COMPETITION TRIBUNAL
REPUBLIC OF SOUTH AFRICA

Case No: 69/LM/Sept02

In the large merger between:

Clicks Pharmaceutical Wholesale (Pty) Ltd

and

New United Pharmaceutical Distributors (Pty) Ltd

Reasons for Decision

APPROVAL

On 5 December 2002 the Competition Tribunal issued a Merger Clearance Certificate approving the merger between Clicks Pharmaceutical Wholesale (Pty) Ltd and New United Pharmaceutical Distributors in terms of section 16(2)(a). The reasons for the approval of the merger appear below.

The Parties

1. The acquiring firm is Clicks Pharmaceutical Wholesale (Pty) Ltd ("CPW")[1]. It is a wholly owned subsidiary of the Clicks Organisation (Pty) Ltd, which is ultimately controlled by New Clicks Holding Limited ("New Clicks"), a publicly listed investment holding company, comprising many institutional and individual investors.

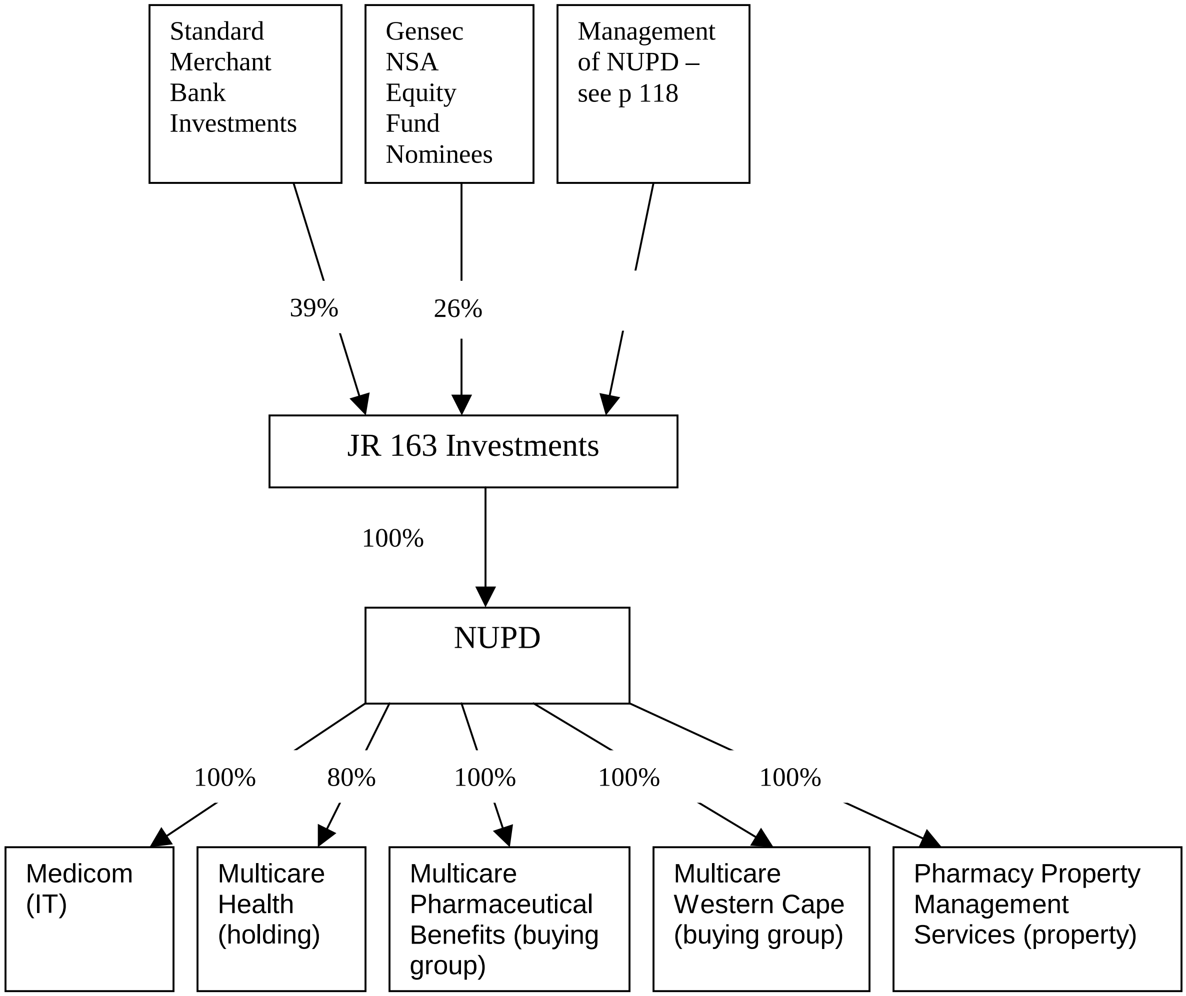
2. New Clicks is a company with operations in South Africa and Australia. trades through the brands Clicks, Discom, CD Wherehouse, Musica, Priceline and the Body Shop. Only the Clicks brand is relevant to this merger assessment.

3. New Clicks further has a 56% interest in the Link Investment Trust ("LIT") and a financing arrangement with Purchase Milton & Associates ("PMA"). These relationships are elaborated further below. 4. The target firm is New United Pharmaceutical Distributors ("NUPD"). The shareholding and subsidiaries of NUPD is set out in the diagram below.[2] NUPD operates as a

[1] This was incorporated in 2000 but has never traded and remains a dormant company.
[2] Medicom Commercial Consultants(Pty) Ltd provides IT services to NUPD; Multicare Health Centre (Pty) Ltd operates as a holding company and Multicare Pharmaceutical Benefit Management (Pty) Ltd and Multicare Western Cape operate as buying groups for various independent retail pharmacies.

wholesaler of scheduled and unscheduled substances and patent products[3].

Pre-merger shareholding in and subsidiaries of NUPD:-



The Merger Transaction

4. The transaction entails Clicks (the retailer) acquiring certain assets and liabilities from NUPD (the wholesaler) relating to its business as a wholesaler of scheduled and unscheduled substances and patent products. NUPD is being acquired as a going concern. In terms of the sale of business agreement, New Clicks nominated CPW to be the purchaser. Post-merger CPW will own and control the NUPD business and CPW will in turn be indirectly controlled by New Clicks.

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[3] The latter includes alternative medicines, baby products; confectionary, toiletries, first aid, foot care, general toiletries, hair care, household, sport, health nutrition, veterinary, patent medicines, skin care, special foods. Patent products refer to branded non-pharmaceutical products sold by NUPD. More on the distinction is set out below.

Rationale for the Transaction

5. The parties assert that the merger will afford NUPD greater growth opportunities whilst its bargaining power in relation to suppliers will be enhanced.

6. It aligns with New Clicks' long-term strategy with regard to healthcare. To the extent that Clicks has its own internal distribution capacity, namely bulk distribution, they will not integrate their activities with those of NUPD but rely on expertise and advice from NUPD with respect to bulk and fine distribution. Accordingly, there are synergistic benefits insofar as NUPD is familiar with distribution at the wholesale level, whilst Clicks' area of expertise is predominantly at the retail level.

The Relevant Market

7. Clicks retails lifestyle, beauty and health products to the end-consumer. NUPD distributes scheduled and unscheduled pharmaceutical and patented products to retailers.[4] The two firms operate in different levels of the supply chain, a vertical relationship, even though there is currently no relationship between the two entities. There is no overlap between NUPD and Clicks in the wholesale market. Clicks sells only to the end-consumer, whilst NUPD distributes to retailers.[5] There is no overlap in retail either, since NUPD does not distribute to final consumers. The Commission nevertheless examined the relevant markets to test whether in either the downstream or upstream markets, either firm is dominant.

8. The Commission examined both the upstream (**wholesale distribution**) and downstream (**retail distribution**) markets. In respect of wholesale distribution, there was further division into scheduled on the one hand and unscheduled and patented pharmaceuticals on the other hand. In the retail market, the Commission looked at the retail distribution of health, lifestyle and beauty products.

9. The distinction between scheduled and unscheduled pharmaceuticals is laid down in terms of the Medicines Control Act, since the former are subject to various regulatory and control requirements.[6] They are controlled in terms of dispensing, delivery conditions, storage conditions and usage. They are distributed by means of "fine distribution" methods, a term of art, referring to delivery of high value scheduled drugs in frequent and smaller batches. By contrast, there are no such stipulations laid down in respect of non-scheduled pharmaceutical products. They can be distributed by anyone without any formal storage or delivery procedures,

[4] NUPD does wholesale certain scheduled substances and unscheduled substances and patent products that are substitutable for certain health, beauty and lifestyle products retailed by New Clicks.

[5] Mention is made of Clicks having its own bulk distribution facilities but this is only for distribution to its own stores.

[6] Medicines are defined in terms of the Medicines Control Act No 101 of 1965.

typically by bulk distribution methods. Patent products are included in the unscheduled category.

Impact on competition

10. Notwithstanding the lack of overlap between the activities of the merging parties, we set out below the competitive position of each, relative to their competitors in the upstream and downstream market, respectively.

Upstream Market

Wholesale distribution of scheduled pharmaceutical products

Firm	***Market share***
NUPD Group	8%
International Healthcare Distributors	35.28%
Kinesis Logistics	25.33%
Adcock Ingram	13.15%
Pharmaceutical Healthcare Distributors	7.4%
Free State Buying Association	3.56%
Transfarm	1.83%
Natal Wholesale Chemists	1.64%
Pharmed	.71%
Létangs	.69%
Resepkor	.05%

11. The barriers in this market are relatively high on account of specific regulatory requirements with respect to specialised delivery systems for fine distribution as well as sophisticated, capital-intensive batch tracking processes. Nevertheless NUPD has a market share of approximately 8%. IHD is the dominant competitor in this market and there are 9 other competent competitors.

Wholesale distribution of unscheduled pharmaceutical products

12. The estimated market share of NUPD is less than 10%. The parties were not able to provide market shares, but indicated that their competitors included:

- Tibbett and Britten
- Specialised Consumer Services
- Interhold Limited (Metro Cash and Carry)
- Massmart Holdings (Makro)
- Free State Buying Association (Alpha Pharm Bloemfonteing)
- Natal Wholesale Chemists
- Adcock Ingram

- Free State Buying Association (Alpha Pharm Eastern Cape)

13. The parties gave an estimate of NUPD's market share being well below 10% when one has regard to the number and variety of alternative suppliers of such products. The non-scheduled pharmaceutical market has low barriers to entry because there is no need for fine distribution but firms can distribute in bulk. Pharmacies can, in addition to the various other avenues, source these products from large retailers such as Pick and Pay. NUPD is not dominant in the upstream market.

Downstream market

14. In this market the market position of Clicks is analysed, insofar as they sell lifestyle, beauty and health products to the final consumer. The parties were unable to furnish market shares in respect of each discrete category. Some reliance was made on a market report by AC Nielsen, which comprised statistics from Clicks, Pick 'n Pay Family Stores and Woolworths in respect of various product categories, including *inter alia*, household, toiletry and health products. However, to the extent that other alternative suppliers of the same products in each category were omitted from this evaluation, we accept that Clicks market share figures may be inflated.

- **Lifestyle products**

15. Nielsen estimated this at approximately 15% but did not account for some products being sold by retailers such as furniture stores. The parties in their Competitiveness Report estimated market share in this category to be 10% or less. Certain specialised grocery and discount chains were also excluded. The Commission indicated that, on investigation, Clicks' share was probably less than 1% of the broader lifestyle market[7].

- **Beauty products**

16. AC Nielsen estimated Clicks' market share at 14%. The management of New Clicks estimated it at between 8 and 10%. Once again, there are a proliferation of competitors in the market, including the large and smaller grocery retail chains which were not taken into consideration.

- **Health products**

17. Nielsen estimated this to be around 22%, since it excluded health products sold by retail pharmacies. Management of Clicks estimated this at between 8 and 12%. Once again, there are a variety of competitors in this market, including grocery chains and independent health shops.

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[7] No market shares were given but instead contribution of each subcategory of lifestyle product to Clicks' total revenue.

18. There are no barriers to entry in the non-scheduled and patent product market since no regulatory requirements or stipulations exist with regard to how products are stored. Countervailing power exists in the form of large buying groups, retail and wholesale chains, informal traders, pharmacies and health shops. For instance, significant competitors of New Clicks in the retail of lifestyle, beauty and health products include Pick ‘n Pay, Shoprite Checkers, Superstar, numerous pharmacies and health stores, Woolworths, Stuttafords, Edgars, Truworths, Foschini, @ Home, Mr Price Home, Game, Makro. There are no exclusive supply agreements between either of the parties.

19. From this analysis we can conclude that there are no dominance concerns in the downstream market either.

20. Further, there are numerous other pro-competitive aspects identified from the parties’ papers:

- The proposed merger will allow NUPD, through access to Clicks’ range of multinational suppliers and enhanced bargaining power, to increase its product range, (as it states, become a “full-line wholesaler” again) affording customers access to a wider variety of products;
- Further, the parties view the merger as necessary in a market where manufacturers are exerting their collective muscle against wholesalers and wholesalers having to in consequence consolidate amongst themselves alternatively form alliances with retail pharmaceutical chains, an essentially proactive strategy.

Pharmacies

21. Click’s elaborated on its relationship with PMA and LIT, which it frankly described as facilitating its corporate participation in the retail pharmaceutical sector. It has an interest in the LIT, a franchisor for the Link Group of pharmacies, a group of pharmacists and other members who operate 307 Link-branded pharmacies across South Africa. Clicks reassured that it merely owns the Link brand but does not presently control the Link branded pharmacies which are independent. It further provides arm’s length short-term services to the Link pharmacies. The relationship with Purchase Milton & Associates (“PMA”) is a commercial one. The PMA is described as a flagship pharmacy company of Clicks and operates 76 pharmacies within South Africa. Clicks provided loan finance to the company to facilitate the purchase by PMA of various pharmacies[8].

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[8] The rationale for Clicks’ relationship with PMA is to do with its anticipation of deregulation of pharmacy ownership, whereupon, in terms of an agreement with PMA, it might later acquire some of these pharmacies. The association further involves certain service level agreements which facilitate Clicks providing specified support services. It has no pre-emptive rights in respect of Link pharmacies.

22. The merged firm will not however have the ability post –merger to influence the distribution strategies of either the Link or PMA pharmacies because it lacks the legal or commercial ability to control them. For this reason foreclosure strategies that vertical mergers can sometimes give rise to, are unlikely here.

23. Nevertheless these relationships caused various pharmacies to voice concern about potentially anticompetitive practices arising in the event that Clicks enters the retail pharmaceutical sector.

24. Currently, the Pharmacy Act No. 53 of 1974 governs the licensing and owning of pharmacies. There are steps afoot to change this and allow corporates to own pharmacies. In the event of pharmacy ownership being deregulated, Clicks would open up dispensaries in its Clicks and Discom branded stores. If this occurred, Clicks would compete with pharmacies at retail level and simultaneously, through its joining with NUPD, would supply them with pharmaceuticals at the wholesale level. While this is not relevant to this merger, it is likely that Clicks will want to use this transaction to facilitate its entry into the pharmaceutical market, so that when it starts retailing scheduled pharmaceuticals, it has its own distribution network to source them. The likelihood of this occurring is uncertain and has no impact on this merger assessment. If and when deregulation of the industry occurs and Clicks acquires any pharmacies in which it presently has an interest, this will form the subject of a separately notifiable transaction/s and will be dealt with accordingly.

Conclusion

No deregulation has occurred as yet and we cannot speculate into the future. As to when this might happen. It suffices for the purposes of this merger, that we conclude that the merger will not lead to a substantial lessening of competition. The Tribunal therefore is justified in approving the transaction unconditionally. There are no public interest concerns which would alter this conclusion since the NUPD business is being acquired as a going concern.

_______________ 13 December 2002

N. Manoim Date

Concurring: D.Lewis, U. Bhoola

For the merging parties:	Sonnenbergs Attorneys
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