



Public Competition Assessment

11 November 2020

Elanco - proposed acquisition of Bayer's animal health business

The ACCC's decision

1. On 9 July 2020, the ACCC announced its decision not to oppose the proposed acquisition by Elanco Animal Health Incorporated (**Elanco**) of Bayer Aktiengesellschaft's (**Bayer**) Australian animal health business (the **proposed acquisition**) after accepting a section 87B undertaking to divest the Avenge+ Fly, Drontal, Profender and Droncit brands (the **Undertaking**).
2. The ACCC considers that the proposed acquisition, taking into account the divestitures required by the Undertaking, is unlikely to contravene section 50 of the *Competition and Consumer Act 2010* (the **Act**). Section 50 prohibits acquisitions that would have the effect, or be likely to have the effect, of substantially lessening competition in any market.
3. The ACCC considers that without the divestments, the proposed acquisition is likely to substantially lessen competition in the markets for sheep lice treatments, and gastrointestinal worming treatments for companion animals. The ACCC also considers that the global divestment of Elanco's Osumnia brand to Dechra is likely to remedy the loss of future competition between Elanco and Bayer in the market for otitis treatments.
4. This Public Competition Assessment outlines reasons for the decision by the ACCC not to oppose the proposed acquisition.
5. Please note that this and other public competition assessments are subject to the following qualifications:
 - The ACCC considers each transaction on a case-by-case basis and so the analysis and decision outlined in one assessment will not necessarily reflect the ACCC's view of another transaction.
 - As assessments are relatively brief and do not refer to confidential information, assessments do not necessarily set out all of the issues and information considered by the ACCC.

The parties and the transaction

The acquirer: Elanco

6. Elanco is a global animal health company that develops, manufactures and markets products to prevent and treat diseases in companion and production animals. It was formed in 1954 as the animal health division of Eli Lilly and was spun off on 11 March 2019.

The target: Bayer's animal health business

7. Founded in 1863, Bayer is a global pharmaceutical and life sciences company active in the areas of pharmaceuticals, consumer health, crop science and animal health. Bayer Animal Health is the Bayer Group's animal health division.

The transaction

8. Elanco proposes to acquire Bayer's animal health business, which covers the development and distribution of prescription and non-prescription products for production and companion animals.

Review timeline

9. The total elapsed time from start to finish was approximately seven months. However, the total period net of time taken by the parties to submit information or documents was 59 business days.

Market inquiries

10. The ACCC conducted market inquiries with a range of industry participants, including competitors, potential competitors, customers, industry associations and other interested parties. Submissions were sought in relation to the substantive competition issues and the proposed Undertaking.

Market definition

11. The ACCC's starting point for considering which markets will be affected by the proposed acquisition is to identify the areas of overlap between the products actually or potentially supplied by the merger parties. The ACCC then considers other actual or potential suppliers of those products, as well as what other products constitute sufficiently close substitutes to provide a significant source of constraint on the merged entity.
12. The ACCC focused on competition between products which treated particular pathologies in each species of animal. The ACCC's investigation showed that consumers typically choose products to prevent or treat specific parasite/s for their pets or livestock, and look to efficacy rather than understanding the particular chemical classes or active ingredients. Accordingly, the ACCC considers that products with claims to treat certain conditions are most likely to compete strongly with products making similar claims, regardless of the underlying chemical components.

13. The ACCC considered the competitive effects of the proposed acquisition in the following markets:
 - Gastrointestinal worming treatments for companion animals
 - Companion animal endectocides
 - External parasite treatments for companion animals
 - Otitis treatments
 - Sheep lice treatments
 - Cattle tick treatments, and
 - Cattle fluke treatments.
14. The ACCC's review focused on the markets for sheep lice treatments and gastrointestinal worming treatments for companion animals as these were the only areas of overlap which raised competition concerns.

Whether product rotation effects market definition

15. For some production animal treatments it is recommended that consumers rotate different chemical classes to avoid parasites building resistance. It was put to the ACCC that this effectively meant these products marketed by the parties provided limited competitive constraint on each other, because consumers would be required to regularly switch between Elanco's and Bayer's brands as they are in different chemical classes.
16. The ACCC considers that even though these products are recommended for rotation, they still compete closely with each other. Not all consumers will rotate products and the timing and extent of rotation will vary. Market feedback indicated that products designed to treat the same parasite compete closely, regardless of the active ingredients.
17. Therefore, the ACCC considers that, for the purpose of analysing the likely competitive effect of the proposed acquisition, different chemical classes treating the same target pathology are in the same market.

Gastrointestinal worming products for companion animal

18. There are two categories of products that can treat gastrointestinal worms. Endectocides, which are broad spectrum products and also treat external parasites as well as gastrointestinal worms, and treatments for gastrointestinal worms only. Whilst some consumers may purchase an endectocide to treat gastrointestinal worms along with external parasites, the relevant issue in considering whether gastrointestinal worming treatments for companion animals are in a separate market to endectocides is whether consumers are likely to switch from one product to another in response to a change in relative price, service or quality.

19. Market feedback indicated that there are a significant number of consumers that require worming-only treatments for their pets, and that in this category of products Elanco's Milbemax competes closely with Bayer's Drontal and Profender brands.
20. Market feedback also indicated that although endectocides can treat gastrointestinal worms, they are primarily marketed as flea and tick treatments. This same feedback indicated that it is unlikely that there would be sufficient substitution by consumers who do not need to treat their pets for external parasites to endectocides in response to a small but significant increase in the price of gastrointestinal worming products.
21. Therefore, for the purpose of analysing this proposed acquisition, the ACCC considers that products which solely treat gastrointestinal worms are in a separate market to endectocides.

Competition analysis

22. The ACCC analysed a range of information, including internal documents and financial information from Elanco and Bayer. The ACCC also conducted extensive market inquiries with interested parties.
23. For production animals, the ACCC identified competition concerns in the market for sheep lice treatments. For companion animals, the ACCC had concerns with the markets for gastrointestinal worming products and otitis treatments.
24. The ACCC considers that the proposed acquisition is unlikely to raise concerns in the following markets:
 - External parasite treatments for companion animals
 - Companion animal endectocides
 - Cattle fluke treatments, and
 - Cattle tick treatments.
25. In relation to the markets for external parasite treatments for companion animals, companion animal endectocides and cattle fluke treatments, the ACCC considers that the proposed acquisition is unlikely to substantially lessen competition due to the number and strength of competing products. In relation to cattle tick treatments, the ACCC considers that Bayer has a limited presence in this market, such that the proposed acquisition is unlikely to remove a constraint on Elanco.

Sheep lice treatments

26. Elanco and Bayer are the two largest suppliers of sheep lice treatments in Australia, and the proposed acquisition would result in Elanco being the dominant supplier with approximately 70 per cent market share¹ post-acquisition.

¹ Baron Strategic Services

27. The ACCC considers that other sheep lice treatments, including generic and rural retailers' private label products, are unlikely to be a sufficient constraint on Elanco as:
- Consumers are primarily concerned with efficacy of a product, and will typically purchase products they have previously had good results with rather than using untrusted products and risking re-infestation which would require additional treatment. This behaviour has led to strong brand loyalty in the market.
 - Elanco's Extinosad and Bayer's Avenge+ Fly are perceived to have superior efficacy and, in line with the point above, are the brands that are most likely to be stocked by agricultural retailers.
 - Lice infestations can reduce the sale price of wool by \$35 - \$40 per sheep, whereas treatments typically cost \$1 - \$1.50 per sheep. As such, consumers are unlikely to switch to other products, including unproven generic and private labels in response to small but significant price increases.
28. Accordingly, the ACCC concluded that the proposed acquisition would remove the closest constraint on Elanco in the sale of sheep lice treatments.
29. To remedy the ACCC's concerns, Elanco gave the Undertaking to the ACCC pursuant to s87B of the Act to divest the Avenge+ Fly brand (the **Avenge Sheep Lice Business**) to an ACCC approved purchaser. Avenge+ Fly is a strong brand with a significant share of the market. The divestment is intended to enable a new or existing supplier of sheep lice treatments to replace the competitive constraint that would have been lost as a result of the proposed acquisition.
30. Taking into account the divestitures required by the Undertaking, the ACCC's view is that the proposed acquisition is unlikely to substantially lessen competition in the market for the supply of sheep lice treatments in Australia. Further information about the Undertaking is set out below.

Gastrointestinal worming treatments for companion animals

31. The ACCC was concerned that the proposed acquisition would remove Elanco's closest competitor in the market for gastrointestinal worming treatments in Australia. Post-acquisition, Elanco would have a market share of approximately 45 per cent.²
32. Information available to the ACCC indicated that Elanco's Milbemax and Bayer's Drontal brands are each other's closest competitors, with strong brand recognition. Market feedback indicated that consumers are typically brand loyal as trust in the safety and efficacy of a product are the most important factors when consumers choose products for their pets.
33. The ACCC found that generic products, including generics of the parties' products, do not have a significant market share, are not widely available in the major retail outlets and are not perceived to have the same efficacy of Elanco's

² Baron Strategic Services

and Bayer's products. As such, the ACCC considers that other gastrointestinal worming treatments, including generics, are unlikely to impose a sufficient constraint on Elanco post-acquisition.

34. To remedy this concern, Elanco gave the Undertaking to the ACCC pursuant to s87B of the Act to divest the Drontal, Profender and Droncit brands (the **Companion Animal Business**) to an ACCC approved purchaser. The divestment of these brands removes the overlap between Elanco and Bayer in gastrointestinal worming products for companion animals.
35. Taking into account the divestitures required by the Undertaking, the ACCC concluded the proposed acquisition is unlikely to substantially lessen competition in the market for the supply of gastrointestinal worming treatments for companion animals. Further information about the Undertaking is set out below.

Otitis treatments

36. The ACCC was concerned that the proposed acquisition would remove competition between Elanco and Bayer for the supply of otitis treatments in Australia. Elanco's Osurnia and Bayer's Neptra products are the only two long acting otitis treatments with regulatory approval in Australia, with the balance being short acting treatments. Short acting treatments require owners to treat their pets daily for one week or longer, by dropping an ointment in their ears. Whereas long acting treatments require only one or two treatments, administered by a vet.
37. The ACCC considers that the significant difference in application means that long acting treatments are more likely to be competitively constrained by other long acting treatments. The ACCC was therefore concerned that the proposed acquisition would have the effect of substantially lessening competition in the supply of otitis treatments.
38. Ultimately the ACCC did not need to reach a concluded view on the potential impact on competition in relation to otitis treatments, as Elanco agreed to divest the global rights for Osurnia to Dechra Pharmaceuticals PLC. Dechra completed the global acquisition 28 July 2020.³ This divestment removes any overlap between Elanco and Bayer in long acting treatments and thus removes any potential competition concern.

Undertaking

39. In order to address the ACCC's competition concerns in relation to the markets for sheep lice treatments and gastrointestinal worming treatments, Elanco offered the Undertaking pursuant to section 87B of the Act. The ACCC spoke to a range of market participants about the Undertaking, including potential purchasers.
40. The ACCC concluded that the Undertaking addressed its competition concerns with the proposed acquisition. A copy of the Undertaking is available on the ACCC mergers register and undertakings register.

³ <https://otp.investis.com/clients/uk/dechra/rns/regulatory-story.aspx?cid=1758&newsid=1404299>

41. A brief summary of the Undertaking offered by Elanco is set out below:

- Elanco will divest the Avenge Sheep Lice Business, and the Companion Animal Business (the **Divestment Businesses**), either to a single or separate ACCC-approved purchasers. Divestiture will include all necessary assets including inventory, business records, contracts, regulatory approvals, and intellectual property rights.
- At the option of the ACCC-approved purchaser(s), Elanco must:
 - supply any technical assistance
 - transfer necessary personnel, and
 - ensure the continued supply of goods or services

which are necessary for the operation of the divestment brands, and are required by a purchaser to establish itself as a competitor in the relevant markets.

- Elanco must appoint an ACCC approved independent manager to manage the Divestment Businesses from completion of the proposed acquisition until the divestiture of the Divestment Businesses.
- Elanco must appoint an ACCC approved independent auditor to monitor Elanco's overall compliance with the Undertaking.

Conclusion

42. Based on the above analysis, the ACCC considers that the proposed acquisition of Bayer Group's Australian animal health business by Elanco, taking into account the divestitures required by the Undertaking, is not likely to have the effect of substantially lessening competition in any relevant market.