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Dear Sarah

Re Proposed acquisition of Neogen's Genomic Business by Zoetis Holdings LLC

1. I have been asked to comment on the approach to market definition in the SOI, specifically as to the treatment of different levels of the supply chain relevant to the merger.
2. In my view:
 - a. It is conventional to draw a distinction between the wholesale and retail levels of a supply chain.¹ The SOI does not do this in relation to genomic testing and instead considers the national market for the supply of genomic testing for beef cattle.
 - b. This appears to be based on a characterisation of the role of PBB and breed societies as providing distribution and marketing services to genomic testing providers as one route for those parties to supply farmers.
 - c. In my view, it is more accurate to say that PBB and breed societies acquire genomic testing services at wholesale in order to provide a bundled genetic evaluation service to their members at retail.
 - d. If a wholesale and retail approach is taken to market definition, then the competition issues become much clearer: there is no aggregation at the retail level (since Neogen does not compete at retail); and whether competition at the wholesale level will be adversely affected will depend on the other sources of supply of genomic testing services to PBB and breed societies.
3. I set out my reasons below.

Background

4. As recognised in the SOI, a genomic test has no utility in itself.² The value comes from being able to use this genomic data to evaluate the genetic merit and potential breeding value of an animal. This can assist selection for breeding, reveal valuable characteristics, and improve the productivity and value of the

¹ CC merger guidelines at [3.36].

² Commerce Commission's Statement of Issues regarding Zoetis Holdings LLC/ Neogen Corporation (SOI) at [33.4].

overall breed over time. In order to unlock that value, however, the results of genomic testing need to be assessed against phenotype and pedigree information using genetic evaluation systems.³

5. The SOI also recognises the role of PBB and breed societies in enhancing the genetic merits of breeds over time. The functions undertaken include:
 - a. Controlling access to phenotype/pedigree information.⁴
 - b. Setting rules for members in relation to genetic evaluations including any situations in which evaluations are compulsory.⁵
 - c. Offering genetic evaluation services to members or allowing third party providers to have access to phenotype/pedigree information to be able to offer those services to members.⁶
 - d. Selecting providers of genomic testing services and genetic evaluation systems to provide the inputs for the genetic evaluation services offered by PBB and breed societies to their members, and contracting with these providers for their services.⁷
6. When it comes to market definition, the SOI adopts a market definition – the national market for the supply of genomic testing for beef cattle – which focusses on the relationship between genomic testing providers and farmers.⁸
7. The absence of a functional level analysis appears to be based on a characterisation of the genomic testing supply chain where providers compete to offer their services to farmers with breed societies playing an “intermediary role”.⁹ The SOI sets out that views that:
 - a. breed societies (and PBB) play a role as *distributors* of genomic testing services: “Zoetis offers its genomic testing services directly to customers (often via breed societies), while Neogen’s genomic testing services are offered and marketed to customers by PBB (who now also markets Weatherbys’ services)”;¹⁰
 - b. [REDACTED];¹¹
 - c. “PBB *facilitates* the supply of Neogen’s genomic testing services in New Zealand, it is not an independent competitor to Zoetis or Weatherbys”;¹² and
 - d. Weatherbys is seen a competitor for the supply of genomic testing services *to farmers*: “While PBB may be able to assist in growing Weatherbys’ presence in New Zealand, it is currently unclear whether

³ SOI at [33.2].

⁴ SOI at [33.2] and [34].

⁵ SOI at [118.2.2].

⁶ SOI at [29], [33.4] and [34].

⁷ SOI at [118.1] and [118.2].

⁸ SOI at [7] and [38].

⁹ SOI at [33.2].

¹⁰ SOI at [89].

¹¹ SOI at [78].

¹² SOI at [89.1].

Weatherbys can provide a competitive reason for farmers to change providers and constrain the merged entity.”¹³

Analysis

8. There are some aspects of the factual background which support the characterisation of PBB and breed societies as fulfilling a distribution or marketing function. For example: genomic testing providers sometimes talk about providing services “through” PBB or a breed society;¹⁴ there are references to PBB or a breed society “sponsoring” entry by a genomic testing provider;¹⁵ PBB presents Neogen and Weatherbys as options which can be ordered through PBB’s platform;¹⁶ and genomic testing providers maintain a distinct brand with farmers.
9. However, in my view it is more accurate to say that PBB and breed societies acquire genomic testing services at wholesale in order to provide a bundled genetic evaluation service to their members at retail.
10. In terms of the commercial relationships and contractual terms:
 - a. PBB and Angus AUS offer genetic evaluation services to members.¹⁷
 - b. As part of these offerings, the farmer can choose between Neogen and Weatherbys on PBB, or between Zoetis, Neogen and Weatherbys on Angus AUS, as the physical provider of genomic testing.¹⁸
 - c. [REDACTED]¹⁹
 - d. Conversely, genomic testing providers contract with PBB and Angus AUS and not with the farmers. [REDACTED]²⁰
 - e. PBB and the breed societies hold the bargaining power in the relationship with genomic testing providers:
 - i. a breed society does not need to use any particular genomic tester, but a genomic tester’s services have no value unless they have an agreement with the breed society to access phenotype and pedigree data (or use generic material);²¹
 - ii. PBB and the breed societies also determine how many options members are given for genomic testing providers and even whether distinct brands are displayed;²² and
 - iii. genomic data is non-proprietary and interchangeable so the results do not depend on who the genomic testing provider is and there is no technical benefit to using the same genomic testing

¹³ SOI at [96].

¹⁴ SOI at [26].

¹⁵ SOI at [119.2].

¹⁶ SOI at [29].

¹⁷ SOI at [29], [33.4.1] and [34].

¹⁸ SOI at [29] and [35].

¹⁹ SOI at [34].

²⁰ SOI at [34], and Zoetis – Neogen – NZCC SOI Response (**SOI Response**) at [REDACTED].

²¹ SOI at [33.4].

²² SOI at [35], and SOI Response at [2.5 (a)] and [8.2].

provider versus switching to another provider.²³

- f. Zoetis does offer some direct services at retail in competition with PBB and Angus Aus. A farmer can order a test on the Zoetis website for inclusion on the TACE/BREEDPLAN evaluation using phenotype and pedigree data from either:²⁴
 - i. Angus NZ or NZ Herefords breed societies; or
 - ii. INHERIT select which is generic US data.

11. There is some suggestion that farmers are relatively “sticky” and that it is uncommon for them to switch between genomic testing providers. I return to this below, but for present purposes it is sufficient to note that the existence of farmer preferences between genomic testing providers would not change the distinct functional levels in the supply chain.

Implications

- 12. The characterisation of PBB and breed societies as fulfilling a distribution or marketing function and the adoption of a market definition without separate functional levels in the SOI means that:
 - a. the competition analysis (in terms of the SSNIP test, closeness of competition, new entry and potential countervailing power) takes places at the retail level even though the merging parties do not compete at retail; and
 - b. the impacts of the merger on competition between Zoetis and Neogen at the wholesale level is not properly analysed.
- 13. Applying a conventional wholesale/retail split makes the competition analysis much clearer.
- 14. In terms of the retail market for the supply of genetic evaluation services:
 - a. This market is dominated by PBB and the breed societies as they control access to the phenotype/pedigree databases.
 - b. Zoetis does compete in this market to some extent.
 - c. But Neogen is not a competitor in this market as it only supplies at wholesale.
- 15. In terms of the wholesale market for the supply of genomic testing services, PBB and breed societies decide which genomic testing providers to engage with, and have changed or added providers in recent years.²⁵
- 16. Returning to the question of stickiness and whether this has an impact on rivalry in the factual, I note that:
 - a. While, in principle, strong end-user preferences for existing providers could make it difficult for an entrant to establish feasible quantities at wholesale, [REDACTED].²⁶ This would suggest there is no particular loyalty or stickiness hurdle for a new entrant to overcome.

²³ SOI Response at Annexure 1 [1.12] and [1.39].

²⁴ SOI Response at [2.5 (c)].

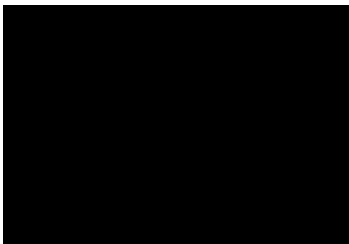
²⁵ SOI Submission – Annexure 6 (NERA Report) at fn 23.

²⁶ [REDACTED].

- b. To the extent that some stickiness exists, it would only seem to be a cause of concern if it prevented a new entrant from becoming established at wholesale. That is, as long as entry and expansion by at least one competing genomic testing provider at wholesale is feasible, it would not seem to matter whether a farmer is sticky to the Neogen brand, the Zoetis brand or a combined brand.
- c. In this regard, there will be some customers who do not yet have a preferred provider (because they have not previously acquired genetic evaluation services) or are experienced but indifferent.
- d. Furthermore, PBB and breed societies are uniquely well-placed to ensure that any stickiness does not prevent a new entrant from becoming established. When the retail and wholesale functional levels are separated out, it is apparent that PBB and breed societies can take a range of escalating steps to shape member preferences and ensure a sufficient volume of testing for an entrant at wholesale, including by:
 - i. educating members that changing genomic testing providers does not impact on comparability over time as the test results are interchangeable;²⁷
 - ii. steering members away from an incumbent through setting the retail price and determining how different testing provider options are presented to members;²⁸ and/or
 - iii. being prescriptive as to the use of a new entrant in certain circumstances or for certain volumes.

17. I trust that this advice is of assistance, and I would be happy to discuss further.

Yours sincerely



James Every-Palmer KC

²⁷ SOI Response, Annexure 2 at [1.17].

²⁸ SOI Response at [2.5 (a)] and [6.8 (a)].