

Omnicell/SurgiChem merger inquiry

Provisional findings report

Notified: 11 July 2014

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The Competition and Markets Authority has excluded from this published version of the provisional findings report information which the inquiry group considers should be excluded having regard to the three considerations set out in section 244 of the Enterprise Act 2002 (specified information: considerations relevant to disclosure). The omissions are indicated by [✂]. Some numbers have been replaced by a range. These are shown in square brackets.

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Glossary

Summary

Background

1. On 14 March 2014, the Office of Fair Trading (OFT) referred the anticipated acquisition by Omnicell, Inc (Omnicell)/MTS Medication Technologies, Inc (MTS) of SurgiChem Limited (SurgiChem) to the Competition Commission (CC) for investigation and report. On 1 April 2014, the CC joined with the competition function, and certain consumer functions of the OFT, to form the Competition and Markets Authority (CMA) which continued with this inquiry. The CMA must decide:
 - (a) whether arrangements are in progress or in contemplation which, if carried into effect, will result in the creation of a relevant merger situation; and
 - (b) if so, whether the creation of that situation may be expected to result in a substantial lessening of competition (SLC) within any market or markets in the UK for goods or services.
2. This document sets out the provisional findings of our inquiry based on the evidence we have reviewed and the analysis we have carried out to date.
3. Omnicell/MTS and SurgiChem (together referred to below as ‘the parties’) currently overlap in the supply of adherence packaging, accessories and support products for adherence packaging (such as labels, spare seals and ring binders). Adherence packaging products are used by pharmacists to repackage a patient’s medicines, in order to help patients to take the correct dosages at the correct time.
4. The parties also overlap in the market for the supply of trolleys and cabinets used for storage of adherence packaging and potentially overlap in the supply of automated filling machines for single-dose blister adherence packaging.
5. We provisionally concluded that: the anticipated acquisition of SurgiChem by Omnicell/MTS would result in the enterprises conducted by the two parties ceasing to be distinct; and, the merger would result in an increased share of supply of greater than one-quarter for adherence packaging in the UK by value. The CMA therefore has jurisdiction to consider whether the creation of that situation has resulted or may be expected to result in an SLC within any market or markets in the UK for goods or services.
6. We considered the situation that would have prevailed absent the anticipated acquisition (the counterfactual). We have concluded that, absent the merger, Omnicell/MTS and SurgiChem would continue to compete independently

(whether SurgiChem is owned by Bupa or another person). We have also found that it is likely that, absent the merger, SurgiChem would have introduced a new automated filling machine and begun offering card-based adherence packaging to pharmacies thereby increasing customer choice in both areas of the market. Accordingly, the counterfactual includes both of these likely developments.

7. We concluded that the relevant markets within which to assess the competitive effects of the merger are:
 - (a) The market for the supply of disposable adherence packaging, related accessories and support products. This includes both disposable card-based adherence packaging products (as supplied by Omnicell/MTS) and disposable plastic-based adherence packaging products (as supplied by SurgiChem). It includes both the single-dose products usually used for patients in care homes and multidose products usually used for domiciliary patients. It also includes semi-disposable systems, and systems suitable for liquids. It excludes plastic pouches (an alternative to card-based and plastic-based adherence packaging more commonly used in mainland Europe). It also excludes reusable adherence packaging.
 - (b) The market for storage facilities, such as trolleys and cabinets.
 - (c) The market for automated filling machines for single-dose packaging.
8. We found the relevant geographic market for the assessment of the merger to be the UK.

Competitive effects

Nature of competition pre-merger in adherence packaging

9. Pharmacists, with the exception of those purchasing multidose packaging through the NHS Scotland framework agreement, must meet the cost of the adherence packaging that they buy themselves. There are a number of factors that pharmacists may consider when making their buying decisions, including: price, the quality of the product, ease of filling and checking the packaging, security of supply and the level of service from the supplier. We have found that there are some differences in the weight that different types of pharmacist put on these factors.
10. We have identified three large customers that buy adherence packaging through tenders, with the prices that these customers pay set during the tender process. Other pharmacists tend to buy adherence packaging either through a wholesaler, a buying group or, most often, directly from an

adherence packaging supplier. We found that some non-tender customers pay a list price, while other customers negotiate different levels of discounts from the list price.

11. We found that barriers to switching in the market are low. We found that tender customers are relatively price sensitive. Among non-tender customers we found that, while some customers are price sensitive, low levels of switching in this segment of the market suggests that many others do not appear to be. Adherence packaging typically accounts for a small proportion of purchases by pharmacists so the incentives for them to actively engage with this market are often limited. Many pharmacists have little knowledge of alternative products and their prices, which reduces the extent to which they have responded or would respond to price increases or put pressure on their current supplier to reduce prices.
12. We opted to assess competitive effects in three segments of the market:
 - (a) adherence packaging procured through formal competitive tenders;
 - (b) non-tender procurement of adherence packaging for care homes; and
 - (c) non-tender procurement of adherence packaging for domiciliary users.

Assessment of competitive effects of the merger on the adherence packaging market

13. We found that SurgiChem does not currently compete in the tender segment of the market, nor, in our judgement, is it likely to become a competitive constraint on Omnicell/MTS within a reasonable period. As a result, we did not think that the merger would lead to a reduction in competitive rivalry in this segment.
14. We identified some evidence to suggest that the parties are not competing across the entire non-tender segment of the market as closely as their market shares might suggest. The two products are differentiated – being made, in part, from different material. We identified some differences in the sizes of customers that the parties have been successful in winning. There are also differences in the way that the parties structure their supply chains and in their routes to market. Further, evidence from our survey, questionnaires and third party hearings indicated that a significant proportion of non-tender customers did not consider the parties to be competing closely – in particular, a significant proportion have a strong preference for either a card-based or a plastic-based product.

15. Nevertheless, we found that the parties do compete closely for a significant proportion of non-tender customers, and that there is potential for the anticipated merger to lessen competition for these customers. Responses to our survey, questionnaires and third party hearings identified a significant proportion of non-tender customers who consider the parties to be competing closely. References in the parties' internal documents also suggest that they consider each other to be close competitors, at least for some non-tender customers. Further, SurgiChem's recent development of a card-based product suggests that it intends to compete with Omnicell/MTS for non-tender customers that currently use card-based adherence packaging.
16. We considered the strength of other competitors to the parties in the non-tender domiciliary segment. We found that Venalink, an established player with an incentive to grow its market share in the non-tender segment of the market, would act as a credible competitive constraint on the merged entity in this segment. We also found that Shantys had emerged as another credible constraint, although we note that Shantys' current marketing approach, selling through wholesalers, may not currently enable it easily to reach customers that prefer to buy their adherence packaging directly from a supplier. We considered that there is some doubt as to whether pouch-based systems are a significant competitive constraint, given the upfront expense for the pharmacy in putting in place the system. However, we also note that a small number of pharmacies that use adherence packaging more frequently consider that the solution is cost-effective overall. We have, therefore, found that there are at least two competitors to the parties in the domiciliary segment of the market that would constitute significant competitive constraints on the merged entity.
17. We considered the strength of competitors other than the parties in the non-tender care-homes segment of the market. We considered that Venalink, for the reasons discussed above, was a credible competitive constraint on the merged entity in the care homes segment of the market. Manrex is also an established long-term competitor in this segment of the market. While, its product is only available to pharmacists, other than Boots, through one wholesaler, this has not prevented Manrex from establishing a significant share of the care-home segment. We also considered the competitive constraint offered by Protomed, which has grown very successfully in recent years. The product is significantly more expensive than the parties' products on a per-pack basis, although we also note that as a multidose product it could be used in place of more than one of the parties' single-dose products in a care-home context. We concluded that Protomed may have a limited constraint on the merged entity's prices. We considered that, in the same way as in the non-tender domiciliary segment, there is uncertainty over whether

pouches could be a credible constraint in the non-tender care-home sector. We therefore identified three established rivals to the parties in the care homes segment of the market. Two are likely to be significant competitive constraints, whereas the likelihood of Protomed constraining the parties' prices is lower.

18. We found that there had been a number of examples of recent entry and that barriers to entry and expansion were fairly low. The most significant barrier is to persuade customers, some of whom we have found not to be particularly engaged, to switch to a new supplier. We also noted that if the merging parties were to attempt to increase their prices materially following the merger, this barrier might be reduced as we would expect there to be a greater willingness among customers to switch suppliers in such circumstances.
19. We considered whether entry and/or expansion would be likely to act as a timely, likely and sufficient constraint on the merged entity. We found that entry, particularly from overseas suppliers, could be achieved on a timely basis, as could the expansion of an existing player. We found that there was a reasonably high likelihood of entry and/or expansion into the market, based on both the recent history of entry and expansion in the market and on our findings on the intentions of Dexapack to enter the UK market in 2014 and the stated intention of a number of existing suppliers to expand. We considered whether any of the firms that have the intention to enter or expand are likely to become a sufficient additional constraint within a reasonable time period. We found that there is a material likelihood that at least one would and that the collective impact of their attempts may also act as a constraint on the parties.

Provisional conclusion on competitive effects of the merger in the adherence packaging market

20. We found that SurgiChem and Omnicell/MTS compete closely for a significant proportion of non-tender customers and that the merger could therefore lead to a reduction in competitive rivalry. However, we found that there are existing players in the market that will offer significant constraints on the merged entity in both the non-tender care-home and non-tender domiciliary segments of the market. Our findings on the potential for entry and expansion provide us with additional indications that the parties could be constrained further within a reasonable period. Taken together this evidence on existing constraints and further potential for entry and expansion leads us provisionally to conclude that the merger is unlikely to result in an SLC in the adherence packaging market.

Provisional conclusion on competitive effects of the merger in the automated adherence packaging filling machines market

21. We considered the extent to which the merger was likely to affect significantly the outcomes for customers in the market for automated adherence packaging filling machines.
22. We found that Omnicell/MTS's single-dose automated filling machine and the one that SurgiChem has developed are different in terms of cost and speed, with SurgiChem's machine likely to be significantly more expensive and faster than the Omnicell/MTS's machine. This indicates that there are unlikely to be many circumstances in which the two products could both fulfil a particular customer's requirements. We have also found that, in circumstances where customers could choose between the two machines, there are a number of other automated or semi-automated solutions for filling adherence packaging available. We have found that these include bespoke machines that are available from other suppliers (eg Ilseemann, Uhlman, TEG), and pouch-based systems. These other providers are likely to provide a sufficient competitive constraint on the parties in terms of semi-automated or automated solutions to pharmacies in the UK.
23. We also note that the machine is still a prototype and that it has not been possible to estimate the future levels of demand for the machine. Further, there is only a small pool of potential customers for whom the parties could compete.
24. On this basis, we have provisionally concluded that the merger is unlikely to result in an SLC in the market for automated filling machines.

Provisional conclusion on competitive effects of the merger in the market for trolleys and cabinets for storage of adherence packaging

25. We considered whether the merger was likely to affect significantly outcomes for customers of trolleys and cabinets for storage of adherence packaging. We found that a significant reduction in competition in the supply of trolleys and cabinets is unlikely as a result of the proposed merger. There is little overlap between the parties in the supply of trolleys and cabinets. While SurgiChem is active in this market, it appears to be a minor area for Omnicell/MTS. Furthermore, we have identified a number of other credible competing suppliers of trolleys and cabinets in the marketplace which could constrain the merged entity.

Provisional conclusion on the SLC test

26. Based on the above, we provisionally concluded that the proposed merger is not expected to give rise to an SLC in (a) the market for the supply of adherence packaging in the UK; (b) the market for the supply of automated adherence packaging filling machines in the UK; or (c) the market for the supply of trolleys and cabinets for the storage of adherence packaging in the UK.

Provisional findings

1. The reference

- 1.1 On 14 March 2014, the OFT under section 33 of the Enterprise Act 2002 (the Act) referred the anticipated acquisition by Omnicell/MTS of SurgiChem to the CC for investigation and report (the proposed merger). Omnicell/MTS and SurgiChem are together referred to below as ‘the parties’.
- 1.2 On 1 April 2014, the CC joined with the competition function, and certain consumer functions, of the OFT to form the CMA, which continued with this inquiry and other work inherited from the OFT and CC.¹ In relation to this inquiry, the CMA must decide:
- (a) whether arrangements are in progress or in contemplation which, if carried into effect, will result in the creation of a relevant merger situation; and
 - (b) if so, whether the creation of that situation may be expected to result in an SLC within any market or markets in the UK for goods or services.
- 1.3 Our terms of reference are set out in Appendix A. We are required to take our final decision and report by 28 August 2014.
- 1.4 This document, together with its appendices, constitutes our provisional findings, published and notified to Omnicell/MTS and SurgiChem in line with the CMA’s Rules of Procedure.² Further information relevant to this inquiry, including a non-confidential version of the main parties’ initial submission, and summaries of hearing evidence, can be found on our website.³

2. The adherence packaging industry

- 2.1 The parties are both active in the adherence packaging industry. Adherence packaging is aimed at patients who find compliance with their medication regimen difficult. These products are used by pharmacists to repackage a patient’s medicines, in order to help patients to take the correct dosages at the correct time. Pharmacists remove the medication prescribed for a patient from the original packaging in which it was supplied by the manufacturer and

¹ The remaining functions of the CC in relation to the reference were transferred to the CMA, under [Schedule 5](#) to the Enterprise and Regulatory Reform Act 2013 and the Schedule to the Enterprise and Regulatory Reform Act 2013 (Commencement No. 6, Transitional Provisions and Savings) Order 2014.

² [Mergers: Guidance on the CMA’s jurisdiction and procedure, CMA2.](#)

³ www.gov.uk/cma-cases/omnicell-surgichem.

load each individual blister with the correct dose for the patient before sealing the pack.

- 2.2 Adherence packaging can be made from different materials. It originally took the form of a rigid plastic box (or other container) with a number of compartments, each of which a pharmacist would load with the correct dosage of pills and/or capsules to be taken by a patient at a particular time. However, disposable adherence packaging – which is now by far the most commonly used type of packaging for hygiene reasons – can be card-based or plastic-based. Card-based products, such as those supplied by Omnicell/MTS, use cardboard to envelop plastic blisters which contain the medication. Plastic-based products, such as those provided by SurgiChem, use a plastic tray to envelop plastic blisters.
- 2.3 Adherence packaging is used both by those patients who are resident in care homes and those who live in their own homes (known as domiciliary patients). The type of adherence packaging tends to vary depending on the type of end user that it is aimed at. Adherence packaging aimed at domiciliary patients tends to be multidose, meaning that more than one type of medication can be fitted into each blister. Much of the adherence packaging aimed at residents in care homes tends to be single dose, which means its blisters only have room for one type of medication, making it easier to monitor and record the medication given to each patient. Some products can also hold liquid medications, such as the Biodose product supplied by Protomed.
- 2.4 An alternative to card-based and plastic-based adherence packaging are plastic pouches. Patients are provided with their medication on a roll of plastic pouches, with each pouch containing the medication to be taken at one time. Pouches are more commonly used in mainland Europe, particularly in the Netherlands, although we identified a small number of UK pharmacists that also use pouches. Pouches are multidose products that are filled by a machine operated by the pharmacist.
- 2.5 There are a number of other related products that a pharmacist may need to buy to be able to use adherence packaging. These include:
- (a) platens or templates;
 - (b) rollers for pressure sealing adherence packaging;
 - (c) replacement blisters and replacement seals;
 - (d) sheets for recording the patient's prescription;
 - (e) hangers, labels and bags;

- (f) trolleys and cabinets, used to store medication (including adherence packaging) securely and to facilitate the distribution of medicines by care-home staff;
- (g) de-blistering machines;
- (h) heat sealers; and
- (i) automated filling machines.

2.6 With the exception of pharmacies purchasing through the NHS Scotland framework agreement, pharmacies are not reimbursed for the cost of each adherence pack used, and must meet the cost themselves within the dispensing fee they receive from the NHS for each medication dispensed (which we understand is around 90p per prescription item). In Scotland, NHS Scotland tenders for the supply of multidose adherence packaging for domiciliary patients to pharmacies [X]. NHS Scotland reimburses the pharmacy for the cost of the packaging. Omnicell/MTS told us⁴ that approximately [X]% of pharmacies in Scotland participated in the framework.

2.7 We have collected a range of evidence which suggests that the adherence packaging market has been growing year on year and is likely to continue to grow:

- (a) In 2012, 1,000.5 million prescription items were dispensed in England, a 62.2% increase (383.5 million items) on 2002.⁵ The volume of GP-prescribed drugs has risen by 204.1% between 1995 and 2008, an annual average increase of 8.9%.⁶
- (b) Omnicell/MTS estimated that the market for multidose packs (mainly used for domiciliary patients) was growing at [X]% a year, a combination of growth in the number of target patients of [X]% a year, an increase in the number of prescriptions per patient, and greater penetration of the potential market by adherence packaging. It also estimated that the market for single-dose packs (mainly used in care homes) was growing at [X]% a year, a combination of growth in the number of care-home patients of [X]% a year and an increase in the number of prescriptions per patient of [X]% a year. The lower growth rate for packs used in care

⁴ Omnicell/MTS main submission, 4 April 2014, paragraph 4.2.1.

⁵ NHS Health and Social Care Information Centre, *Prescriptions Dispensed in the Community: England 2002–2012*, paragraph 26.

⁶ Office for National Statistics, *Public Service Output, Inputs and Productivity: Healthcare – Extended Analysis*, released 24 March 2010, paragraph 4.4.4.

homes reflected the greater levels of adherence packaging penetration in relation to care-home patients in contrast to domiciliary care patients.

- (c) Omnicell/MTS told us⁷ that there were a significant number of patients who were not currently provided with their oral medications in adherence packaging but for whom such packaging would be beneficial, as there was evidence that as many as 50% of prescribed medicines taken by older people were not taken in compliance with dosage regimes.

3. The companies

Omnicell/MTS

- 3.1 Omnicell is a public company listed on the NASDAQ stock exchange. It is a supplier of automation and software solutions for patient medication and supplies management for acute care hospitals, post-acute nursing, long-term care facilities, and domiciliary patients.
- 3.2 Omnicell owns MTS, a provider of adherence packaging, adherence support products for patients and carers, and technological solutions that support the dispensing process in pharmacies. In the UK, its subsidiary MTS Medication Technologies Limited (MTS Limited) supplies adherence packaging under the brand name 'Easyblist', as well as own brand products for some larger pharmacy chains and related support products. It also supplies:
 - (a) three types of machine: de-blistering machines, automated filling machines and machines used for heat-sealing adherence packaging;
 - (b) trolleys and cabinets; and
 - (c) a range of other products for use alongside adherence packaging, including platens or templates and rollers for pressure-sealing, and associated products such as medication administration record sheets, hangers, labels and bags.
- 3.3 MTS Limited's total sales for the year ended 31 March 2013 were approximately £6.9 million, including sales outside the UK. In calendar year 2013, MTS Limited's sales in the UK were approximately £[REDACTED] million. £[REDACTED] million of these UK sales were adherence packaging. We would expect revenues to increase, given MTS Limited's success in winning a tender to supply Boots with adherence packs for domiciliary patients in early 2013.

⁷ [Omnicell/MTS initial submission](#), 4 April 2014, paragraph 4.3.4.

- 3.4 Adherence packaging and the various machines that MTS Limited supplies are manufactured in the USA by MTS. Other products, such as trolleys and cabinets, are sourced when required from [REDACTED].

SurgiChem

- 3.5 SurgiChem is also a supplier of adherence packaging and adherence support products for patients and carers and is currently owned by Bupa Care Homes (CFG) plc (Bupa). SurgiChem was established in 1989 by a community pharmacist as a means to supply a new medication management system to the community and care-home markets. It was incorporated into the Bupa portfolio when Bupa acquired the care homes business of its parent company, Care First, in 1997.
- 3.6 SurgiChem supplies a range of adherence packaging and adherence support products for use by domiciliary and care-home patients, comprising:
- (a) adherence packaging products, which are plastic-based and sold under the brand name 'Nomad';⁸
 - (b) trolleys and cabinets;
 - (c) components required to enable pharmacies to fill and use the adherence packaging; and
 - (d) medication fridges, which are supplied to pharmacies, which in turn provide them to their care-home customers.
- 3.7 SurgiChem has also been developing:
- (a) an automated filling machine, although it is not yet fully developed and the company has [REDACTED]; and
 - (b) a card-based adherence packaging product sourced from a [REDACTED] supplier.
- 3.8 All SurgiChem's manufacturing is outsourced: plastic trays are made by a thermoformer in [REDACTED], seals by a company in [REDACTED], and trolleys and fridges are made by third party manufacturers in [REDACTED].
- 3.9 In 2013, the company's turnover was approximately £7.6 million, of which £[REDACTED] million was for sales of adherence packaging, £[REDACTED] million was for sales of trolleys and cabinets, and £[REDACTED] million was for sales of fridges. SurgiChem has experienced an average of approximately [REDACTED]% growth in revenues year

⁸ A large majority of SurgiChem's adherence packs are pressure-seal packs.

on year for the past seven years. A large part of this growth is attributable to sales of Nomad Clear (a disposable weekly pack for use by domiciliary patients) which was launched in 2005 and now achieves average sales of £[X] per year.

Areas of overlap

- 3.10 The parties currently overlap in adherence packaging, and accessories and support products for adherence packaging (such as labels, spare seals, ring binders, and other), and in trolleys and cabinets. SurgiChem has recently developed an automated filling machine for single-dose blister adherence packaging, therefore there is a potential overlap between the parties in automated filling machines.

4. Other providers of adherence packaging

- 4.1 There are a number of other providers of adherence packaging. The most significant of these providers include the following:

- (a) **Venalink** started trading more than 20 years ago and was the first company to supply adherence packaging in the UK. It is the third-largest supplier of adherence packaging by volume (fourth by value) in the UK for non-tender customers. It supplied approximately 4.8 million packs in 2013, with total sales of adherence packaging and ancillaries amounting to £1.4 million, with around 82% of this being multidose packaging intended for the domiciliary segment. It is the second largest supplier to customers served through tenders (it supplies NHS Scotland, and used to supply Boots). It supplies a card-based product, which is similar to Omnicell/MTS's product, and it supplies both cold-seal and heat-seal packs. It also supplies trolleys in small volumes. Card for Venalink's adherence packaging is manufactured in Canada by its parent company, Jones Packaging, and imported into the UK, and blisters are sourced from either Canada or Sweden.
- (b) **Shantys** had been making pill boxes since the 1990s, and it started supplying disposable adherence packaging around four years ago. It supplies plastic-based multidose adherence packaging manufactured on its behalf by third parties, under the brand name Pillmate MD Pack (previously Medipack). It also supplies reusable adherence packaging. Shantys told us that it sold only to wholesalers and distributors in the UK and not direct to pharmacies. It sold around [X] units of plastic-based disposable adherence packaging in the UK in 2013, a significant increase on its 2011 sales.

- (c) **Manrex** is a Canadian company, founded in 1973, which has licensed Boots to manufacture and supply its products in the UK. Boots self-supplies Manrex products to care homes, but it also supplies Manrex to independent pharmacies through the wholesaler, Bunzl. We understand that Manrex products are used exclusively in care homes in the UK. Manrex supplies a semi-disposable single-dose system for which the envelopes are made from plastic and are reusable, and blisters are disposable.
- (d) **Protomed** supplies a plastic-based product (under the brand name Biodose) that has removable, sealed pods which can accommodate both liquid and solid medication (though not in the same pod at the same time). It also supplies trolleys and cabinets for use with its adherence packaging at care homes. It targets the care-home market, including promoting its product directly to care homes and introducing them to pharmacies that can supply it, and sells direct, mainly to independent pharmacies and smaller chains. Protomed entered the market in 2008. In 2013, it supplied nearly [REDACTED] units, which is double the sales it had in 2011. Biodose is significantly more expensive (on a per-pack basis) than other blister-pack alternatives in the market, as its additional features (such as the removable, sealed pods and the ability to hold liquids) make it more expensive to manufacture.
- 4.2 Other providers of adherence packaging that we have identified are discussed in our consideration of the existing and potential competitive constraints on the parties in paragraphs 9.53 and 9.90.
- 4.3 There are a number of other providers of trolleys and cabinets, including Sunflower Medical, Norseman, Bristol Maid and Venalink.
- 4.4 There are a number of other providers of filling machines for blister-pack adherence packaging that could supply customers in the UK, including K&M, Technical Engineering Group (TEG),⁹ Ilseemann, Uhlman and SynMed.

5. The transaction

- 5.1 In April 2013, Bupa considered its options regarding SurgiChem. It had earlier received an approach from Omnicell to buy it, which it had rejected. Bupa then decided that adherence packaging was not part of its long-term strategy and, in [REDACTED], informed SurgiChem that it was to be put up for sale.

⁹ This is a company which, according to its website, designs and supplies tooling for pharmaceutical tablet blister packaging and tablet feeding systems. See www.teg.com.

- 5.2 Discussions with Omnicell started in [REDACTED], and the parties signed heads of terms on 23 September 2013. Following due diligence, the share purchase agreement for the sale and purchase of SurgiChem was signed on 6 December 2013, under which MTS ([REDACTED]) agreed to purchase SurgiChem for £12 million in cash subject to certain adjustments (the transaction). The share purchase agreement was expressed to be conditional on UK competition clearance (that is, either clearance by the CC following the reference from the OFT, or acceptance, at Omnicell's discretion, of undertakings that remedy or prevent any lessening of competition identified by the CC).¹⁰

The rationale for the merger

- 5.3 Omnicell's rationale for the acquisition of SurgiChem has been expressed to us as follows. [REDACTED]
- 5.4 Omnicell told us that the merged entity would be better placed to consider capital investments to meet the evolving expectations of the market and to benefit pharmacies and ultimately carers and patients. In particular, Omnicell and MTS Limited believed that [REDACTED], would be an important feature of the adherence packaging market in the future. Omnicell told us that it believed that the acquisition of SurgiChem would provide it with the critical mass to make the required investment in the R&D [REDACTED] worthwhile.
- 5.5 It also told us that, based on the increased scale of its operations in the UK following the merger, it intended to [REDACTED].
- 5.6 MTS Limited told us that, if it acquired SurgiChem, [REDACTED] to its own sales approach, which was better designed for larger groups.

Proposed merger and the relevant merger situation

- 5.7 Under section 23 of the Act, the test to determine whether the proposed merger will result in the creation of a relevant merger situation has two limbs:
- (a) we are required to decide whether two or more enterprises have ceased to be distinct; and
 - (b) whether the value of the turnover in the UK of the enterprise being taken over exceeds £70 million or, if not, the share of supply of goods or services of any description in the UK (or a substantial part) is at least one-quarter.

¹⁰ See footnote 1. The remaining functions of the CC in relation to the reference were transferred to the CMA on 1 April 2014.

Enterprises cease to be distinct

- 5.8 The Act defines an ‘enterprise’ as ‘the activities or part of the activities of a business’. ‘Business’ is defined as ‘including a professional practice and includes any other undertaking which is carried on for gain or reward or which is an undertaking in the course of which goods or services are supplied otherwise than free of charge’.¹¹
- 5.9 In this case we are satisfied that Omnicell, MTS and SurgiChem are all businesses for the purposes of the Act. Omnicell is a public company listed on the NASDAQ stock exchange and is a supplier of automation and software solutions for patient medication and supply management for acute care hospitals, post-acute nursing, long-term care facilities, and domiciliary patients. MTS is a provider of adherence packaging, adherence support products for patients and carers and technological solutions that support the dispensing process in pharmacies. SurgiChem is a supplier of adherence packaging and adherence support products for patients and carers. We are therefore satisfied that the activities carried on by each of Omnicell, MTS and SurgiChem constitute enterprises for the purposes of the Act.
- 5.10 The concept of ‘ceasing to be distinct’ is described in section 26 of the Act. This provides that any two enterprises cease to be distinct if they are brought under common ownership or common control (whether or not the business to which either of them formerly belonged continues to be carried on under the same or different ownership or control). We are satisfied that the transaction will result in SurgiChem being brought under the ownership and control of Omnicell/MTS and accordingly, the enterprises will cease to be distinct for the purposes of the Act.

Turnover and share of supply tests

- 5.11 The Act requires the CMA to establish that the transaction has a sufficient nexus with the UK to give us jurisdiction to consider the reference. This will be the case if either the turnover test or the share of supply test is satisfied.
- 5.12 The turnover test applies where the value of the annual turnover in the UK of the ‘enterprise being taken over’ exceeds £70 million.¹² The annual turnover of SurgiChem in 2013 was approximately £7.6 million and therefore the statutory turnover test under the Act is not met. We therefore considered the share of supply test.

¹¹ [Section 129\(1\)](#) of the Act.

¹² [Section 23\(1\)\(b\)](#) of the Act.

- 5.13 The share of supply test is satisfied if the merger creates or increases a share of at least one-quarter in the supply of goods or services of any description in the UK, or in a substantial part of the UK.¹³ The share of supply used for the purpose of the test is different from a market share, and goods or services to which the share of supply test is applied need not amount to the market defined for the economic analysis.¹⁴
- 5.14 The merged entity will have a combined share of [60–70]% in the supply of adherence packaging in the UK by value ([70–80]% by volume).¹⁵ The parties will therefore have an increased share of supply of greater than one-quarter for the supply of adherence packaging in the UK and therefore the share of supply test is met.

Conclusions on relevant merger situation

- 5.15 For the reasons given above, we are satisfied that a relevant merger situation would be created by the proposed merger and accordingly we have jurisdiction to consider whether the creation of that situation has resulted or may be expected to result in an SLC within any market or markets in the UK for goods or services.

6. Counterfactual

- 6.1 In carrying out our competitive assessment, we compared the prospects for competition with the merger against the competitive situation without the merger (the counterfactual). In assessing this counterfactual, a number of scenarios may be possible, but ultimately only the most likely scenario is selected. In our assessment, we have taken into account the extent to which events or circumstances and their consequences are foreseeable and have incorporated only those aspects that appear likely on the facts available to us.

Possible counterfactual scenarios

- 6.2 We found no financial or strategic reasons to believe that, absent the merger, either Omnicell/MTS or SurgiChem would exit the market for adherence packaging (and neither party has suggested that it might do so).
- 6.3 We did, however, gather evidence which suggested that SurgiChem has been developing both a card-based adherence pack and an automated filling

¹³ [Section 23\(2\)\(b\)](#) of the Act.

¹⁴ [Merger Assessment Guidelines, CC2](#), paragraph 3.3.5.

¹⁵ CMA analysis based on 2013 figures including sales to tender and non-tender customers but excluding self-supply of Manrex adherence packaging to Boots.

machine. In light of this evidence, we have considered whether SurgiChem's potential expansion into the sale of card-based adherence packaging and automated filling machines should be incorporated within our counterfactual.

The parties' views

- 6.4 Each party, in their respective submissions, said that the transaction should be assessed against the prevailing conditions of competition. The parties disagreed with the OFT's view that there was a realistic prospect of a counterfactual that was more competitive than prevailing conditions, in that (in the OFT's view) SurgiChem would have had the ability to supply card-based packaging absent the merger and might therefore bid for card-based packaging tenders in the future.

Likely to remain independent competitors

- 6.5 MTS and SurgiChem are both private companies, owned respectively by Omnicell and Bupa. Omnicell is a public company quoted on NASDAQ and Bupa is a company limited by guarantee. Omnicell and Bupa and, by extension, MTS and SurgiChem are independent of one another.
- 6.6 SurgiChem told us that Omnicell's original approach to Bupa was unsolicited and that Bupa had not sought a sale prior to that time. Bupa had not spoken to, or received any approaches from, any other potential purchasers (although it had initially planned to go to a wider market). In its strategic options paper, Bupa outlined a number of strategic options that it could take with respect to SurgiChem, including 'do nothing'.¹⁶ Although it chose the sale of SurgiChem as its favoured option (provided an acceptable price could be agreed), it is clear that there was no requirement on it to do so. Bupa told us that if the sale to Omnicell/MTS fell through, it was likely that it would look for another buyer as it had now made the decision that SurgiChem's activities were non-core to Bupa.
- 6.7 Given that we are examining an anticipated merger and neither company has acquired shares in the other,¹⁷ we observed that at present Omnicell/MTS and SurgiChem are independent competitors. Absent the merger, we consider that Omnicell/MTS and SurgiChem are likely to remain independent competitors whether SurgiChem remains under the ownership of Bupa or is sold to another buyer.

¹⁶ [§<]

¹⁷ Although the Share Purchase Agreement has been signed, clearance by the merger control authorities is a condition precedent to completion of the share purchase.

Other potential developments

- 6.8 After concluding that Omnicell/MTS and SurgiChem would remain independent competitors absent the merger, we considered whether an independent SurgiChem might have:
- (a) launched a new type of automated filling machine; and/or
 - (b) broadened its sales strategy to include supplying a card-based adherence pack for smaller, independent pharmacies and for supply to large pharmacy chains which go out to tender for their adherence packaging requirements.

Automated filling machines

- 6.9 SurgiChem is developing an automated filling machine for the first time and currently has a prototype which it is [REDACTED]. If [REDACTED], SurgiChem anticipates achieving sales of the machine in [REDACTED].
- 6.10 On the basis of evidence received from SurgiChem, we have concluded that, absent the proposed merger, it is likely that SurgiChem would begin supplying an automated filling machine for single-dose adherence packaging. We consider in our analysis of competitive effects (see paragraphs 10.17 to 10.41) the extent to which this product would compete with either of the automated filling machines sold by Omnicell/MTS.

Card-based packs

- 6.11 On 24 January 2013, SurgiChem received an invitation to tender from [REDACTED] for its adherence packaging contract, specifying a card-based product. Although SurgiChem initially indicated that it wished to tender for the contract, it quickly withdrew from the tender process (by 22 February) as it said it was not going to be in a position to guarantee the supply of product in time for the start of the [REDACTED] contract in May 2013. Despite withdrawing from the [REDACTED] tender, SurgiChem continued developing a card-based product. In February 2014, it placed an order with its [REDACTED] supplier for [REDACTED] cards, and it told us that it expected to be able to offer a multidose card-based product for sale to independent pharmacies from June 2014.
- 6.12 Based on the evidence available we found it likely that, absent the merger, SurgiChem would have begun offering card-based adherence packaging. We have considered in our competitive effects analysis the impact of the anticipated merger on the development of potential competition in the supply of card-based adherence packaging for: (a) pharmacies which go out to

tender for their adherence packaging requirement (see paragraphs 9.31 to 9.36); and (b) those pharmacies that do not buy through tenders (paragraphs 9.44 to 9.49).

Provisional conclusion on the counterfactual

- 6.13 We have concluded that, absent the merger, Omnicell/MTS and SurgiChem would continue to compete independently (whether SurgiChem is owned by Bupa or another person). We have also found it likely that, absent the merger, SurgiChem would have introduced a new automated filling machine and begun offering card-based adherence packaging to pharmacies, thereby increasing customer choice in both areas of the market. Accordingly, the counterfactual includes both of these likely developments.

7. Market definition

- 7.1 The purpose of market definition is to provide a framework for our analysis of the competitive effects of the merger. The relevant market (or markets) is the market within which the merger may give rise to an SLC and contains the most significant competitive alternatives available to the customers of the merged companies.¹⁸ However, market definition is not an end in itself, and the boundaries of the market do not determine the outcome of the CMA's analysis of the competitive effects of the merger in a mechanistic way. In its assessment of whether a merger may give rise to an SLC, the CMA may take into account constraints outside the relevant market, segmentation within the relevant market, or other ways in which some constraints are more important than others.¹⁹ Appendix G contains further details of our approach to market definition.
- 7.2 As part of the market definition analysis, we considered two dimensions of the relevant markets – product and geographic. Supporting evidence and analysis for our findings in relation to market definition are detailed in Appendix G.

¹⁸ The relevant product market is identified primarily by considering the degree of demand-side and, to a lesser degree, supply-side substitution. It is usual to define markets using the hypothetical monopolist test. This test delineates a market as a set of substitute products over which a hypothetical monopolist would find it profitable to impose a small but significant non-transitory increase in prices (SSNIP). The test is described in detail in paragraphs 5.2.10–5.2.20 of [CC2](#). However, the hypothetical monopolist test is often used as a framework for analysis rather than applied in a mechanistic way.

¹⁹ [CC2](#), paragraphs 5.2.1–5.2.2.

Product market

7.3 Both parties either currently supply or have recently been developing products in the following categories:

- (a) adherence packaging;
- (b) accessories and support products for adherence packaging;
- (c) automated filling machines for adherence packaging; and
- (d) trolleys and cabinets.

7.4 We have therefore considered the product market definition for each of these product categories.

Adherence packaging

7.5 We considered whether card-based and plastic-based adherence packaging products formed part of the same market. We found that, while these are differentiated products and some pharmacies and indeed end-users have preferences for either card-based or plastic packaging, there does not seem to be a significant distinction between them and it therefore seems appropriate to include both card-based and plastic-based products in the relevant market for adherence packaging on the basis of demand-side substitutability. Nevertheless, our competitive assessment took into account the extent of the competitive constraint of card-based packaging on plastic-based packaging, and vice versa.

7.6 We considered whether single-dose or multidose products should form part of the same relevant market for adherence packaging, or whether they should be defined as two separate markets for the purposes of assessing the merger. There is a lack of demand-side substitutability between single-dose and multidose adherence packaging products as they are aimed at two distinct groups of end-users, some of the producers only sell either single-dose or multidose products, and some suppliers are more active in one segment than in the other. On the other hand, there appears to be significant substitutability on the supply side as many suppliers supply both types of product and most pharmacies purchase both. On balance, we decided to proceed on the basis of a relevant product market that includes both single-dose and multidose adherence packaging products, and to consider the different competitive constraints in relation to the two types of product/end-user as part of our competitive assessment.

- 7.7 We have also considered whether plastic pouches should be included within the same market as adherence packaging. Pouches are broadly comparable in price to card- and plastic-based blister packs. However, unlike blister packs, pouches cannot be filled manually, and switching to a pouch-based system requires a significant capital outlay to purchase a filling machine. In light of this, the cost of switching to pouches is likely to be significant and it is unlikely that customers would switch from blister packs to pouches in response to a SSNIP, even though, in terms of functionality, the two products are similar. Based on this, and noting that pouches currently account for a very small proportion of sales of adherence packaging, we propose to proceed with the assessment of the merger on the basis of a relevant product market for adherence packaging that excludes pouches. However, we recognise that pouch-based systems may pose an increasing constraint on the suppliers of blister packs in the future, and we therefore consider any relevant competitive constraints from pouches as part of our competitive assessment of the proposed merger.
- 7.8 We have also considered whether reusable adherence packaging should be included within the same market as adherence packaging. There is no overlap between Omnicell/MTS and SurgiChem in reusable adherence packaging. Further, switching from disposable to reusable adherence packaging is unlikely in response to a SSNIP on disposable packaging given the convenience and other advantages of disposable packaging. We have therefore assessed the merger on the basis of a relevant product market for adherence packaging that excludes reusable products, and considered any relevant competitive constraints from reusable packaging as part of our competitive assessment.

Customer segments

- 7.9 We considered whether large pharmacy chains which held a formal tender in order to appoint suppliers of adherence packaging for domiciliary patients, and other pharmacies which do not use tenders, should be considered as separate relevant markets. We found that there are indications that the supply and demand conditions may be different for customers who have tendered if compared with other, non-tender customers, with the set of competitors for these contracts more limited than it generally has been for non-tender customers and the prices achieved by some tender customers usually significantly lower than those paid by most non-tender customers. We have not found it necessary to conclude on whether these customer groups represent separate relevant markets, but have considered these segments individually in our competitive assessment in order to take account of any differences in the competitive constraints.

Support products and accessories

- 7.10 We have identified a number of products – such as label flaps, replacement seals, rollers, templates, ring binders and dividers – that are only purchased and used as a consequence of having purchased adherence packaging. Adherence packaging can be considered to be a primary product and these support products to be the associated secondary product. We found that many of these support products would typically only be compatible with adherence packaging of the same products (eg platens, replacement seals), that customers tended to purchase support products from the same supplier, and that the parties did not sell support products to customers that did not purchase adherence packaging from them. We therefore considered it appropriate to consider the effect of the merger on adherence packaging and related support products together, ie the relevant product market for adherence packaging should include related support products.

Filling machines

- 7.11 As noted in paragraph 3.10, Omnicell/MTS and SurgiChem would potentially overlap in the supply of single-dose automated filling machines for blister packs. Therefore the narrowest candidate market in this case is the supply of single-dose filling machines. We have considered whether other types of machines, including multidose filling machines, should be included in the relevant market. However, multidose machines tend to be more complex and are significantly more expensive (approximately [X] times the cost) than single-dose machines, therefore it seems unlikely that customers would switch from single-dose to multidose filling machines in response to a SSNIP for single-dose filling machines.
- 7.12 We also considered whether filling machines and adherence packaging products form part of the same relevant market for adherence packaging. We found that both Omnicell/MTS's single-dose filling machine, the MTS 350, and SurgiChem's developed machine [X]. Thus, this would suggest that the machines are in a separate relevant market from adherence packaging products. We therefore found that there is a separate market for single-dose filling machines for the purposes of assessing the proposed merger of Omnicell/MTS and SurgiChem. Our competitive assessment has therefore considered the extent to which the parties' single-dose filling machines would compete, as well as competitive constraints from other machines and systems, such as pouch-based systems.

Trolleys, cabinets and bags

- 7.13 Both parties sell trolleys and cabinets specialised for use with adherence packaging, as well as bags in which adherence packaging can be stored and transported. Based on evidence set out in Appendix G, we found that trolleys and cabinets for storage and distribution of medicines contained in adherence packaging or otherwise for distribution to care-home, hospital and domiciliary patients form a separate relevant market for the assessment of the effects of the proposed merger between Omnicell/MTS and SurgiChem. We considered any relevant competitive constraints within this market and from outside in our competitive assessment.

Geographic market

Adherence packaging

- 7.14 Both parties told us that the location of customers did not affect their ability to supply adherence packaging and related products. Customer responses to our questionnaire did not indicate that a supplier's location within the UK was an important consideration for them, and hearings with customers or competitors did not raise this as a relevant issue either.²⁰ Neither of the two major card-based manufacturers – Omnicell/MTS and Venalink – [X] manufactures within the UK. Therefore, UK production does not appear to be necessary to operate in the UK. All the main competitors have UK presence through sales and distribution businesses, although some suppliers import the products themselves. Based on evidence set out above, we consider that the relevant geographic market for the assessment of the merger is the UK. We will consider the competitive constraint of firms which operate partially or wholly overseas in further detail in our assessment of competitive effects and of entry and expansion.
- 7.15 We considered whether a narrower geographic market, for customers in Scotland, may be appropriate, given that pharmacies are reimbursed for Omnicell/MTS's and Venalink's multidose adherence packaging by NHS Scotland. This may mean that the effect of the merger differs for these customers. We have not considered it necessary to determine whether Scotland represents a separate geographic market. We have taken account of the fact that there may be different competitive conditions in the supply of

²⁰ We note that parties' customers in the UK operate in the UK only – they are local independent pharmacies or pharmacy chains – although some of the larger chains, such as Boots, may have an international majority owner or parent company.

adherence packaging for domiciliary patients in Scotland as part of the competitive assessment.

Automated filling machines

- 7.16 Automated filling machines are high-value products, and there have been indications that non-UK suppliers of machines could or do supply UK customers (see paragraph 4.4). The market may therefore be global, or at least wider than the UK. However, as the main geographic overlap between the parties for adherence packaging is in the UK, we have assessed the effect of the merger on the market for filling machines at a UK-wide level. We have considered whether competitors from outside the UK can and do compete in the UK market in our analysis of competitive effects.

Trolleys

- 7.17 The narrowest candidate geographic market for trolleys and cabinets appears to be the UK, since the supply and demand conditions appear not to vary by narrower geographic areas. We noted that some suppliers produce trolleys and cabinets in the UK, while others outsource production and import the finished products into the UK. However, we did not find it necessary to conclude on the exact geographic boundaries for the relevant market for the supply of trolleys and cabinets for the purposes of assessing the effects of the proposed merger, and based our assessment on a UK-wide market.

Conclusions on market definition

- 7.18 We found that for the purposes of assessing the competitive effects of the proposed merger between Omnicell/MTS and SurgiChem, the relevant markets are:
- (a) The supply of adherence packaging and related accessories and support products in the UK. This includes both card-based and plastic-based products, and both single-dose and multidose products, but excludes reusable adherence packaging. It also includes semi-disposable systems such as Manrex and Nomad MDS, and systems suitable for liquids, such as Biodose. We also consider that pouches should be excluded from the relevant market.
 - (b) The supply of automated filling machines for single-dose²¹ packaging in the UK.

²¹ The machine that SurgiChem is developing only fills single-dose packaging.

- (c) The supply of storage facilities for adherence packaging and medicines, such as trolleys and cabinets in the UK.²²

7.19 In relation to these product markets, we note that there may be different competitive constraints in relation to card- and plastic-based products, single-dose and multidose products, and different customers (ie large customers who go out to tender for their adherence packaging requirements compared with those who do not tender). We have considered those as part of the competitive assessment.

8. The nature and extent of competition in the adherence packaging market pre-merger

8.1 In this section, we describe how competition works in the market for adherence packaging in the UK. We consider other relevant markets where the merging parties currently or potentially overlap in Section 11. Our consideration of the nature and extent of competition in the adherence packaging market has informed our assessment of the impact of the anticipated merger in the market for the supply of adherence packaging in the UK, set out in Section 9 of the report.

8.2 This section of the report sets out our findings on:

- (a) how the procurement process works, including the different routes that pharmacies use to procure adherence packaging, and how the price that a buyer pays is set;
- (b) the factors that influence a customer's purchasing decision;
- (c) the level of switching in the market;
- (d) the key competitors in the adherence packaging market and their market shares; and
- (e) the prices that are currently being paid and the margins that are currently being made by competitors in the market.

The procurement process

8.3 We identified four different methods that pharmacists use to procure adherence packaging: (a) using tender exercises; (b) spot buying or regular purchasing of adherence packaging directly from a supplier; (c) buying

²² We have not considered fridges as these are only supplied by one of the parties (SurgiChem).

adherence packaging through a buying group; and (d) buying it via a wholesaler. Our analysis of the data from the merging parties and third parties suggests that sales via tender exercises account for [20–30]% of sales; spot buying or regular purchasing of adherence packaging directly accounted for [60–70]%; buying adherence packaging through a buying group – [5–10]%, and (d) buying it via a wholesaler – [10–20]%.²³

- 8.4 There are formal supply contracts in place with customers who have procured adherence packaging via tenders.²⁴ There are three customers of adherence packaging who have tendered in the past two years. These are: Boots, Lloyds Pharmacy and NHS Scotland. The Boots and Lloyds Pharmacy tenders were awarded to Omnicell/MTS, and the NHS Scotland tender was awarded to both Omnicell/MTS and Venalink.
- 8.5 These three customers aside, there are no formal or binding contracts between suppliers and customers. SurgiChem noted that it did not have contracts in place with any of its customers and hence they could switch or multisource without notice. Similarly, Omnicell/MTS noted that except for tenders, supply/purchase contracts were not used.
- 8.6 Customers generally purchase on an ongoing basis, but the frequency of purchases varies, as does the volume of purchases. For instance, Omnicell/MTS noted that most customers placed an order every few weeks or months, but orders could be less frequent; in rare cases up to 18 months could elapse between orders. SurgiChem noted that some customers may also elect to order in bulk.
- 8.7 We found that some customers purchase adherence packaging from more than one supplier.²⁵ Out of 2,980 customers of either Omnicell/MTS or SurgiChem’s multidose packaging in the period from 2011 to 2013, [X] customers purchased from both parties at one point or another.²⁶ We understand that multisourcing is often due to different products addressing

²³ This is a lower bound estimate for the proportion of sales to buying groups and wholesalers as we were unable to classify all of Omnicell/MTS’s and SurgiChem’s customers according to the method of purchases. We also made a number of assumptions regarding other competitors’ customers; all Protomed and Venalink’s sales were considered as direct sales, while all Shantys and Manrex sales were regarded as being sold through wholesalers for the purposes of this analysis.

²⁴ [X]

²⁵ Our analysis of the parties’ sales data suggests that there is a degree of overlap in customers between the parties, including some of the larger customers such as Co-op, Rowlands, Paydens, in addition to tender customers Boots and Lloyds Pharmacy.

²⁶ These customers represented [X]% of Omnicell/MTS’s total multidose sales in the period and around [X]% of SurgiChem’s total sales. Out of 866 single-dose packaging customers of Omnicell/MTS and SurgiChem in the period from 2011 to 2013, [X] customers purchased from both parties at one point or another (these customers represented [X]% of Omnicell/MTS’s and around [X]% of SurgiChem’s total single-dose sales in the period. This includes customers who multisourced as well as customers who have switched between the merger parties. Further details are provided in Appendix C.

different end-users' needs or preferences, pointing to a differentiation in the suppliers' products.²⁷ We also found that multisourcing by some pharmacy chains may be for historical or legacy reasons. For instance, if a pharmacy chain had acquired stores where a different supplier or product was used than its existing supplier, these acquired stores might continue to use the legacy products.²⁸ We noted that the dual-sourcing customers include some of the parties' larger customers, as evidenced by the small number of customers that purchase from both parties accounting for a large proportion of the parties' sales, particularly so for Omnicell/MTS.²⁹

8.8 We have reviewed the way that prices are set. Omnicell/MTS and SurgiChem, as well as other suppliers in the market, have list prices for their adherence packaging products.³⁰ Tender customers will set the price they pay through the tender process. Non-tendering customers either negotiate an individual price or simply pay the list price. Our analysis suggests that [X]% of Omnicell/MTS's adherence packaging sales and [X]% of SurgiChem's adherence packaging sales are at list prices. In terms of customers rather than sales volumes, we found that around [X]% of Omnicell/MTS's and around [X]% of SurgiChem's customers paid list prices, with the remaining customers getting a discount from the list price.³¹ Overall, we found a [X] in prices that customers pay. Appendix B reports the details of our analysis. We found that:

- (a) the average discount for Omnicell/MTS's main generic multidose adherence pack was [X]%, and for SurgiChem's it was [X]%;³² and
- (b) the average discount for Omnicell/MTS's generic single-dose product was [X]%, and for SurgiChem's main single-dose product, Nomad Concise, it was [X]%.

²⁷ This is what some of the larger customers suggested when we spoke to them, eg Lloyds Pharmacy, Rowlands, Co-op. For example, Lloyds Pharmacy noted that although for internal governance and procurement processes its preference was to have available for its stores a single product rather than multiple products, if a customer, for example a care home, stated that it had a certain system need, then, providing it met quality and governance requirements, it would use alternative products. Similarly Rowlands told us that if a care home wanted a specific system, it would do everything it could to provide the customer with that system, although it would try to push it towards Omnicell/MTS as the most efficient system for Rowlands.

²⁸ See, for instance, [hearing summary with The Co-operative Pharmacy](#).

²⁹ Omnicell/MTS has a relatively concentrated customer base, with a few large customers accounting for a large proportion of its sales. SurgiChem's customer base is more dispersed. See details in Appendix C.

³⁰ The list price is the standard published price online or in marketing material.

³¹ To calculate these figures all branded versions of adherence packs are taken as being below list price. See Appendix B for further details, in particular paragraphs 24 and 48 which explain which products are included in this analysis.

³² This is the average discount among all volume (ie includes some volume that was sold at list price). The average discount among those that got at least some discount was [X]% for Omnicell/MTS's generic multidose pack and [X]% for SurgiChem's Nomad Clear.

- 8.9 We have assessed the factors that allow customers to negotiate discounts. We received evidence from customers, competitors and the parties indicating that purchasing larger volumes could result in greater discounts. However, our analysis of the parties' pricing data shows that, for both Omnicell/MTS and SurgiChem, [REDACTED]. Our analysis shows that [REDACTED]. We also considered the impact that being part of a buying group or a customer sourcing its products from more than one supplier has on prices that the customers pay. [REDACTED]
- 8.10 Qualitative evidence we have gathered on negotiations from some customers and from the parties' internal documents also suggests that the extent to which customers try to negotiate, and are successful in doing so, may explain some of the variation in prices that they pay. For example, both parties noted that discounts were given in relation to retaining or winning business from a competitor. We found that both parties' internal documents in relation to sales, while not a systematic and complete record of price negotiations, often referred to retaining or winning customers by offering discounts to match competitors (see Appendices B and C for further details).

Factors that influence procurement decisions/price sensitivity

- 8.11 As discussed in paragraph 2.6, the cost of adherence packaging is borne by the pharmacy along with other costs of delivering prescriptions to patients (with the exception of adherence packaging purchased through the NHS Scotland framework agreement for which pharmacies could be reimbursed). It is important to note, however, that we found that adherence packaging tends to represent a small proportion of pharmacies' business or costs,³³ particularly in the context of pharmacists' procurement of medicines and other supplies.
- 8.12 The parties differ in their views on the importance of price in pharmacies' choice of adherence packaging. This may to some extent reflect differences in the make-up of their customer bases (eg Omnicell/MTS's focus on supplying larger customers, including those which procure adherence packaging through tenders):
- (a) Omnicell/MTS submitted that pharmacies tended to be very price driven in their choice of packaging as they saw it as a commodity product, and that ultimately their choices would be driven by price. It told us that once a

³³ For instance, Lloyds Pharmacy dispensed approximately 150 million prescriptions per year. Of those, approximately 4.5 million for the care-home market and approximately 6 million prescriptions for the domiciliary market required adherence packaging. Rowlands said that prescriptions requiring adherence packaging amounted to [REDACTED]% of its business. Our survey evidence on smaller customers suggested that adherence packaging was used by pharmacies in only a small proportion of prescriptions: on average 12% of Omnicell/MTS customers' prescriptions used adherence packaging and 14% of SurgiChem customers' prescriptions, with under half of customers of both parties saying adherence packaging was used in 5% or less of their prescriptions.

supplier's product met the minimum quality threshold such that it would be accepted by pharmacies, the key differentiating factor between different suppliers' products was price.³⁴ Omnicell/MTS also submitted that a price increase was likely to result in a loss of customers because, despite the differences between the various suppliers' products, it was not possible to differentiate the individual packaging products sufficiently to secure a material non-price advantage. Omnicell/MTS told us that it had not [✂] in order to avoid risk of switching away to other products.³⁵

(b) By contrast, SurgiChem submitted that its discussions with independent pharmacies had not tended to focus on price on the basis that, other than a single price increase for Nomad Clear, SurgiChem had held its list prices steady since 2007 and focused on building long-term relationships with customers.

8.13 We have found that there are a number of factors that a pharmacist may consider when making his buying decision, including: price, the quality of the product, ease of filling and checking the packaging, security of supply and the level of service from the supplier. This suggests that customers consider products may be differentiated in terms of these features.

8.14 In making their choice of adherence packaging, pharmacists are likely to take particular account of the needs and preferences of the end-users. In particular, pharmacies may be willing to use a different supplier in order to cater for the preference of a particular care-home customer and we understand that this factor is a key driver of multisourcing by pharmacies. In relation to domiciliary customers, a key concern of pharmacies appears to be a view that customers would be unhappy or resistant to changing their packaging from a product that they are familiar with. For example, in our survey of small and medium-sized pharmacies, around half of the small number of pharmacies which thought it would be difficult to switch felt that their customers would not wish to change to an unfamiliar product. The survey also asked those customers who said that switching was easy, but who had not switched in the last three years, the reasons for not switching. End-users' familiarity with the product was one of the reasons mentioned by a significant proportion of respondents. We have found that there are some differences in the weight that different types of customers put on these different factors, and therefore we consider these in turn for tender and non-tender customers separately.

³⁴ Source: [Omnicell/MTS initial submission](#), Annex 13.

³⁵ We noted that Omnicell/MTS [✂].

Tender customer priorities

- 8.15 Evidence we gathered in relation to tender customers suggested that price was high on their list of priorities when selecting a supplier, but that other factors, such as quality of product and service, were also considered as part of the tender award criteria:
- (a) Boots switched from Venalink to Omnicell/MTS following a tender exercise in 2012. We were told that Omnicell/MTS won the business from Venalink because it had a better proposition and it was lower priced. Omnicell/MTS told us that Boots paid [REDACTED].
 - (b) Lloyds Pharmacy indicated that cost, delivery and service level were most important when considering the tender bids, and that there was a cost benchmark for assessing the bids. Omnicell/MTS [REDACTED] to Lloyds Pharmacy [REDACTED] pence per card when it moved to purchasing by way of tender in 2013.³⁶
 - (c) NHS Scotland indicated that price was important but that it was not the sole deciding factor, as it would weight a range of other factors – such as disposability, tamper evident, space for labels, moisture resistance, after-sales service, and other factors – along with price before deciding whether to source from a given supplier. It said that it rated Venalink first and Omnicell/MTS second.

Non-tender customers

- 8.16 The evidence we received from the parties, customers (including survey evidence) and competitors suggested that price is not necessarily the ultimate dimension of competition in this segment of the market, and that other factors, such as quality, the product itself, end-users' preferences, and hence preference for a particular product (indicating product differentiation), were important factors in the choice of pharmacies.³⁷
- 8.17 Our customer survey asked customers what they would do in the event of a hypothetical 5% price increase for adherence packaging by their current supplier. Responses indicated that 69% of Omnicell/MTS customers and 60% of SurgiChem customers would switch supplier. Even if, in reality, not all of those who said they would switch would actually do so, the level of price

³⁶ [Omnicell/MTS initial submission](#).

³⁷ For instance, when customers of our survey of small and medium-sized pharmacies were spontaneously asked why they used their current supplier rather than another, the most commonly mentioned reasons were related to the product itself (61% mentioned some aspect of the product); 28% mentioned the quality of the product, while 22% mentioned the pharmacy's own customers being familiar with the product (compared with 27% mentioning price).

sensitivity suggested by this hypothetical price increase is very high, and at odds with other evidence we have seen, set out in paragraphs 8.25 to 8.28 below, which suggested that many non-tender customers are ‘sticky’.³⁸ This may be due to the hypothetical nature of the question, along with many respondents’ belief that there are many alternative suppliers they could turn to in the event of a price increase. We consider some evidence on customers’ reactions to an actual price increase event in paragraphs 8.26 to 8.28 below.

Customer switching

- 8.18 We have considered the extent to which customers in the market switch. In markets where switching is low, this may indicate that customers are not price sensitive, which in turn may indicate that unilateral effects are more likely. However, evidence on switching should be interpreted with care, together with other evidence, since (a) observed switching may not necessarily reflect threats of switching and renegotiations that occur between customers and their existing suppliers, which are also important when considering competitive constraints in the market, and (b) a lack of switching may be due to stability in parts of the market in terms of pricing and quality of products, with customers seeing no reason to change something that works well and is competitively priced.
- 8.19 Customers that procure adherence packaging via tenders indicated that they would consider their options and switch suppliers on a regular basis.³⁹ This suggested to us that tender customers are relatively price sensitive and would be prepared to switch suppliers regularly. Evidence on the ease and the extent of switching by non-tender customers is more extensive and varied, and we have therefore considered it in more detail below.

Ease of switching

- 8.20 Omnicell/MTS told us that customers could switch easily, either to another card- or plastic-based product, or between card- and plastic-based products, as there are no technical issues or costs to doing so. Omnicell/MTS also said that there was considerable scope for suppliers to persuade a pharmacy to

³⁸ We have carried out some further analysis to understand better the context of customers’ responses to the hypothetical price increase question. We compared responses between subgroups of respondents based on their characteristics (customer size, spend and number of stores) as well as their responses to other survey questions. Generally speaking, this analysis has not produced any striking results. We have found that those SurgiChem customers who find price an essential or a very important factor in their choice of producer as well as the ones who think it would be easy to switch are slightly more likely to say they would switch than other SurgiChem customers. However, due to small sample sizes, it was not possible to establish whether the same pattern exists among Omnicell/MTS customers. Small sample sizes also meant that we could not establish whether there are differences in responses to the hypothetical price increase question between any other subgroups of customers mentioned above (for either of the parties).

³⁹ For instance, the Lloyds Pharmacy contract runs from [X] to [X].

switch suppliers. Omnicell/MTS submitted that its customers [REDACTED] switched to and from Omnicell/MTS, with it losing between [REDACTED] and [REDACTED] customers each month, and that the net loss in 2013 was [REDACTED] customers (although we note that this is [REDACTED]% of its total number of customers).

- 8.21 SurgiChem also submitted that switching was easy, that customers switched between suppliers, and that price was the most important factor why pharmacies would switch. SurgiChem submitted that, while it did not consistently track the switching of its customers, it estimated that around [REDACTED]% of its sales per year came from new business (although we note that some of these pharmacists may have been buying adherence packaging for the first time rather than switching from another provider).
- 8.22 We have found that neither customers nor other third parties considered switching to be difficult. However, some customers did suggest that there were some costs associated with switching, such as: staff briefings and training, communication, and risks around the product and its quality. Further, many third parties noted that even though switching may be relatively easy, there was a reluctance to do so. A number of explanations for this included general consumer inertia, the potential reaction of their own staff in pharmacies and the reaction of end-users.⁴⁰ We also gathered evidence on the ease of switching through our customer survey of small and medium-sized pharmacies. The response showed that most customers regard switching as being easy, with 83% of Omnicell/MTS customers and 68% of SurgiChem customers saying that it would be 'very easy' or 'quite easy' to switch producers of adherence packaging.
- 8.23 However, while switching is generally regarded as being easy to do, actual switching by non-tender customers appears to be relatively low. Most non-tender customers we have spoken to said they had not switched suppliers in any significant way in the past three years.⁴¹ One exception was PharmAssist, [REDACTED]. Our customer survey of small and medium-sized pharmacies indicates that 13 to 19% of the parties' smaller and medium-sized customers have switched supplier during the preceding three years.
- 8.24 One potential explanation for the relatively low levels of switching is that there has not been much reason to switch as prices and products have not changed much. Our analysis of the parties' data suggests that this may be true in the case of Omnicell/MTS's customers, with [REDACTED]% of Omnicell/MTS's customers

⁴⁰ [REDACTED]

⁴¹ We held hearings with some of Omnicell/MTS's and SurgiChem's largest customers. We also received written responses from some of the parties' largest customers. The largest customers included the major pharmacy chains, a sample of the largest buying groups and distributors/wholesalers. Details of their purchases are provided in Appendix C.

who have been with it for the last three years seeing no change in prices. However, in SurgiChem's case around [X]% of customers have experienced a price rise in the past three years, after the price of Nomad Clear was increased in October 2012. We have analysed the impact of this price rise below from paragraph 8.26.

8.25 We have analysed a number of sources of evidence about switching in the non-tender segment of the market:

(a) Our analysis of the parties' sales data found that the level of customer churn (ie a customer being lost by a particular provider)⁴² each year was around [X]% of Omnicell/MTS's customers and around [X]% of SurgiChem's customers (depending on the particular year and whether the product was multidose or single-dose). However, annual churn appeared to be higher for smaller customers, as the 'lost' value of sales for those customers' purchases was far lower.⁴³

(b) PWC analysis of switching and churn by single-store pharmacies, submitted by the parties, suggested that around [X]% of the single-store pharmacies were lost as exclusive customers in any given year (in the period from 2011 to 2013) (see Appendix C).

Nomad Clear price increase

8.26 Following a rise in raw material prices, SurgiChem increased the list price of Nomad Clear in October 2012 from [X] pence per pack to [X] pence ([X]% increase). The average price that its customers paid also increased by [X]% from around [X] to [X] pence. Alongside this price change, SurgiChem introduced a new product (Clear 2) which uses less plastic and has a lower price. SurgiChem submitted that by raising the price on its existing Clear product and introducing a new Clear 2 product it was able to retain customers. We noted that no other suppliers had changed list prices of their adherence packaging products in the period from 2011 to 2013.

8.27 We examined SurgiChem's customers' immediate response to this event. Details of our analysis can be found in Appendix C. In summary, we found that:

⁴² These 'lost' customers have either switched away from one of the parties to an alternative provider, or stopped buying adherence packaging altogether.

⁴³ Between [X] and [X]% for Omnicell/MTS and between [X] and [X]% for SurgiChem, indicating that it was the smaller customers that switched away more regularly (see Appendix C).

- (a) Of the [X] of SurgiChem's customers which purchased Nomad Clear in the year preceding the price increase,⁴⁴ [X]% had continued to purchase in the year following the price increase, with [X]% of these paying a higher price (and with [X]% of volume then being sold at a higher price).
- (b) [X]% of customers had reduced the volume of their purchases by more than [X]%, while [X]% did not reduce or increase their purchases of Clear in the year following the increase.
- (c) [X] customers ([X]%) were lost, but these accounted for only [X]% of sales volumes; [X] customers ([X]%) purchased at least some volumes of Clear 2; but only [X] customers ([X]%) had switched to Clear 2 in 2013 entirely.
- (d) When we compared the growth in sales volumes of [X] branded version of Nomad Clear, which did not have its price increased, and those of the non-branded version (most of which had been increased in price), we found that for non-branded Nomad Clear overall volumes were [X] after the price increase, whereas Nomad Clear [X].

8.28 Overall, our analysis suggested that there was some switching away from Nomad Clear by SurgiChem's customers, particularly among smaller customers, following the price increase (although a significant element of this could be churn or switching that may have occurred regardless of the price increase). We also note that the event appears to coincide with a slowdown in the growth of sales of the product. This suggests that some of SurgiChem's customers may be price sensitive. However, we also note that the [X] of customers ([X]) continued to make purchases (of the same or increased volumes) at a higher price.

Competitors in the adherence packaging market

8.29 In addition to the parties, we have identified a number of other competitors in the adherence packaging market. These competitors include Venalink, Shantys, Protomed and Manrex (all of which have been described in paragraph 4.1 above). We note at this point that, with the exception of Venalink, these firms do not compete across the entire adherence packaging market. The other competitors set out above largely focus their efforts on either the non-tender domiciliary segment of the market or the non-tender care-home segment. In the section which follows we have set out the market shares of these competitors, along with those of the parties.

⁴⁴ This excludes [X], which have branded products.

Market shares

- 8.30 We have considered the market shares of the parties, and the other competitors that we have identified, in the UK adherence packaging market. A large market share might be one potential indicator of how credible a competitive constraint on a supplier may be. If a number of competitors have a significant share of supply in the market, or in a segment of the market, this might indicate that competitive rivalry is stronger. Nevertheless in some markets, particularly those where barriers to entry and expansion are low, new entrants or incumbents capable of expanding could also present a significant competitive constraint. Further, we note that market shares may not necessarily fully reflect the competitive constraints in the market where products/suppliers' offerings are differentiated, as appears to be the case in adherence packaging.
- 8.31 We conducted an analysis of market shares based on data collected from known suppliers in the market. Details of this analysis are set out in Appendix F, along with the parties' submissions of their market share analysis. In the adherence packaging market as a whole, Omnicell/MTS had a [40–50]% share and SurgiChem had a [30–40]% share by volume of sales in 2013. Venalink was the third largest supplier, with a [10–20]% share, followed by Manrex ([0–5]%), Protomed ([0–5]% and Shantys [0–5]%).⁴⁵ Below we consider market shares in the tender and non-tender segments of the market separately.

Market shares in the tender segment

- 8.32 In the tender segment of the market, Venalink and Omnicell/MTS are the only competitors that have been supplying adherence packaging to the three customers that procure through tenders. SurgiChem does not have any market share in the tender segment. As our analysis, which is set out in Appendix F, shows, Venalink had around [30–40]% of the domiciliary tender market in 2011 and 2012, but its share fell to [20–30]% as it lost the Boots tender to Omnicell/MTS, which now has a share of [80–90]% in the tender customer segment.

Market shares in the non-tender segment

- 8.33 For sales to non-tender customers, we considered separately shares of supply in the care-home segment and the domiciliary segment of the

⁴⁵ If we consider market shares by value, Protomed's share is slightly larger and everyone else's share is slightly lower. This is because its products are much more expensive than those of other suppliers. See Appendix F for results on market shares by value.

adherence packaging market.⁴⁶ We observe that Omnicell/MTS and SurgiChem are the two largest suppliers in both segments of the market, with a combined share of [60–70]% in the care-home segment and [70–80]% share in the domiciliary segment. Manrex is the third largest supplier in the care-home segment, and Venalink is the third largest supplier in the domiciliary segment.

TABLE 1 Volume-based market shares in adherence packaging – non-tender segment, 2013

	%		
	<i>Care homes</i>	<i>Domiciliary</i>	<i>All non-tender</i>
Omnicell/MTS	[10–20]	[30–40]	[20–30]
SurgiChem	[40–50]	[40–50]	[40–50]
Venalink	[5–10]	[10–20]	[10–20]
Protomed	[5–10]		[0–5]
Shantys		[0–5]	[0–5]
Manrex (Bunzl)	[10–20]		[5–10]
<i>O+S combined</i>	[60–70]	[70–80]	[70–80]

Source: CMA analysis.

Note: Sales of single-dose adherence packaging are a proxy for sales in the care-home segment (except Protomed), and sales of multidose adherence packaging are a proxy for sales in the domiciliary segment. Sales used to calculate market shares do not include Manrex self-supplied to Boots.

8.34 Over time, from 2011 to 2013, we see that the parties' shares have [X] and Venalink's and Manrex's have [X] (see Appendix F). Shantys' share of supply has [X] in the non-tender domiciliary segment. Protomed's share [X].

Adherence packaging prices and margins

8.35 We have gathered evidence on both the prices of adherence packaging and margins being made in the market, in order to establish what it tells us about the nature and extent of competition.

Prices

8.36 We examined the merger parties' prices for adherence packaging across products and customers and over time (see Appendix B for details). We found that list prices and average prices have remained largely stable for many customers, including some of the largest customers with branded products. The one notable exception to this is when SurgiChem raised the list price of its main multidose product in October 2012, as discussed in paragraph 8.26.

⁴⁶ The details and methodology of this analysis are set out in Appendix F, and the results are summarised in Table 1, which shows suppliers' market shares by volume in 2013. These figures include sales of both card- and plastic-based adherence packaging. If we consider market shares by value, Protomed's share is larger and other competitors' shares are slightly lower in the care-home segment. This is because its products are much more expensive than those of other suppliers.

However, we also observed that a small proportion of customers have had some price reductions on the generic, non-branded products over the period from 2011 to 2013, in particular for [REDACTED] customers.

8.37 We considered the prices paid by customers in different segments of the adherence packaging market, based on the merger parties' data, and we found that:

- (a) Generally, tender customers paid the lowest prices, with prices ranging from approximately [REDACTED] to [REDACTED] pence for multidose packs.⁴⁷
- (b) Omnicell/MTS's and SurgiChem's list prices for generic single-dose packs were [REDACTED] and [REDACTED] pence respectively, while the average price paid by customers were [REDACTED] and [REDACTED] pence respectively. Omnicell/MTS's branded single-dose pack negotiated prices ranged from approximately [REDACTED] to [REDACTED] pence.⁴⁸
- (c) List prices for the parties' generic multidose products were [REDACTED] pence for Omnicell/MTS's product and [REDACTED] pence for SurgiChem's product. The average price paid by non-tender customers was [REDACTED] and [REDACTED] pence respectively. The prices of branded versions ranged from [REDACTED] pence to [REDACTED] pence for Omnicell/MTS's products and from [REDACTED] pence to [REDACTED] pence for SurgiChem's product.⁴⁹

8.38 Appendix B also presents our analysis of competitors' prices. We observe that, overall, competitors' prices have remained relatively stable. Further, with the exception of Protomed, whose Biodose product is several times more expensive than the parties' single-dose or multidose products on a per-pack basis, we see that competitors' pricing is broadly similar to that of Omnicell/MTS and SurgiChem.

Margins

8.39 We considered both the level of, and the trend in, the parties' variable margins. The detailed results of our analysis of margins is reported in Appendix E. In markets where the margins of the merging firms are high, this might indicate that unilateral effects may be more likely, as the value of sales lost as a result of a price increase and then recaptured by the merged firm will be greater, making the price rise less costly. In particular, where there is also

⁴⁷ To put this in context, tender sales amounted to [REDACTED] of Omnicell/MTS's sales of adherence packaging by value in 2013.

⁴⁸ Sales to of single-dose adherence packaging represented [REDACTED]% of Omnicell/MTS's (non-tender) sales by value in 2013, and [REDACTED]% of SurgiChem's.

⁴⁹ Sales to of multidose adherence packaging represented [REDACTED] of non-tender sales by value in 2013: [REDACTED]% of Omnicell/MTS's and [REDACTED]% of SurgiChem's.

evidence that the parties were close competitors, evidence on high margins adds to incentives to increase prices post-merger.⁵⁰ The margins that we have calculated are measured with reference to the cost of goods sold, and do not capture other relevant variable costs such as distribution, administrative or marketing overheads.⁵¹ Therefore the results of this analysis should be interpreted with care.

8.40 Our analysis shows that Omnicell/MTS's overall margin on adherence packaging was [X]%, and SurgiChem's was [X]% in 2013. For sales to non-tender customers, we found that Omnicell/MTS's margins for sales to non-tender customers appear to be [X] at [X]%.

8.41 We also observe that there are differences by product type and thus, approximately, type of end-user:

(a) The average margins that we calculated for Omnicell/MTS (including the three tender customers) for multidose adherence packaging (ie domiciliary end-user) is [X]% if compared to the margins that we calculated for single-dose packaging (ie care-home end-users) of [X]%.

(b) By contrast, the average margins that we calculated for SurgiChem for multidose adherence packaging (ie domiciliary end-user) are [X], at [X]%, than for single-dose average variable margin of [X]% for single-dose packaging (ie care-home end-user). This suggests that SurgiChem might be competing in the care-home segment of the market [X].⁵²

(c) The average margin for ancillary products, such as labels, replacement seals, rollers, templates, dividers, hangers and binders, is [X]% for Omnicell/MTS and at [X]% for SurgiChem.

8.42 These differences in margins may reflect the fact that in some segments of the market there may be different levels of competitive rivalry because of the number and strength of the various competitors in each segment of the market, or for some other reasons (eg relative negotiating strength of customers). We also noted that margins have not changed much over time. The variable margins we have calculated appeared to be [X] – although we put limited weight on this finding given that they do not take into account all variable costs – omitting distribution, administrative and sales force costs.

⁵⁰ CC2, paragraph 5.4.9.

⁵¹ We noted that, for example, for SurgiChem in 2011, cost of sales represented [X]% of the total of cost of sales and operating costs, and that carriage (delivery) costs represented [X]% of the total cost of sales and operating costs.

⁵² Average price analysis suggests that SurgiChem's average single-dose prices ([X] pence) are [X] than Omnicell/MTS's ([X] pence).

Conclusions on pre-merger competition

8.43 In summary, evidence on the way competition in adherence packaging market currently works indicates the following:

- (a) With the exception of adherence packaging procured through tenders by a few large customers, there are no formal contracts in place between suppliers and customers.
- (b) While there are list prices for adherence packaging, [X], and we also observed that while prices have been relatively stable over the last three years, there are customers who have obtained price reductions, possibly through negotiations or threats to switch. The parties told us and we learned from internal documents that discounts are typically given on the basis of volume purchased and/or to match competitors.
- (c) Products are differentiated to an extent based on materials used to produce them (ie card- and plastic-based packs). A significant proportion of customers have a preference for one or another type of adherence packaging. In the care-home segment of the market, in some instances it may be care homes that drive the choice of adherence packaging procured by pharmacies, which may explain why some customers multi-source (ie purchase from a number of different suppliers at the same time).
- (d) There are currently three large customers which procure all or most of their adherence packaging needs through formal tenders. These tender customers appear to be price sensitive.
- (e) For the non-tender segment of the market, there is some evidence to suggest that switching adherence packaging products and/or suppliers is easy as we have not identified significant barriers to switching, and survey evidence suggested that, hypothetically, many small and medium-sized pharmacies would switch suppliers in response to a small increase in price.
- (f) However, in relation to non-tender customers, we found that in practice the switching rates appeared to be relatively low, that there was reluctance to switch unless there were good price or non-price reasons to do so, and that there had been little switching in response to the only recent price increase. Survey evidence suggested that there was little awareness of suppliers and products available in the market.
- (g) For the non-tender segment of the market, we also observed that, with the exception of the SurgiChem price increase for Nomad Clear, prices have

been relatively stable over the last three years, although there are some customers for which prices have decreased. The parties' variable gross margins have been relative stable. Market shares have been largely stable, with the shares of the three largest suppliers (SurgiChem, Omnicell/MTS and Venalink) being reduced slightly as the smaller suppliers have grown share in the care-home (Protomed) and domiciliary (Shantys) segments of the market.

- 8.44 Overall, the market for adherence packaging has been relatively stable. Many non-tender customers tend to be 'sticky', either because obtaining value for money when buying adherence packaging is not a business priority or because they have a strong preference for a particular type of product. However, there also appear to be some customers which are switching suppliers and actively considering alternative suppliers. It is through these 'marginal' customers that competitive pressures on price are exerted most directly. To the extent that suppliers are not able to distinguish perfectly between the 'marginal' customers and the more 'sticky' customers and price accordingly, competitive pressures in the market may also affect outcomes for the more 'sticky' customers and thus the merger could also have some impact on these customers.
- 8.45 We noted that competitive conditions appeared to be different in different parts of the market in terms of the nature of customers and the number and identity of competitors. In particular, we observed differences between supply to customers who have procured adherence packaging via tenders and all the other, non-tender customers. Within the non-tender part of the market, we noted differences in the number and identity of competitors by type of end-user, ie the care-home segment and the domiciliary segment.

9. Assessment of competitive effects of the merger in the adherence packaging market

- 9.1 This section sets out our assessment of the competitive effects of the merger in the adherence packaging market. It starts by explaining how we have carried out this assessment. It then goes on to set out the potential impact of the proposed merger. This includes our analysis of whether the parties competed closely in the adherence packaging market, our assessment of whether existing rivals in the market will act as a constraint and whether there may be additional constraints on the parties from the entry and/or expansion. It then concludes on the potential for a reduction in competitive rivalry in the adherence packaging market as a result of the merger.

Analytical approach

- 9.2 We have considered whether the removal of an existing or a potential competitor in adherence packaging, as a result of the merger, could allow the merged firm to increase the prices of its products or otherwise worsen its offering. Thus our assessment of the competitive effects of the merger focused on the possible unilateral effects in relation to prices, and whether the loss of Omnicell/MTS or of SurgiChem as an independent competitor could be expected to result in an SLC.
- 9.3 In light of evidence on the nature and extent of pre-merger competition discussed in Section 8, we considered that the loss of a close competitor may lead to an increase in prices post-merger for at least those customers who obtained better prices due to availability of the other merger party as an alternative supplier. However, we also considered that the incentives to increase prices, which arise due to a loss of a close competitor, may be counteracted by sufficiently strong constraints from the remaining competitors and, potentially, new entrants into the market.⁵³
- 9.4 We considered evidence on the following in order to assess the potential for a loss of competition:
- (a) the closeness of competition between the merger parties currently and in the future; and
 - (b) the constraints posed by other suppliers in the market, ie the extent of the constraints which would remain after the merger and whether these constraints are likely to change in the future.
- 9.5 Prima facie evidence on the market shares of the parties reported in paragraph 8.31 suggests that they are likely to be important competitors in the adherence packaging market as they are the two largest suppliers with a significant combined market share. However, where products and the offering are differentiated to an extent – as, we find, is the case in the market for adherence packaging – evidence other than the market shares may be more informative on the strength of competitive constraints posed by the different suppliers in the market. Therefore we considered evidence on the nature and extent of competition between Omnicell/MTS and SurgiChem gathered from the parties themselves and from their customers and competitors in order to assess how strongly they competed (and would compete) with each other and with other competitors.

⁵³ See [CC2](#), paragraphs 5.4.6–5.4.12.

9.6 Given the differences that we have observed in the competitors in different parts of the market, we have, as far as the evidence allows us, separately analysed the impact of the merger in the following three segments of the market:

- (a) adherence packaging procured through formal competitive tenders;
- (b) non-tender procurement of adherence packaging for care homes; and
- (c) non-tender procurement of adherence packaging for domiciliary users.

Closeness of competition between the merger parties

9.7 We considered the closeness of competition between the parties in the segments of the market described above in paragraph 9.6. Some of the evidence that we have gathered is pertinent to competition in all segments of the market. We considered this first (paragraphs 9.9 to 9.36 below). This includes evidence on the substitutability of the parties' products; the parties' business models and routes to market; what the parties' have said about their rivals in their own internal strategy documents; the parties' sales data; and the views of customers and competitors.

9.8 We have then gone on to consider other evidence on closeness of competition that is pertinent to particular segments of the market (paragraphs 9.37 to 9.49).

Evidence on closeness of competition in general

Views of the parties on closeness of competition

9.9 The parties argued that they were not each other's closest competitors, because their business models and routes to market were different since:

- (a) Omnicell/MTS focused on large chains (including customers who tendered) and buying groups, and mainly used telesales to reach other customers; whereas
- (b) SurgiChem focused on smaller independent pharmacies and emphasised customer relationships and the provision of additional services, and relied more on individual visits to pharmacies to promote its products; and

- (c) their analyses suggested that customers switched or threatened to switch to the other party to a much lesser extent than would be suggested by their market shares.⁵⁴

Substitutability of the product

- 9.10 We considered the extent to which Omnicell/MTS's and SurgiChem's products are substitutable. The key difference between the two ranges of products appears to be that for Omnicell/MTS's products, the blister packs that hold the medication are enveloped by card, whereas SurgiChem's blister packs are enveloped by plastic. In terms of utility, from an end-user's perspective, they appear to be very similar. We therefore found that the products are substitutable from a demand-side perspective – although as discussed in paragraph 8.16, some customers have preferences for either a card- or a plastic-based product.

Evidence on the parties' business models and routes to market

- 9.11 We considered evidence on Omnicell/MTS's and SurgiChem's business models and routes to market as an indication of whether the parties competed for the same customers in a similar manner. Similarities in the merging parties' business models and routes to market might suggest closer competition between the parties than if they were to differ markedly.
- 9.12 Omnicell/MTS submitted that its promotional strategy and sales efforts were focused on large pharmacy chains, multiple pharmacies and buying groups and the majority of its sales were to such customers. It told us that, in relation to multiple pharmacies and independent pharmacies, Omnicell/MTS promoted its products by means of telesales and individual customer visits. It did not seek any direct contact with care homes and it dealt only with the pharmacies which supplied care homes.
- 9.13 SurgiChem also told us that it had a different business model and a different customer focus model from Omnicell/MTS. SurgiChem submitted that it promoted its products by relying on individual pharmacy visits using its direct sales team, noting that such visits tended to be more effective in gaining business from the small chains and independent pharmacies which accounted for a large part of demand for SurgiChem's adherence packaging products.⁵⁵ It told us that it made appointments for its sales reps to visit pharmacies in

⁵⁴ [Omnicell/MTS initial submission](#).

⁵⁵ For instance, SurgiChem's Annual Operating Plan 2013 states that '[X]'.

person, and then sales reps discussed pharmacies' needs, new products, and additional services such as targeting care homes and providing training.

- 9.14 Overall, the parties suggested that there were some significant differences in emphasis between their strategies. Omnicell/MTS appears to have a greater focus on larger pharmacy chains, whereas SurgiChem's strategy seems to focus more on smaller chains and sole traders. This may explain why their marketing approaches also differ, with Omnicell/MTS focusing on individual customer relationships with bigger customers and telesales with smaller customers. By contrast, SurgiChem used a direct sales team, believing that this was more effective in gaining business from the small chains and sole traders.

Parties' discussion of the closeness of rivals in internal documents

- 9.15 Our review of Omnicell/MTS's internal documents has identified a number of references to SurgiChem, as well as other competitors:

- (a) An Omnicell/MTS presentation on competitor products refers to SurgiChem, along with a number of other competitors including Medi-Clear, Dosebliss, Shantys, Protomed's Biodose, Venalink and Manrex (further details on these suppliers are set out in paragraphs 9.57 to 9.90). It also notes that they compete with plastic pouches, such as those supplied by HD Medi and Robotik.⁵⁶
- (b) A competitor analysis carried out in 2012 by Omnicell/MTS, comparing itself with its main competitors along various dimensions in the care-home segment of the market,⁵⁷ shows that Omnicell/MTS is very similar to SurgiChem across factors which relate to the basic features of the product,⁵⁸ but there are differences between the two in terms of factors relating to the customer relationships and marketing strategy,⁵⁹ with Omnicell/MTS scoring [X]. There are also differences in production

⁵⁶ These competitors are both discussed in greater detail in our analysis of entities which might constitute a competitive constraint on the parties in paragraphs 9.66–9.73.

⁵⁷ The report states:

A strategy canvas was used to compare different factors in the competitor analysis. The competitors analysed were SurgiChem, Venalink, Manrex and Biodose. Fourteen different factors were considered and scored from 0-10. This is relevant for considering the way that Omnicell/MTS compares itself to its competitors on both the features of its product, and the associated services it offers. It also provides an insight into who those competitors are.

The report explains that a 'strategy canvas' was used to compare 14 different factors in the competitor analysis, where each factor was scored from 0 to 10 (with '0' meaning 'no/low' or 'poor' and a '10' meaning 'high' or 'good').

⁵⁸ These include price, quality of product, customer perception of innovation, electronic Medication Administration Records, features and functions of products, customer service, ease of use, eco-friendly packaging.

⁵⁹ [X]

methods, with Omnicell/MTS scoring [REDACTED] on flexibility in terms of branding small runs, and automation.⁶⁰

- (c) We found that minutes of monthly and weekly internal management meetings of MTS Limited from 2011 to 2014 (to April)⁶¹ contain some references to other suppliers of adherence packaging and competition. The [REDACTED] competitors mentioned in a number of documents are [REDACTED], although Ecobliss/Dosebliss and Robotik are also noted in the context of actions following a pharmacy show.

9.16 Our review of SurgiChem's internal documents also identified a number of references to Omnicell/MTS, as well as other competitors:

- (a) SurgiChem's Board Reports from 2011 and 2012 consider only Omnicell/MTS and Protomed in the section on competitors, although the impact on SurgiChem's growth due to competition from Venalink is also mentioned.
- (b) Competitor analysis contained in SurgiChem's 3 Year Plan (2013–15) from November 2012 refers only to Omnicell/MTS and Protomed.
- (c) Our review of SurgiChem's internal sales meetings reports from between 2011 to 2013⁶² found that Omnicell/MTS was mentioned frequently in the reports. The documents referred relatively frequently to SurgiChem [REDACTED]. We also noted there were cases where a customer was multisourcing from both Omnicell/MTS and SurgiChem. When Omnicell/MTS was mentioned in the reports, price relatively often figured as an important factor for competition.^{63,64} A number of competitors other than Omnicell/MTS were also mentioned and, of these, Protomed was mentioned most frequently.⁶⁵

9.17 Overall, based on the evidence available in the parties' internal documents, it appears that both Omnicell/MTS and SurgiChem consider the other merger

⁶⁰ Omnicell/MTS scored [REDACTED] Venalink on most features except on brand awareness (with [REDACTED] scoring higher), customer service (with [REDACTED] scoring lower), customer support (with [REDACTED] scoring higher) and automation (with [REDACTED] scoring much lower). Protomed (Biodose) scored [REDACTED] relative to Omnicell/MTS on most features, except [REDACTED].

⁶¹ For example, actions in relation to non-UK business, machines, transport issues, stock management, storage, other management and sales issues.

⁶² The reports contain, among other things, updates on existing, potential and lost accounts and SurgiChem's sales team's efforts to win other competitors' customers. When looking at the reports, in particular, we looked at how frequently SurgiChem competes with other suppliers, and which suppliers it most frequently competes with.

⁶³ For example, we found an instance where [REDACTED].

⁶⁴ Another example was a [REDACTED].

⁶⁵ Protomed's product Biodose was mentioned with a relatively similar frequency as Omnicell/MTS and competition with Biodose appeared to be close and in some instances the sales report mentions [REDACTED]. Other competitors mentioned in the reports included Venalink, and, somewhat less frequently, Pillmate/Shantys and Boots/Manrex. [REDACTED], but references to Venalink were less frequent than references to Biodose or Omnicell/MTS. Pillmate/Shantys and Boots/Manrex were also mentioned in the response – for example, there were [REDACTED].

party to be among their closest competitors. SurgiChem appears to be one of the competitors that Omnicell/MTS monitors most closely along with Venalink. Omnicell/MTS appears to be one of the competitors that SurgiChem monitors most closely along with Protomed.

Analysis of the parties' sales data

9.18 We analysed the parties' sales records in order to understand on which segments of the market they were focusing their activities. In particular, we looked at the extent to which the parties' sales data suggests that the parties were competing with each other for:

- (a) customers in the care-home and domiciliary segments; and
- (b) customers of different types and sizes.

9.19 Since single-dose packaging is primarily used in care homes and multidose packaging is primarily used by domiciliary patients, we looked at parties' sales of single-dose and multidose adherence packaging in order to understand the extent to which the parties service the care homes and domiciliary segments. We also note that the split between sales of multidose and sales of single-dose adherence packaging is similar for Omnicell/MTS and SurgiChem.⁶⁶

9.20 We examined the parties' customer base. The details of this analysis are set out in Appendix C. In summary, we find that Omnicell/MTS's customer base is [REDACTED] than SurgiChem's with the majority of Omnicell/MTS's sales being made to large pharmacy chains and buying groups, whereas the distribution of SurgiChem's sales is more dispersed.

Views of competitors and customers on closeness of competition between the parties

9.21 We considered what the parties' rivals told us regarding the closeness of competition between Omnicell/MTS and SurgiChem. Venalink told us that Omnicell/MTS was its main competitor because the price was similar, and that SurgiChem was less of a competitor than Omnicell/MTS. It also told us that it tended to hear more about Omnicell/MTS than SurgiChem from its customers, possibly because SurgiChem was more focused on the care-home segment. Shantys told us that its main competitors were Omnicell/MTS, SurgiChem and Venalink. It also told us that MTS and Venalink concentrated on price,

⁶⁶ Our analysis, detailed in Appendix C, shows that around [REDACTED]% of Omnicell/MTS's sales of adherence packaging is multidose, ie for the domiciliary end-user segment, whereas around [REDACTED]% of SurgiChem's sales of adherence packaging are multidose. Thus, [REDACTED] of both parties' sales of adherence packaging are to the [REDACTED] segment of the market.

whereas SurgiChem competed on ease of use and aesthetics, for which Shantys' products were comparable.

- 9.22 We found that customers' views on the closeness of competition between the parties differed. Some customers did not view Omnicell/MTS and SurgiChem as competing closely to supply their adherence packaging needs, often because they had a preference for either a plastic- or a card-based product.⁶⁷ However, other competitors that did not have such strong preferences tended to be more likely to view the parties as closer competitors.⁶⁸

Additional evidence on closeness of competition in tenders

- 9.23 We have set out above findings from a range of evidence on the closeness of competition between the parties in the adherence packaging market in general. This section sets out further evidence, specifically on the closeness of competition between the parties in the tender segment of the market.
- 9.24 As described in paragraph 8.32 above, Omnicell/MTS is the only one of the two parties that currently has a share of supply in the tender segment of the market. We have therefore considered below whether:
- (a) SurgiChem is currently a competitor in the tender segment of the market;
 - (b) SurgiChem could potentially become a competitor in the tender segment of the market, either with its existing plastic products, or with a new card-based product; and
 - (c) what implications, if any, SurgiChem's direct sales of products to customers that mainly buy adherence packaging through tenders has for the closeness of competition in the segment.

⁶⁷ Paydens said that it preferred Omnicell/MTS's card-based product, and would not consider switching to SurgiChem as it did not like the product (although it currently purchased small amounts from SurgiChem). It considered Venalink and Protomed as alternative suppliers for its needs of adherence packaging. Day Lewis, a large pharmacy chain of over 200 stores in the South of England, said that it strongly preferred Omnicell/MTS's card-based product, and that it would switch new stores it acquired to the Omnicell/MTS product. It said it had been approached by, or had itself approached, Venalink, SurgiChem and Protomed as alternative suppliers. PCT Healthcare, which presently uses mainly Omnicell/MTS but also purchases some adherence packaging from SurgiChem, told us that it considered Venalink to be the closest alternative to Omnicell/MTS as the products were virtually identical, followed by SurgiChem, and then pouch-based systems.

⁶⁸ For instance, Rowlands said that Omnicell/MTS and SurgiChem were the main known alternative suppliers for adherence packaging with a proven track record. Norchem told us that Omnicell/MTS's and SurgiChem's products were different and each had advantages. [X] Waremooss/Kamsons, a pharmacy chain of 53 pharmacies currently purchasing from Omnicell/MTS, told us that Venalink and SurgiChem were the other suppliers it had approached or had been approached by.

- 9.25 The parties submitted that Omnicell/MTS did not overlap in the supply of adherence packaging to tender customers as SurgiChem currently did not supply adherence packaging pursuant to tenders of the large chains.^{69,70}
- 9.26 We reviewed recent examples of tender exercises for adherence packaging. We did not identify any examples of SurgiChem competing in tenders against Omnicell/MTS, although we did note that SurgiChem showed some interest in the [X] tender (this is discussed in further detail in paragraph 6.11). However, SurgiChem subsequently declined to participate in that tender.
- 9.27 We have therefore gone on to consider whether SurgiChem could become a close competitor in the tender segment of the market for adherence packaging with either a plastic-based or a card-based product.

Entering tenders with a plastic-based product

- 9.28 All three tender customers indicated to us that there was no intrinsic reason why they would not consider a plastic-based product or a bid from SurgiChem. They told us that aside from cost considerations, it was their 'business decision' or preference/habit to use a card-based product, that they believed that card-based, as opposed to plastic-based, were disposable and hygienic, or they believed that SurgiChem was constrained by its ownership (Bupa) from bidding in certain tenders.
- 9.29 However, while in theory SurgiChem could opt to compete in future tenders with a plastic-based product, it is unlikely that SurgiChem would be a credible competitor with such a product because of the higher production costs of producing plastic products. The cost of SurgiChem's main multidose adherence packs (Clear and Clear 2) are [X] higher (at [X] pence for Clear 2 and [X] pence for Clear) than the cost of Omnicell/MTS's card-based multidose product (the generic version costs [X] pence to produce).^{71,72}
- 9.30 Tender customers negotiate heavily on price and, given that SurgiChem's plastic-based products are more expensive to produce, it is unlikely that

⁶⁹ Omnicell/MTS initial submission, p16.

⁷⁰ We have also observed that, while SurgiChem does not participate in tender exercises, it nevertheless supplies adherence packaging to both [X] and Lloyds Pharmacy, on an ad-hoc basis rather than on a tender basis. Omnicell/MTS sales to Boots and Lloyds Pharmacy amounted to around £[X] million in 2013, whereas SurgiChem's sales to [X] and Lloyds Pharmacy amounted to only £[X] million.⁷⁰ We asked why tender customers also buy SurgiChem's plastic-based adherence packaging in addition to a card-based product. Lloyds Pharmacy told us that it purchased some adherence packaging from SurgiChem because some customers (end-users) preferred the SurgiChem product, so it would supply it. Therefore, the fact that SurgiChem also supplies those customers that run tender processes for adherence packaging on an ad-hoc basis does not necessarily indicate that the parties competed in tender markets.

⁷¹ See Appendix E.

⁷² In the extreme, [X] pays for its Omnicell/MTS card-based multidose product ([X] pence) [X] of its Clear or Clear 2. See Appendix B.

SurgiChem could compete closely with Omnicell/MTS, or indeed Venalink (the other card-based provider) based on its current production costs of its plastic-based product.

Entering tenders with a card-based product

- 9.31 We have also considered whether SurgiChem could potentially compete closely with Omnicell/MTS by supplying a card-based product.
- 9.32 We considered the costs at which SurgiChem would have to be able to produce its card-based product in order to be competitive. We have been told that the machinery required to produce the card for card-based packs is bespoke (that is, unlike a thermoforming machine used to produce plastic-backed packs where changing the mould would allow it to be used to produce other products, it cannot be used for a variety of other purposes) and also quite expensive.⁷³ This would suggest that the unit price of a card-based pack is heavily dependent on volume.⁷⁴ Therefore, without a very high throughput, the cost of purchasing and running the machinery to produce card-based packs, together with the cost of purchasing the relevant raw materials (where, Omnicell/MTS told us, very high volumes enabled large-scale producers to achieve material discounts), would result in a price per unit that would be uncompetitive. The parties also told us that with production outsourced, the end price needed to include both the manufacturer's margin and SurgiChem's, which might put SurgiChem at a disadvantage to a vertically integrated supplier such as Omnicell/MTS or Venalink.⁷⁵
- 9.33 SurgiChem estimated that, for the card-based product that it has recently developed, the cost price per unit (including delivery to customers) was [REDACTED] pence. When compared with the price paid by, for example, Boots and Lloyds Pharmacy following their recent tenders ([REDACTED] and [REDACTED] pence per card respectively), it is clear that SurgiChem would have been unlikely to be competitive.

⁷³ MacPac told us that it had been to dozens of UK printers to see who could make card-based packs, including getting the foil to stick to the board and then adding an adhesive back with a sealed paper on it, and none were interested. It said that to do so required very large, dedicated machinery, and it would cost millions to get a printing machine that could make the volumes required by the major suppliers of adherence packaging.

⁷⁴ By way of indirect comparison, MacPac, which supplies plastic trays to SurgiChem, told us that a new entrant supplying plastic-based packs would need to be selling in the low millions of units per year in order to be able to achieve a competitive unit price.

⁷⁵ The indication that there are significant economies of scale in the production of the card is consistent with the way in which existing manufacturers organise their production. MTS produces its cards in the USA, where the machines are also used to supply cards for other geographical markets. In total, Omnicell/MTS manufactured approximately [REDACTED] million cards in 2013, of which approximately [REDACTED] million were sold in the UK. Likewise, Venalink (the other major supplier of card-based packs in the UK) produces its cards at its parent company in Canada where, similarly, the same machines are used to produce cards for other geographical markets.

- 9.34 We also considered the evidence available on whether SurgiChem intended to compete to supply card-based packs to large pharmacy chains. SurgiChem told us that it had decided, as a matter of strategy, not to compete in the supply of adherence packs to customers purchasing via tender or other large pharmacy groups (despite the fact that it had originally intended to participate in the [X] tender). We note that SurgiChem has not provided us with any internal documentation or communication evidencing this decision. However, we also note that in SurgiChem's three-year plan (November 2012), a number of growth initiatives which the company intended to pursue were outlined (such as [X]), but card-based packaging was not listed among these growth initiatives.⁷⁶ The Bupa strategy document on SurgiChem from April 2013 similarly lists growth options for SurgiChem but these did not include card-based packaging.

Conclusion on closeness of competition between the parties in tenders

- 9.35 Overall, the evidence and analysis we have to date suggests that SurgiChem was not in competition with Omnicell/MTS in tenders of the three large customers (Boots, Lloyds Pharmacy and NHS Scotland) previously. We also considered that SurgiChem is unlikely to compete with Omnicell/MTS in future tender exercises. The evidence available suggests that SurgiChem's card-based product would not be price competitive and that tendering with a card-based product is not part of SurgiChem's strategic or business focus.
- 9.36 Given this conclusion on the lack of close competition between the parties for tenders and the lack of evidence to suggest that they may compete closely in the future, we concluded that the merger is unlikely to lead to a reduction in competitive rivalry in this segment of the market.

Additional evidence on closeness of competition in the non-tender segment

- 9.37 We also considered other evidence on the closeness of competition that is solely relevant to the non-tender segment of the market, including evidence on switching in the segment and responses to our customer survey, which focused on small and medium-size pharmacies. This has been considered, alongside findings from a range of evidence on the closeness of competition between the parties in the adherence packaging market in general, in order to draw conclusions on closeness of competition between the parties in the non-tender segment of the market.

⁷⁶ We note that, since the date of the strategy document, SurgiChem has continued to develop its plans in a number of these areas, such as [X] etc.

Evidence on switching and customer diversions in the non-tender segment of the market

9.38 We examined evidence available on customer switching between Omnicell/MTS and SurgiChem, including analysis performed by PwC submitted by the parties,⁷⁷ and our own analysis of the parties' sales data⁷⁸ (see Appendix C for details), both of which suggested that rates of switching between the parties are [X]. However, the assumptions underlying this analysis means that the switching rates are likely to be underestimated, and PwC analysis covers only a fraction of the market (single-store pharmacies). Given our reservations about both sets of analysis, we do not think much weight should be given to this evidence in terms of determining the closeness of competition between the parties in the non-tender segment of the market.

Survey evidence on closeness of competition

9.39 A number of the questions in our customer survey generated responses that are relevant to the consideration of closeness of competition between the parties in the non-tender segment of the market.⁷⁹ Further analysis is provided in Appendix D.

9.40 Customers surveyed were asked about diversion in the hypothetical case that their current supplier increased prices or shut down. Among those who specified a diversion destination(s) (it was 49 out of 143 Omnicell/MTS customers, and 95 out of 279 SurgiChem customers), the most frequently cited alternatives were the other merger party and Venalink, although Biodose (Protomed), Manrex, Pillmate/Shantys and Sigma⁸⁰ also featured.⁸¹ Venalink was the most frequently mentioned by Omnicell/MTS customers (24 mentions), followed by

⁷⁷ We reviewed an exercise carried out by PwC looking at switching. PwC's analysis estimated the diversion ratio from Omnicell/MTS to SurgiChem for sole pharmacies to be [X]%, and from SurgiChem to Omnicell/MTS to be [X]% (depending on assumptions/scenario). We note, however, that this analysis is based on a limited number of pharmacies, and relies on some unrealistic assumptions (such as any pharmacy not purchasing adherence packaging from either Omnicell/MTS or SurgiChem is purchasing from someone else). We therefore believe that this analysis is likely to underestimate switching between the two parties.

⁷⁸ The details of our analysis are set out in Appendix C. Our own analysis of parties' sales data suggests that annually, around [X]% of Omnicell/MTS's lost customers divert to SurgiChem, and around [X]% of SurgiChem's lost customers divert to Omnicell/MTS. The various caveats and limitations of this analysis mean that switching between the parties could be understated in the results described above and that therefore limited weight should be put on this evidence.

⁷⁹ The customer survey was conducted among customers of Omnicell/MTS and SurgiChem, other than those who tendered; the few largest customers with which we engaged separately were also excluded from the eligible sample.

⁸⁰ Sigma is a distributor which appears to sell both SurgiChem's products (Sigma Plc is SurgiChem's [X] largest customer by value), and Shantys' products.

⁸¹ Customers who indicated that they would divert 100% of their spend in response to a hypothetical 5% price increase at an earlier question were not actually asked the question on forced diversion but it has been assumed that, had they been asked the question on closure, they would have switched their spend and to the same suppliers identified at the price diversion questions. Responses have therefore been imputed accordingly and included in the results. See [Customer Survey report](#).

SurgiChem (18 mentions). Omnicell/MTS was the most frequent mention by SurgiChem's customers (30 mentions), followed by Venalink (27 mentions). However, most customers of both parties who indicated that they would divert spend did not know which supplier(s) of adherence packaging they would divert to (more details are provided in Appendix C and the Customer Survey report prepared by the GfK). It is reasonable to assume that for these customers the distribution of diversion to other suppliers, should they actually need to divert, would follow that of survey respondents who did state alternative suppliers – although this assumption affects that amount of weight that we are able to place on this evidence.

- 9.41 The survey asked those customers who bought products directly from a producer and obtained some kind of discount/promotion whether they used other suppliers' prices to negotiate prices, and, if so, which those suppliers were. The base numbers for this subset of customers are too small to allow us to assign much weight to the results (21 Omnicell/MTS customers and 28 SurgiChem customers), but we noted that the most frequently mentioned supplier for customers of each party was the merger party, with Venalink also featuring.
- 9.42 The survey also asked all customers which other suppliers they would consider using (allowing the respondents to mention multiple options). The responses indicated that the alternative merger party was considered most often, with Venalink being the second most frequently mentioned. Biodose (Protomed) and Shantys/Pillmate also featured. However, the majority of customers either did not consider any one supplier specifically, or did not know which supplier they would consider using.
- 9.43 Further, the survey asked which suppliers customers have used in the last three years but do not use currently (ie from which suppliers they have switched). Of the 145 Omnicell/MTS customers, 11 said they had used SurgiChem and 9 Venalink. Of the 278 SurgiChem customers, 9 said they had used Venalink and 9 Omnicell/MTS.⁸² This indicates a low amount of switching between the parties themselves and from Venalink. Further, the vast majority of responses (over 80%) mention 'None specifically' and 'Don't know', which makes it difficult to attach any weight to this evidence in terms of measuring switching between the suppliers.

⁸² There were also a few mentions of Biodose, Manrex, Pillmate/Shantys and Sigma.

SurgiChem's development of a card-based product for the non-tender segment

- 9.44 As discussed in our consideration of the counterfactual, in paragraph 6.8, SurgiChem has developed and is about to start offering a card-based adherence packaging product in the UK. This is a multidose product that would be aimed at domiciliary patients; however, SurgiChem said that producing a single-dose card-based product would not be difficult and would only require new tooling.
- 9.45 We have therefore considered whether the anticipated merger might result in a loss of potentially closer competition with Omnicell/MTS in the non-tender segment, when SurgiChem launches its card-based product to compete with Omnicell/MTS's.
- 9.46 Card-based adherence packaging represents approximately [X] of the UK's non-tender disposable adherence packaging market by value. While SurgiChem is already present in the non-tender segment of the market with its plastic-based products, for those customers which strongly prefer card-based products, SurgiChem may be able to compete more closely with a card-based product. SurgiChem told us that the new card product was intended to fill a gap in its portfolio as some pharmacies might prefer a card-based product or might be required to supply a card-based product to care homes. It submitted that it expected to use the card product as [X], and would still primarily promote its Nomad Clear product range.
- 9.47 On the basis of SurgiChem's projections (as set out above in paragraph 9.33), its card-based product would, at [X] pence per unit, be more expensive to produce than its plastic-based products (eg [X] pence for Nomad Clear and [X] pence for Nomad Clear 2 – see Appendix E), and [X] expensive as Omnicell/MTS's cost price for its multidose card-based pack of [X] pence (see Appendix E). Thus SurgiChem's card-based product would not be price-competitive unless it managed to achieve further economies of scale in the future.
- 9.48 This evidence suggests that, while SurgiChem would be able to supply and compete for the part of the non-tender segment of the market which strongly prefers card-based products, there are questions as to how credible a competitor to Omnicell/MTS it would become with its card-based product, given its significantly higher cost price. Thus, preliminarily, it appears that, while SurgiChem would have competed with Omnicell/MTS in the non-tender segment with its card-based product, it is unlikely that it would be a close competitor in this particular part of the market (ie for customers which strongly prefer a card-based product) in the near future.

- 9.49 Nevertheless if, as suggested by SurgiChem, its card-based product constituted [X] that would primarily be used to promote its Nomad Clear product range, then this development appears to be an indicator that SurgiChem intends to compete with Omnicell/MTS, and for that matter Venalink, for customers that currently use card-based adherence packaging, either with its new card-based product or with its existing plastic-based product.

Conclusion on closeness of competition in the non-tender segment of the market

- 9.50 We found that the parties are not competing across the non-tender segment of the market as closely as their market shares might suggest. We identified some differences in the sizes of customers that the parties have been successful in winning. There are also differences in the way that the parties structure their supply chains and in their routes to market. Further evidence from our survey, questionnaires and third party hearings indicated that a significant proportion of customers have a strong preference for either a card-based or a plastic-based product.
- 9.51 Nevertheless, we found that the parties do compete closely for a significant proportion of non-tender customers, and that there is potential for the anticipated merger to lessen competition for these customers. Responses to our survey, questionnaires and third party hearings identified a significant proportion of customers who consider the parties to be competing closely. References in the parties' internal documents also suggest that they consider each other to be close competitors. Further, SurgiChem's recent development of a card-based product suggests that it intends to compete with Omnicell/MTS for customers that currently use card-based adherence packaging.
- 9.52 We also note that there could be an asymmetry in the competitive constraint that the two parties currently place on each other, with the results of survey suggesting that Omnicell/MTS may be a greater competitive constraint on SurgiChem in the non-tender segment than SurgiChem is on Omnicell/MTS. This is considered in further detail in paragraph 9.93, after considering the other competitive constraints in the market.

Other competitive constraints

- 9.53 This section considers the ability of existing competitors currently competing in the non-tender domiciliary and non-tender care-home segments of the market to act as competitive constraints on the merged entity in order to mitigate the potential lessening of competition in the segments of the market where we have found that the parties compete most closely (the non-tender domiciliary and non-tender care-home segments).

- 9.54 We then go on to consider the extent to which entry and/or expansion by other competitors may act as an additional competitive constraint in these segments. Our competitive assessment draws on these sets of evidence together to conclude on the likelihood and scale of a lessening of competition.

Existing competitive constraints in the non-tender part of the market

- 9.55 In order to be a credible competitive constraint, a competitor would need the following characteristics:
- (a) a product or products of comparable quality to the parties, in terms of ease of use, robustness and aesthetic appeal;
 - (b) the ability to be able to produce and sell the product or products at a price that would make it a constraint on the parties' prices; and
 - (c) the ability to market and sell its product or products to a sufficient proportion of customers in the market, or a segment of the market, for it to constrain the parties' behaviour.
- 9.56 We have identified a number of other competitors in the non-tender segment of the adherence packaging market, in addition to the parties (see paragraph 4.1 for our description of these competitors). We consider the credibility of each of these competitors as a constraint below. We begin by considering the only competitor that may be able to provide a competitive constraint on the merged entity across all non-tender customers, Venalink. We then go on to consider competitors that could provide constraints in particular segments of the non-tender part of the market.

Venalink

- 9.57 There is strong evidence to suggest that Venalink is a credible constraint on the parties across the non-tender adherence packaging segment. In particular, evidence suggests that Venalink is a strong competitor to Omnicell/MTS, probably its closest competitor based on similarities in their products, supply chains and the responses of Omnicell/MTS's customers to our customer survey. It is also a competitor to SurgiChem for non-tender customers.
- 9.58 In terms of Venalink's ability to price its products competitively, we note that it is in a position to generate significant economies of scale. It supplied approximately [REDACTED] packs in 2013 in the UK, with its total sales of adherence packaging and ancillaries amounting to £[REDACTED]. Further, it has a vertically integrated approach to manufacturing that seems to be necessary to produce card-based products at a competitive price per unit (see paragraph 9.32 for

further discussion of this). We also found that there do not appear to be any capacity constraints to Venalink increasing production, if required, to meet further demand.

- 9.59 We found that Venalink offers a credible constraint across the non-tender segment, although it may be a stronger constraint for some types of customers, ie those that prefer a card-based product, than others. Like the parties, Venalink makes the most of its sales in the domiciliary segment. In 2013, around [X]% of its sales in the non-tender segment of the market were of multidose packaging intended for domiciliary patients compared with [X]. Venalink told us that, having lost the Boots tender business to Omnicell/MTS in late 2012/early 2013, [X]. We would therefore expect Venalink to compete even more strongly in the non-tender segment of the market in the future.

Other competitors in the non-tender domiciliary segment

- *Shantys*

- 9.60 Shantys supplies plastic-based multidose adherence packaging aimed at the domiciliary segment of the market. The product it supplies would not offer any constraint on the parties in the care-home segment. SurgiChem told us that Shantys' product was similar to its own adherence packaging products. There is little suggestion of any issue with the quality of the product, the one exception being that PharmAssist thought that Shantys' products were very similar to SurgiChem's, but were cheaper and of lower quality.
- 9.61 We considered Shantys' ability to supply the product at a competitive price. Shantys told us that for the small pack, the list price was [X] pence and that the wholesalers/distributors could [X]. This appears to be comparable to SurgiChem's list price of [X] pence (for Nomad Clear). Shantys sold around [X] units of plastic-based disposable adherence packaging in the UK in 2013 (worth £[X]), a significant increase on its 2011 sales. Based on evidence provided by Macpac, the thermoformer used by SurgiChem, a volume of about a million units per year is sufficient to realise the available economies of scale for the supply of plastic products. Further, there do not appear to be any capacity constraints to Shantys increasing production, if required, to meet further demand.
- 9.62 We considered whether Shantys has the ability to market and sell its product or products to a sufficient proportion of customers in the non-tender domiciliary segment of the market for it to constrain the parties' behaviour. Our analysis suggests that it had a [X]% share of supply in this segment of the market in 2013. However, Shantys told us that it sold to wholesalers and distributors in the UK, [X], but not direct to pharmacies, which might limit the

constraint it places on the parties in respect of those customers that prefer to buy directly from a supplier. On the other hand, Shantys does take other steps to market its product: it sends out flyers to all independent pharmacies, and it advertises in its wholesaler/distributor marketing and promotion brochures. Shantys/Pillmate and Sigma (which distributes Shantys' products) were mentioned relatively often in the various customer survey questions.

9.63 We considered other evidence on the extent to which Shantys might currently be seen as a competitive threat by the parties. Omnicell/MTS's internal documents (eg board meeting minutes) do not mention Shantys/Pillmate a great deal, although its price-approval reports include a single mention of Shantys in relation to [X]. Venalink said that it was aware of advertising from Shantys/Pillmate, but it had not encountered Shantys in the marketplace. On the other hand, SurgiChem's sales reports mention Shantys/Pillmate a number of times in relation to winning and losing customers, albeit not as often as Omnicell/MTS or Biodose.

9.64 We note that, until recently, Shantys has had a limited presence in the adherence packaging market and as a result it does not have the same profile among customers or competitors as some of the more established players. However, it appears to have a credible product, to have reached the type of sales volumes that generate economies of scale, and has grown its market share strongly over recent years, albeit from a low base.

9.65 On the basis of the evidence available, we found that Shantys is in a position to offer a credible competitive constraint in parts of the domiciliary market, competing strongly for customers who buy through wholesalers, distributors and buying groups (given that it does not yet have a sales force). As it offers a plastic-based product, it is likely to be competing for those customers who prefer plastic-based products or those without a strong preference for card. We will consider the potential for Shantys to expand further in paragraph 9.131.

- *Suppliers of pouch-based systems*

9.66 We have identified two pouch-based manufacturers currently operating in the UK market. HD Medi and Medication Management supply pouch dispensing machines and consumables (and some other related products) for multidose adherence packaging in pouches.

9.67 We considered whether these suppliers had the necessary economies of scale to be able to sell at a competitive price point. While neither company has made significant inroads into the UK market to date, HD Medi and Robotik (which supplies machines to Medication Management) are both large

suppliers of pouch machines in Europe and elsewhere. HD Medi claims to have approximately 5,000 machines installed worldwide⁸³ and Robotik more than 1,400.⁸⁴ Therefore both companies are likely to have achieved the necessary economies of scale to price their systems competitively.

- 9.68 To be able to offer pouch-based packaging to its patients, pharmacies must purchase an automated filling machine (together with the appropriate consumables). This upfront investment might put some pharmacies off, as the parties' systems do not require such investment. Rowlands Pharmacy (Rowlands) told us that it had considered purchasing a pouch-based system, but its set-up costs for the system would have been approximately £100,000. The HD Medi machine cost Norchem £[REDACTED] to purchase, and consumables cost £[REDACTED] per roll of pouches, with around [REDACTED] rolls being used annually. The cost of the cellophane rolls means that a roll of 28 pouches (equivalent to a weekly 'pack' of four multidose pouches per day) is priced at [REDACTED] pence. The cost is therefore broadly comparable to prices paid for card- and plastic-based blister packs after the initial capital outlay on a filling machine.
- 9.69 However, we note that a simple comparison of the cost per unit of pouches compared with the parties' adherence packaging might ignore some of the advantages of a pouch-based system. These include a reduction in the labour costs required to fill adherence packaging and the potential to reduce the number of dispensing errors.⁸⁵
- 9.70 To the extent that pouch-based manufacturers offer a constraint, it is more likely to be greater for chains that provide a significant number of prescriptions in adherence packaging, which would make the upfront investment required more justifiable. There are, however, also some indications that the systems might be cost effective even for smaller chains too.⁸⁶
- 9.71 We considered whether the suppliers of pouch-based systems had the ability to market and sell its product or products to a sufficient proportion of customers in the non-tender domiciliary segment or the non-tender care-home segment of the market for it to constrain the parties' behaviour. There is

⁸³ www.hdmedi.eu.

⁸⁴ www.robotiktechnology.com.

⁸⁵ Medication Management said that it sold and negotiated directly with pharmacies, and that the process always involved a consideration of the existing manual filling system, and sometimes involved a consideration of a competing pouch-based product. One of HD Medi's customers, Norchem (which also uses Omnicell/MTS and SurgiChem products), said that pouches would be used in all of its 20 pharmacy branches. It said that it used the pouch-based system because of efficiency savings in centralisation and automation, improved accuracy, safety for customers, and differentiation from other competitors.

⁸⁶ Medication Management said that around [REDACTED]% of its sales had been to small and medium-sized pharmacy chains (pharmacies with 5–250 stores), and the rest had been to 'micro' pharmacy customers (pharmacies with fewer than five stores). It said that it had sold [REDACTED]. HD Medi has two customers in the UK: Norchem, which uses the pouch machine for around 1,000 patients, and Hellesdon Hospital, which uses the pouch machine for around 1,100 psychiatric patients.

limited evidence available to suggest that they have such ability – as take-up in the UK has been limited to date – although we understand it is growing.

- 9.72 In terms of the views of the parties, Omnicell/MTS submitted that, while pouches were not yet prevalent in the UK, they were becoming increasingly attractive where pharmacies were moving towards more automation. SurgiChem submitted that pouches were used as part of automation and thus may be used by larger pharmacies only, as pouch-based systems required a purchase of an expensive machine.
- 9.73 Overall, there is limited evidence to suggest that pouch-based manufacturers currently represent a credible competitive constraint on the parties in the domiciliary or care-home segments of the market. We considered that there is some doubt as to whether there will be widespread take-up of pouch-based systems in the UK, given the upfront expense for the pharmacy, which is not directly remunerated by the NHS. However, we also note that there appear to be signs that a small number of pharmacies that use adherence packaging more frequently have considered the solution worth the investment overall. We have considered their potential future impact of pouches further as part of our consideration of barriers to expansion (paragraph 9.131).

- *Protomed*

- 9.74 Protomed supplies a plastic-based product (Biodose) that is differentiated from other products on the market. Protomed has been successful in achieving growth with its product. After entering the market in 2008, by 2013 it had grown to the extent that it supplied nearly [X] units (double the sales it had in 2011). It had a market share of [5–10]% by volume in the care-home segment of the market in 2013.
- 9.75 The Biodose product is significantly more expensive per unit than its rivals. Protomed said that its Biodose product was more expensive than other adherence packaging, at £[X] per package list price, and was not directly comparable to other products as it offered additional features. Further, the use of its system required a heat-sealing machine, at a cost of £[X] or a rental fee of £[X] per month, and use of software for tracking and labelling the medication (at a cost of £[X] per year for a full licence). Protomed said that its product was a premium product which was more expensive, and not all pharmacies wanted to use it for that reason. For this reason, it is difficult to envisage Protomed providing a significant constraint on the pricing of the merging parties, particularly given that (as explained in paragraph 9.76) it markets to care homes rather than to pharmacists. Care homes are unlikely to be particularly sensitive to price as the pharmacists pay for the product. However, we also note that, unlike other adherence packaging marketed at

care homes, Biodose is a multidose rather than single-dose product and fewer units of its packaging could be required per patient than would be used with a single-dose system such as those supplied by the parties. This might mean that Biodose could be closer to being comparable on a cost per patient basis than suggested by the price per unit of its product.

- 9.76 Protomed's marketing model involves promoting products directly to care homes and introducing the care homes to pharmacies that can supply them with Biodose. It sells direct, mainly to independent pharmacies and smaller chains, rather than using wholesalers or distributors. This approach appears to have enabled it to grow reasonably rapidly.
- 9.77 Protomed has been a rapidly growing competitor in the care-home segment of the market. It is, however, significantly more expensive than the parties' products on a per-pack basis – although we also note that as a multidose product it could be used in place of more than one of the parties' single-dose products in a care-home context. We therefore concluded that Protomed may have a limited constraint on the prices that the merged entity can charge.

- *Manrex/Boots*

- 9.78 While Boots self-supplies with Manrex products, it also supplies Manrex to independent pharmacies through the wholesaler Bunzl. Boots told us that it did not restrict in any way which pharmacies could purchase Manrex. Manrex, supplied to independent pharmacies through Bunzl, is estimated to have around [10–20]% market share by value in the care-home segment.
- 9.79 Manrex has achieved a significant and relatively stable share of the care-home segment and there is little evidence to suggest that the product is not of comparable quality to the parties' or that it is not price competitive.
- 9.80 As to whether Manrex has sufficient visibility to customers in the care-home segment of the market, we note that the product is sold through only one wholesaler, although this does not appear to have been a barrier to the product becoming an established competitor.
- 9.81 Overall, Manrex appears to have a credible product, which is competitively priced, and a marketing approach which has allowed Boots to sell its product to a sufficient proportion of customers in the segment of the market to be a constraint on the parties' behaviour.

MultiMeds

- 9.82 MultiMeds, currently supplied by Medication Systems Limited (MSL), is a plastic-based multidose adherence packaging product, consisting of a plastic tray with individual pods. It is similar in appearance to Biodose, but can be used for solid medication only. MSL noted that presently its sales of MultiMeds were less than £[REDACTED] per month,⁸⁷ and that it supplied to around [REDACTED] independent pharmacies (out of total of around 14,000 pharmacies), which means it is currently a negligible player in the adherence packaging market.
- 9.83 In terms of pricing, a MultiMeds unit costs around [REDACTED] pence, which is less than Biodose but around [REDACTED] as expensive as standard blister packs used in care homes. However, MSL noted that fewer units of its packaging would be required per patient than if compared with the traditional single-dose systems, which meant that MultiMeds might be comparable in cost overall. Thus, while more expensive than Omnicell/MTS's and SurgiChem's adherence packaging, MultiMeds could potentially still be attractive from a price perspective.
- 9.84 None of the survey customers mentioned MultiMeds as an alternative supplier. None of the customers we spoke to, or from whom we received questionnaire responses, mentioned the product or the supplier. Further, it was not identified as a competitor by any of the merger parties' main competitors, although Venalink mentioned MultiMeds as a new product in the market. In a few places in the parties' submissions, they noted MultiMeds as a competitor, but it did not appear anywhere in the parties' internal documents and the parties have not strongly argued that MultiMeds is a credible competitive constraint.
- 9.85 MSL told us that, were the merger between Omnicell/MTS and SurgiChem to go ahead, it would launch a product designed to compete directly with SurgiChem's in the domiciliary patient segment.
- 9.86 Thus, it appears that MultiMeds is a recent entrant and potentially growing supplier in the UK market for adherence packaging. However, it is not obvious that it would pose a significant competitive constraint on Omnicell/MTS or SurgiChem in the near term.

⁸⁷ Given that the size of the market is around £[REDACTED] million, this would mean its share is at most [REDACTED] %.

Other competitors identified

- 9.87 SurgiChem submitted that it increasingly faced competition from Chemistree, an independent pharmacy chain, which had begun to self-supply adherence packaging for care homes, which it sourced from [REDACTED]. SurgiChem believed that Chemistree [REDACTED]. However, we noted that no third parties and no customers in the survey mentioned Chemistree and therefore conclude that it is not currently a competitive constraint.
- 9.88 In some instances in the survey a plastic-based adherence packaging product called MediPack has been mentioned. However, we have not seen any evidence from the main or third parties that this is an active competitor in the marketplace. Venalink said that MediPack was a Dutch company and it had a product comparable to existing ones (we noted that the website showed a plastic-based product), but Venalink had not seen it much in the marketplace. It could refer to a Shantys product, as its disposable product used to be called Medipack. Given its limited visibility in the market, this product is unlikely to be a competitive constraint.
- 9.89 In terms of other pouch-based system suppliers in addition to the two suppliers discussed above, we have seen mentions of KLS from some third parties including Medication Management and [REDACTED]. However, we have seen no evidence that they are active in the UK.
- 9.90 Customers in the survey also mentioned some other alternatives which we have not identified in the course of our evidence gathering, such as Medi-dose (which appears to be a US-based company). Other products mentioned included suppliers of reusable packaging, such as W&W and Pivotell. However, none of these alternative products were mentioned with sufficient frequency to indicate that they could currently constitute a significant competitive constraint on the parties.

Provisional findings on constraint provided by other competitors

- 9.91 We considered the strength of other competitors to the parties in the non-tender domiciliary segment. We found that Venalink is an established player, with an incentive to grow its market share in the non-tender segment of the market, and would act as a credible competitive constraint on the merged entity in this segment. We also found that Shantys had emerged as another credible constraint, although we note that Shantys' current marketing approach may not currently enable it easily to reach customers that prefer to buy their adherence packaging directly from a supplier. We considered that there is some doubt as to whether there will be a widespread take-up of pouch-based systems in the UK, given the upfront expense for the pharmacy,

which is not directly reimbursed by the NHS. However, this may change in the future as a small number of pharmacies that use adherence packaging more frequently have considered that the solution is worth the investment overall. Therefore, we have found that there are at least two competitors to the parties in the domiciliary segment of the market that constitute significant competitive constraints on the merged entity.

- 9.92 We considered the strength of competitors other than the parties in the non-tender care-home segment of the market. We considered that Venalink, for the reasons discussed above, was a credible competitive constraint on the merged entity in the care-home segment of the market. Manrex is also an established long-term competitor in this segment. While its product is only available to pharmacists, other than Boots, through one wholesaler, this has not prevented Manrex from establishing a significant share of the care-home segment. We also considered the competitive constraint offered by Protomed, which has grown very successfully in recent years. The product is significantly more expensive than the parties' products on a per pack basis, although we also note that as a multidose product it could be used in place of more than one of the parties' single-dose products in a care-home context. We therefore concluded that Protomed may have a limited constraint on the prices that the merged entity can charge. We considered that, in the same way as in the non-tender domiciliary segment, there is uncertainty over whether pouches could be a credible constraint in the non-tender care-home sector. We therefore identified three established rivals to the parties in the care-home segment of the market. Two are likely to be significant competitive constraints, whereas the likelihood of Protomed constraining the parties' prices is lower.
- 9.93 We considered the asymmetry in the competitive constraint that the two parties appear to place on each other. Our analysis of closeness of competition suggested that Omnicell/MTS may be a greater competitive constraint on SurgiChem in the non-tender segment than SurgiChem is on Omnicell/MTS. Our findings on the strength and closeness of other competitors to the parties in the adherence packaging market appear to go some way towards explaining this asymmetry (paragraphs 9.53 to 9.86). Venalink has a very similar card-based product to Omnicell/MTS; it also prices its products similarly, targets the same segments of the market and has a similar supply-chain structure. It therefore appears individually to constitute a greater constraint on Omnicell/MTS than any of the alternative products to the parties do on SurgiChem.
- 9.94 This finding might indicate that, should the merger proceed, SurgiChem's current customers could be more likely to be adversely affected than Omnicell/MTS's. However, while we have not identified an alternative to SurgiChem that competes as closely with it as Venalink does with Omnicell/

MTS across the adherence packaging market, we have found that there are a number of competitors other than Omnicell/MTS that compete closely with SurgiChem in different parts of the market: Shantys in the domiciliary segment of the non-tender market, and Manrex (and to some extent Protomed) in the care-home segment.

- 9.95 The parties currently have the largest market shares in the adherence packaging market and therefore the greatest level of name recognition. However, prices have not risen recently for a significant proportion of customers, and many customers may not have explored the alternatives to their current suppliers. If, however, the merged entity were to raise its prices or the quality of its product were to be reduced, we would expect marginal customers to investigate other available options, at which point they would have a number of other credible alternatives available either to switch to or, potentially, to use as leverage in a future negotiation, thus applying competitive pressure to the parties. At such a time those customers will find that there are other alternatives to the parties' products that are likely to be considered to be as close, or closer, to the parties as the parties are to each other.

Entry/expansion in the adherence packaging market

- 9.96 This section considers the 'dynamic' competitive constraints on the parties that result from potential entry into the adherence packaging market and from the threat of expansion of existing competitors, which might supplement the 'static' constraints on the parties from existing competitors discussed above. We then go on to consider the combined impact of these constraints on the merged entity in paragraphs 9.140 to 9.145.
- 9.97 This section begins by considering recent examples of entry. It then considers the barriers to entry and expansion that we have identified in the market, and then the criteria set out in our guidelines in relation to whether, given any barriers we have identified, entry and expansion can be:
- (a) timely: whether entry or expansion can be 'sufficiently timely and sustained to constrain the merged firm';⁸⁸
 - (b) likely: whether firms have the 'ability and incentive to enter the market'; and

⁸⁸ CC2, paragraph 5.8.3, notes that: 'The Authorities may consider entry or expansion within less than two years as timely, but this is assessed on a case-by-case basis, depending on the characteristics and dynamics of the market, as well as on the specific capabilities of potential entrants.'

- (c) sufficient: whether the scope or scale of entry or expansion would be sufficient to act as a competitive constraint on the merged entity.

Overview of recent entry and expansion

9.98 We identified a number of examples of entry in the market for adherence packaging in the last few years:

- (a) Shantys entered the market with a plastic-based product manufactured by third-party suppliers focused on products destined for domiciliary patients, which it sold through wholesalers/distributors. Shantys told us that it took [REDACTED] years and somewhere between £[REDACTED] and £[REDACTED] to become properly established and that it took three years to break even.
- (b) In 2008, Protomed entered the market with its Biodose product. It has grown successfully by promoting the product direct to care homes and then introducing those who are interested to pharmacies that can supply them. The number of end-users who use Biodose trays has approximately doubled over the last three years to approximately [REDACTED] in 2013.
- (c) Medication Systems Limited, a more recent entrant, supplies MultiMeds which is aimed at care homes. When it launched in 2012, it was initially sold via an arrangement with SurgiChem. However, this arrangement ended in 2014 and Medication Systems Limited now sells direct to independent pharmacies and smaller groups. Sales of MultiMeds are still modest, and the company estimated that it would take five years or more to become a sizeable competitor.
- (d) HD Medi's pouch-based system has about [REDACTED] customers in the UK (having invested approximately €300,000 in the UK market over the last five years).
- (e) Medication Management Solutions' pouch-based system is two years old. It has used trade exhibitions, email communications and social media, among other methods, to make itself known to potential customers, concentrating on independent pharmacies and small and medium-sized groups as well as hospital pharmacies. So far, it has sold [REDACTED] machines in the UK.

Assessment of barriers to entry and expansion

9.99 We have used information gathered from these recent examples of entry, and other information gathered from competitors and customers on how to

compete successfully, to identify the key components of successful entry. We have found that operators need to:

- (a) set up an appropriate mechanism for production that is capable of generating economies of scale;
- (b) manufacture a product that meets the appropriate quality standards;
- (c) set up a marketing, warehousing and a sales operation; and
- (d) persuade pharmacies to switch to their product.

9.100 We have also considered the impact that the size of the adherence market may have on the attractiveness of entry.

Manufacturing/economies of scale

9.101 An entrant into the adherence packaging market will need to invest in the appropriate manufacturing capability, either in-house or via third-party manufacturers, to produce a product that meets the appropriate quality standards, and to generate economies of scale.

9.102 In order to offer card- or plastic-based adherence packaging, an entrant will need access to manufacturing facilities for the tray (or card), blisters and seals. Plastic trays and blisters are produced using thermoforming machines. Cards require printing machines. We found that there are considerable economies of scale in both processes, more so in the case of card than plastic as the printing machines for card are both expensive and specialised (they cannot be used to manufacture other products), whereas a thermoforming machine is more flexible and only requires different moulds to enable it to produce different products.⁸⁹ It is therefore possible that a potential new entrant may seek, at least initially, to source its product from third party manufacturers – unless it had already achieved economies of scale in production overseas.

9.103 In the case of plastic-based packaging, we have been told that there are a number of thermoformers in the UK with the capability of manufacturing

⁸⁹ We have also been told (by Omnicell/MTS) that there are significant economies of scale in purchasing raw materials for card products and that only packaging manufacturers with very large volumes will be able to purchase raw materials at a price which enables them to compete with the established market players. According to MacPac (which supplies plastic trays and blisters to SurgiChem), a new entrant wishing to sell plastic-based packs would need to achieve sales in the low millions of units per year in order to benefit from economies of scale and achieve a unit price that would allow it to be competitive with incumbent players.

plastic trays and blisters to an appropriate standard.⁹⁰ As it is unlikely that any of these thermoformers would have machines available with sizeable idle capacity,⁹¹ a new entrant that wished to grow organically in the UK may have to plan and phase production over a period of some months, particularly if larger volumes were required. Alternatively, an entrant that wished to enter more aggressively might seek to arrange with a thermoformer for new machines to be purchased to meet demand.

9.104 Typically, a new entrant seeking to source a plastic-based product would be expected to pay for the tooling. A single tool costs approximately £6,000 to £10,000. As it is likely that a new entrant would wish to offer more than a single product/size to the market (for example, single-dose and multidose, with a variety of different blister sizes), upfront tooling costs could amount to some tens of thousands of pounds.

9.105 The manufacture of card-based packs requires large, dedicated machinery. We have been told that the machinery required to make the sort of volumes required by the major players (such as Omnicell/MTS or Venalink) would cost several million pounds. We have also been told that it is unlikely that any printers in the UK would be willing to make the required investment. There are some companies in the Far East who have such machinery and could supply card-based packs to a new entrant but, [X] (see paragraph 9.47 above), without a large volume commitment to allow the entrant to benefit from the considerable economies of scale involved, its margins are likely to be lower than those of existing manufacturers such as Omnicell/MTS and Venalink.

9.106 We therefore considered that the economies of scale involved in manufacturing a card-based product as opposed to a plastic-based product would mean that it is easier to enter the market organically by supplying a plastic-based product. However, we also note that suppliers already established in overseas markets may have achieved economies of scale (in terms of unit production costs) and could therefore enter with lower costs than an entrant that has grown organically in the UK.

9.107 We also considered the potential for expansion of existing suppliers. We found that should these suppliers wish to expand, they already have production arrangements in place and should face little difficulty in increasing supply if there is an opportunity to make further sales. For example, Shantys

⁹⁰ MacPac told us that it thought there were about ten such thermoformers in the UK. It said that there were also larger thermoformers, which would not be interested in the relatively low volumes involved in the adherence packaging market, and smaller ones which would probably not have the capacity or capability.

⁹¹ MacPac told us that suitable machines could cost about £350,000 each, so owners tried hard to avoid having their machines standing idle.

told us that it could increase production by 100%, although it would incur some additional storage and inventory costs in doing so.

Meeting quality standards

- 9.108 We considered the extent to which quality standards might create a barrier to entry or expansion. We reviewed evidence available on whether customers need to be reassured that a new entrant's product meets certain quality standards, so that, for example, they could be confident that medicines would not degrade while stored in the blister packs. We have been told that the British Retail Consortium Institute of Packaging Category 1 Standard for manufacturing of packaging for the food industry, which is a stringent standard, is often applied (though it is not universally required). A good thermoformer should be able to meet this standard. We also note that a supplier with an established reputation will find it easier to persuade customers that its product is of an acceptable quality than a new entrant.
- 9.109 Seals also need to be effective. There are some intellectual property rights associated with certain flaps and sealing systems (for example, the seals used by [X]). We were told by MTS and SurgiChem that it was relatively easy to devise a sealing system that did not contravene existing patents, although we were also told that such seals were not of as good a quality and were slightly more prone to allowing moisture to seep into the blisters. We also note that SurgiChem was able successfully to build up its blister pack business while using its own seals (which were not protected by a patent) before switching to seals manufactured under [X].
- 9.110 Alleged infringement of patent rights could, however, constitute a potential barrier. For example, Medication Systems Limited, which produces a plastic tray with detachable pods (sold under the name MultiMeds), found itself the subject of a patent infringement action from Protomed, which claimed that the MultiMeds product infringed certain patents applicable to its own Biodose product. Protomed lost its case.
- 9.111 Overall, we considered that the potential cost (both in terms of cash and time) to a new entrant in defending itself against possible legal action for infringement of a rival's intellectual property may be a factor that could potentially discourage entry or expansion.⁹²

⁹² [X] We note that Medication Systems Ltd was not enjoined from continuing to supply its product to the market while the legal proceedings progressed.

- 9.112 A potential entrant will typically need to establish an appropriately sized warehousing operation,⁹³ together with a sales force. Warehousing space can be leased, or it can be outsourced to a third party fulfilment (back-office) organisation or to a supplier. The total size of the workforce required is modest (for example, MTS Limited and SurgiChem each have approximately [X] employees, covering warehousing, sales and marketing, finance and management, and a new entrant would initially require a much smaller workforce).⁹⁴
- 9.113 The entrant will also need to market its product to pharmacies. We were told that lists of pharmacies were available at low cost from public sources such as Binleys. SurgiChem told us that marketing a new product typically involved sending out samples to pharmacies together with marketing literature and then following up with customer calls. SurgiChem said that the cost of such an operation was modest. When it launched Nomad Clear, the overall cost was less than £[X] in total, which included tooling, artwork and mailshots.⁹⁵
- 9.114 Omnicell/MTS told us⁹⁶ that it estimated the annual cost for a new entrant's sales team capable of achieving a 5% share of supply of adherence packaging to be at most between £[X] and £[X]. It said that this would cover the cost of two sales representatives, an office assistant, as well as a manager. It said that, in addition, the marketing spend might be at most between £[X] and £[X]. Marketing spend might, for instance, include attendance at trade fairs in order to gain credibility in the UK market. We noted that some recent entrants (for example, Protomed) also marketed direct to care homes and introduced them to pharmacies which would supply them with their products. Medication Systems Limited, however, told us that paying for a field sales force to build up sales to independent pharmacies and smaller chains, as well as care homes, represented a considerable expense for a fledgling business. Without such a sales force, it would take longer to grow sales.
- 9.115 An alternative, lower-cost route to market for a new entrant would be to send marketing literature to pharmacies but sell via wholesalers rather than invest in a dedicated sales force. We note that Shantys has adopted the wholesaler

⁹³ If product is to be sourced from overseas, for example the Far East or the USA, the warehouse may need to be larger than if it is sourced from the UK to allow for correspondingly longer delivery times.

⁹⁴ MTS told us ([Omnicell/MTS initial submission](#), paragraph 5.1) that it estimated that office and warehouse space and rates might cost no more than £[X] a year.

⁹⁵ [SurgiChem initial submission](#), paragraph 25. It also said that set-up costs for other products, including tooling, artwork and mailshots, were £[X] for Nomad Concise, £[X] for Nomad Clear XL, £[X] for Nomad Duo and £[X] for Nomad Clear 2. However, we note that this was not strictly new entry, but rather the introduction of a new product by an already established supplier of adherence packaging.

⁹⁶ [Omnicell/MTS initial submission](#), paragraph 5.1.

route. While this might limit a new entrant's rate of growth to a degree, as some pharmacies may prefer to purchase direct from the supplier rather than via a wholesaler, it saves on the cost of employing a sales force.

- 9.116 We did not consider that, for a new entrant, setting up a warehousing, marketing and sales operation constituted a significant barrier to entry, in that the costs involved were not particularly significant.

Persuading customers to switch

- 9.117 The most significant challenge for an entrant to this market is to attract a sufficient number of pharmacies as customers (and hence volume of sales) in order to operate profitably, given both the economies of scale already discussed and the strategic advantage possessed by incumbent suppliers with an established reputation.

- 9.118 We have set out our analysis of customer switching in paragraphs 8.18 to 8.28. We found that customers believe that there are limited costs associated with switching. Customers also indicated to us that they considered themselves to be price sensitive. Nevertheless, the level of switching in the adherence market has been low. This might affect a new entrant's ability to grow market share and therefore make entry into the market less attractive.

- 9.119 While customers' inertia may make entry less attractive and means that expansion requires greater investment and/or time, it does not appear to have deterred entry or prevented expansion in the adherence packaging market. Further we considered that, were the merging parties to attempt a material price increase following the merger, then this barrier might be reduced, as we would expect there to be (at least to some degree) a greater willingness among customers to switch suppliers in such circumstances. This may deter the parties from increasing their prices in the first place.

Size of the market

- 9.120 The adherence packaging market is small, which could act as a barrier to entering a market in circumstances where other barriers to entry and expansion are relatively high. However, the market for adherence packaging appears to be growing.⁹⁷ This growing demand may increase the attractiveness of the market to both potential entrants and incumbents, and

⁹⁷ Omnicell/MTS estimated that the market for domiciliary care (mainly multidose packs) was growing at approximately [X] % per year and that for long-term care (mainly single-dose packs) at [X] % per year (MTS main submission, paragraph 4.3.4).

might explain the number of attempts to enter the market that we have seen over the last few years (see paragraph 9.98).

- 9.121 Overall, we found that barriers to entry and expansion are low, with the greatest hurdle facing those who wish to enter or expand being the challenge of persuading potential customers to switch away from their existing supplier. We also note that if the merging parties were to attempt materially to increase their prices following the merger, then this barrier might be reduced.

Assessment of timeliness, likelihood and sufficiency of entry or expansion

Timeliness

- 9.122 In order for new entry to be timely, the entrant would, within a reasonable time (usually taken to be two years⁹⁸), need to be able to grow to a level where it constituted a sufficient constraint on the merging parties either through organic growth or by entering the UK from an overseas market.
- 9.123 If a new entrant intended to grow organically, this might involve a period of time putting in place the requisite manufacturing arrangements before production can begin (see paragraph 9.103). A new entrant from overseas may already have such production capability in place. It may therefore be easier for an overseas entrant to get its product out into the market and build up its visibility to customers, in order to become a constraint within a reasonable period.
- 9.124 Further, based on the speed with which successful recent entrants Protomed and Shantys have grown organically, new entry may not be a timely constraint – unless it comes from overseas and/or the entrant has the financial backing to market itself more aggressively than these firms did. However, we also note that if, post-merger, the merged entity did attempt to raise its prices, this might lead some customers to look at alternatives to the merged entity, potentially enabling a new entrant to become a credible constraint more easily.
- 9.125 In terms of the potential for new entry from overseas, Dexapack, a Turkish company which produces blister and high-visibility packaging for the pharmaceuticals industry and supplies adherence packaging across Europe, told us that it was due to enter the UK in the summer of 2014 with a card-based adherence packaging product (similar to those produced by Omnicell/MTS and Venalink) under the name ‘MedTime’. Dexapack told us that it aimed to sell 5–15 million units within the first three years after entering the market. It therefore intended to grow to a level where, if successful, it would constitute a

⁹⁸ CC2, paragraph 5.8.11.

sufficient constraint in the UK market within a reasonable period. However, we also note that a wholesaler that Dexapack is currently negotiating a potential distribution agreement with suggested that this is likely to be [REDACTED]. The wholesaler told us that it could probably sell around [REDACTED] units of Dexapack's card product over the next two years.

- 9.126 We have also considered whether an incumbent competitor in the adherence packaging market could, within a reasonable time, be expected to expand in order to constrain the merging parties. For example, we considered whether an incumbent could expand its focus from the care-home segment into the domiciliary segment, or expand from marketing only to smaller chains via wholesalers to selling directly to larger chains. Consumer inertia might constitute a barrier to such expansion. However, this could be overcome if an incumbent competitor was prepared to invest in its marketing capability and/or benefited from a greater willingness on the part of pharmacists to shop around following a price rise by the merging parties.

Likelihood

- 9.127 We note that there have been several examples of entry over recent years. Further, this is not only with products that are differentiated from those of the parties (such as Protomed's Biodose or HD Medi's pouch-based system). Shantys entered the market with plastic-based packs that are directly comparable with those produced by SurgiChem. This is consistent with a market that appears to be growing in size (according to the merging parties) and where barriers to entry are low. We also note that if the merged entity were to attempt to raise the price of one or more of its products, this might increase the likelihood of entry further.
- 9.128 We have identified an additional new entrant, Dexapack, that appears likely to enter the UK market with a card-based product during 2014. We note that Dexapack is in the final stage of testing a plastic-based product, which it also intends to market in the UK.
- 9.129 We have also identified a number of firms that could enter the UK market, although we have not identified evidence that they plan to do so:
- (a) Omnicell/MTS told us that there were a number of existing US players which did not currently sell in the UK (such as RX, Medicine-on-Time and Dispill USA) [REDACTED].
 - (b) CareFusion, which already supplies automated dispensing machines to hospitals, has designed a pouch-based system (the Rowa Dose system), although it has not yet commenced supplying this system to the UK

market. CareFusion already has a UK sales affiliate so would not incur significant additional costs should it decide to launch its product in the UK.

- (c) We were told that Chemistree, a pharmacy chain, had opted to 'self-supply' with plastic-based adherence packs, although we have no evidence that it intends to supply other pharmacies with this product.

9.130 In terms of whether expansion is likely, we consider that if conditions of the market were such as to make entry likely, then those same conditions would be equally (if not more) likely to make expansion by an incumbent competitor likely. This because barriers to expansion appear to be lower than barriers to entry because an incumbent competitor is already likely to have some of the infrastructure it would require to expand in place.

9.131 The following competitors told us about their potential expansion plans:

- (a) Medication Systems Limited told us that, in the event of the merger going ahead, it would probably introduce a plastic-based product in direct competition to SurgiChem's Nomad product.
- (b) Two suppliers of pouch-based systems told us that they planned to increase their sales significantly over the coming years.

9.132 We therefore found that both entry and expansion were likely, particularly if the merged entity attempted to raise prices.

Sufficiency

9.133 We have set out, in paragraph 9.55, the characteristics that a competitor would need to constitute a sufficient constraint.

9.134 Our review of the recent history of organic entry into the market indicates that there are examples of entrants that have grown into credible competitive constraints. For example, Shantys has developed into a significant competitive constraint in the domiciliary segment of the market. However, we note that Shantys has taken around [X] to grow organically to its current level. Protomed has also grown very successfully over recent years to the point where it constitutes a competitive constraint.

9.135 We have received evidence that Dexapack intends to enter the market in the near future. As set out in paragraph 9.125, Dexapack has ambitious growth plans although there is some uncertainty over how likely it is to achieve them.

9.136 Of those players in the market which have told us about their plans to expand (for example, MSL and the pouch-based suppliers), there is some doubt in

each case over whether they can reach a sufficient level of market penetration to constitute a competitive constraint within a reasonable period given that in each case they are starting from a low base.

- 9.137 Given that barriers to expansion in this market are low, it seems possible that either one of these suppliers or another existing incumbent might grow its sales or develop a new product that would allow it to become a greater competitive constraint on the merged entity. As discussed in paragraph 9.124, if the merged entity attempted to raise its prices, the likelihood of an incumbent expanding in this way would become greater.

Conclusion on entry and expansion

- 9.138 We considered past entry and expansion in the adherence packaging market and found that there had been a number of examples of recent entry including Shantys, Protomed and two firms offering plastic pouch-based systems. We found that barriers to entry and expansion are fairly low, the most significant being the challenge of persuading customers, some of which we have found not to be particularly engaged, to switch to their product. We also noted that if the merging parties were to attempt to increase their prices materially following the merger, then this barrier might be reduced as we would expect there to be a greater willingness among customers to switch suppliers in such circumstances.
- 9.139 We considered whether entry and/or expansion would be likely to act as a further constraint on the merged entity. We found that entry, particularly entry into the market from overseas suppliers, could be achieved on a timely basis, as could the expansion of an existing player. We found that there was a reasonably high likelihood of entry and/or expansion into the market based on both the recent history of entry and evidence in the market, our findings on the intentions of Dexapack to enter the UK market in 2014 and the intention of a number of existing suppliers to expand. Further, we considered that the likelihood of entry of other suppliers would increase if the merged entity attempted to raise its prices or reduce the quality of its packaging. We considered whether any of the firms that have the intention to enter or expand are likely to become a sufficient additional constraint within a reasonable time period. We found that there is a material chance that at least one would and that the collective impact of their attempts may act as a constraint on the parties.

Provisional conclusion on the competitive effects of the merger on the adherence packaging market

9.140 In order to reach a conclusion on the competitive effects of the merger in the adherence packaging market, we considered:

- (a) the segments of the market the parties were competing in, how closely the parties were competing in those segments and the extent to which competitive rivalry in these segments could be reduced by the proposed merger;
- (b) which other competitors currently in the adherence packaging market could provide a competitive constraint in the segments of the market where competitive rivalry may be reduced; and
- (c) how far entry and expansion might further constrain the parties.

9.141 In terms of how closely the parties competed, we have found that:

- (a) SurgiChem does not currently compete for customers which tender for their adherence packaging requirements, nor, in our judgement, is it likely to become a credible competitive constraint in this segment of the market within a reasonable period. As a result, we did not think that the merger would lead to a reduction in competitive rivalry in this segment.
- (b) The parties do compete closely for a significant proportion of non-tender customers, and there is potential for the anticipated merger to lessen competition for these customers. Responses to our survey, questionnaires and third party hearings identified a significant proportion of customers who consider the parties to be competing closely. References in the parties' internal documents also suggest that they consider each other to be close competitors. Further, SurgiChem's recent development of a card-based product suggests that it intends to compete with Omnicell/MTS for customers that currently use card-based adherence packaging.

9.142 We considered the strength of other competitors to the parties in both the non-tender domiciliary and care-home segments. We found that there are two competitors to the parties in the domiciliary segment of the market that constitute significant competitive constraints on the merged entity. We identified three established rivals to the parties in the care-home segment of the market. Two are likely to be significant competitive constraints, whereas the likelihood of the other competitor (Protomed) constraining the parties' prices is lower.

9.143 We considered whether entry and/or expansion would be likely to act as a further constraint on the merged entity. We found that entry, particularly entry

into the market from overseas suppliers, could be achieved on a timely basis, as could the expansion of an existing player. We found that there was a reasonably high likelihood of entry and/or expansion. Further, we considered that the likelihood of entry of other suppliers would increase if the merged entity attempted to raise its prices or reduce the quality of its packaging. We considered whether any of the firms that have the intention to enter or expand are likely to become a sufficient additional constraint within a reasonable time period. We found that there is a material chance that at least one would and that the collective impact of their attempts may act as a constraint on the parties.

9.144 On the basis of the evidence available, it seems possible that the merger will lead to a reduction in competitive rivalry for those non-tender customers for which SurgiChem and Omnicell/MTS compete closely. However, the significance of the reduction in rivalry will depend on the constraint that other competitors in the market will place on the merged entity.

9.145 Overall, we found that there are existing players in the market that will offer significant constraints on the merged entity in both the non-tender care-home and non-tender domiciliary segments of the market. Our findings on the potential for entry and expansion provide us with additional indications that the parties could be constrained further within a reasonable period. Taken together, this evidence on existing constraints and further potential for entry and expansion leads us provisionally to conclude that the merger is unlikely to result in an SLC in the adherence packaging market.

10. Assessment of competitive effects of the merger in other markets where there may be an overlap between the parties

10.1 We have identified two other product markets where the parties' commercial activities currently overlap or would overlap in the future:

- (a) trolleys and cabinets; and
- (b) automated filling machines.

10.2 This section of our provisional findings considers the evidence gathered in relation to these product markets and assesses the competitive effects of the proposed merger in each of these product markets.

Trolleys and cabinets

10.3 Omnicell/MTS and SurgiChem both currently supply trolleys and cabinets in the UK. These products are used for storing and carrying (eg within care

homes or hospitals) medicines packed in adherence packaging as well as medication more generally. We have therefore considered the impact of the loss of a competitor in this market should the merger proceed. First, we have assessed how closely the parties compete. Second, we have assessed whether sufficient competitive constraints on the merged entity would remain in the market following the merger.

Closeness of competition

Views of the main parties

- 10.4 Omnicell/MTS submitted that, while trolleys and cabinets were a major area of business for SurgiChem (it was a leading supplier of trolleys and cabinets and fridges to pharmacies which supplied these products to pharmacy customers), it was a negligible area for Omnicell/MTS. Omnicell/MTS explained that it only supplied trolleys and cabinets when a specific request was made from a customer, and that it supplied trolleys and cabinets manufactured by a [REDACTED].⁹⁹

Sales data

- 10.5 We looked at the parties' sales data for trolleys and cabinets and we found that SurgiChem's revenues from these product lines were far greater than Omnicell/MTS's.
- 10.6 Omnicell/MTS sales of trolleys and cabinets amounted to £[REDACTED] in 2013; this represented [0–5]% of its total business of adherence packaging and related products.¹⁰⁰ In volume terms, Omnicell/MTS sold [REDACTED] trolleys at an average price of £[REDACTED], and [REDACTED] cabinets at an average price of £[REDACTED].¹⁰¹ Omnicell/MTS's main customers for trolleys and cabinets were [REDACTED]. These customers accounted for [REDACTED]% of Omnicell/MTS's total sales of trolleys and cabinets in 2013 (it had [REDACTED] customers for trolleys and cabinets in total).
- 10.7 SurgiChem sales of trolleys and cabinets amounted to £[REDACTED] million in 2013; this represented [10–20]% of its total business of adherence packaging and

⁹⁹ Omnicell/MTS further submitted that its distributor Avantec (in which Omnicell has a minority shareholding) did, however, sell cabinets (but not trolleys) to hospitals in the UK, typically around [REDACTED] a year, with a value of approximately £[REDACTED] a year, and thus these were [REDACTED] more expensive than those of Omnicell/MTS or SurgiChem. Omnicell/MTS explained that the cabinets supplied by Avantec contained various electronic value-added features, with the result that in terms of their price level and characteristics, they could be regarded as not being in the same market as the cabinets supplied by Omnicell/MTS and SurgiChem. Source: [Omnicell/MTS initial submission](#), section 4.1.4.

¹⁰⁰ Total business includes adherence packaging and ancillaries/support products, trolleys, cabinets, and de-blistering, sealing and filling machines.

¹⁰¹ There were, however, seven different types of trolley and five different types of cabinet, and they varied in price.

related products.¹⁰² In volume terms, SurgiChem sold [X] trolleys at an average price of £[X], and [X] cabinets at an average price of £[X].¹⁰³ SurgiChem's main customers for trolleys and cabinets are [X]. Sales to these customers accounted for [X]% of total sales of trolleys and cabinets in 2013 (it had [X] customers for trolleys and cabinets in total¹⁰⁴).

Review of internal documents

- 10.8 We reviewed the parties' internal strategy documents for references to their trolleys and cabinets product lines. We noted that, while SurgiChem's internal documents referred to their trolleys and cabinets business, we did not see any evidence in relation to trolleys and cabinets in Omnicell/MTS's internal documents, or any evidence indicating intentions to expand in this area. This may imply that this area was not of much importance to Omnicell/MTS.
- 10.9 This evidence suggests that there is currently little overlap and competition between Omnicell/MTS and SurgiChem in the supply of trolleys and cabinets, and it is unlikely that this would change to a more competitive situation as we have seen no evidence that Omnicell/MTS is interested in expanding or competing more strongly in this market.

Constraints from other suppliers

Views of the parties

- 10.10 Omnicell/MTS submitted that the cabinets and trolleys supplied by each of the parties were similar to the types of products used in hospitals. It argued that these cabinets and trolleys should also be included within the same market. It also told us that there was a large number of suppliers of such equipment to hospitals, and that SurgiChem believed that competition between suppliers of trolleys and cabinets was fierce and that Bristol Maid was a strong competitor and had reduced prices in recent years.¹⁰⁵
- 10.11 Further, the Information Memorandum, prepared by Deloitte for Bupa in relation to the proposed merger between Omnicell/MTS and SurgiChem, notes that SurgiChem supplies trolleys to the three main pharmacy chains in the UK (Boots, Lloyds Pharmacy, [X]), and estimates its market share to be [80–90]%.¹⁰⁶ However, we understand that this relates to the supply of trolleys

¹⁰² Total business includes adherence packaging and ancillaries/support products, trolleys, cabinets and fridges.

¹⁰³ There are, however, seven different types of trolleys and seven different types of cabinets, and they varied in price.

¹⁰⁴ This is the number of customers purchasing for a value in excess of the least expensive trolley or cabinet in 2013.

¹⁰⁵ [Omnicell/MTS initial submission](#), section 4.1.4.

¹⁰⁶ Information Memorandum, prepared by Deloitte, July 2013, p8 ([Omnicell/MTS initial submission](#), Annex 2).

for adherence packaging to be used by care homes, and does not include suppliers of similar trolleys more generally.¹⁰⁷

- 10.12 SurgiChem submitted that its competitors in the supply of trolleys and cabinets were Bristol Maid, Sidhil, Sunflower Medical and W Shuttleworth. It noted that the range of trolleys and cabinets these competitors supplied were wider and included products supplied to hospitals.¹⁰⁸

Views of customers

- 10.13 Large customers of SurgiChem for trolleys and cabinets indicated that they actively considered and sourced trolleys and cabinets from suppliers other than the main parties:
- (a) Boots said that, while it currently sourced cabinets and trolleys from SurgiChem, it was in a process of reviewing the suppliers and was considering alternative suppliers like Sunflower Medical, in order to make sure it was getting a good deal. It noted that there were further alternative suppliers of these products, such as Norseman, Hospital Metalcraft, Bristol Maid and Windsor. Boots said that it had spoken to Omnicell/MTS about the supply of trolleys and cabinets, and that Omnicell/MTS had indicated that it would [REDACTED].
 - (b) Lloyds Pharmacy told us that it used to purchase care-home equipment from both Bristol Maid and SurgiChem in equal proportions until around mid-2012. It then switched to purchasing mainly from SurgiChem until around mid-2013, and, following a review of service, quality and price, it now mainly sourced from Norseman and had switched away from SurgiChem.

Evidence from other competitors

- 10.14 We noted that, of the other suppliers of adherence packaging in the UK, Venalink and Protomed also sold trolleys and/or cabinets:
- (a) Venalink sold [REDACTED] of trolleys in 2013. It said that these were sold through [REDACTED] and that it mainly sold these trolleys to customers using Venalink adherence packaging products.

¹⁰⁷ Omnicell/MTS noted that supply to care homes was merely a part of the broader market for supply of such products to the healthcare sector including hospitals, and that therefore on that broader market SurgiChem's share of supply would be considerably lower (Source: [Omnicell/MTS initial submission](#), p13).

¹⁰⁸ [SurgiChem initial submission](#), Appendix 3.

(b) Protomed sold approximately £[REDACTED] worth of trolleys and cabinets in 2013, all of which are designed to hold Biodose adherence packaging trays. It noted that the majority of its customers were the same pharmacies that purchased its Biodose adherence packaging trays, and that some sales were direct to care homes. Protomed said that its share of supply of trolleys and cabinets to care homes might be around [REDACTED]%, but that it had no firm information to enable it to establish this with any precision. It told us that other suppliers included Bristol Maid (Pharmacy Equipment Direct), drugtrolley.co.uk (same operator as the supplier of MultiMeds), and Boots and Lloyds Pharmacy (with their own equipment).

10.15 Therefore evidence suggests that there are a number of credible alternative suppliers of trolleys and cabinets available, including Norseman, Sunflower Direct and Bristol Maid, and that the largest customers actively look for and switch between alternatives.

Provisional conclusion on impact of the merger on the trolleys and cabinets market

10.16 Based on evidence above, it appears that unilateral effects in the supply of trolleys and cabinets are unlikely as a result of the proposed merger between Omnicell/MTS and SurgiChem. There is little overlap between the parties in the supply of trolleys and cabinets because, while SurgiChem is active in this market, this appears to be a minor area for Omnicell/MTS. Furthermore, we have identified a number of other credible competing suppliers of trolleys and cabinets in the marketplace which could constrain the merged entity.

Automated filling machines

10.17 Automated filling machines fill adherence packaging with medicines and heat-seal them, in place of a pharmacy worker performing the filling and sealing manually, and, as such, offer advantages in terms of the time and resource required to fill adherence packaging.

10.18 SurgiChem has developed and intends to supply an automated machine for filling single-dose adherence packaging. We have therefore considered whether the merger will result in the loss of a potential competitor to Omnicell/MTS. We have assessed whether the parties would have competed closely in the filling machines market absent the merger, and the extent to which other competitors in the filling machine market will constrain the merged entity.

Closeness of competition

10.19 Omnicell/MTS currently supplies automated machines for filling multidose and single-dose blister pack adherence packaging in the UK.¹⁰⁹ SurgiChem [REDACTED] has developed a prototype and intellectual property for a single-dose automated filling machine. Thus, there is a potential overlap and competition between Omnicell/MTS and SurgiChem in the supply of single-dose automated filling machines.

10.20 We have found that [REDACTED].¹¹⁰

10.21 Omnicell/MTS submitted that there were [REDACTED] of its MTS 350 single-dose filling machines supplied in the UK as of December 2013 ([REDACTED] such machines as of April 2014), all of which were [REDACTED]. Omnicell/MTS told us that the volume of consumables (adherence packaging) sold to customers of these machines (which may include consumables not used with these machines) in comparison with Omnicell/MTS's overall sales of consumables was [REDACTED] low, amounting to [0–5]% of overall sales in 2013.¹¹¹

10.22 We have reviewed lease payment revenues for MTS 350 in 2013. It appears that there were a number of pharmacies leasing MTS 350 machines, including [REDACTED]. Total lease payments amounted to around £[REDACTED], which represented [20–30]% of Omnicell/MTS's revenue from machines, and less than [0–5]% of their overall sales of adherence packaging and related products. Thus, MTS 350 machines themselves appears to be a relatively small part of Omnicell/MTS's adherence packaging business.

10.23 SurgiChem told us that its single-dose machine was originally developed by ElectroMec to be used with [REDACTED]. It explained that its machine was a [REDACTED] and as such was aimed at high-volume customers. It was of the view that automated machines were only likely to be purchased by large pharmacy chains due to cost, and that, with developments in electronic solutions, it thought some pharmacies may be delaying purchasing machines.

Parties' views on closeness of competition

10.24 SurgiChem told us that its machine was not directly comparable to any Omnicell/MTS machines, and that it differed from the MTS 350 machine in a number of ways: it could be used up to the level of pharmaceutical production (ie the speed of the machine could be increased to [REDACTED] packs per minute,

¹⁰⁹ [Omnicell/MTS initial submission](#), pp10–11.

¹¹⁰ [REDACTED]

¹¹¹ [Omnicell/MTS initial submission](#), p11.

which was similar to the speed of machines used in pharmaceutical production); it was designed for larger-scale operations than MTS 350 (although multiple MTS 350 machines could be used to achieve larger throughput); and it could be adapted to other forms of packaging. SurgiChem submitted that its machine was more comparable to the machines supplied by K&M and Technical Engineering Group, in particular, but also the machines supplied by Ilseemann, Uhlman, SynMed and pouch-dispensing machine suppliers such as HD Medi, Robotik and Tosho, on the basis that such machines were used by large pharmacy chains and pharmacy warehouses.

Evidence on speeds and prices of the machines

- 10.25 Evidence available on the speeds and prices of the two machines suggests that SurgiChem's single-dose filling machine is faster and more expensive if compared with the Omnicell/MTS MTS 350 machine.
- 10.26 Omnicell/MTS's MTS 350 machine can fill [X] blisters per minute, and its list price is £[X].¹¹² By contrast, SurgiChem's filling machine can fill [X] blisters per minute in its current set-up, and, if attached to a full-scale pharmaceutical production unit, it would fill up to [X] blister packs per minute (currently the filling rate is limited to the speed of the heat-sealing machine).
- 10.27 SurgiChem said that the machine currently cost £[X] for a single machine manufactured to the full specification, and that this could be reduced to approximately £[X] if SurgiChem were to order [X]. It would price the machine at around £[X], although this would be reduced if SurgiChem made sufficient sales to enable it to order [X] or more machines from its supplier.
- 10.28 Therefore, SurgiChem's machine would be up to [X] times the price and around [X] the speed of the MTS 350 machine. As SurgiChem had suggested, two or more MTS 350 machines could be used in place of one SurgiChem machine in order to achieve [X] at broadly similar cost. However, using multiple machines instead of one machine would have labour cost implications (ie it would be more expensive to operate multiple machines instead of one machine). Further, the way that pharmacies use machines to fill blister packaging might impact whether one machine (eg in one central location) or multiple machines (eg at several stores or locations) would be more suitable for a given pharmacy's logistical needs. For instance, SurgiChem suggested that its machine was more suited to large-scale pharmaceutical production and was aimed at high-volume customers, such

¹¹² [Omnicell/MTS initial submission](#), p9.

that investment in the machine would only be worthwhile for large pharmacy chains.

Evidence from customers

- 10.29 Rowlands told us that MTS 350 machines enabled it to fill single-dose adherence packaging with common drugs much more efficiently than manual dispensing, and that this was the main reason why it preferred to source adherence packaging from Omnicell/MTS rather than SurgiChem or someone else. It believed that the machine would be compatible only with Omnicell/MTS's packaging (and possibly with Venalink's, but not with SurgiChem's).

[REDACTED]

- 10.30 Overall, it appears that in the future Omnicell/MTS and SurgiChem would be the only suppliers of blister-pack adherence packaging in the UK also offering single-dose filling machines if the SurgiChem machine were to be made available on the market. No other supplier of blister-pack adherence packaging (for example, Venalink, Protomed, Shantys) currently offers or is developing a filling machine. Thus, for customers wishing to source (blister-pack) adherence packaging together with single-dose automated filling machines in the UK, Omnicell/MTS and SurgiChem would be the only options. However, given the differences in the speed and cost of the machines, it appears unlikely that many pharmacies would consider both machines potentially suitable to meet their needs.

Constraints from other suppliers

Views of the parties

- 10.31 Omnicell/MTS submitted that the overall market for automated filling machines was very small for multidose and single-dose packaging, but that it was likely to expand as pouch-based systems become more and more established in the UK (pouch-based systems are for multidose filling). It told us that the main competitors for multidose filling machines were the suppliers of pouch-based systems (such as HD Medi and Robotik), and separately also SynMed ([REDACTED]).

- 10.32 SurgiChem submitted that its main competitors in filling machines could include K&M ([REDACTED]), Technical Engineering Group (TEG),¹¹³ Ilseemann, Uhlman, SynMed and pouch-dispensing machine suppliers – HD Medi, Robotik, and Tosho. It noted that the suppliers of pouch-dispensing machines

¹¹³ This is a company which, according to its website, designs and supplies tooling for pharmaceutical tablet blister packaging and tablet feeding systems. See www.teg.com.

all supplied to pharmacies, and that all the others (K&M, TEG, Ilseemann and Uhlman) offered more bespoke solutions.

Evidence on other competitors

- 10.33 SurgiChem explained that currently Ilseemann machines were used by Boots to fill its Manrex blister cards on an industrial scale. It noted that one difference between Ilseemann's and its own filling machine was that the Ilseemann machine required 50 change parts, each costing around £10,000, but that SurgiChem's machine used only [REDACTED] change parts, all included in the cost of the machine. The Ilseemann machine also had a thermoforming station which produced the blisters themselves.
- 10.34 SurgiChem told us that the Uhlman machine was a similar machine to the Ilseemann machine, but it was slower and ran on a smaller scale, and would typically be run by a pharmaceutical company to package drugs for clinical trials.
- 10.35 SurgiChem submitted that SynMed, a Canadian company, produced multi-dose filling machines, which could also be used for filling single-dose packaging and that looked similar to pouch-dispensing machines but filled blister packs. It noted that the SynMed machine was much slower than SurgiChem's machine, and required much more manual input. It believed that no such machines had been sold in the UK yet.
- 10.36 We understand that HD Medi and Robotik (through Medication Management Ltd) currently supply pouch-based filling systems in the UK market. We have been told that CareFusion, which is active in the UK through ARX with its Pyxis highly automated dispensing machines used in hospitals, is currently developing a single- and multidose pouch-dispensing machine, Rowa Dose System, [REDACTED].
- 10.37 Pouch-based systems are for multidose filling, and are more expensive than single-dose filling machines. For example, the price of Robotik (Medication Management) pouch-based automated filling machines, sold in the UK in 2013/14, ranged from £[REDACTED] to £[REDACTED]. The cost of a roll of 28 pouches (equivalent to a weekly 'pack' of four multidose pouches per day) is priced at [REDACTED] pence (this is comparable to the price of blister pack adherence packaging consumables). SurgiChem told us that, for example, Robotik's machines filled [REDACTED] pouches per minute with different types of medicines, and that Tosho's machines could fill [REDACTED] pouches per minute.
- 10.38 HD Medi said that it did not view card manufacturers as its competitors since in Europe everyone chose pouches based on economics, efficiency and

quality. In the UK, it presently competed with Robotik. Medication Management (a distributor of Robotik) said that its main competitors were other pouch-dispensing suppliers; in the UK these were HD Medi and KLS. It explained that it saw Omnicell/MTS and SurgiChem as competitors, too, as these were existing suppliers they were trying to displace.

Provisional conclusions on competitive effects

- 10.39 If and when SurgiChem starts selling its machine, the main parties would be the only suppliers offering a readily-available solution in terms of automated filling for single-dose blister packs, and the only suppliers of blister packs in the UK which offered such automated filling machines. However, the evidence suggests that Omnicell/MTS's single-dose automated filling machine and the one developed by SurgiChem are different in terms of cost and speed, with SurgiChem's machine likely to be significantly more expensive and faster than the Omnicell/MTS MTS 350 machine. This indicates that there are unlikely to be many circumstances in which the two products could both fulfil customers' requirements. Further, even in circumstances where this is the case, there are a number of other automated solutions for adherence packaging, including bespoke machines available from other suppliers (eg Ilseemann, Uhlman, TEG), and including competition from pouch-based systems. These other providers are likely to provide a sufficient competitive constraint on the parties in terms of automated solutions to pharmacies in the UK.
- 10.40 We also note that the machine is still a prototype, that [REDACTED], and that it has not been possible to estimate the future levels of demand for the machine. As set out in paragraph 10.24, the UK market for automated filling machines is limited to large pharmacies with sufficient scale to justify the capital investment to use these machines. There is only a small pool of potential customers for which the parties could compete, as demonstrated by the fact that Omnicell/MTS currently [REDACTED] filling machines in the UK. SurgiChem would be entering a market that is limited in scope and activity in the UK. Moreover, the parties' automated filling machines are highly differentiated in terms of cost and speed and, resultantly, rivalry (at the most) would only be lost for a particular subset of this small pool of customers who could feasibly use either party's machine. On this basis, combined with the competitive constraints already existing in the market, it seems unlikely that the merger would result in the loss of significant rivalry and competition in this market.
- 10.41 It therefore appears that unilateral effects in the supply of filling machines are unlikely as a result of the proposed merger.

11. Provisional conclusions on the SLC test

- 11.1 Based on the above, we have provisionally concluded that the proposed merger is not expected to give rise to an SLC in (a) the market for the supply of adherence packaging in the UK, (b) the market for the supply of automated adherence packaging filling machines in the UK, or (c) the market for the supply of trolleys and cabinets for the storage of adherence packaging in the UK.