

Amcor/Bemis: Flexible Medical Packaging Overlaps Draw DOJ Scrutiny

Deal Update

DOJ staff attorneys investigating Amcor's proposed \$5.2 billion purchase of packaging rival Bemis (BMS) have keyed in on two healthcare product lines in which the merging parties overlap, sources familiar with the matter said.

The deal would combine two of the three dominant producers of coated TyVek, a breathable medical packaging film that can be sterilized. The tie-up would also join two significant U.S. converters of vented medical bags.

DOJ staff has interviewed industry participants about these overlaps as recently as two weeks ago, the sources said.

Given market shares and competitive dynamics, the merging firms' overlap in coated TyVek raises a more significant antitrust issue than the vented medical bag overlap, industry sources said. Reflecting this dynamic, sources said that over time, DOJ interviews have become more focused on coated TyVek, to the exclusion of vented medical bags.

The merging parties also overlap in food packaging, but these markets are generally fragmented and characterized by a more robust competitive environment than their medical counterparts.

Amcor and Bemis, who announced their deal on August 6, have not disclosed the receipt of a DOJ second request.

Spokespeople for Amcor and the DOJ declined to comment. Bemis did not respond to requests for comment.

Coated flexible medical packaging. Amcor and Bemis both produce various types of sterile flexible medical packaging, which is sold to medical device manufacturers to protect medical equipment and devices ultimately sold to hospital groups and doctors.

Most sterile medical packaging utilizes TyVek, a breathable polyethylene film made solely by DuPont that can be sterilized by ethylene oxide gas, and durably maintains the sterility and integrity of the package over time.

Medical packaging converters manufacture uncoated TyVek packaging for various medical films, bags, and pouches. A few converters, including Amcor and Bemis, also produce coated TyVek,

which provides a sterilized sealant for products such as IV bags, surgical trays, and other sealed products.

DOJ's interviews with industry participants have homed in on the merging firms' overlap in coated TyVek production, sources familiar with the discussions said.

Post-merger, the combined Amcor/Bemis and one other firm, Oliver, would control roughly 90 percent of the coated TyVek market, industry executives said. "With Bemis and Amcor coming together you'll have them and Oliver that will really dominate that area," one executive said.

Moreover, the post-merger entity would account for the lion's share of the market, a second executive said, estimating that Amcor and Bemis together control 70 to 75 percent of coated TyVek sales.

Given the distinct technology, assets, and expertise—including developing a coating formulation—required to manufacture coated TyVek, entry barriers into the market are high, the sources said. "You have to have a certain coating that's got some technology to it that not everyone has" the second executive said, adding that "only those three guys have it."

Though the industry has worked toward creating uncoated TyVek products that could replace coated products in certain end uses, executives said those alternatives are less reliable, and the lengthy, expensive process of switching would likely deter converters from doing so.

"You can use uncoated Tyvek, but it's not done a lot because it's a little bit more problematic for getting good seals that will peel without fiber tear," the first executive said.

The second executive added that uncoated Tyvek seal alternatives are still in early stages of development. "There's no quick option," the second executive said, adding that because coated TyVek is already significantly more expensive than uncoated alternatives, customers may be unlikely to switch in response to a post-merger increase in coated products' prices.

Vented medical bag. DOJ staff is also investigating the deal's impact on vented medical bags, sources said.

DOJ has previously shown an interest in this product line—in 2010, the antitrust division brought a suit against Amcor's acquisition of Rio Tinto's Alcan Medical packaging business due to the deal's effects in the vented medical bag market.

DOJ's complaint said that "Amcor, Alcan Packaging and one other competitor are the only significant competitors in the U.S. market for vented bags for medical use." That unnamed third competitor was Bemis, industry sources said.

To settle the lawsuit, Amcor divested Alcan's vented bag assets to Printpack, a new entrant into the vented bag space.

However, the vented medical bag market has evolved since 2010—market shares have shifted, producers have expanded their capacity, and a number of firms are capable of producing the sterilized bags, industry sources said.

As a result, some executives dismissed vented medical bag as a significant concern in the deal, citing more competition and capacity in the space relative to coated TyVek. "Quite a number of other people have the capability, there's capacity, I just don't think it should be an issue," the first executive said.

That said, DOJ's lawsuit identified vented bags as a relevant product market, and said entry or repositioning was unlikely to mitigate the deal's anticompetitive effects. The complaint also described the transaction as likely to increase the likelihood of anticompetitive coordination, meaning that the Amcor/Bemis tie-up, which would increase concentration in the vented bag market, could similarly raise coordinated effects questions.

Timing questions. The companies' overlaps in flexible medical packaging, combined with DOJ staff's ongoing interviews, provide some indication that the deal is likely to attract a DOJ second request, if it hasn't already.

And especially in coated TyVek, absent some showing that it is not a valid product market, or that barriers to entry are low, market concentration metrics indicate that DOJ would likely demand a divestiture of one of the merging parties' overlap assets as a condition of clearance.

Separate technology and production capacity suggest that Amcor could resolve the coated TyVek overlap through divestiture.

Bemis's investor presentations indicate that its entire healthcare and medical device packaging business generates around \$360 million in worldwide sales, below the merger agreement's \$400 million 2017 net sales divestiture cap. Furthermore, coated TyVek and vented medical bag represent just a portion of Bemis's broader healthcare packaging product line, meaning that a divestiture demand encompassing Bemis's entire healthcare business would be over inclusive.

However, especially with DOJ's antitrust division generally adopting an increasingly rigorous approach to evaluating structural remedies, a divestiture requirement, even if firmly under the merger agreement's divestiture cap, would create at least some incremental timing and outcome risk around U.S. antitrust clearance.

The merging parties have said that they expect the deal to close in the first quarter of 2019.