

Statement of Preliminary Issues

Universal / EMI

30 March 2012

Introduction

1. On 16 March 2012, the Commerce Commission (the Commission) received an application from Universal Music New Zealand Limited (Universal) seeking clearance to acquire up to 100% of the shares in the recorded music business of EMI Music New Zealand Limited (EMI). The public version of the application can be accessed on the Commission's website at:

<http://www.comcom.govt.nz/clearances-register/detail/757>
2. This Statement of Preliminary Issues outlines the key competition issues the Commission currently considers will be important in deciding whether or not to grant clearance. The issues highlighted in this statement are based on the information available at the time of publication, and may change as the Commission's assessment of the application for clearance progresses. Therefore, the issues highlighted in this Statement of Preliminary Issues are in no way binding on the Commission.
3. The Commission invites interested parties to make comment on the likely competitive effects of the proposed merger. The Commission requests that parties who wish to make a submission do so by 13 April 2012.

The Transaction

4. The proposed acquisition by Universal of EMI's recorded music business is part of the global split of the business of EMI into two separate businesses, each being purchased by a separate party. EMI's Music Publishing business is being purchased by a consortium led by Sony Corporation of America and Mubadala Development Company PJSC.
5. The Application received by the Commission (and therefore this Statement of Preliminary Issues) relates only to the purchase of EMI's recorded music business by Universal.

Relevant Parties

The acquirer – Universal Music New Zealand Limited

6. Universal Music New Zealand is a wholly owned subsidiary of the Universal Music Group, a worldwide music recording and publishing company owned by Vivendi S.A. In New Zealand, Universal undertakes a range of activities including the promotion, development, and distribution of local and international artists.

The target – EMI Music New Zealand Limited

7. EMI Music New Zealand is a wholly owned subsidiary of the EMI Group, also a worldwide music recording and publishing company. The EMI Group is ultimately owned by Citigroup Inc. Like Universal, EMI is active in the promotion, distribution, and development of artists in New Zealand.

Analytical framework

8. In the context of an application for clearance, the Commission must consider whether or not an acquisition substantially lessens competition. An important step in the Commission's analytical framework is to determine the relevant market or markets. To do this, the Commission identifies the areas of overlap between the acquirer and the target where aggregation of market share may arise from the acquisition. The Commission then considers the relevant products and geographic regions that may be close substitutes from both a customer's and a supplier's point of view.
9. The Commission uses a forward looking type of analysis to assess the degree of any potential lessening of competition in the relevant market or markets arising from a proposed acquisition. Therefore, the next step is to establish the two hypothetical future scenarios:
 - with the acquisition
 - without the acquisition
10. The impact of the acquisition on competition is then viewed as the difference between those two scenarios.
11. The Commission analyses the extent of competition in each relevant market for both the with and without scenarios, in terms of:
 - 11.1 Existing competition – the degree to which existing competitors compete and their ability to expand production in the event that the combined entity raises prices.
 - 11.2 Potential competition – the ability of businesses to readily enter the market and thereafter expand, given an inducement to do so.
 - 11.3 The countervailing market power of buyers – the potential for a business to be sufficiently constrained by purchaser's ability to exert an influence on price, quality and/or terms of supply.
 - 11.4 Coordinated behaviour – whether the acquisition would enhance the ability of market participants to collude either tacitly or explicitly.
12. A comparison of the extent of competition in the relevant markets both with and without the acquisition enables the Commission to assess the degree by which the

proposed acquisition might lessen competition. If the lessening is substantial, the Commission may not give clearance to the proposed acquisition.

Preliminary issues

13. Of the factors outlined in the previous section, the Commission currently considers its focus in respect of the proposed acquisition will be on the following areas:

Market definition

14. The Application relates to both parties' involvement in the provision of artist and repertoire services and the wholesale supply of recorded music to retailers.

Artist and repertoire services

15. The Commission understands that artist and repertoire services incorporate a variety of services. These include the discovery of new artists, the signing of a record contract with the artists, and the creative development and promotion of the artist.
16. The Commission will examine whether the different services provided under artist and repertoire should be considered together as a single market, or examined separately.

Distribution services

17. The Commission will also consider whether or not the distribution of recorded music on behalf of third parties should be considered as a separate market.

Existing competition

18. There are a number of businesses operating in the recorded music industry in New Zealand. These businesses include large international record companies such as Sony BMG and Warner Music, as well as a large number of smaller New Zealand based independent recording labels.
19. Universal has submitted that independent record labels currently enjoy a strong competitive position in New Zealand and will continue to do so post acquisition.
20. The Commission will examine the extent to which independent recording labels are able to provide a competitive alternative to the major labels for the provision of artist and repertoire services and the wholesale supply of recorded music in New Zealand.

Potential Competition

21. The Commission will examine the extent to which artists can bypass record labels and record, promote and distribute their own music. The Commission will also examine any barriers to establishing a record label in New Zealand.

Impact of music piracy

22. The Commission will also assess the extent to which music piracy constrains the price of legitimate physical and digital music recordings.

NEXT STEPS

23. In line with the Commission's Merger and Acquisitions Clearance Process Guidelines (available on the Commission's website at www.comcom.govt.nz), the Commission has established a draft timeframe for consideration of the issues and Universal's application for clearance. An extension of time was agreed to by the Applicant such that the Commission should make its final decision by 13 May 2012. However, also in line with the Merger and Acquisitions Clearance Process Guidelines, this timeframe could change. To keep abreast of possible changes in relation to timing and to find relevant documents, visit the Clearance Public Register on the Commission's website at:

<http://www.comcom.govt.nz/clearances-register/>

24. As part of its investigation, the Commission will identify the parties it believes will provide the best information to help it assess the preliminary issues identified above. The Commission will be contacting those parties over the next few weeks.
25. The Commission also invites submissions from any other parties who consider they have information relevant to the Commission's consideration of this matter. If you wish to make a submission, please send it to the Registrar, at registrar@comcom.govt.nz with the reference Universal/EMI in the subject line of your email, or The Registrar, PO Box 2351, Wellington 6140 by **Friday 13 April 2012**. Please clearly identify any confidential information contained in the submission and provide contact details.