shouldn't be so blithely dismissed in the return-on-capital analysis to test for competitive dysfunction.

A veterinary entrepreneur is no more deserving of economic success than a landscape gardener but, from the perspective of capital value, they have simply picked a better sandbox to build in. The key point is that it is the nature of the economic utility consumed which dictates whether, at an aggregate or industry level, business value above its required real capital is possible.

Now, the CMA may concede on this initial point but argue that the benefits of consumer protection would more than justify the costs of acting to ensure industry wide compliance with the admittedly flawed 'fair-market' constraint of profits, just, attaining real capital costs. I would stoutly disagree - as follows.

Assuming the UK vet-care industry generates revenues of approximately £6bn per-annum, acting to reduce, for example, medicine prices such that industry profits just attain the cost of necessary capital would probably, as a rough guess, give an additional £600 million pounds per-annum to about 16 million pet-owning households in the UK.

Consider the potential downsides<sup>iv</sup> of this annual bonus of £38 pounds to half the UK's households:

- I have heard anecdotally from objective industry participants that the standards of care for UK pets are of the very highest level in a global context. These standards are made possible by an innovative and well-trained workforce of vets utilizing modern equipment that is funded by practice income. Reducing practice income will inevitably put a squeeze on the spend which has been, until now, responsible for delivering ever increasing standards of care. It would not, I suspect, be long before those standards drop. It is difficult to predict, a priori, the impact of this negative consumer outcome.
- It would be rational for owners of veterinary practices to reduce or defer investment (which has to some extent already happened) in equipment or leasehold improvements in response to such CMA measures. Acting to constrain investment which would otherwise support jobs around the UK is not in the best interest of the consumer.
- It should be obvious that such a CMA measure would dramatically reduce the capital value of a typical individual veterinary practice. This badly damages the incentive for entrepreneurship. For a dramatically diminished potential prize, would all the sweat, tears (and maybe blood) be worth it?

This would in the medium-term, at best, constrain competitive vet-care capacity in the UK – with implications on consumer choice.

- I believe the Government and thus the CMA should be weary of setting a precedent incompatible with the UK being an attractive environment for global capital in the outcome of this investigation. Significantly reducing the profitability of the industry would impair both equity capital and, probably, debt associated with some of the large corporate groups. This precedent would surely discourage future in-bound investment. In an increasingly volatile global economic backdrop, the UK should be doing all it can to sell itself as a safe harbour for long-term investment, rather than further debilitating its already frail capital markets. I believe I can confidently say the UK pet-owner, who is at the end of the day just part of the wider consumer population which relies on a robust job market for its disposable earnings, will not be well served by a short-sighted, if well-meaning, intervention by the CMA to boost their net income.

In a recent speech to the BSAVA Congress, you (as Inquiry Chair) pointed out the significant mark-up on medicines, and the dispersion of prices for the same medicine in various channels.

I think the argument, which I note has been submitted by several industry participants, that medicine prices *can not* be viewed exclusively from other services, is a robust one. There are *no* potential offsets in the vet-care cost structure to the impact of a reduction in the profits generated from medicines. Clearly the industry would dutifully attempt to raise the prices at which vet-time is charged to consumers, to recover any shortfall. Assuming they were (largely) successful, what benefit would the intervention on medicine pricing have had?

I also should point out that a substantial part of the medicine mark-up has been made possible because of the consolidation of the industry by the large corporate groups. The consolidators have wielded their increased buying power in negotiations with medicine suppliers to secure lower prices. Imagine a world in which there had been no consolidation in the UK vet-care industry: do you believe that medicine prices would be lower (to consumers) in that scenario? I think not. The mark-up would certainly be lower, but does that mean fairer consumer treatment? This hypothetical context should contribute to your considerations on the implications of the mark-up on medicine.

Price dispersion is widespread throughout the consumer economy. The next time you buy lip balm and sun cream as you rush to your airport gate ask yourself how much you could have saved by shopping around in advance of the trip. To be fair, there is an element of need, rather than choice, which is usually associated with a trip to the vet. You may argue this differentiates vet-care and justifies an intervention. Should we then act to ensure no differentiated (i.e. higher) prices for emergency plumbing services, or a locksmith's call-out charge after midnight. If yes, where would we stop in the quest to ensure the prices for a product are always and everywhere equivalent? While I certainly agree it can be extremely frustrating to pay higher prices for things that would, at another time or in another place, be less expensive, it is a feature of our economic system, not a bug, and certainly not indicative of unfair competition.

I think it is important that consumers, *especially* in times of distress, can make informed choices. What sense would there be, for the sake of short-term profits, of turning off a pet-parent from the notion of owning a pet again if they feel particularly aggrieved by opacity during a moment of pet-health distress? This brings me back to the nobility of the CMA's mission - which I do recognize. I applaud the CMA's focus on transparency as a veritable win, win, win – it is in the interest of pets, their owners and the long-term health of the industry. I also commend you for the measured and careful approach of the CMA as it conducts its investigation, which was especially evident in the recent working paper.

I am not an objective observer in all of this: I manage a US investment partnership which owns shares of CVS Group Plc. I know, only too well, how difficult it is to process an opinion piece without prejudice. I thus waited until the end to reveal the author's incentives in the hope you might read the foregoing with as little bias as possible. However, there is no shame for me in noting my partners and I are aligned to an investigation outcome which would not impede future capital formation, business investment or a healthy jobs market in the UK. I appeal to the authority to put sufficient weight, in its final deliberations, on the negative eventual consequences on the consumer of an outcome particularly unfriendly to business.

Yours sincerely,



Patrick McNulty

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<sup>i</sup> As expounded in Section 4 of the November 2024 Working Paper: Approach to profitability and financial analysis

<sup>ii</sup> Empirical evidence for its failure has been aggregated in the following paper: <https://www.analysisgroup.com/globalassets/insights/publishing/2020-challenges-of-using-return-on-capital-as-an-indicator-of-monopoly-power.pdf>

<sup>iii</sup> Industries which tend to exhibit returns on necessary capital far above the cost of capital include freight forwarding, branded consumer goods, exhibition organizers, two- and three-sided digital marketplaces, academic journal publishing, asset management, vertical software, fragrance and perfumery manufacturers, etc.

<sup>iv</sup> I note the consideration by the CMA of unintended and derivative consequences of potential interventions in the working paper and applaud it. From a process perspective, it is important that sufficient weight is placed on these (and other) potential negative consequences in the analysis, as opposed to a perfunctory mention.