

CELESIO / SAINSBURY'S PHARMACY BUSINESS MERGER INQUIRY

Summary of hearing with Day Lewis plc on 22 January 2016

Background

1. Day Lewis stated it had 275 stores altogether. 250 of these were owned pharmacy stores, and the remaining 25 were pharmacies it owned with others.
2. Day Lewis said it had four different formats of pharmacy. It said it had about 20 health and beauty store pharmacies, and 50 health centre pharmacies. The remainder of its pharmacies were either high street pharmacies or community pharmacies.
3. Day Lewis emphasised that the main driver of change in the pharmacy services market was regulatory change. It stated that these changes had detrimentally affected planned expansion within Day Lewis.

Market definition

4. Day Lewis specified two main types of pharmacy, namely a large departmental store type of pharmacy and a community pharmacy, which was usually an independent shop. It stated that a large majority, over 80%, of any pharmacy business whatever the type came from the NHS. It said a minute amount of business came from over the counter sales.
5. Day Lewis distinguished chronic patients from acute patients and said they were different customer groups. It said 80% of its customers were chronic patients and the remainder were acute. As a result of this, Day Lewis stated that there was a lot of competition in the industry for chronic patients around collection, repeat prescription management and delivery.
6. Day Lewis stated that the electronic prescription service was a threat to pharmacies. This service allowed for an electronic prescription to be sent on behalf of the patient, as opposed to the traditional paper prescription. For the electronic service the patient had nominated a pharmacy. All future prescriptions for that patient would go to the same pharmacy unless the patient nominated a different pharmacy. Day Lewis stated that as a result of

this service, the physical location of a pharmacy was not as important as in the past.

7. Day Lewis recognised that this system favoured pharmacies that were able to speak with patients directly and convince them to switch pharmacy. It said pharmacies with the bigger footfall and electronic connectivity were at a better advantage. It said it would speak with patients to have itself nominated as the patients' pharmacy of choice.
8. Day Lewis said its pharmacy-only medicines were priced centrally. It undertook local pricing in the past but had found this method to be inefficient.
9. Day Lewis stated that it considered pharmacies nearby to its stores as competitors, regardless of the owner. It said that pharmacies that were closer to the local GP surgery than a Day Lewis store were also considered competition. Day Lewis added that it considered supermarket pharmacies and online pharmacies as competition.
10. In terms of physical community stores, Day Lewis said it believed that 1 mile was the distance over which competition occurred. However, it felt that for supermarket pharmacies, 3 to 5 miles was the distance over which competition occurred. Day Lewis said the distance was greater with supermarket pharmacies because customers who went to supermarkets were transient and mobile. It said that supermarket pharmacies served in terms of convenience, as customers were able to park their vehicles and complete their grocery shop while they collected their medication.

Care homes

11. Day Lewis confirmed that it supplied medication to care homes; it said it supplied roughly 350 care homes.
12. Day Lewis said that the care home market presented fierce competition. It said in the past Boots drove most of the competition as it gave away free Monitored Dosing Systems compliance packs. It said that the independent sector lost a lot of care home business because of this and had to compete.
13. With larger care homes, Day Lewis said that the agreements between the home and the pharmacy were negotiated centrally. Day Lewis said it supplied mostly independently owned care homes; it did not have a share of the national ones.
14. Day Lewis stated that independent care homes sought free services when they decided which pharmacy they selected as their supplier. Day Lewis said these care homes sought services such as: prescription management,

compliance packs, medication trolleys, waste collection and staff training. It added that a good relationship was essential between the pharmacy and the care home. In contrast, Day Lewis believed that the relationship was less important in contracts that were centrally negotiated. It said that economics was the main driver in those agreements.

15. Day Lewis said it considered Celesio as a competitor for care homes. It stated that it did not consider Sainsbury's Pharmacy as a competitor, since it believed, supermarket pharmacies were not equipped enough, in terms of manpower or expertise to ensure care homes were sufficiently serviced.

Out-patient dispensing

16. Day Lewis stated that out-patient dispensing was a very complex, and difficult, area to get into.
17. Day Lewis said it had submitted a bid for an outpatient dispensing contract two years ago but was unsuccessful.
18. Day Lewis said ideally it would have submitted further bids but felt that Hospital Trusts preferred the larger companies with prior experience in OPD. It said most out-patient dispensing contracts were awarded to either Celesio or Boots. It added that the market was saturated towards the very large players purely because of the choice of the hospital managers. It also said the larger players had the expertise requisite and could tackle the complexity of those tenders.

Wholesale sector

19. Day Lewis stated that it was supplied with prescription medicines and pharmacy-only medicines by two different suppliers – Alliance and AAH.
20. Day Lewis said that the merger would not have had an impact on the general wholesale of pharmaceutical products. It stated that the merger had not detrimentally impacted Day Lewis on the wholesale side.

Competition and competitors

21. Day Lewis said its pricing was decided centrally. However, its stores' opening hours, stock levels and staffing levels were decided locally. It added that opening hours were decided by the group managers, not the shop managers.

22. It said it had a better economy of scale than the standalone independent pharmacies but a lower economy of scale than the larger pharmacy chains. Day Lewis said it focused more on the customers than the procurement.
23. Day Lewis said it reacted to the entry of a new pharmacy in its locality. It fought new contract applications and relocation applications. It said all other pharmacies within the relevant locality also fought new entrants in the same manner.
24. As doctors could also nominate pharmacies for a patient, when it gave a prescription, Day Lewis said pharmacists were worried about doctors who used their position and directed patients to pharmacies where the doctor had an interest or prior relationship. It said there was guidance given by the BMA to a doctor saying not to direct patients.
25. Day Lewis stated that the electronic pharmacy system used in the UK was supplied by EMIS. It said that EMIS was vertically integrated with an online pharmacy called Pharmacy2U. Day Lewis said that each time a doctor's system went live onto the area, Pharmacy2U contacted all the patients in the locality and encouraged them to send their pharmacy prescriptions chronically upstream. Day Lewis said it has fought this, but at a cost.
26. Day Lewis said if a supermarket pharmacy opened within 500 yards of one of its stores, it would lose about 40% of its business overnight. This was essentially because supermarket pharmacies were open 100 hours, which gave those pharmacies greater opportunities to convert patients to them using the electronic prescription service. This resulted in the community pharmacies losing the prescriptions for those patients.
27. Day Lewis said it had attempted to compete with supermarket pharmacies by ensuring it offered additional services. It had also entered the private medical market to gain back some of its lost market share.
28. Day Lewis did not categorise customers that went to supermarket pharmacies differently from customers who shopped at its pharmacies. Day Lewis noted that it believed that very elderly customers would be less inclined to use supermarket pharmacies. However, it said that where the patient was very elderly, or had mobility issues, the carer or a family member collected the prescription, which would make a supermarket pharmacy a viable option to them.
29. Day Lewis had not viewed any particular type of pharmacy as more of a competitor than others.

30. Day Lewis said it had not considered Sainsbury's to be a competitive threat to Celesio, but said that this would be dependent upon each locality.
31. Day Lewis acknowledged the growth of online pharmacies but had not considered them to be critical competitors. Day Lewis said the biggest online threat to pharmacies were distance-selling pharmacies; it stated that there was no way to control the entry of these pharmacies. Day Lewis said that this was a local issue as opposed to a national issue.

Barriers to entry/expansion

32. Day Lewis said the main barrier to entry was the NHS contract, which could only be acquired by way of a pharmaceutical needs assessment. It added that current pharmacies that objected to a new entrant in its locality was also a major barrier to entry.
33. Day Lewis said that the Department of Health had announced a £170 million cut to the pharmacy services budget. Moreover, it added that the Department of Health had also announced the removal of the £25,000 establishment payment pharmacies received.
34. Day Lewis stated that there was a consultation about the role of pharmacies amongst pharmacy bodies. It said that the consultation implied that there were too many pharmacies and implied the number of pharmacies would reduce through financial attrition.
35. Day Lewis added that pharmacies were paid per prescription. It said that there was a consultation that looked into having the optimum reduced course of prescriptions extended from 28 days. This would reduce the amount of prescriptions pharmacies received and reduce the amount paid to pharmacies.
36. Day Lewis believed that such radical budgetary changes would be a main driver of change in the pharmacy market.

The transaction and counterfactual

37. Day Lewis stated that, absent the merger, it believed that Sainsbury's pharmacy business would have continued in the market as it understood that the pharmacy business increased the general sales of the supermarket. Thus it would have been advantageous for Sainsbury's to have remained in the market.

Views on the merger

38. Day Lewis said Sainsbury's pharmacies would be run more efficiently as a result of the merger, as it believed that Celesio was a top-end operator and would implement necessary changes.
39. Day Lewis said there would be a minimal effect on the wider market from the merger; however, it noted that there would be increased local competition in some areas.
40. Day Lewis said the Boots and Walgreens merger produced a bigger player into the pharmacy market than a Celesio / Sainsbury's merger would. Based upon this, Day Lewis thought the merger should go through.