Monday, 27 June 2016

The Registrar
Business Acquisitions and Authorisations
New Zealand Commerce Commission
PO Box 2351
Wellington 6140
New Zealand

Fairfax New Zealand Ltd/Wilson & Horton Ltd
Submission in relation to the notice seeking authorisation or clearance of a business acquisition pursuant to s67(1) of the Commerce Act 1986

Summary

NZME (Wilson & Horton) and Fairfax's application to create NZ's first newspaper monopoly should be rejected on the terms it has proposed.

The application results in a substantial lessening of competition for the provision of print advertising services in the Auckland region in particular. Print advertising is a distinct market that complements marketers' other media choices, including online. It appears to have retained substantial and sustainable volumes for certain marketing segments such as real estate and national retail advertising.

The resulting monopoly in the provision of print advertising services would preclude the prospect of any new entrant in the Auckland region. A potential competitor would be unable to attain the scale and reach of either the NZ Herald or Fairfax's Auckland Suburban Newspaper network, let alone a combination of the two, in a timeframe or financial manner that its entry could be considered "likely, sufficient in extent, timely and sustainable".

There is no discernible public benefit arising from the merger sufficient to offset the lessening of competition. The largely isolated geographic footprints of both companies means that there are virtually no savings available from rationalised production, logistics or distribution activities. Therefore any significant cost savings expected from the merger must come from editorial resources. This can only mean diminished coverage, less diverse opinion and comment and fewer employment options for journalists.

If the merger is to go ahead, the Commission should consider creating the conditions capable of supporting competition in the Auckland print advertising market. This would require the divestment of either the Auckland suburban network or the *NZ Herald*.

Analysis

The basis of the application by NZME and Fairfax to merge can be summarised as follows:

- The internet has destroyed the main publisher's business models and left them squeezed between its dominant players - Facebook and Google - and low-cost digital natives.
- As a result, they claim that the only viable position is to produce quality editorial content which they then claim is only possible by achieving efficiencies of scale.
- Furthermore they argue there is little overlap between the two based on historical analyses and therefore no substantial lessening of competition in any event.

Horton Media contends that the applicants' assertions about the diminishing influence of newspapers and newspaper-owned websites are exaggerated.

For a start, printed newspapers are not racing to extinction at nearly the pace they are popularly believed to be. In fact, recent Australian research shows that newspapers remain the most popular platform for news media in that country with 76 per cent of the adult population picking up a copy. That compares with 72 per cent of the same population consuming news through digital platforms.[1]

Newspapers still control the daily agenda. They maintain the largest newsrooms of any media and, as such, provide the most comprehensive coverage of daily events. News broken or opinions aired in the morning newspapers set the agenda for the biggest radio format by audience –talkback – and lay the foundations for that night's TV news. Along the way they become the lightning rods for comment and discussion in social media.

It is also notable that the biggest news websites in New Zealand and Australia are not only owned by newspaper publishers but largely follow their physical distribution footprints. Readers of nzherald.co.nz are more likely to come from Auckland and the upper North Island, where the *Herald* mainly distributes, whereas the audience of Stuff.co.nz reflects the distribution of Fairfax's newspapers in the lower North Island, Wellington and the South Island.

Newspaper publishing still dominates news media profitability too. Print revenues still make up about 60% of NZME's revenues and profits whereas digital media contributes about ten percent of that company's top line. Radio makes up the difference.

Fairfax and NZME assert the increasing threat of online media to support their proposition that there is no shortage of countervailing forces that would normally apply to an aggregated traditional media market.

Citing past decisions in which the Commission has agreed that individual markets are potentially threatened by the entry of single community newspapers or bloggers, the applicants argue that:

1. The two applicants have settled into exclusive geographic territories that are therefore not competitively compromised by aggregation,

[1] *emma, conducted by lpsos Media CT, people 14+ for the 12 months ending February 2016, Newsmediaworks http://www.newsmediaworks.com.au/93pc-of-australians-consume-news-media-emma/*

2. The nature of the applicants’ products is also different in most areas where they do compete, ie: one has a metro paper whereas the other has a regional or community paper, so they complement rather than compete with each other, and
3. There is such a plethora of countervailing forces from potential entrants either online or by publishers of single community newspaper titles such that the combined forces of NZME and Fairfax would be unable to exploit their combined position In any event.

The NZ Commerce Commission has traditionally commenced its decision-making process with analysis that splits most media into “two-sided” markets that serve consumers with news and information and businesses with advertising services.

Horton Media’s submission focuses on the advertising services market and argues that Fairfax and NZME’s printed media compete strongly in the Auckland market notwithstanding the editorial differences that have traditionally separated Fairfax’s community papers and NZME’s daily metropolitan newspaper, the *NZ Herald*.

The Auckland region is currently served by the *Herald*, the *Herald on Sunday*, *The Sunday Star Times*, *The Sunday News* and the Auckland Suburban Newspapers group comprising 12 titles from Rodney to Pukekohe. All titles listed above are owned by either NZME or Fairfax.

The NZ Herald claims weekly readership of 760,000 readers whereas the Auckland Suburban network claims aggregate readership of 594,000 people. The *Herald* distributes widely north and south of Auckland and does not break out its metropolitan readership.

A combination of the two would present a powerful threat to advertisers including the applicants’ single biggest revenue segment - property advertising.

Agencies such as Barfoot and Thompson choose to advertise in either the *NZ Herald* or the suburbans largely on their analysis of the titles’ respective reach into particular areas. They could easily switch between either provider according to the terms on offer. Some advertisers also choose *Property Press* - a weekly property advertising title published by Bauer Media. However this is generally regarded as a complementary choice as it does not offer the reach of either the *Herald* or the suburban network.

The removal of competition between these groups would significantly diminish agents’ negotiating position when deciding whether to advertise with the *NZ Herald* or the suburban network.

This is also true of other advertisers, particularly national retailers, who have increasingly deserted the *Herald* as its coverage of Auckland readership declines and switched to the freely distributed community titles. National retailers often prefer newspapers to host their catalogues or other inserts as research shows this method of distribution produces higher reader engagement than with free-standing inserts distributed by non-publishers.

Contrary to the applicants’ contention, the threat of aggregation in print advertising services media is not much diminished by digital media where it can be seen that the non-exclusive presence of real estate advertising on digital platforms such as realestate.co.nz proves the limits of that medium’s substitutability with print.

If old and new were completely interchangeable, real estate advertisers would have fled to the cheaper online alternatives by now. Classified advertisers have already done so to the extent that Trademe is now regarded as a mature business.

Bu the fact that real estate advertisers haven't proves that print continues to provide a unique service that is best suited for a particular job. In this case, agents generally feel that print gives them better exposure to passive buyers and potential house sellers and therefore attracts listings. Real estate internet sites, on the other hand, tend to be used more by active house buyers.

Research commissioned by Bauer Media shows that property print media also still attracts more readers than their online alternatives.

Another potential consequence of aggregation is the threat it poses to independent publications. Many currently rely on representation to national advertisers by NZME or Fairfax who tend to place advertising for areas in which they do not have their own title in non-competing independent publications. A potential merger would very likely see this advertising withdrawn from independent publications. One example is the *Weekend Sun* in Tauranga which is represented nationally by Fairfax. A merger of Fairfax and NZME would most likely see this advertising directed to NZME's Bay of Plenty titles instead.

However it is the forgotten element of the commission's formal analysis that is potentially the most powerful argument against the merger. That is the countervailing force provided in the form of potential market entry by a new competitor of sufficient scale to pose a real threat to the incumbents.

This test was last highlighted in the media sector by the Commission's 1996 decisions to decline The Radio Network's proposed purchases of c93FM in Christchurch and Radio Fifeshire in Nelson.

In the Commission's decision to reject The Radio Network's bid for Radio Fifeshire, chairman Alan Bollard noted that several frequencies were available to potential radio entrants.

However, more careful examination revealed that a viable entrant would have had to establish several stations - not just one - to effectively compete with the merged entity and that it would have struggled to achieve an acceptable return on investment even if it had been possible to do so.

"When looking at potential entry, for the threat of market entry to be a sufficient constraint on the exercise of market power, entry of new participants must be likely, sufficient in extent, timely and sustainable," the commission ruled in the Fifeshire case.

"Given that these parties [new entrants] would encounter considerable start-up costs, and would compete with parties having experience, expertise, reputation and economies of scale, it appears unlikely that such an entrant would be successful.

"As discussed earlier, the Commission believes that if a new entrant were to enter the market, the extent of that entry would not exceed the threshold level of 10% in the first three years. Below this level, the new entrant would be unable to effectively constrain the combined entity. Based on the financial modelling of each of the parties, entry at this required level would be commercially unsustainable over a three year period. It seems unlikely therefore, that entry to the market for radio advertising services would be sustainable."

The decision went on to say that the merged entity would have controlled 99 per cent of the Nelson radio market – clearly a daunting prospect for any potential entrant – and noted concerns by existing competitors that the combined entity would be able to offer heavily discounted advertising bundles with which they could not compete.

It also noted advertisers' concerns that the monopolistic nature of the proposed TRN/Fifeshire merger would give them very little bargaining power and that they would lose their current freedom to "pick and choose" between the two existing players.

The Commission reiterated this approach a year later when it rejected TRN's bid for Christchurch station c93FM.

The situations faced in Christchurch and Nelson 20 years ago have obvious parallels with the proposed merger of NZME and Fairfax's print titles in Auckland if not throughout New Zealand.

The combination of the *Herald* and Fairfax's community network would probably account for more than 80 per cent of all high-frequency print advertising in the region – and that's counting every small community newspaper and ethnic title which wouldn't even rate as competitors in most analyses.

The likelihood of a new entrant emerging and sustainably achieving a 10 per cent share of that market within three years is implausible.

The *Herald* and the suburban networks are individually powerful let alone as a combination. The *Herald* has seen off every print challenger since the *Auckland Star* folded in 1991. The suburban network has also proven itself resilient following APN's failed to bid to establish a challenger with *The Aucklander*. Even the well-established and well-resourced *Property Press* group has failed to penetrate the outer suburban areas of Auckland where it has been beaten by Fairfax's distribution scale.

Finally one must also consider the public benefit test in which an authorisation might be granted if the advantages to the NZ public were so overwhelming that a merger should go ahead.

The applicants contend that the plethora of online producers of news content is sufficiently ubiquitous to serve consumers of NZ news should the combined publishers fall short of public demand.

However this seems unlikely. Nielsen research to December 2015 shows nzherald.co.nz and stuff.co.nz are clearly the two largest news and information websites in NZ (depending on the characterisation of the Microsoft site). In fact, the only sites that rank ahead of them are Google (search), Microsoft and related services sites (MSN/Outlook/Bing/Skype), Facebook (social) and Youtube (video). Neither TVNZ nor Mediaworks, both with significant news-gathering resources, rank among the top ten NZ sites.

Comparatively well-resourced internet-based news sites such as newsroom.co.nz, which was established 20 years ago, have also failed to make any dent in these figures let alone single bloggers.

The applicants have also suggested their merger might even enhance coverage and diversity of opinion.

How this would be achieved 46 years after the US Justice Department modified its antitrust laws so that newspapers could enter joint operating agreements specifically to preserve editorial diversity is unclear. Under these agreements competing papers could merge all their non-editorial functions - such as printing, administration, distribution and advertising - in order to create the efficiencies needed to support separate mastheads and editorial teams.

This line of thinking was adopted 135 years ago in New Zealand by the creation of the NZ Press Association and, much later, the Newspaper Advertising Bureau in which newspapers recognised the benefits of sharing common editorial content such as international news and joint representation to advertisers. This reduced editorial duplication in the same manner as the US agreements and, ironically, is now proposed by the merger applicants five years after they closed the NZPA.

Fairfax and APN's argument that rationalisation would "enable them to invest in better quality journalistic content and greater breadth of coverage" seems unlikely when one considers where the cost benefits of merging would actually come from.

APN and Fairfax have already merged their printing and distribution north of Taupo and don't physically overlap much south of that point. APN's titles in the Hawkes Bay, Bay of Plenty, Masterton and Wanganui are already printed by a third party and Fairfax has no choice but to go it alone in Wellington and Christchurch where it is the only player.

Other than some head-office costs, which can't be significant in either case because they are managed as subsidiaries of their Australian parent companies, it's hard to see where most of the savings would come from other than the sales and editorial functions with all the attendant consequences for coverage and diversity.

Conclusion

Horton Media does not support the application in its current form.

We consider that the parties should be forced to divest print media assets of sufficient scale in the region of the applicants' single biggest overlap, Auckland, to support a significant second operator.

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