Statement of Preliminary Issues

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Wilson & Horton Limited and Fairfax New Zealand Limited – Application for authorisation of a business acquisition

14 June 2016

Introduction

1. On 27 May 2016, the Commerce Commission registered a joint application from Wilson & Horton Limited (trading as NZME) and Fairfax NZ Limited (Fairfax) seeking authorisation to merge their media operations in New Zealand.

2. The public version of the application is available on our website at: http://www.comcom.govt.nz/business-competition/mergers-and-acquisitions/authorisations/merger-authorisation-register/detail/940

3. This Statement of Preliminary Issues outlines the key competition issues we currently consider to be important in deciding whether or not to grant authorisation.

4. We invite interested parties to provide comments on the likely competitive effects of the proposed merger. We request that parties who wish to make a submission do so by **01 July 2016**.

The applicants

5. Fairfax operates the largest print media network in New Zealand, featuring nine daily and three weekly newspapers, 61 community publications, ten magazine titles and six websites, including stuff.co.nz. It also has a minority shareholding in social media site Neighbourly.

6. NZME owns eight daily and two weekly newspapers, 24 community publications, six magazine titles, ten radio stations and 38 websites, including nzherald.co.nz. As well as websites related to its print and radio offerings, NZME owns a number of individual websites such as Grabone, Shop Green and Adhub.

7. NZME and Fairfax are also joint venture owners, with TVNZ and MediaWorks, in KPEX Limited. KPEX operates as an ad exchange to sell remnant digital advertising inventory across qualifying publishers' online and mobile websites. Each of the joint venture parties hold a quarter share in KPEX.

Background to the transaction

8. The ownership structure for the proposed merged entity has not yet been established. NZME's parent company, APN, is seeking approval from its shareholders to demerge NZME and have it listed as a separate company on the NZX and ASX.

9. In the event shareholder approval is gained, it is currently proposed that NZME will acquire Fairfax assets or shares from parent company Fairfax Media Limited (Fairfax Media), for a mix of new shares in NZME and cash. Fairfax Media's shareholding in the merged entity is expected to be less than 50%.

Our framework

10. Our approach to analysing the competition effects of the proposed merger is based on the principles set out in our Merger and Acquisition Guidelines and Authorisation Guidelines.[1] As required by the Commerce Act 1986, we assess authorisation applications using a two-step process.

11. For mergers, when we receive an application for authorisation we must first assess whether the merger would be likely to substantially lessen competition in a market. If we are satisfied that the merger would not be likely to have that effect, then we would clear the merger.

12. We determine whether a merger is likely to substantially lessen competition in a market by comparing the likely state of competition if the merger proceeds (the scenario with the merger, often referred to as the factual), with the likely state of competition if the merger does not proceed (the scenario without the merger, often referred to as the counterfactual).[2]

13. We define markets in the way that we consider best isolates the key competition issues that arise from the merger. In many cases this may not require us to precisely define the boundaries of a market. A relevant market is ultimately determined, in the words of the Commerce Act, as a matter of fact and commercial common sense.[3]

14. We compare the extent of competition in each relevant market both with and without the merger. This allows us to assess the degree by which the proposed merger might lessen competition. If the lessening is likely to be substantial, we will not give clearance to the proposed merger. When making that assessment, we consider, among other matters:

    14.1 existing competition – the degree to which existing competitors compete;

    14.2 potential competition – the extent to which existing competitors would expand their sales or new competitors would enter the market and compete effectively if prices were increased; and

    14.3 the countervailing market power of buyers – the potential for a business to be sufficiently constrained by purchaser's ability to exert substantial influence on negotiations.

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1 Commerce Commission, *Merger and Acquisition Guidelines*, and *Authorisation Guidelines*, July 2013. Available on our website at www.comcom.govt.nz

2 *Commerce Commission v Woolworths Limited* (2008) 12 TCLR 194 (CA) at [63].

3 Section 3(1A).

15. For authorisation applications, if we are not satisfied and cannot grant clearance, we then apply the public benefit test to determine whether to authorise the merger.

16. The public benefit test requires us to balance the detriment that may result from the substantial lessening of competition against the public benefits that the merger may bring about. We must authorise a merger where we are satisfied that the merger will be likely to result in such a benefit to the public that is should be permitted.

17. In our assessment we regard a public benefit as any gain to the public of New Zealand that would result from the proposed merger. We also take into account any costs that might be incurred in achieving those benefits. The benefits that we take into account must result from the merger and we do not take into account any benefits that would occur without the merger.

18. For example, we would consider a reduction in operating costs resulting from the removal of duplication as a benefit, so long as this reduction is a direct result of the merger. The benefits claimed by the merging parties are outlined in Appendix 13 to the Application.[4]

19. In contrast, in assessing detriments we only consider anti-competitive detriments that arise in the markets where we find a substantial lessening of competition and these are typically associated with a decrease in efficiency. We assess detriments on the basis of the facts of each case.

Preliminary issues

20. We will investigate whether the proposed merger is likely to substantially lessen competition in the relevant markets by focusing on the unilateral and vertical effects that might result from this merger.

21. We will consider whether the merged entity will be able to raise the price or reduce the quality of the services it provides to readers and advertisers. In particular, we will consider:

    21.1 whether separate product markets exist for the supply of online and print advertising and content;

    21.2 the closeness of competition between the merging parties and other suppliers;

    21.3 the ability for new suppliers to enter or for existing suppliers to expand, by extending the range and geographic coverage of their operations;

    21.4 the ability of customers to exert substantial influence on the price the merged entity charges and on other terms; and

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[4] Found at http://www.comcom.govt.nz/dmsdocument/14289

21.5 the ability and incentive of the merged entity to restrict access (or provide access on less advantageous terms) to upstream printing assets, or the KPEX platform.

Areas of overlap

22. According to the applicants, the proposed merger may result in aggregation in five main areas:

22.1 paid Sunday papers – between Fairfax's Sunday Star Times and Sunday News, and NZME's Herald on Sunday;

22.2 paid metropolitan newspapers – between Fairfax's Dominion Post and NZME's Hawkes Bay Today, and between NZME's NZ Herald and Fairfax's Waikato Times;

22.3 free community publications;[5]

22.4 the supply of online advertising; and

22.5 the supply of digital news/information content – between Fairfax's stuff.co.nz and NZME's nzherald.co.nz.

23. We will consider whether the applicants have a material overlap in any of the markets affected by the proposed merger.

The without the merger scenario

24. We must identify what is likely to happen in the relevant markets if the proposed merger does not go ahead. The applicants have suggested that the appropriate scenario without the merger is the status quo. We will consider to what extent (if any), Fairfax and NZME intend to re-position or expand their offering without the merger.

Market definition

25. Media companies (such as the applicants) operate a number of multi-sided media platforms in the form of hardcopy publications (newspapers, community papers, magazines and other publications), websites, and radio stations. Each of these platforms typically provides services in two markets:

25.1 an audience for advertisers; and

25.2 content for readers.

26. In previous decisions, the Commission has considered the impact of media mergers in a number of markets.

27. On the advertising side:

[5] The areas of overlap are outlined in Appendix 15 to the Application.

27.1 local regional specific print advertising services;

27.2 national print advertising in category specific magazines; and

27.3 local regional specific radio advertising.

28. On the reader side:

28.1 national category specific magazines;

28.2 local regional specific (not-daily) print community newspaper / local news and information services markets;

28.3 local regional specific print metropolitan / regional newspaper / national and international news and information services markets; and

28.4 local regional specific free-to-air radio content services markets.

29. The applicants suggested that these markets are no longer necessarily the appropriate markets in which to consider the competition impacts of the proposed merger. They suggested that online advertising and content are increasingly seen as substitutes to print advertising and content.

30. The applicants stated that there is a trend towards increasing competition across different media such that all media may be in the same market for both the advertiser and reader sides of the platform. The applicants submitted that it is no longer appropriate to draw distinctions between:

30.1 online and print advertising; and

30.2 print and online news/information services.

31. We will examine the extent to which both advertisers and readers view different media as substitutes.

32. As part of this assessment on the reader side, we will consider the extent to which content is created with a specific platform (print, digital or radio) in mind. We will also assess whether there are separate 'content' markets, defined by the specific subject matter or focus of the news/information (for example New Zealand or regional news).

33. The applicants stated that advertising customers demand offerings that reach the largest number of potential purchasers and that they are 'agnostic' as to which media platform they use. We will assess the extent to which advertisers have a preference for specific media for specific needs, and the extent to which they would switch among them. For example, the extent to which an advertiser would utilise Google or Facebook services as opposed to stuff.co.nz or nzherald.co.nz.

34. We will also consider whether there are separate customer markets on the advertising side, including whether the competitive alternatives differ for local versus

national advertisers, and whether these markets should be further delineated on a geographic basis.

Existing competition – readers

35. The applicants submitted that with the merger they will continue to face strong competition for readership from a number of different parties, including TVNZ, Mediaworks, Radio New Zealand, blogs, and overseas content creators such as *The New York Times* and *The Guardian*.

36. We will assess the extent to which websites such as TVNZ.co.nz and newshub.co.nz compete with the merging parties for readers, and the extent to which international media companies are able to offer comparable content to New Zealand based parties. Factors we will consider include the importance of New Zealand specific news content to readers and the extent to which competitors can offer local and regional content.

37. There has been movement among a number of media companies both internationally and within New Zealand towards the introduction of charges for readers to access online content, known as a paywall. We will assess whether or not the merged entity would have the ability and incentive to introduce such a paywall and whether or not this would encourage other content providers to follow suit.

Existing competition – advertisers

38. The applicants have submitted that with the merger, they will continue to face significant competition from Google and Facebook for the provision of print and online advertising services to advertisers. In addition, the applicants submit they also face constraint from outside the market from other advertising sources, for example, TV, radio, billboard and cinema.

39. We will consider the extent to which the merging parties face competition from these parties and whether this competition would effectively constrain the merged entity from raising prices above the competitive level.

Entry and expansion

40. The applicants submit that entry into the online news market is relatively easy and can be achieved quickly. Entry into print markets is, in the applicants' view, more difficult but not insurmountable with readily available third party printing providers. The applicants also point to large international media companies such as *Vice Media* and *The Guardian* as being potential entrants or expanding their presence further into New Zealand.

41. We will assess whether entry (or expansion of an existing supplier) would be of likely, of sufficient extent and occur in a timely fashion to prevent a substantial lessening of competition.

Vertical issues – KPEX and printing

42. Both Fairfax and NZME (along with MediaWorks and TVNZ) are owners of a company called KPEX, which operates as an ad exchange to sell remnant digital advertising inventory across certain online and mobile platforms. We will consider whether the parties increased ownership stake in KPEX will enable them operate the KPEX platform to their advantage, and increase costs to other advertising suppliers.

43. Both NZME and Fairfax operate physical printing assets and the Commission understands that these are utilised by competitors. The Commission will consider whether access to printing services will be impacted by the merger and whether independent publishers will be able to continue to access these on competitive terms.

Next steps in our investigation

44. The Commission is currently scheduled to make a decision on whether or not to give clearance to the merger by **22 August 2016.** However, this date may change as our investigation progresses.[6]

45. If the Commission considers that the merger is likely to result in a substantial lessening of competition, and therefore proceeds to assessing whether or not the merger should be authorised, this timeframe is likely to be extended.

46. As part of our investigation, we will be identifying and contacting parties we consider will be able to help us assess the preliminary issues identified above.

Making a submission

47. If you wish to make a submission, please send it to us at registrar@comcom.govt.nz with the reference NZME/Fairfax in the subject line of your email, or by mail to The Registrar, PO Box 2351, Wellington 6140. Please do so by close of business **01 July 2016**.

48. Please clearly identify any confidential information contained in your submission and provide both a confidential and a public version. We will be publishing the public versions of **all** submissions on the Commission's website.

49. All information we receive is subject to the Official Information Act 1982 (OIA), under which there is a principle of availability. We recognise, however, that there may be good reason to withhold certain information contained in a submission under the OIA. For example, if disclosure would unreasonably prejudice the supplier or subject of the information. In assessing the confidentiality of information contained in submissions for the purposes of publication on our website, we intend to apply an approach that is consistent with the OIA.

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[6] The Commission maintains a merger authorisation register on our website at http://www.comcom.govt.nz/business-competition/mergers-and-acquisitions/authorisations/merger-authorisation-register/where we update any changes to our deadlines and provide relevant documents.