

Review of the local and regional media merger regime

Final report

June 2009

OFT1091

© **Crown copyright 2009**

This publication (excluding the OFT logo) may be reproduced free of charge in any format or medium provided that it is reproduced accurately and not used in a misleading context. The material must be acknowledged as crown copyright and the title of the publication specified.

CONTENTS

<i>Chapter/Annexe</i>	<i>Page</i>
1 Executive summary	4
2 Background to review	7
3 The UK merger regime	17
4 Merger assessment	31
5 Media public interest considerations	51
6 Competition from public sector sources	57
7 Other issues	62
A List of respondents	64
B LMA advertiser survey	66
C Types of evidence	71
D Selected media merger case studies	72
E US DoJ statement on newspaper mergers	104

1 EXECUTIVE SUMMARY

- 1.1 The local and regional press is facing very significant structural and cyclical challenges to its traditional business model. Local and regional newspaper advertising revenues have been in steady decline, in particular due to traditional advertisers moving to online and innovative platforms, and the current economic downturn has exacerbated this decline. The situation is worse still for some of the larger newspaper groups who are highly leveraged, as a result of heavily debt-financed past consolidation.
- 1.2 In this context and at the request of the Secretary of State for Business, Innovation and Skills, the OFT has carried out a review of the merger regime as it applies to the local and regional media sector, with a particular focus on the press. This review has involved significant consultation with interested parties.
- 1.3 The existing UK merger regime is designed to protect competitive rivalry between firms to the benefit of consumers. Whilst the vast majority of mergers will be beneficial or neutral in their effects on competition, mergers can sometimes enable firms to raise prices, lower quality, reduce innovation, or otherwise offer poorer value for money to customers.
- 1.4 The regime is evidence-based and is therefore already capable of reflecting market developments, such as increasing competitive constraints between media, when assessing local or regional media mergers. It is quite possible that print advertising faces sufficient competitive pressure from advertising on other media, especially the internet, to protect consumers (readers and advertisers) in the face of a merger. **However**, this will depend on the specific facts of the case.
- 1.5 The regime is also flexible, in that it is capable of taking account of valid 'failing firm' arguments, efficiencies and customer benefits. For example, if there is clear and compelling evidence that the merger will be beneficial (or neutral) for the market, and therefore consumers, it will normally be cleared. Opinion from stakeholders was divided on whether

regional press consolidation would in fact deliver efficiencies or customer benefits. It is important that the merged entity should have the incentive, as well as the ability, to deliver potential customer benefits arising from the merger. This may be unlikely if competitive pressures are substantially reduced.

- 1.6 Since evidence on the closeness of competition between the merging parties and the strength of countervailing constraints will vary by case, the OFT considers there would be limited value to be gained from 'blue skies' work, carried out without any particular merger in mind.
- 1.7 This review therefore recommends that no further OFT research is currently warranted in this area in the absence of a notified merger. This report, however, provides relevant guidance to market participants and interested parties.
- 1.8 Any merger or transaction involving local or regional press may well benefit from pre-notification discussion with the OFT in order, for example, to discuss the type of evidence that would help in assessing the relevant market definition. Alternatively the parties to such a merger may consider requesting the OFT to 'fast-track' the merger to the Competition Commission in order to allow a more detailed investigation into the issues raised, whilst reducing the length of time taken for the OFT's Phase I review. It is possible under the combination of a longer review, and a different legal test, that a more advantageous outcome could be achieved by merging parties at second phase.
- 1.9 In addition, and notwithstanding the fact-specific nature of any given merger, there may be some lessons that could be learnt from a detailed inquiry into a specific merger or transaction involving the local and regional press. For example, the analytical methodologies employed are likely to be similar across mergers within the same sector.
- 1.10 Given all the above, this review also recommends that no legislative change is required to the existing merger regime under the Enterprise Act 2002.

- 1.11 In media mergers involving newspaper publishing and/or commercial radio or television broadcasting, and raising competition issues, the OFT will ask Ofcom to provide views, arising from its understanding of media markets, on factors relevant to the OFT's decision. The OFT will confirm this in its forthcoming revised guidance on merger jurisdiction and procedure.
- 1.12 Media public interest provisions have so far played no role in local and regional newspaper consolidation under the current regime. Indeed, media plurality considerations might tend to be expected to point in the same direction as competition considerations. Nevertheless, various representations were received that they should be altered, for example to include 'independent investigative journalism' as a consideration. We recommend that the Department for Business, Innovation and Skills (BIS) should consider these representations, as well as take account of the ongoing Ofcom review of Media Ownership Rules.
- 1.13 We note broad concern amongst stakeholders about the potential impact on commercial publishers of local authority publications. We recommend that BIS and/or DCMS¹ should consider the costs, benefits and effects of any intervention or guidance on the scope of local authority publications.

¹ The Department for Culture, Media and Sport.

2 BACKGROUND TO REVIEW

Digital Britain context

- 2.1 The Digital Britain Review is a joint BIS²/DCMS project, described as 'An action plan to secure the UK's place at the forefront of innovation, investment and quality in the digital and communications industries'.³
- 2.2 In its Digital Britain Interim Report⁴ in January 2009, the Government stated that in order to inform whether any change to the merger regime was desirable or necessary, it would invite the Office of Fair Trading (OFT) to undertake an exploratory review across the local and regional media sector and make appropriate recommendations. This was in the context of concerns raised by local media groups that the media merger regime may be preventing or deterring consolidation seen as necessary for the transition of such groups to digital business models.
- 2.3 The OFT launched its review on 13 February 2009,⁵ and issued a Discussion Paper on 10 March⁶ inviting submissions from interested parties. Submissions were received from around 30 respondents, listed at Annexe A. The OFT review team also held meetings with a range of key stakeholders, including groups representing publishers, advertisers and journalists.
- 2.4 We received a detailed submission from the Local Media Alliance (LMA), which represents seven of the largest UK regional publishers. In preparing its submission the LMA commissioned surveys of local

² Formerly the Department for Business, Enterprise and Regulatory Reform (BERR)

³ www.culture.gov.uk/reference_library/media_releases/5548.aspx

⁴ BERR/DCMS, Digital Britain: The Interim Report, January 2009.

⁵ www.of.gov.uk/news/press/2009/14-09

⁶ www.of.gov.uk/shared_of/business_leaflets/general/of1069.pdf

advertisers in a number of local catchment areas, and collated a range of specific examples and qualitative evidence in relation to its members' publications.

- 2.5 In accordance with the Government's original invitation to undertake the review, the primary focus of this review has been on local and regional print news media. However, we also received submissions in relation to radio, magazines, and national newspapers. We expect that many of our findings and recommendations are also broadly applicable to commercial radio, and potentially to other media.
- 2.6 High level conclusions and recommendations from this review were discussed with and submitted to Government during April and May 2009, to fit in with the timetable for publication of the final Digital Britain Report.
- 2.7 The OFT would like to thank all those who have participated in the review process. We are particularly grateful to the Newspaper Society for giving us access to relevant data sources.

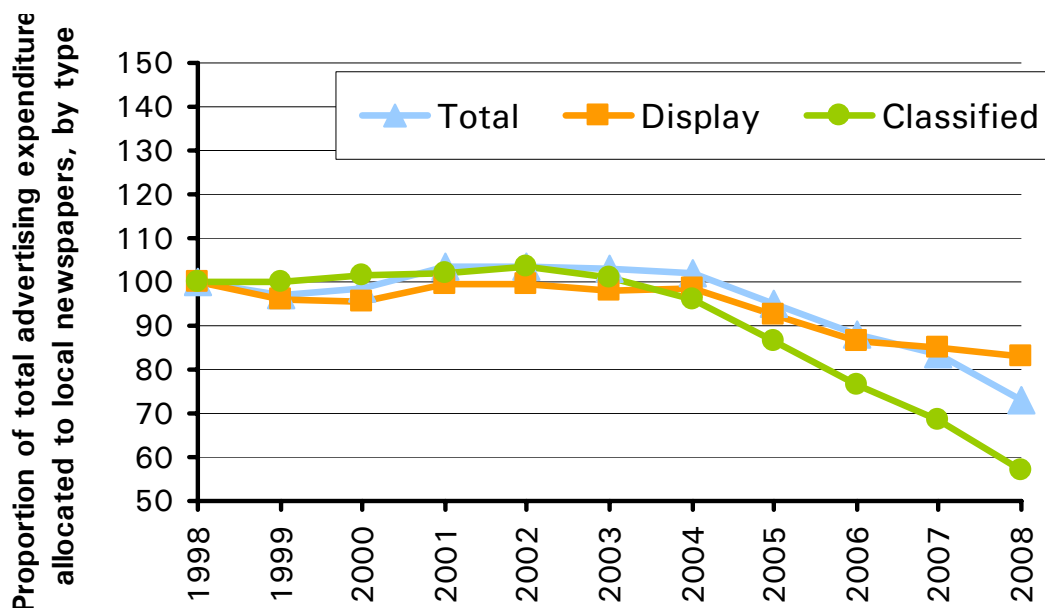
Market developments in local and regional press

- 2.8 Recent trends in the advertising revenues of local newspapers have raised questions about the commercial future of the local and regional press. Local newspaper revenues have fallen by 29 per cent in real terms from their peak in 2004. This decline has gathered pace in the past year, and has brought into question the long-term viability of the advertising-funded business models on which the industry has traditionally relied. In this section, a brief review of some of the key developments in the local and regional newspaper sector is provided, with the intention of giving some perspective on the wider context surrounding the OFT's review of the local and regional media merger regime.
- 2.9 The local newspaper industry is of significant scale, employing over 30,000 people. Approximately three billion local and regional newspapers were distributed in 2008, generating around £3 billion in combined advertising and copy-sale revenues. At the start of 2009,

approximately 1,145 weekly local or regional publications and 124 dailies were published in the UK, and there were over 1,200 local newspaper websites. Local newspaper markets are typically highly concentrated, and in nearly 37 per cent of local authorities a single publisher accounts for over 90 per cent of total circulation. At the national level, the five largest publishing groups supply about 72 per cent of total circulation.

- 2.10 More than 80 per cent of local newspaper revenues are derived from advertising, and this proportion has been increasing over time. Figure 2.1 illustrates the trend in expenditures on advertising in local and regional newspapers over the past ten years, as a proportion of total advertising expenditures. It is clear that the years since 2004 have seen a large-scale shift in advertising spending away from local newspapers.

Figure 2.1: Indices charting the trend in relative advertising expenditures on local and regional newspapers since 1998⁷



Source: Advertising Association's *Advertising Statistics Yearbook 2008* and Newspaper Society.

2.11 One factor contributing to this trend has been the decline in the popularity of local newspapers, which has decreased the attractiveness of the medium to advertisers. The past 20 years have seen sustained decline in the number of local and regional publications. Estimates from the Newspaper Society suggest that, on average, the number of local newspaper buying points has fallen by about 23 per year on average in the past 20 years.⁸ Readership too has been falling – particularly for

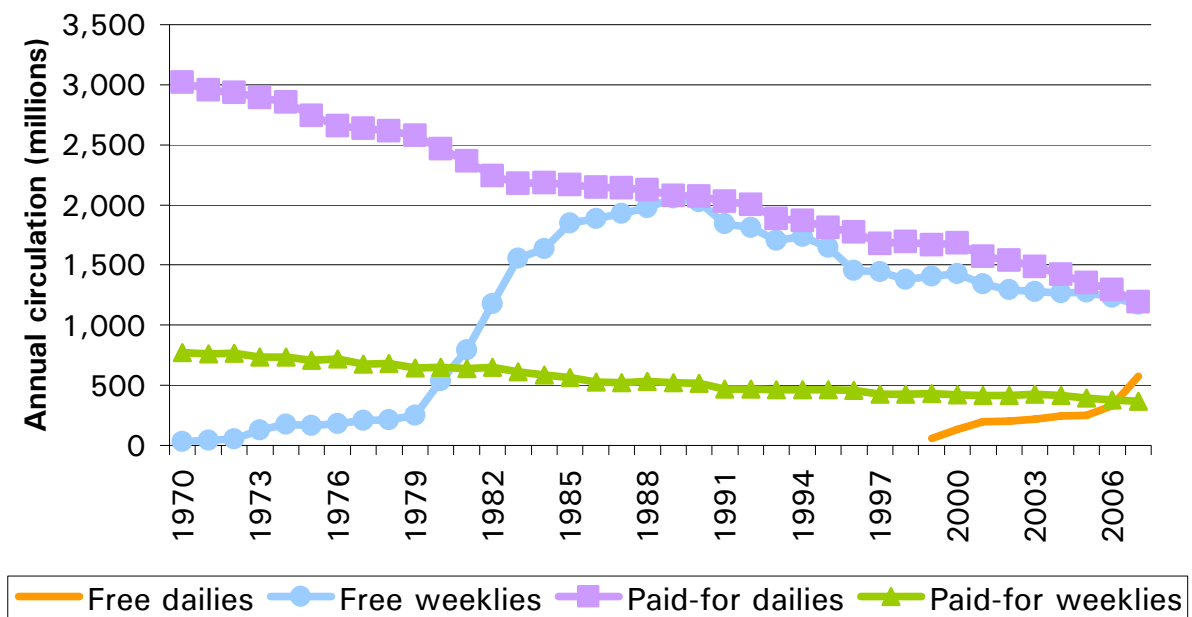
⁷ Here (and in Figure 2.3) classified expenditures on directories for 2008 have been estimated by averaging the trend in the proportion of classified spending accounted for by directories over the past five years, and then using this to extrapolate 2007 expenditure. Spending on online advertising services offered by local newspapers has been allocated to the internet category, rather than being counted as local and regional newspaper advertising expenditures.

⁸ A 'buying point' is defined by the Newspaper Society as 'the lowest level at which an audited circulation certificate is available and national run-of-paper advertising can be bought'. Buying

daily publications, for which the average readership per issue fell by over 20 per cent between 2001 and 2009.

2.12 The combined average circulation per issue of all audited local and regional newspaper titles fell by nearly 40 per cent between January 1989 and January 2009. As Figure 2.2 - which shows the long-term trend in annual circulations - makes clear, this decline has been particularly strongly felt amongst paid-for publications (which account for about half of the total circulation). The annual circulation of free weekly newspapers has followed a similar downwards trend since the early 1990s. Only free daily newspapers have grown in circulation in the past two decades.

Figure 2.2: The trend in the annual circulation of local and regional newspapers since 1970



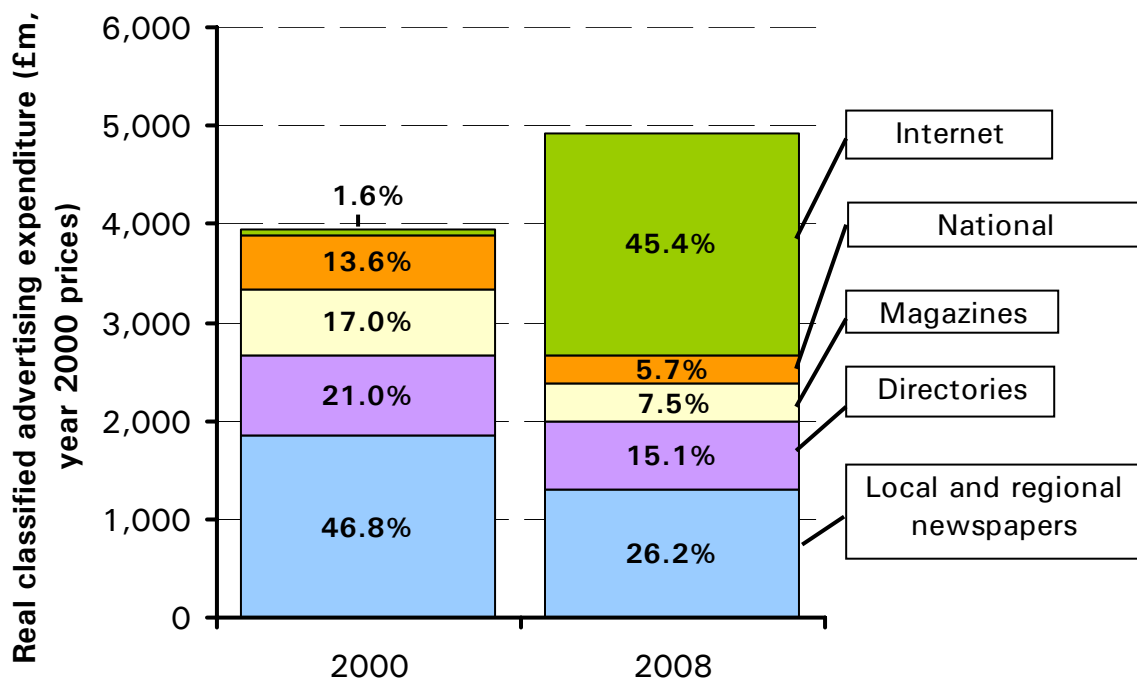
Source: Advertising Association's *Advertising Statistics Yearbook 2008*

points are usually counted instead of titles because different titles in a series will often essentially comprise the same newspaper.

- 2.13 A second factor which has contributed to the structural decline in local newspaper advertising has been the rapid expansion of internet advertising. Expenditures on internet advertising have grown dramatically in the current decade – rising from representing about one per cent of total advertising spending in 2000 to about a fifth in 2008. Advertising expenditures that would previously have been allocated to traditional media types, including the press, have been diverted to online services. While local newspapers have seen rapid growth in their own digital revenues, advertising revenues generated by their websites still only account for a small proportion of overall revenues⁹, and the increases have not been sufficient to offset the decline in the proportion of expenditures allocated to local and regional newspapers.
- 2.14 The internet has been particularly effective at capturing classified advertising spending, which accounts for over two thirds of local newspapers' advertising revenues (recruitment, property and motors being the most important categories). Figure 2.3, which shows the proportion of expenditure allocated to different media types in 2000 and 2008, illustrates how dramatic the rise of internet advertising has been.

⁹ For example, while Northcliffe Media's digital revenues rose by 42% on a like-to-like basis in 2008, they still only accounted for approximately 4% of total revenues.

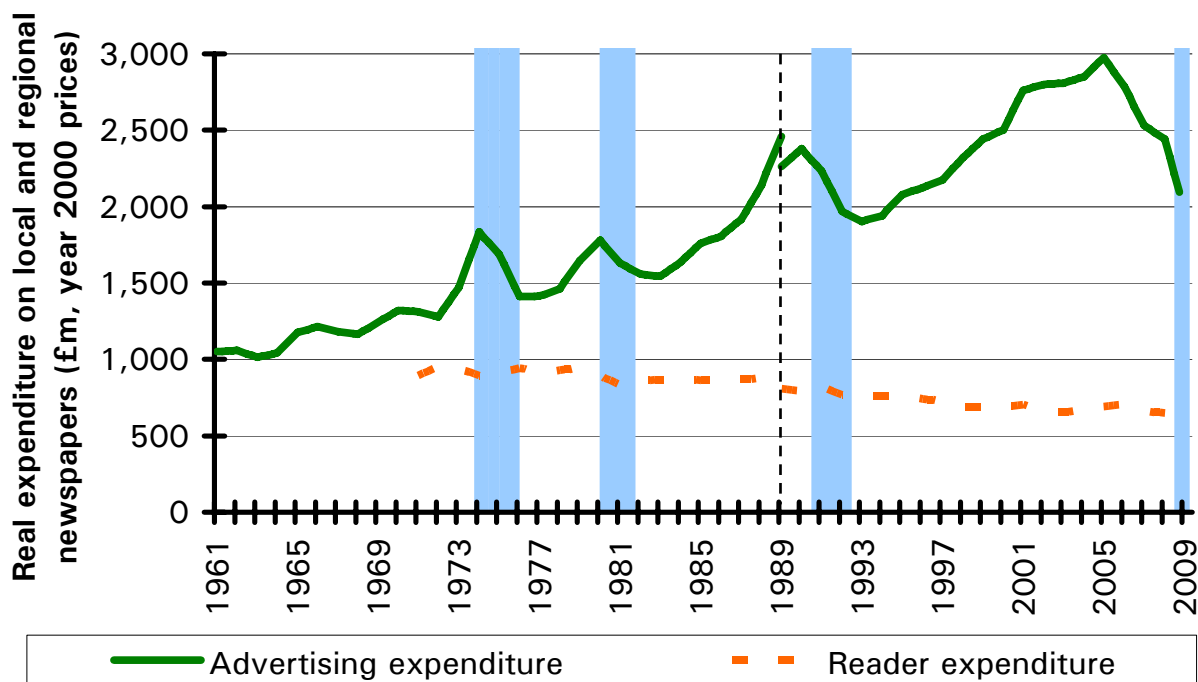
Figure 2.3: Real classified advertising expenditure, 2000 and 2008



Source: Advertising Association's *Advertising Statistics Yearbook 2008* and Newspaper Society.

2.15 The structural decline in spending on advertising in local newspapers has been exacerbated by recent events in the wider economy. Figure 2.4 shows advertising spending in the local and regional press since 1961. Economic downturns are marked by the blue shaded bars. As with advertising spending more generally, previous recessions have been accompanied by falls in the amount spent on advertising in local newspapers.

Figure 2.4: The trend in real annual advertising and reader expenditures on local and regional newspapers since 1961



Source: ONS *Quarterly National Accounts* and Advertising Association's *Advertising Statistics Yearbook 2008*.

The blue shaded bars represent zero or negative seasonally-adjusted GDP growth in the highlighted quarter relative to the same quarter in the previous year. Expenditures do not include advertising expenditures on local and regional newspaper's websites. Advertising expenditure data to the left of the dashed line have been adjusted using the Retail Price Index, data to the right using the Consumer Price Index.

2.16 The depth of the current downturn has put substantial and increasing pressure on local and regional newspapers' advertising revenues. In absolute terms, advertising expenditure on local and regional newspapers is estimated to have fallen by over £400m in 2008 - a year-on-year decline of nearly 19 per cent after accounting for inflation. Indications suggest that the decline has been even more marked this year, with the largest four publishers all reporting drops in advertising revenues of over 30 per cent in the first quarter of 2009. The effect of this has been to

drive down the revenues and margins of the large publishing groups (although the large publishing groups all retained relatively large operating margins in 2008).

- 2.17 Given current predictions there seems little reason to expect these pressures to ease in the immediate future. Even when advertising expenditure picks up again – Enders Analysis predict a return to growth in 2011¹⁰ – it appears unlikely that spending on local and regional newspapers will return to previous levels. There is little reason to expect a reversal in the downwards trend in the proportion of advertising expenditures allocated to local and regional newspapers, and there is consensus amongst industry commentators that, given current business models, increases in the newspapers' digital revenues will not be sufficient to offset the decline in print revenues. Analysis prepared by Enders Analysis as part of the Digital Britain Interim Report forecast that the revenues of local newspapers would decline by over 20 per cent in 2009, and by a significant proportion – around 5 per cent per annum – from 2010 to 2013.¹¹ Given this, further title closures - and so increased concentration in local newspaper markets - appear probable.
- 2.18 These revenue challenges for publishers are further compounded by the fact that some of the larger local and regional newspaper groups are highly leveraged as a result of past consolidation that was heavily debt-financed. These groups are required to make substantial debt repayments.
- 2.19 The past 18 months have been marked by title closures by regional publishers. Estimates vary, but the number of titles closed in 2008 was over 50. The majority of these closures were amongst weekly free titles (which are of course entirely reliant on advertising revenues). As noted

¹⁰ See Annex 1 to the Digital Britain Interim Report; *Key Trends and Issues in UK Media and Telecoms to 2012*, Enders Analysis.

¹¹ *Ibid.*

in a recent market research report,¹² the free weekly sector has always been the most liable to fluctuation in response to changing market conditions, not least because the set-up and operating costs for a free title are far lower for an already established publisher. There have also been some instances of paid daily titles converting to less frequent publication schedules.

¹² Mintel, *Regional Newspapers*, Market Intelligence, May 2009.

3 THE UK MERGER REGIME

Overview

- 3.1 The general framework for the assessment of mergers (including media mergers) under UK law is set out in the Enterprise Act 2002 ('Enterprise Act' or 'the Act'), which came into force in 2003. The OFT carries out a relatively short 'first phase' examination of mergers, at the end of which a decision is taken on whether a more detailed 'second phase' examination by the Competition Commission (CC) is warranted, or whether the merger should instead be cleared by the OFT (with or without remedies). The CC determines the outcome (clearance, prohibition or remedies) of merger cases referred to it by the OFT.
- 3.2 Whilst the vast majority of mergers will be beneficial or neutral in their effects on competition (as the merger outcome statistics provided above demonstrate), mergers can sometimes reduce competitive constraints and thereby enable firms to raise prices, lower quality, reduce innovation, or otherwise offer poorer value for money. This is detrimental for customers, and potentially also for productivity over the longer term. The primary objective of the merger regime is to protect against such harm.
- 3.3 There are five main outcome scenarios for qualifying mergers which are decided through the OFT and/or CC investigation process under the Enterprise Act.¹³ These are:

¹³ Merger proposals can also be withdrawn.

OFT

- Phase 1 unconditional clearance¹⁴,
- Phase 1 clearance subject to remedies (often referred to as undertakings in lieu of reference),

CC

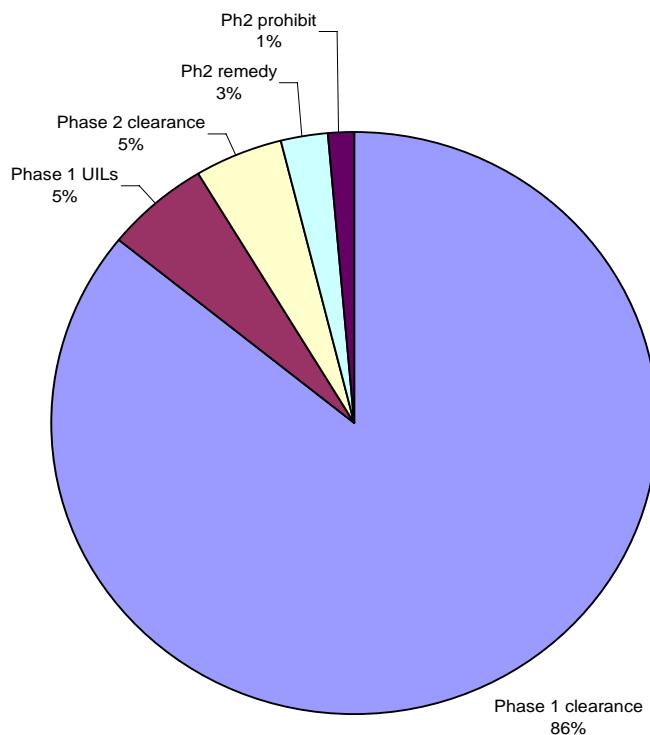
- Phase 2 unconditional clearance,
- Phase 2 clearance subject to remedies,
- Phase 2 prohibition of the merger.

3.4 The great majority of qualifying mergers examined by the OFT are cleared (unconditionally or subject to remedies) at the end of its first phase investigation. Of cases referred to the CC the majority are ultimately allowed to proceed – either unconditionally or with certain conditions attached (such as partial divestment or behavioural remedies). As a proportion of all qualifying cases that are examined under the regime, only around one to two per cent result in an outright prohibition.

3.5 Approximate proportions of cases falling into each of these five categories are shown in the chart below:

¹⁴ This includes cases where the OFT's duty to refer is triggered but the OFT exercises its discretion not to refer on the basis that the affected market(s) is of insufficient importance to justify a reference to this CC (often referred to as the '*de minimis*' exception to the duty to refer).

Figure 3.1: Enterprise Act merger case outcomes (approximate; excludes cancelled references)



Source: OFT estimates

Legal framework applicable to media mergers

3.6 As is shown in the table below, the majority (four out of six) of qualifying newspaper mergers investigated by the OFT over the past five years have been cleared at the OFT stage (at least in terms of the newspapers element). Another was found to give rise to an SLC, but referral to the CC was avoided through acceptance of a partial divestment. Only one of these six mergers therefore reached the CC for investigation, and this was subsequently cleared.

Table 3.2: Selected relevant cases considered by the competition authorities under the Enterprise Act 2002

Merger parties	Case decided by:	Year	Outcome
Newspapers			
Dunfermline Press / Berkshire Regional Newspapers*	OFT	2008	SLC. Partial divestment remedy accepted.
Johnston Press / Archant Scotland	OFT	2007	Cleared
DC Thomson / Aberdeen Journals	OFT	2006	Cleared
Johnston Press / Scotsman Publications	OFT	2006	Cleared
Johnston Press / Local Press	OFT	2006	Newspaper aspects cleared. ¹⁵
Archant / Independent News & Media*	CC	2004	Cleared
Radio			
Global Radio / GCap Media*	OFT	2008	SLC. Partial divestment remedy accepted.
Capital / GWR	OFT	2004	SLC. Partial divestment remedy accepted.
Other broadcasting			
BSkyB / ITV*	Secretary of State	2008	Adverse public interest finding (but on competition grounds only).

* Reviewed in Annexe D

¹⁵ The OFT decided that the reference test was met in relation to farming publications in Northern Ireland. The OFT accepted divestment of one such title as a remedy, such that a reference to the CC was not necessary.

3.7 The merger control regime applicable to newspaper mergers was significantly scaled back in 2003 to make it less burdensome.¹⁶ For the most part, therefore, UK newspaper-on-newspaper mergers are now subject to the same general merger regime (the same 'merger rules') as most other industries in the economy.

OFT's duty to refer

3.8 The Act imposes a duty on the OFT, except in certain specified circumstances, to refer to the CC for further investigation any relevant merger situation if it believes there is a realistic prospect that the merger will result in a substantial lessening of competition (SLC) within any market or markets in the UK for goods or services. The OFT's usual administrative timetable to reach a decision on reference is 40 working days from receipt of a satisfactory submission.¹⁷ The OFT has stated publicly that it may be possible to accelerate the treatment of cases for referral to the CC where this corresponds with the wishes of the merging parties and where there is sufficient evidence available to meet the OFT's statutory threshold for reference. In such 'fast track reference' cases, the OFT would expect that the overall time taken from formal notification to reference decision could be as little as 10 working days.

3.9 The OFT can (and does) seek views from other government departments or sectoral regulators where appropriate as part of its merger assessment process. Other government departments and regulators with sectoral expertise may be given, in confidence, information relevant to the merger so that the OFT can take account of their views on any competition issues and about a possible reference to the CC.

¹⁶ Under the previous (Fair Trading Act 1973) regime a transfer of a newspaper that met the criteria for the application of the regime was unlawful and void if it proceeded without the prior consent of the Secretary of State. With certain limited exceptions, the Secretary of State could not consent to qualifying newspaper transactions without a reference to the CC.

¹⁷ The timetable is twenty working days (with a maximum extension of a further 10 working days) in the case of anticipated mergers where the statutory voluntary pre-notification merger notice procedure is used.

A relevant merger situation

3.10 A merger must meet all three of the following criteria to constitute a relevant merger situation for the purposes of the Act:

- two or more enterprises (broadly speaking, business activities of any kind) must cease to be distinct, or there must be arrangements in progress or in contemplation which will lead to enterprises ceasing to be distinct,
- the merger must not yet have taken place or must have taken place within four months of the reference being made (subject to specified exceptions), and
- **either** the UK turnover associated with the enterprise being acquired exceeds £70 million (the turnover test), **or** the enterprises ceasing to be distinct each supply or acquire goods or services of any description and after the merger will together supply or acquire at least 25 per cent of all those goods or services of that kind supplied in the UK as a whole or in a substantial part of it (the share of supply test).

3.11 The Act provides that the share of supply test (on which the OFT may assert jurisdiction over a merger) may be applied to the UK as a whole or to 'a substantial part' of it. There is no statutory definition of 'a substantial part'. The House of Lords ruled in the context of similar provisions in the Fair Trading Act 1973 (FTA) that, while there can be no fixed definition, the area or areas considered must be of such size, character and importance as to make it worth consideration for the purposes of merger control.¹⁸ The OFT will take the following factors into account in determining whether an area should properly be regarded as a substantial part of the UK in this context: the size, population, social, political, economic, financial and geographic significance of the

¹⁸ See *Regina v Monopolies and Mergers Commission and another ex parte South Yorkshire Transport Limited* [1993] 1 WLR 23.

specified area or areas, and whether it is (or they are) special or significant in some way.¹⁹

- 3.12 In line with the approach taken previously by the CC and OFT, there is no need for the substantial part of the UK for application of the share of supply test to constitute an undivided geographic area. This interpretation gives effect to the purposes of the Act. The economic significance of a merger, in terms of an SLC, does not necessarily depend on whether several localities are contiguous or separated.²⁰
- 3.13 On reference, the CC has 24 weeks to prepare and publish its report. It also applies an SLC test but against a 'balance of probabilities' standard (that the merger has resulted, or may be expected to result, in an SLC), rather than the OFT's lower 'realistic prospect' standard. On this basis, the CC determines the outcome (clearance, prohibition, or remedies) of merger cases referred to it by the OFT.

Public interest considerations

- 3.14 The Act also permits intervention by the Secretary of State for Business, Innovation and Skills ('the Secretary of State') in certain mergers. In these cases the Secretary of State may take into account public interest factors specified in the Act other than the OFT's competition assessment in deciding whether or not to refer a merger to the CC or to remedy any adverse effects of a merger.

¹⁹ The CC has found, applying the House of Lords' test as to whether an area was of such size, character and importance as to make it worth consideration, that the Borough of Slough represented a substantial part of the UK. In reaching this conclusion, the CC had regard to such considerations as population and economic factors, as well as the fact that the markets in which the merging parties competed were local in nature (CC: A report on the acquisition of the Co-operative Group (CWS) Limited's store at Uxbridge Road, Slough, by Tesco plc 28 November 2007).

²⁰ See CC Report - Archant Limited and the London newspapers of Independent News and Media Limited: A report on the acquisition by Archant Limited of the London newspapers of Independent News and Media Limited (2004), Appendix C paragraph 28.

- 3.15 The Communications Act 2003 amended the Enterprise Act by adding public interest considerations relating to mergers involving media and newspaper enterprises. These media public interest considerations are divided into two tests: a newspaper test for mergers involving newspaper enterprises, and a broadcasting and cross media test for mergers involving broadcasting enterprises or mergers involving broadcasting enterprises and newspaper enterprises. The regime is intended to provide a safeguard to prevent media mergers bringing about undue concentrations of ownership, which may operate against the public interest. It enables the Secretary of State to intervene so as to ensure a sufficient plurality of media ownership, to protect the availability of a wide range of high quality broadcasting and to ensure that those with control of media enterprises have a genuine commitment to the broadcasting standards objectives set out in the Communications Act 2003. It is important to note that both the newspaper and the broadcasting and cross-media public interest considerations may be relevant to newspaper mergers.
- 3.16 The regime provides an advisory role for the Office of Communications (Ofcom) after the Secretary of State intervenes in a merger on the grounds of media public interest considerations. In such circumstances, Ofcom has a duty to provide the Secretary of State with advice and recommendations on the specified media public interest considerations, and to do so within a deadline specified by the Secretary of State. The Secretary of State decides on whether to refer the merger to the CC, based on advice from Ofcom on the public interest considerations and the OFT's decision on the competition aspects of the merger.
- 3.17 In public interest references the CC will deliver a report to the Secretary of State, who will then decide whether to make an adverse public interest finding. The Secretary of State must accept the CC's determination on the competition aspects of the merger, but can reach his own view on the public interest issues, whether the merger results overall in an adverse public interest finding, and if so what remedies to impose. Ofcom may also give advice to the Secretary of State as it considers appropriate in relation to either the CC's report or the taking of enforcement action by the Secretary of State (remedies).

Special merger situations

- 3.18 The Act also provides for an exceptional category of media mergers which can be referred on public interest consideration grounds alone when the normal jurisdictional thresholds relating to turnover or share of supply in the Act are not satisfied (referred to as a 'special merger situation').
- 3.19 A media merger is categorised as a special merger situation if either:
- in relation to the supply of newspapers of any description, at least one-quarter of all the newspapers of that description which were supplied in the UK, or in a substantial part of it, were supplied by one of the parties to the merger, or
 - in relation to the provision of broadcasting of any description, at least one-quarter of all broadcasting of that description provided in the UK, or in a substantial part of it, was provided by one of the parties to the merger.
- 3.20 Similar procedures to those in public interest cases apply. The Secretary of State must issue a special intervention notice, the OFT makes a report as to whether it is or may be the case that a special merger situation has been or will be created, and Ofcom is required to produce a report on the effect of the relevant media public interest consideration. The Secretary of State may refer the case to the CC where he believes that, taking account of the relevant public interest consideration, it is or may be the case that the merger operates or may be expected to operate against the public interest. Where a special merger situation is referred to the CC, the CC cannot consider the question of whether the merger will result in an SLC.
- 3.21 If the CC considers that the merger operates or may be expected to operate against the public interest, it makes recommendations as to the action the Secretary of State or others should take to remedy any adverse effects. It reports on those matters to the Secretary of State,

who then makes the final decision on the public interest test and takes whatever remedial steps he considers necessary.

- 3.22 In practice, no media merger has yet been categorised as a special merger situation, and the media public interest provisions have been invoked only once, in relation to BSkyB's acquisition of a 17.9 per cent stake in ITV. The public interest provisions have not been used with respect to any newspaper-on-newspaper acquisitions since the current arrangements were put in place in 2003.

OFT approach to the 'markets of insufficient importance' exception

- 3.23 Under the Act,²¹ the OFT may exceptionally decide not to refer a merger to the CC if it believes that the market(s) to which the duty to refer applies are not of sufficient importance to justify a reference (commonly referred to as the 'de minimis' exception). By precluding a reference, use of this provision has the same effect as an exemption that clears the merger unconditionally. Its purpose is to avoid references being made where the costs involved to the public purse would be disproportionate to the potential harm caused to consumers by the merger.
- 3.24 The OFT is generally likely to consider the affected market(s) to be of sufficient importance to justify a reference (such that the exception will not apply) where their annual value in the UK, in aggregate, is more than £10 million.
- 3.25 Below the £10 million market size threshold, the OFT will consider whether a reference, overall, would be proportionate. In making this determination of proportionality, it will consider three issues: first, whether undertakings in lieu could in principle be offered by the merging parties to remedy in a clear-cut way any SLC concerns created by the

²¹ Sections 22(2)(a) and 33(2)(a).

merger;²² second whether the impact of the merger is likely to be particularly significant in the market(s) in question; and third whether a reference would be proportionate given its deterrence effect, potentially outside the individual market(s) in question.

- 3.26 The OFT may determine not to exercise its discretion to apply the exception on the basis of any one of these considerations, or on more than one of them.²³
- 3.27 In the *Dunfermline Press/Berkshire Regional News*²⁴ (DPL/BRN) case, the OFT concluded that the SLC (in relation to the supply of weekly local newspapers and the supply of advertising space in local newspapers in Slough and Windsor) could be remedied in a clear-cut way because it was open to DPL to divest either BRN's *Express* series or DPL's *Observer* series to a suitable purchaser, thus removing the problematic overlap created by the merger. Accordingly, the OFT determined in that case that it would not be appropriate to exercise its discretion to apply the 'de minimis' exception.

²² This is because the costs of a reference – in any given case where undertakings in lieu are in principle available but are not in fact offered by the parties – is outweighed by the long-run and recurring benefit of remedial and/or deterrent action at the OFT stage that, in aggregate, has resulted and would continue to result in substantial welfare savings for consumers and which would itself result from the deterrence effect of the reference in the case in question.

²³ For recent cases involving the consideration of the 'de minimis' exception, see Anticipated acquisition by Spectris plc of Lochard Ltd, 29 January 2009, Anticipated acquisition by Orbital Marketing Services Group Ltd of Ocean Park Ltd, 14 November 2008, and Anticipated acquisition by Prince Minerals Limited of Castle Colours Limited, 6 May 2009.

²⁴ Completed acquisition by Dunfermline Press Limited of the Berkshire Regional Newspapers business from Trinity Mirror plc, 4 February 2008.

Guidance and Informal Advice

Published merger guidance

3.28 There is a considerable amount of published guidance on both the general merger regime and the media merger regime, reflecting the roles of different organisations in applying the regime. These include:

- **OFT** – Mergers: Procedural guidance, and Mergers: Substantive assessment guidance (as revised);²⁵
- **CC** – Merger References: Competition Commission Guidelines;²⁶
- **BIS** – Guidance on the operation of the public interest merger provisions relating to newspaper and other media mergers;²⁷
- **Ofcom** – Ofcom guidance for the public interest test for media mergers.²⁸

3.29 The OFT and CC guidance is of general application across sectors, whereas the BIS and Ofcom guidance relates specifically to media mergers. Some of this guidance is in the process of being updated. The OFT published in 2008 draft revised jurisdictional and procedural guidance on mergers²⁹ which it expects to finalise shortly. The OFT and CC are also currently in the process of developing new joint substantive assessment guidance on mergers, which will include an updated explanation of their approaches to both market definition and

²⁵ www.ofcom.gov.uk/advice_and_resources/resource_base/Mergers_home/guidelines/

²⁶ www.competition-commission.org.uk/rep_pub/rules_and_guide/pdf/cc2.pdf

²⁷ www.berr.gov.uk/files/file14331.pdf

²⁸ www.ofcom.gov.uk/tv/ifi/guidance/pi_test/pi_test.pdf

²⁹ www.ofcom.gov.uk/shared_ofcom/consultations/oft526con.pdf

competitive assessment of mergers. Draft joint OFT/CC Merger Assessment Guidelines were issued for consultation in April 2009.³⁰

- 3.30 The OFT also publishes detailed, fully reasoned decisions on merger cases considered, and this too provides an extensive source of guidance as to how it assesses competition issues arising in mergers.

Informal advice arrangements

- 3.31 In order to assist the planning and consideration by companies and their advisers of future mergers, the OFT's Mergers Group offers extra-statutory advice on an informal basis on competition issues (and, where relevant, jurisdictional issues) arising out of a prospective merger situation that has not yet been made public, where certain conditions are met.³¹
- 3.32 In brief, the OFT will provide Informal Advice where (i) there is a good faith intention to proceed with the transaction (that is, it is not hypothetical) and it is confidential (not in the public domain), and (ii) the transaction raises a genuine competition issue. Notably, Informal Advice can encompass specific advice on the potential application of the failing firm defence (in the context of the counterfactual) and the applicability of the markets of insufficient importance (or 'de minimis') exception to the duty to refer.
- 3.33 The OFT's Informal Advice procedures and caveats are set out in its 2006 note on Informal Advice procedures and its draft jurisdictional and procedural guidance. The most important caveat - which explains why Informal Advice cannot be binding on the OFT - is that the OFT is unable to test with third parties the parties' submissions to verify information

³⁰ www.of.gov.uk/shared_of/consultations/OFT1078con.pdf

³¹ The OFT revised its Informal Advice procedures in 2006 to replace previous arrangements for both Informal Advice and Confidential Guidance.

provided in an Informal Advice application: any advice given is based on the assumed accuracy of that information.

- 3.34 Since the introduction of the OFT's revised procedures on Informal Advice in 2006, the OFT has not been approached in writing for Informal Advice on any potential local or regional newspaper transactions.

4 MERGER ASSESSMENT

4.1 In this chapter we discuss submissions and findings in relation to the basic merger regime applicable to mergers between local or regional newspaper titles.

Arguments put forward by the major publishers

4.2 Several regional publisher groups believe that consolidation is required to ensure the long term survival and success of local and regional newspapers. In this context, they have concerns that the media merger regime is outdated, and is preventing or deterring consolidation seen as necessary for the transition of such groups to digital business models. They argue therefore that changes must be made to the regime for it to apply more effectively in the 21st Century.

4.3 There are a number of strands to the publishers' argument.

4.4 **First**, they argue that the merger regime should recognise that local and regional newspapers no longer compete for advertising solely with other print media, but increasingly compete in a wider market, facing competition from other media platforms such as TV, radio, cinema and, most importantly, the internet. The publishers are not, in this respect, asking for a change to the legislation, but rather for the merger regime to be applied differently, to reflect changed market conditions.

4.5 **Second**, they argue that the merger regime should recognise that consolidation will sometimes be the only way to ensure the continued viability of a particular group of local newspapers.

4.6 **Third**, they argue that consolidation is required to achieve much-needed efficiencies, such as centralised production, or other customer benefits, such as the development of effective and attractive online offerings. They argue that this will improve the overall proposition to customers, and that the merger regime should recognise this.

4.7 **Fourth**, they argue that they currently face substantial uncertainty as to the workings of the merger regime, which makes deal planning difficult.

They argue that this uncertainty is compounded by the length of time and costs (such as management time and adviser fees) associated with a merger inquiry.

- 4.8 **Fifth**, they argue that consolidation will deliver additional benefits, such as the preservation of strong local investigative journalism or local media plurality, which are in the public interest, and that this should be recognised within the public interest element of the current media merger regime.
- 4.9 **Finally**, the publishers highlight the increasing competitive pressure that local newspapers face from public sector bodies setting up their own local media platforms, and selling advertising space on these platforms.
- 4.10 In its review, the OFT has examined each of these arguments. The first four strands are discussed in the section below. The remaining two are discussed later in dedicated chapters.
- 4.11 We also note that several smaller local newspaper publishers submitted views that regional title consolidation would damage existing competition between large and small operators, and that it remains appropriate for the merger regime to protect against excessive regional concentration of newspaper ownership.

Applying the merger regime to local and regional media

- 4.12 The primary objective of the merger regime is to protect against harm to consumers from mergers. In the context of print media mergers, two sets of customers are considered: readers and advertisers.
- 4.13 On the reader side of the market, cover prices account for a limited proportion of local newspaper revenues (around 20 to 25 percent for paid-for titles), with the great majority of revenue derived from advertising. The incentive to maximise circulation or readership due to the positive impact this has on advertising revenues might be expected to mitigate some concerns that a reduction in competition might result in cover price increases or lower quality for readers. That said, where there are competing titles, competition for readers based on cover price and

editorial quality would typically be expected to deliver additional benefits. Even if a single player would have a larger scale and ability to generate efficiencies and quality improvements, it may have less incentive to do so if direct competitive pressures from a rival have been dampened.

4.14 In practice, though, media mergers are more usually found to raise concerns on the advertiser side (that is, if concerns arise at all), and the OFT's review therefore focussed in particular on effects on advertisers. Advertising is a key input to the competitive process in other markets, and so if advertising rates increase, then the increase in costs will tend to be passed on by the advertisers to their customers. As such, harm to advertisers will typically also generate harm to end-consumers in those other markets. We note, in particular, that advertisers in the local press will include a large proportion of SMEs, which are themselves facing significant challenges in the current economic climate.

4.15 The key findings of the OFT's review in respect of the merger regime are as follows.

Print advertising may face sufficient competitive pressure from other media to protect consumers in the face of a merger, but an OFT view can only be reached on a case by case and area by area basis

4.16 Advertisers allocate their spending across a portfolio of different platforms in order to achieve their objectives in the most cost-effective way. The development of the internet has changed the advertising options available, and there has been a significant shift of spending away from local and regional press advertising towards the internet, especially for classified advertising. Local and regional newspapers' (print editions) share of classified advertising spending fell from nearly 50 per cent in 2000 to a little over 25 per cent in 2008, while the internet's share rose from below two per cent to around 45 per cent over the same period (see Figure 2.3 above). Display advertising in local and regional newspapers has held up somewhat better, but has also experienced long-term decline.

- 4.17 The key question for merger analysis, however, is the extent to which the potential for advertisers to switch spend to these other media acts to constrain the prices that the local and regional press can charge for advertising. If this constraint is strong, then consolidation in the local and regional press, whether through swapping titles or full merger of publisher groups, would not be likely to have a substantial detrimental impact on advertisers (and ultimately end-consumers).
- 4.18 The LMA, representing seven of the largest publishers, submitted that there are a broad range of competitive media in each of the core local newspaper advertising categories across all catchments in the UK, and more specifically that:
- Competing media are increasingly taking share of local advertising spend as they become increasingly relevant and affordable versus local newspapers.
 - As technology and functionality has improved (for example, internet classified, display or search advertising) the range of options for local advertisers has increased.
 - Competing media are more affordable for local advertisers as advertising prices have fallen significantly and media have started to focus on serving more localised businesses (for example, radio, TV or outdoor).
 - Barriers to entry have fallen for new entrants, and advertising outside recognised third party media (for example, print self-publishing or investing in your own website) has created a credible alternative for local advertisers.
- 4.19 In support of these arguments, the LMA provided evidence of numerous specific examples where its publisher members had responded to competitive threats from other media. A range of alternative advertising options were identified and described for each of the key classified segments (property, motors, jobs) and for display advertising. Examples given of local newspapers changing their pricing strategy in reaction to other media included:

- reduced cost per page in response to the launch of a local property magazine
- reduced rate in response to a local radio price promotion, and
- reduced cost of listing motors, and increased number of titles in which the advert would appear, in response to a price reduction by a print/online motor-specific competitor.

4.20 Results from advertiser surveys undertaken on behalf of the LMA in four local areas indicated that, amongst newspaper advertisers, the internet is typically the preferred alternative advertising option from the range of options available, and that, for certain customer groups, print media does seem to be constrained by other media. The LMA submitted that its survey evidence, albeit based on limited sample sizes, showed that demand for local newspaper advertising is 'relatively elastic', such that advertising price increases would lead to a more than proportionate reduction in advertising volume. While this evidence was broadly supportive of the case for a wider market, it is worth highlighting that in the context of a normal merger inquiry the OFT would need carefully to consider the strength of this evidence in the specific circumstances of the case and the local area, market test the evidence with third parties, and assess it against other sources of evidence from the parties (for example, internal documents) and third parties. The OFT was not able to do this fully here.

4.21 Other stakeholders in this review provided contrasting arguments and evidence suggesting that print advertising may face only limited constraints for some customers (particularly for display advertising), thereby potentially enabling a local newspaper to leverage its position with advertisers. In relation to online options, one advertiser group submitted that online represents an alternative in some instances, but penetration and site development varies across the country, the user profile is narrower and younger than local press, and it does not have the immediate localness of local press (or where it does, it is likely to be the website owned by the local print publication).

- 4.22 One way to test whether the internet is as strong a constraint as another publisher is to compare multi-publisher areas with single publisher areas. The LMA submitted that achieved advertising yields do not systematically vary with the presence or absence of multiple print publishers in a local area. If true, this would suggest that other media were as strong a constraint on prices as another publisher. However, there was insufficient data to test this robustly.
- 4.23 We also note that comparison of LMA survey sample results for single and multiple operator catchment areas suggested that the elasticity of demand for newspaper advertising was typically higher in single operator catchments. This would be consistent with the existing exercise of market (pricing) power in single operator areas, which in turn would suggest that competition between publishers is stronger than that across media. However, again, the data was not sufficiently robust to conclude on this point. In addition, one advertiser representative group supplied some pricing data that suggested systematically lower advertising rates in areas where there is direct newspaper competition between local publishers, but this was again based on a limited sample.
- 4.24 Some smaller publishers also put forward the view that high (or increased) levels of local or regional newspaper concentration do (or would) result in local market power, reflected in local newspaper advertising rates. However, they provided little or no evidence to substantiate these claims.
- 4.25 Finally, some smaller publishers argued that increased regional consolidation would provide larger regional publishers with an unfair advantage in remaining areas where they compete with smaller local publishers. This might suggest that there may potentially be regional concerns arising from mergers – not just local.
- 4.26 In this exploratory review, the OFT did not reach a final conclusion on the competitive constraint placed on local and regional press advertising by other media. This is not least because the extent of this constraint may well differ by local area, and thus findings relevant to one local market would not necessarily carry over to another. In those areas

surveyed for the LMA's submission, the evidence was broadly supportive of a wider market³² although, as noted, the OFT did not carry out a full analysis to reach a definitive view even in these areas. As recognised by the LMA, its survey obtained limited sample sizes for current newspaper advertisers in each local area.

- 4.27 More detail on the surveys commissioned by the LMA in support of its submission, and some of their outputs, is provided at Annexe B.
- 4.28 Given its statutory duties under the Enterprise Act, the OFT cannot prejudge the outcome of cases which have not yet been considered, and would need to assess the strength of the constraint from other media on local and regional press advertising on a case by case (and area by area) basis.

The existing merger regime is evidence-based, and capable of reflecting market developments

- 4.29 The existing merger regime is evidence-based, and capable of reflecting developments in markets over time, such as the growth of the internet as an advertising medium. There is no binding precedent on the OFT or CC to apply a particular market definition (that is, the economic market in which the merging parties are considered to operate), or to carry out its competition assessment in a particular way, for a merger in a sector which has been looked at before. This flexibility can result in different market definitions being applied in different cases, with the market definition being determined by the evidence.
- 4.30 Further, while market definition is a useful tool, it is not an end in itself. For example, competition concerns arising from a 'horizontal' merger (that is, between two players operating at the same level of the supply chain) will typically still arise regardless of whether the merger is framed as one resulting in a high concentration of suppliers within a narrow

³² Subject to the data issues and caveats discussed above and in Annexe B.

market, or as one involving the loss of close, direct competition between two suppliers but within a broader market of many players.

- 4.31 An example of the latter is the *Dunfermline Press/Berkshire Regional News* case in 2008 (the most recent newspaper merger to be reviewed by the OFT),³³ in which the OFT focused on the closeness of competition between the parties' newspaper titles from an advertiser's perspective, and the extent to which the titles represented the best alternative to the other for a substantial volume of advertising business. In that case, while survey evidence indicated that the internet and advertising via direct mail and leaflets did provide some constraint (such that the relevant market might have been wider than just print media), other evidence (such as views of advertisers and the parties' internal documents) suggested that the parties had been each other's closest competitor in Slough and Windsor and that the identified constraints from other media were not sufficient to rule out a realistic prospect of an SLC.
- 4.32 Because the regime is evidence-based, the OFT's finding in the *Dunfermline* case does not mean that the OFT or CC would come to the same conclusion in relation to a different merger involving two competing newspaper titles in a different local area.³⁴ The issue would largely depend on the strength of evidence regarding the level of competition between the merging titles and the closeness of alternative options (including the internet) for readers and advertisers – evidence that would, in the main, be provided by the merging parties and tested with third parties.
- 4.33 The evidence that is used by the competition authorities to define relevant markets in mergers (and to apply a competition assessment) can

³³ Completed acquisition by Dunfermline Press Limited of the Berkshire Regional Newspapers business from Trinity Mirror plc, 4 February 2008.

³⁴ For example, the CC cleared the Archant/INM transaction on the basis of the evidence reviewed in that case.

take a variety of forms. Generally, evidence based on actual behaviour (of firms or customers) will usually carry more weight than that based on speculative or hypothetical responses.

4.34 Evidence of how customers have actually reacted to price, or other, changes that have previously occurred can provide **direct** evidence of customer behaviour. Although in practice this evidence is often difficult to gather in sufficient detail, it can potentially be a very powerful source of information about the relevant market. Examples of this type of evidence include:

- evidence of customers switching in response to past price changes
- customers' responses to survey questions asking how they reacted to a previous, actual, price increase
- evidence of customers threatening to switch and achieving price reductions as a consequence, and
- econometric analysis of demand based on firms' sales data.

4.35 In addition to direct evidence of customer behaviour, the OFT and CC may draw evidence of likely customer behaviour by inference through the behaviour of firms. This can be a powerful source of evidence since if customers view another product as an alternative this will be reflected in how the relevant firms react to each other. Examples of evidence of this type include:

- evidence that firms monitor and react to each other
- evidence that firms deliberately target and seek to win their rivals' customers with price offers or other promotions, and
- evidence that firms have responded to a rival offer in order to retain customers.

4.36 In addition to direct evidence of customer or firm behaviour, the authorities may also draw on other sources of evidence about customer

preferences or likely behaviour. This might provide information about the ranking of customer preferences, or customers' opinions about their likely behaviour in response to a price increase. Examples of this type of evidence include:

- assessments of product characteristics
- responses to survey questions asking where customers would divert their demand if the product they currently use were no longer available, and
- survey responses on customers' likely behaviour in response to a price increase.

4.37 Care needs to be taken when interpreting evidence based on opinion about likely behaviour, as it may be influenced by a range of biases. For example, customers may exaggerate or be over-optimistic about the extent of their response or their negotiating power, and how a question is phrased can affect the results obtained. Sample selection (the process used to identify and select survey respondents) can also raise issues. Interpretation of responses to particular questions, and survey evidence generally, therefore need to be placed in the context of the whole of the evidence available, some of which may be more informative than the survey evidence.

4.38 Some of these potential problems with survey evidence might be overcome, or controlled for, with careful survey design. It is therefore advisable for parties to discuss survey proposals in some depth with the authorities before commissioning their own surveys, if the evidence obtained is to be relied upon significantly.

4.39 The OFT's March Discussion Paper identified some types of evidence of particular potential relevance to local or regional newspaper cases. See Annexe C for this (non-exhaustive) list. As discussed above, amongst these potential sources, direct evidence of actual customer or firm behaviour will typically carry more probative weight than inferences based on opinion.

- 4.40 In any merger case the OFT will also seek views on potential merger effects from relevant third parties likely to have knowledge of the market concerned.³⁵ This will typically include competitors and customers of the merging parties, and may also include suppliers. Generally, the OFT will give more weight to the views of customers than competitors, though this partly depends on the quality of the opinions given.
- 4.41 The OFT has not in the past specifically sought views from Ofcom in considering newspaper transactions. However, it recognises that Ofcom has expertise and knowledge in this area, and intends to do so in future. This mirrors existing practice for transactions in broadcasting and telecommunications markets.
- 4.42 The CC will typically be able to undertake more detailed market analysis given the longer timescale of its merger inquiries. This will include detailed questionnaires issued to the merging parties, their competitors and customers. The CC may also commission its own customer surveys carried out by market research specialists to obtain detailed relevant data.
- 4.43 By way of further guidance on how different sources of evidence are used by the competition authorities to carry out market definition and competitive assessment in media sector transactions, Annexe D contains a number of case studies drawn from OFT and CC decisions. The majority of these case studies concern media sectors other than local or regional newspapers, but they are mainly fairly recent, and hence reflect current application of the merger regime.

The existing merger regime is already able to take account of valid 'failing firm' arguments

- 4.44 Some publishers argue that consolidation should be allowed on the basis that the 'target' title(s) is failing and therefore would have exited the

³⁵ Using both a general 'Invitation to Comment' placed on its website and the London Stock Exchange Regulatory News Service (RNS), and targeted enquiries.

market in any event. Thus, there is no reduction in competition relative to the true 'counterfactual' – what would have happened absent the merger. The OFT recognises that the local and regional newspaper sector is going through difficult times and that a significant number of titles have closed.

- 4.45 The existing regime is already able to take account of such arguments, and to clear mergers where the evidence strongly supports the supposition. Where a firm's exit from the market is inevitable in any event (for example, for reasons of financial distress), then the merger itself will not cause a reduction in the number of competitors, and therefore will not itself reduce competition. It is, however, also important for the OFT to assess whether there were any alternative realistic options that would have been less anti-competitive, such as the purchase of the 'failing' title by an alternative publisher.
- 4.46 In December 2008 the OFT restated its approach to such so-called 'failing firm' merger cases,³⁶ in particular highlighting that it will take account of current economic and market conditions in its assessment, and confirming that it will provide informal advice in appropriate 'failing firm' cases. 'Failing firm' arguments may apply to an entire business, or to divisions or stand-alone business units. For example, they have been applied by the OFT in respect of individual retail stores (such as in the Homebase/Focus case in 2008).³⁷
- 4.47 Failing firm considerations were central to the OFT's recent clearance of the acquisition of a number of Zavvi stores by HMV,³⁸ which was the first application of failing firm considerations to clear a transaction since the OFT's restatement of its approach. Given the strong evidence

³⁶ www.offt.gov.uk/shared_offt/business_leaflets/general/offt1047.pdf

³⁷ OFT, *Completed acquisition by Home Retail Group plc of 27 leasehold properties from Focus (DIY) Ltd*, 15 April 2008.

³⁸ Anticipated acquisition by HMV of 15 Zavvi stores, 28 April 2009

pointing in favour of a failing firm defence in that case, the OFT did not consider it necessary to undertake a detailed market analysis, enabling it to carry out its investigation in a more proportionate and timely manner.

The existing regime is already capable of taking into account any efficiencies and customer benefits, if supported by evidence

- 4.48 Some publishers also argue that consolidation should be allowed on account of the efficiencies and customer benefits that would be created.
- 4.49 Again, the existing merger regime is already capable of taking account of, and in some cases clearing mergers on the basis of, these factors, so long as there is clear and compelling evidence in their support. Hence mergers which clearly deliver net benefits to customers can be allowed (although there may be conditions attached).

Efficiencies

- 4.50 In some mergers, the existence of merger efficiencies can prevent a merger from resulting in an SLC. For example, a merger can generate cost synergies that are passed on to consumers in the form of lower prices.
- 4.51 Efficiencies on the demand-side were used by the OFT to support clearance of the *Global Radio/GCap Media* radio merger in the London regional media market.³⁹ Here, the OFT found that the London radio stations of Global and GCap were largely complementary—appealing to different listener demographics — and not substitutable, meaning there were 'economies of scope' in operating them jointly. On this basis, the OFT concluded that advertisers would be able to purchase airtime on a bundle of radio stations more cheaply from the merged firm than they had from Global and GCap individually pre-merger. As a result, the OFT

³⁹ Completed acquisition by Global Radio Ltd of GCap Media plc, 8 August 2008 (decision by OFT to suspend its duty to refer while undertakings in lieu being considered).

did not find an SLC in London, and cleared the London part of the merger.

- 4.52 In the context of print media, publishers claim that previous consolidation has enabled them to make substantial cost savings, for example in gaining economies of scale in printing.

Customer benefits

- 4.53 In other mergers, efficiencies may not prevent an SLC but nonetheless represent 'relevant customer benefits'⁴⁰ that can outweigh the adverse effect of the SLC. In these circumstances, the OFT has the discretion to decide not to refer the merger to the CC for a detailed investigation. Alternatively, at the CC stage, the CC may take these relevant customer benefits into account by considering the extent to which alternative remedies may preserve such benefits.
- 4.54 For example, although the CC concluded that Macquarie UK Broadcast Ventures' acquisition of National Grid Wireless⁴¹ resulted in an SLC, it allowed the merger subject to certain safeguards on the merged firm's behaviour, rather than forcing Macquarie to divest all or part of National Grid Wireless. In doing so, the CC sought to preserve the merger's beneficial effect in reducing risks to the UK's Digital Switch Over programme; a beneficial effect that would have been lost without the merger. Customer benefit considerations have also been applied by the CC in the case of a water merger.⁴²
- 4.55 Situations where customer benefits might be weighed against an identified loss of competition are when the merger results in lower

⁴⁰ Defined in Section 30 of the Enterprise Act.

⁴¹ Macquarie UK Broadcast Ventures Limited / National Grid Wireless Group: Completed acquisition, 11 March 2008.

⁴² Competition Commission, *A report on the completed water merger of South East Water Limited and Mid Kent Water Limited*, 1 May 2007.

prices, higher quality, greater choice or greater innovation. For the OFT to exercise its discretion not to refer a merger on this basis, the claimed customer benefits must be clear, timely, and merger-specific. Claimed customer benefits must accrue to customers of the merging parties, but need not necessarily arise in the market(s) where SLC concerns have arisen. It is conceivable, given clear and compelling evidence, that sufficient customer benefits might accrue in one market as a result of the merger that would outweigh an SLC finding in another market(s). However, it is important that the merged entity has the incentive to deliver benefits to customers as well as simply the ability. This may be unlikely if competitive pressures are reduced.

- 4.56 It should be noted that the customer benefits exception has not thus far been used as a reason to clear a merger (and not insist on remedies) at the OFT (phase 1) stage under the Enterprise Act merger regime. The CC has more flexibility in this regard than the OFT, in that it may adopt a remedy, short of prohibition or complete divestment, which reduces the detrimental effects of the merger's SLC while preserving all or most of the customer benefits. In circumstances where the OFT applies the customer benefits exception to its duty to refer, it would not be able to remedy the identified SLC.

Opinion from stakeholders was divided as to whether consolidation in this sector would in fact deliver efficiencies or customer benefits

- 4.57 Opinion from stakeholders was divided on whether further local newspaper consolidation would deliver efficiencies of either kind discussed above.
- 4.58 Some publisher groups suggested further consolidation would deliver customer benefits, with scale economies making more local newspaper titles viable and leading to enhanced investment in the new digital era. It was argued that mergers help create scale to support investment in building a more competitive online proposition for both audience and advertisers. Some advertisers also noted that previous consolidation has produced benefits in terms of print and production costs and quality,

although they were unsure of the extent to which further consolidation would be able to add to this.

- 4.59 Another body of opinion suggested, however, that the same consolidation would cause customer detriment from the 'de-localisation' of editorial resources and coverage that could follow from increased centralisation, with a particular adverse impact on local investigative journalism, and therefore the newspapers' quality.
- 4.60 Journalist groups submitted that consolidation would extend a recent trend of closure of local offices, and the centralisation of production to regional hubs, leading to pooled news and less localised coverage for readers. We note that Guardian Media Group's decision to close local satellite offices and centralise production in the Manchester area, for example, has generated significant concerns of this type in some quarters, including in parliament.⁴³ Journalist respondents also doubted whether any cost savings arising from consolidation would be used by publishers to invest in quality journalism, given their need to meet debt repayments. The Campaign for Press and Broadcasting Freedom also voiced concerns about publisher consolidation, and submitted that more concentrated local newspaper markets have had a negative impact on the quality of news content.

Publishers are currently uncertain about the application of the merger regime, which makes deal planning difficult

- 4.61 There appears to be some lack of understanding amongst local newspaper publishers around the workings of the media merger regime. This may stem in part from changes made to the regime in 2003, in the form of the Enterprise Act. Under this Act, the rules applicable to newspaper mergers are now broadly the same as those which apply to most other industries across the economy. There are no longer any fixed maximum market share thresholds above which a reference to the CC is automatically triggered; each case is assessed on its merits.

⁴³ For example in the House of Commons debate on local and regional news on 19 March 2009.

4.62 The uncertainty faced by publishers about the regime may also stem from the lack of recent case precedent in this sector. Over recent years, most local and regional newspaper mergers examined under the Enterprise Act have been cleared. As already noted above, out of only six newspaper-on-newspaper mergers assessed under the Act, five have been cleared unconditionally (one by the CC, the rest by the OFT). The sixth (the *Dunfermline* case) was cleared by the OFT subject to a divestment remedy, an outcome which may have been a catalyst for the arguments from publishers that the regime needs to be amended to reflect changed market conditions. Overall, though, there have been few complex newspaper cases reviewed by the OFT or CC to provide guidance.

There would be only limited value in further 'blue skies' work in this area

4.63 In assessing a given merger, the authorities will draw upon evidence from the particular markets involved in order to assess the closeness of competition between the merging parties and the strength of any countervailing competitive constraints, as well as any failing firm or efficiency arguments. Since such evidence can vary between cases, a 'one-size-fits-all' approach to mergers in a particular sector may not be appropriate.

4.64 This means that there would be limited value gained from a piece of 'blue skies' market definition work, carried out without any particular merger in mind – given the lack of specific evidence, in a clear context, to assess.

4.65 Nonetheless, there may still be some general lessons that could be learnt from a detailed inquiry into a specific proposed merger in this sector. The analytical methodologies employed are likely to be similar across mergers within the same sector. As such, additional research by the OFT and CC in this area is likely to be most beneficial in the context of an actual merger, then giving the sector a clearer picture of how the OFT will consider local media mergers in practice.

- 4.66 It is also worth highlighting the different roles of the OFT and CC within the merger regime. The OFT is the first phase merger authority in the UK. It has a relatively short period to assess a merger; typically four to eight weeks, although this could be shortened substantially under its 'fast track procedure', to as little as two weeks, to the extent that the merging parties considered this would be appropriate. However, although the OFT's actual review process is short, merging parties sometimes seek to maximise their prospects of a first phase outcome by engaging with the OFT in 'pre-notification' contact and correspondence. This generally takes the form of review by the OFT of a draft submission from the parties; this often assists parties in identifying key evidence which they may wish to gather and prepare before notification takes place.
- 4.67 The CC, as the UK's second phase authority, has longer to assess the merger (typically 24 weeks), and is therefore able to carry out a fuller analysis. It also adopts a different threshold in its SLC assessment. The OFT is required to take a relatively cautious approach, referring a merger to the CC if it considers there to be a 'realistic prospect' that it will substantially lessen competition.⁴⁴ The CC's 'balance of probabilities' standard for assessing mergers is higher than this 'realistic prospect' reference threshold. Hence the design of the UK merger regime is entirely consistent with an outcome where a transaction is referred by the OFT and subsequently cleared by the CC based on the same set of facts. The combination of a longer review, and a different legal test, can therefore sometimes mean that a more advantageous outcome can be achieved by merging parties at second phase.⁴⁵

⁴⁴ For the avoidance of doubt, the OFT can only refer a merger to the CC where it is under a statutory duty to do so (sections 22 and 33 of the Enterprise Act).

⁴⁵ This could include application of the failing firm defence, as in the CC's recent clearance of the Long Clawson Dairy/Millway merger (January 2009). The OFT referred this merger, on the basis of the evidence it had at Phase I and its 'realistic prospect' standard. The OFT cleared it, within 15 weeks, on the basis of further assessment and a different standard.

- 4.68 Some stakeholders asked for specific guidance on the application of the merger regime to the media sector. This report aims to meet some of the industry's needs in this respect by including case studies and commentary on some of the more complex aspects of the merger regime, and the types of evidence which may be valuable. In addition, as noted above, the OFT already offers Informal Advice for appropriate mergers. This can encompass advice on specific narrow issues (for example, 'failing firm' cases, or the 'de minimis' exception).
- 4.69 The OFT and CC also have in preparation revised and new guidance on the general merger regime, including on OFT jurisdictional and procedural aspects,⁴⁶ guidance on substantive assessment,⁴⁷ and guidance on the various exceptions to the OFT's duty to refer.⁴⁸ The latter will include revised guidance on the *de minimis* exception, reflecting experience since introduction of the OFT's revised approach in late 2007,⁴⁹ since which eight mergers have been cleared on the basis of this exception.⁵⁰

The US approach to newspaper mergers

- 4.70 The Antitrust Division of the United States Department of Justice recently set out its approach to newspaper mergers in a statement to a Congressional Committee by Carl Shapiro.⁵¹ Some key extracts are reproduced at Annexe E. The approach outlined on the part of the US competition authorities is in very large part consistent with the UK

⁴⁶ www.of.gov.uk/shared_of/consultations/oft526con.pdf

⁴⁷ www.of.gov.uk/shared_of/consultations/OFT1078con.pdf

⁴⁸ Forthcoming.

⁴⁹ www.of.gov.uk/news/press/2007/156-07

⁵⁰ There have also been a number of other cases where the discretion to apply the *de minimis* exception was considered but was not applied.

⁵¹ Deputy Assistant Attorney General for Economics, Antitrust Division.

merger regime as described above. The statement emphasises a forward-looking flexible approach, founded on evidence-based case-by-case analysis.

Merger regime – Recommendations

4.71 On the basis of the above:

- **This review recommends that no legislative change is required to the existing merger regime under the Enterprise Act.** The existing merger regime is flexible and evidence-based. It can reflect market developments such as to take account of constraints arising from competition between media when assessing local or regional media merger transactions. A merger can also be cleared due to efficiencies, customer benefits or failing firm arguments. If there is compelling evidence that the merger will be beneficial (or neutral) for consumers, then the merger is likely to be allowed.
- **This review recommends that no further OFT research is warranted in this area in the absence of a notified merger.**
- **In media mergers involving newspaper publishing and/or commercial radio or television broadcasting, and raising competition issues, the OFT will ask Ofcom to provide views, arising from its understanding of media markets, on factors relevant to the OFT's decision.** The OFT will confirm this in its forthcoming revised guidance on merger jurisdiction and procedure.

5 MEDIA PUBLIC INTEREST CONSIDERATIONS

Current arrangements

- 5.1 While media mergers fall under the general merger rules of the Enterprise Act, the Act also provides for intervention by the Secretary of State in media mergers where there are public interest considerations which he considers should be taken into account (for newspapers, these are: accurate presentation of news, free expression of opinion, and plurality of views).⁵² Intervention was anticipated as being an exception rather than the norm. This has been reflected in practice – the Secretary of State has only intervened once in a media merger under the Enterprise Act (in relation to BSkyB plc's acquisition of a 17.9 per cent shareholding in ITV plc). This was under one of the broadcasting (as opposed to newspaper) public interest considerations.
- 5.2 There are three elements to the newspaper public interest considerations under the Enterprise Act. The considerations specified are:⁵³
- the need for accurate presentation of news in newspapers
 - the need for free expression of opinion in newspapers, and
 - the need for, to the extent that it is reasonable and practicable, a sufficient plurality of views in newspapers in each market for newspapers in the UK or a part of the UK.
- 5.3 Further to the introduction of the Act, the then Department of Trade and Industry (now BIS) published guidance on public interest intervention in media mergers under the Act in May 2004 (BIS guidance).

⁵² For broadcasting and cross-media transactions, the considerations are plurality, range and quality of broadcasting, and commitment to broadcasting standards.

⁵³ Section 58(2A) and (2B).

- 5.4 As well as providing guidance on jurisdictional and procedural issues in media mergers, the BIS guidance provides (i) guidance on the scope of newspaper and broadcast public interest considerations, and (ii) some indications of the general approach that the Secretary of State will adopt in deciding whether or not to intervene in a particular case. The guidance also states that this approach will develop in the light of experience in operating the new newspaper public interest merger regime.
- 5.5 Under section 58(3) of the Enterprise Act, the Secretary of State may by order modify section 58 for the purpose of specifying a new public interest consideration, or removing or amending any specified consideration. Under section 57(2) of the Act, the OFT has a duty to bring to the attention of the Secretary of State any representations about exercising his powers under section 58(3) which have been made to it.

Summary of submissions

- 5.6 The OFT's Discussion Paper asked whether the newspaper public interest considerations, set out in section 58 of the Enterprise Act, remain appropriate in their current form. We received various representations that the newspaper public interest considerations should be either removed or amended.
- 5.7 The LMA submitted that the public interest considerations as presently drafted arguably focus unduly on concentration of ownership and do not give sufficient weight to the need to maintain vibrant independent news provision in each local area.
- 5.8 The question was raised whether the Secretary of State could in principle intervene to clear a media merger which would otherwise be referred to the CC (as the Secretary of State did on October 2008 in the acquisition of HBOS plc by Lloyds TSB plc on financial stability public interest grounds). The LMA suggested that intervention to clear a merger that might otherwise be referred could be warranted in cases where, absent consolidation, the ability of the titles in question to continue as independent providers of local news content is at risk. Although media

plurality considerations might tend to be expected to point in the same direction as competition considerations, it was argued that such consolidation may actually serve to maintain plurality of views.

- 5.9 Although we received no specific evidence that the newspaper public interest considerations had deterred potential merger transactions, one respondent did state that, in their view, public interest considerations had deterred potential transactions from being pursued in the past.
- 5.10 Several stakeholders submitted that the public interest considerations should be expanded to incorporate provisions related to the impact of a merger on news-gathering. Journalists' groups cited the House of Lords Communications Committee's 2008 report on 'The ownership of the news'⁵⁴ which recommended, amongst other things, 'that the public interest considerations for newspaper mergers and broadcasting and cross-media mergers are amended to refer specifically to a need to establish whether a merger will impact adversely on news gathering.'⁵⁵ One stakeholder suggested that any takeovers sanctioned through the merger regime should be subject to clear and enforceable conditions related to plurality of views and quality journalism.
- 5.11 One respondent submitted that the public interest considerations are unnecessary, and that the best way to guarantee plurality and diversity is to protect competition in the media market. They also suggested that the considerations, in their current form, lack clarity. The same respondent submitted that the newspaper-specific public interest considerations should be widened to take account of the contribution to plurality of public sector and other news sources available on the internet. A number of other stakeholders agreed that the public interest considerations are too narrow, and should be widened to reflect the growing importance of digital media and online news sources.

⁵⁴ www.publications.parliament.uk/pa/ld200708/ldselect/ldcomuni/122/122i.pdf

⁵⁵ Ibid (p70)

- 5.12 Stakeholders in the commercial radio sector were concerned that the focus of the OFT's review on the local press could lead to an asymmetric outcome and inconsistency across local media markets. They urged that any proposed changes to the local media merger regime should be approached in conjunction with reform of the radio-specific and cross-media ownership rules.
- 5.13 One association of commercial radio groups submitted that the current regulation of local radio is disproportionate to the size of the sector, and restricts the activities of local radio more severely than the television and newspaper industries. They suggested that the justifications for specific radio ownership rules - such as those included in the Communications Act – were not apparent, and that it would be more appropriate to rely on the public interest considerations to safeguard competition and plurality of ownership. The same argument was made in the submission of a large commercial radio group, who put it to the OFT that the public interest considerations which apply to media mergers, combined with the general application of competition law, are sufficient to ensure media plurality.
- 5.14 Finally, one respondent suggested to the OFT that any relaxation of the public interest considerations or media ownership rules should seek to avoid allowing the emergence of dominant firms in the radio sector. They argued that dominant firms are able to use their size to disadvantage secondary players, and that because of this they posed a threat to the diversity and quality of the overall radio offering.

OFT Assessment

- 5.15 On the question of whether plurality in (small) local newspaper markets is a realistic or desirable objective, we note that BIS's stated policy on intervention is already flexible with respect to the realistic scope for plurality in smaller local areas.⁵⁶ It is plausible that some areas will only be capable of supporting one printed title. However, plurality in some

⁵⁶ www.berr.gov.uk/files/file14331.pdf , paragraph 5.12

'parts of the UK' may in fact be considered of particular importance (for example, Northern Ireland⁵⁷), which may argue against strictly limiting plurality considerations to national (UK-wide) newspapers. More generally, it is not clear that there is a trade-off between competition and plurality considerations in circumstances where intervention to retain competition appears justified (since this would usually also be expected to maintain plurality). A further general point is that using public interest considerations to override review of otherwise potentially anti-competitive mergers should only be done sparingly, in the interests of maintaining the independence of the competition regime.

- 5.16 BIS's published guidance in this area dates from 2004, and would benefit from updating to reflect experience (albeit limited) of applying the media public interest considerations, and also some of the practical changes made in the merger review process (such as in relation to revised Informal Advice arrangements⁵⁸).
- 5.17 This part of the OFT's report also fulfils its statutory duty under section 57(2) of the Act to inform the Secretary of State of representations received about the public interest considerations.

Media Ownership Rules (Communications Act 2003)

- 5.18 In addition to the newspaper and broadcasting public interest considerations, there are further media ownership rules, which govern the ownership of television, radio and newspapers in the UK. The OFT has no role in enforcing these rules. Ofcom is required to review these rules every three years, and, as a result of that review, make recommendations to the Secretary of State if in Ofcom's view changes to the rules are needed. Ofcom is in the process of undertaking its latest

⁵⁷ From BIS's guidance, it appears that previous merger cases relating to newspaper titles in Northern Ireland provided important background to the 'plurality of views in newspapers' consideration.

⁵⁸ And to the discontinuation of Confidential Guidance arrangements.

review, and is expected to make its recommendations to the Secretary of State by the autumn. The OFT understands that Ofcom will include the newspaper and broadcasting public interest considerations in its review.

5.19 We received some comments about the cross-media ownership rules set out in the Communications Act 2003. As discussed above, these are subject to Ofcom's review. In cross-media merger proposals, it could be the case that it is these rules rather than the merger regime which are preventing significant consolidation. If cross-media ownership rules were to be relaxed, however, the merger regime may then have a more active role in considering cross-media transactions.

Recommendations

5.20 In the light of above:

- **This review recommends that BIS should consider the representations received on the media public interest considerations, and any case for legislative change.** This process should take account of Ofcom's wider review of Media Ownership Rules, the scope of which will encompass the media public interest considerations.
- **This review recommends that BIS should review, and may wish to restate, its published guidance on its anticipated public interest intervention policy.** This should include whether it foresees any scope for intervention to permit media mergers on public interest grounds. Again, this should be carried out in light of Ofcom's findings.

6 COMPETITION FROM PUBLIC SECTOR SOURCES

Overview

- 6.1 Local authority publications can potentially impact on commercial providers in a number of ways, including:
- withdrawal of council advertising revenue from commercial papers where the relevant material is placed in a council publication instead
 - competition for third party local advertising revenues (such as from local retail and leisure outlets), and
 - competition for audience attention (readership).
- 6.2 We asked stakeholders for views and evidence relating to public sector news and information sources.
- 6.3 Publishers submitted that local commercial newspapers are facing increasing competitive pressure from public sector bodies that develop their own media platforms, and sell advertising space on them. They provided a number of examples. There was broad concern amongst stakeholders about the potential threats to commercial newspapers' revenues from such publications. There was also general consensus that local authority publications should not be treated as contributing to plurality of independent news sources.
- 6.4 Submissions from local government sources expressed concerns about reduced newspaper coverage of council activities, and explained their objective of informing local populations about the services provided by, or available from, local authorities. Practice appears to vary as to whether local authority publications compete directly for local advertising revenues (in order to defray the cost to local taxpayers of producing their publications).

Summary of submissions

- 6.5 The LMA submitted that in many areas competition is increasingly coming from council operated publications, which it argues may be a threat to plurality if they divert advertising revenues away from independent commercial publishers. The Newspaper Society has itself been active in making previous submissions on this issue to Government and to relevant consultations (for example⁵⁹ to the DCLG consultation⁶⁰ on the Local Authority Publicity Code).
- 6.6 This concern was also raised by a number of other stakeholders – including a number of smaller publishers and a journalists' association. An advertising group agreed that the rise of local authority publications has increased pressure on the advertising rates and volumes achieved by local newspaper groups.
- 6.7 One respondent submitted that in Scotland the newspaper industry's problems are being exacerbated by the loss of local authority recruitment advertising to the CoSLA (Convention of Scottish Local Authorities) electronic portal and the prospective loss of public notices going online.
- 6.8 A number of stakeholders argued that local authority publications do not contribute to plurality in local media. For instance, the NUJ submitted that local authority publications contain public relations materials rather than news, and so do not add to plurality. An advertising group questioned whether local authority publications are likely to have the journalistic talent or political inclination to act as an independent voice.
- 6.9 Some publishers suggested that while public media services should be permitted, local authorities should be required to conduct – similar to the requirements on the BBC – a Public Value Test (PVT) and Market Impact Assessment (MIA) prior to introducing new services.

⁵⁹ www.newspapersoc.org.uk/Docs/Local-Authority-Publicity-Code_16-March-2009.doc

⁶⁰ www.communities.gov.uk/publications/localgovernment/publicitycodeconsultation

- 6.10 The Local Government Association (LGA) submitted that it supported a vibrant local and regional press as being essential for local democracy. While the LGA has actively encouraged local authorities to operate their own publications as part of a campaign to increase residents' knowledge of their local government, the LGA submitted that local authority publications are typically distributed only four or six times during a year and do not operate as rivals to the local press. They pointed out that local authorities spend substantial sums of money advertising in the local media – particularly at times of the year when they are not producing a publication of their own. In the LGA's view, public value tests or market impact assessments would be unnecessary, as local councils are accountable to voters.
- 6.11 Other local government stakeholders submitted that the recent decline in the readership of local newspapers, combined with the less than universal coverage of local titles, meant that local authorities had to produce their own publications in order to communicate effectively with their constituency. They stated that local authorities have an obligation both to place their own advertisements and to produce their own publications in the most cost-effective way possible. Not every local authority sells advertising space in their publications – one council that responded to our discussion paper told us that it sees a distinction between directly competing for third party advertising revenues - a practice in which it did not engage - and redirecting its own advertising and public notices to its own publication.
- 6.12 Radio stakeholders commented on the BBC's share of radio audience, and the impact that this has on commercial operators' ability to generate advertising revenues.

Interaction with the merger regime

- 6.13 Submissions on this issue did not generally relate to the merger regime.
- 6.14 The merger regime does not distinguish between public and private competition. That is, the authorities will take account of all competitive constraints in their competition assessment regardless of whether they

originate from a public or private undertaking. For example, local authority titles were explicitly considered and taken account of by the CC in its *Archant/INM* inquiry⁶¹. Indeed, the CC found in that case that some local authority titles were more significant competitors (in terms of how effective they were as substitutes for local advertisers) than others.

OFT Assessment

- 6.15 We note the comments made by stakeholders about the potential impact on commercial publishers of local authority publications.
- 6.16 There are potentially conflicting public policy agendas in this area: the promotion of effective local authority communications, and the provision of independent commercial newspapers. It is possible that the encouragement of local engagement and innovative (cost-effective) approaches in local authority communications (including moving public services or notices online) could conflict with the desire to support the provision of quality independent commercial local news and journalism. One possible approach would be the specific regulation of local authority activity. However, this would impose its own costs, whereas new or revised guidance may have limited impact if it is not enforceable.
- 6.17 Generally, where the public sector provides services (such as the supply of advertising space) in competition with the private sector, it needs to be alive to the possibility that its activities might distort wider markets.

Recommendations

- 6.18 In the light of the above:
- **This review recommends no change in respect of the existing merger regime to take account of local authority publications. Merger**

⁶¹ Archant Limited and the London newspapers of Independent News and Media Limited: A report on the acquisition by Archant Limited of the London newspapers of Independent News and Media Limited, 22 September 2004.

assessment would already take account of them to the extent that they represent competition with commercial providers (for readers or advertisers).

- **This review recommends that BIS and/or DCMS⁶² review this area further, and consider the costs, benefits and effects of potential intervention or regulation, or of appropriate guidance.**

⁶² And devolved governments where appropriate.

7 OTHER ISSUES

- 7.1 We received several submissions from commercial radio stakeholders, and have noted some of their specific comments above. More generally, commercial radio sector respondents called for the merger regime to allow strong local multi-media companies to be created. It was argued that radio consolidation would create efficiencies via increased investment in content, which would drive up audience figures and be more attractive to advertisers. The ability of consumers and advertisers to substitute across different media, together with the radio activities of the BBC, were cited as sufficient external constraint on commercial radio.
- 7.2 As with newspapers, radio mergers are assessed on a case-by-case basis, in light of evidence relevant to the specific circumstances of a transaction. This approach was reflected in the OFT's consideration of the Global Radio/GCap Media merger in 2008. A second phase detailed investigation of that merger by the CC was not required since the parties chose to offer a partial divestment remedy which was accepted by the OFT.
- 7.3 In addition to submissions relating to newspaper publishing and commercial radio, we also received submissions relating to national newspapers and magazine publishing. The common position held in these submissions was that merger assessment should take account of a broad range of constraints in advertising and media markets.
- 7.4 The Periodical Publishers Association, which represents magazine publishers, submitted that scrutiny of transactions by the competition authorities had created uncertainty and stifled merger and acquisition activity in the magazine sector.
- 7.5 We note these comments from radio, magazine, and national newspaper industry stakeholders. Whilst our primary focus in this review has been on local and regional newspapers, many of the issues raised and discussed are likely to apply more widely to other media sectors.

ANNEXE(S)

LIST OF RESPONDENTS

A.1 The following interested parties provided submissions or comments to the OFT's review:

- Bauer Media
- Baylis Media
- Blackburn with Darwen Borough Council
- Campaign for Press & Broadcasting Freedom
- Chartered Institute of Journalists
- Central Office of Information
- David Hutchison (Glasgow Caledonian University)
- Global Radio
- Google
- Institute of Practitioners in Advertising
- Incorporated Society of British Advertisers
- Kent Messenger Group
- LGCommunications
- Local Government Association

- Local Media Alliance⁶³
- London Borough of Hammersmith & Fulham
- News International
- The Newspaper Society
- National Union of Journalists
- Northwest Regional Development Agency
- Observer Standard Newspapers
- Odey Asset Management
- Periodical Publishers Association
- RadioCentre
- Scottish Daily Newspaper Society
- Society of Editors
- Space and Time
- ThinkBDW
- Tindle Newspapers
- UTV Radio

⁶³ Comprising: Johnston Press, Newsquest, Trinity Mirror, Northcliffe, Archant, Guardian Media Group, DC Thomson, and the Newspaper Society.

B LMA ADVERTISER SURVEY

B.1 The LMA and its advisers, OC&C Strategy Consultants (OC&C), commissioned Ugam, a market research company, to carry out a telephone-based survey of 800 local advertisers in four catchment areas. 200 respondents were sourced from each catchment, which were chosen to reflect a range of competitive scenarios for the relevant local newspapers and their advertising customers:

- Worcester – small city, multiple publishers
- Brighton – small city, sole publisher
- Coventry – large city, multiple publishers
- Newcastle – large city, sole publisher.

B.2 Within each catchment area, 50 respondents were sourced from each of four advertising categories – property, recruitment, motors, and retail/leisure – giving 200 respondents from each advertiser category in total. The sample of respondents included advertisers who do not currently advertise in local newspapers.

B.3 The main questions that the survey sought to address were:

- How is local advertising split across media currently?
- How might advertising spend on newspapers change if the price of newspaper advertising increased? This can generate estimates of demand elasticities.
- Where would advertising customers switch to if their main current newspaper closed? This can generate estimated diversion ratios.

B.4 Across all the main advertising categories there were relatively few local advertisers who currently only use local newspapers for their advertising (a range of 6 to 16 per cent as a proportion of advertisers, or 4 to 12 per

cent when weighted by amount of spend). This is consistent with the idea that most advertisers use a portfolio of advertising options.

B.5 Other survey questions asked about the share of local advertising allocated to different media for the different advertising categories. Responses suggested some significant variation across categories in terms of the share allocated to local newspapers. According to the responses, local newspapers were a relatively less important medium for motors and recruitment advertising (where online sources had a larger share) than they were for property and display advertising (where local newspapers accounted for more spend than online).⁶⁴

Table B.1: Survey results on media shares of local advertising spend by advertising category

	Property	Motors	Jobs	Display
Local newspapers	48%	22%	26%	34%
Internet	34%	42%	48%	16%
Radio	n/a	5%	n/a	5%
Other	18%	30%	27%	46%

Source: LMA survey

B.6 OC&C used responses to a combination of questions to try to derive estimates of an implied (own price) elasticity of demand for local

⁶⁴ Reported shares (from LMA advertiser survey) of local advertising spend allocated to local newspapers for each advertising category: Property 48%, Motors 22%, Jobs 26%, Display 34%.

newspaper advertising for the different advertising categories. Results were also reported separately for single operator and multiple operator catchment areas. The relevant questions asked whether the respondent would switch advertising spend away from local newspapers in response to a given percentage increase in the cost of advertising, and if so, the proportion of spend which they would reallocate.

- B.7 Around 40 per cent of surveyed local newspaper advertisers said that they would switch (some) advertising spend to other media in response to a 10 per cent increase in newspaper advertising rates. For single operator catchment areas, implied elasticities reported by OC&C ranged (across the different advertising categories) from 2.9 to 6.1 for a 5 per cent price increase, and from 1.6 to 3.7 for a 10 per cent price increase. For multiple operator catchment areas, the implied elasticities ranged from 1.9 to 3.1 for a 5 per cent price increase, and from 1.2 to 2.8 for a 10 per cent price increase. In the context of a merger analysis the authorities may use elasticity estimates combined with margin data to consider whether a hypothetical monopolist of the products under consideration could profitably raise its prices.
- B.8 While much of the implied elasticity data suggested significant switching, relevant cost and margin data was not available in this exercise to calculate whether the implied loss of business would render the hypothetical advertising price increases unprofitable. In the context of this exercise, the LMA also noted that the limited sample sizes achieved meant that the estimates obtained were not statistically rigorous.
- B.9 The survey also asked local newspaper advertisers where they would advertise if the main local paper they use was not available. This type of question may be useful in generating information about the closeness of competition between alternative options in a differentiated product market. Significant diversion ratios⁶⁵ between products owned by the merging parties will typically indicate scope for unilateral merger effects

⁶⁵ The proportion of switched demand accounted for by each alternative product.

(internalisation of pre-merger competition generating an incentive to raise prices or worsen non-price factors).

B.10 Results from this survey question were difficult to interpret, partly because most advertisers use a portfolio of advertising sources. Hence if forced to switch spending away from a current local newspaper they may switch part to another paper and part to other media. Also, the reported response data was aggregated across multi-publisher and sole publisher local areas, and this could be biased by limited available newspaper switching options in sole operator areas.⁶⁶ Nevertheless, for each advertising group the proportion of respondents which said they would switch to other (non-newspaper) media was at least as high as the proportion who said they would place all their switched spend with another local newspaper instead. For those who said they would switch to other media, online alternatives were comfortably the most popular alternative identified.

Caveats in relation to elasticity estimates derived from survey evidence

B.11 As discussed in Chapter 4, care needs to be taken when interpreting inferences of likely customer behaviour based on opinion, such as some survey results. The range of potential problems with such evidence include:

- Customers may exaggerate the extent to which they would respond to a price increase to appear virtuous, as they may be reluctant to appear vulnerable to exploitation, or reluctant to admit to an irrational decision.
- The responses may measure a short run reaction with customers switching back to the product over time.

⁶⁶ In sole operator areas, advertisers in free weekly local newspapers may not have had a similar frequency alternative local paper available to switch to. This may tend to bias the reported aggregated results for the combined catchment areas.

- Customers may be over-optimistic about their ability to negotiate to ensure that they would not be faced with higher prices.
- How the question is phrased, for example whether the price increase is expressed as a percentage of the total price or as an absolute increase, can affect the results of the survey.

B.12 Some potential problems with survey evidence can be overcome, or controlled for, with careful survey design. It is therefore advisable for parties to discuss survey proposals in some depth with the authorities before commissioning their own surveys, if the evidence obtained is to be relied upon significantly. In any case, the OFT would usually use survey results alongside other evidence, with more weight being given to survey evidence where it is not contradicted by other available evidence.

C TYPES OF EVIDENCE

C.1 As noted in Chapter 4, the OFT's March Discussion Paper identified types of evidence of particular potential relevance to local media cases as including the following:

- internal documents – including those providing evidence on customer bargaining and threats to switch to other media; competitor monitoring; SWOT analyses; evidence on the transaction rationale and expected cost/pricing implications; business plans for the post-merger entity
- advertiser and/or reader surveys (subject to quality assurance on methodology)
- evidence of advertisers switching, or threatening to switch, spend between different newspaper titles, to achieve better prices
- evidence of customer (advertisers or readers) switching in response to relative price changes between newspapers, from newspapers to other media, or from other media to newspapers
- elasticity estimates
- pricing and margin data for relevant business units
- evidence on whether or not advertisers consider the merging parties' publications to be close substitutes (for example, their first and second best choices), and
- evidence on entry conditions, such as any history of, or prospects for, new entry in the market under consideration, including where one of the merging parties is the only publisher present in a particular area.

