Executive Summary to Determination

NZME Limited and Fairfax New Zealand Limited [2017] NZCC 8

Date of Determination: 2 May 2017
On 27 May 2016 Fairfax and NZME (the Applicants) sought clearance or authorisation to merge their respective New Zealand operations. The merger would bring New Zealand’s two largest newspaper networks and two largest online news sites under common ownership.

On 8 November 2016 the Commission issued a Draft Determination signalling our preliminary view that the proposed merger would be likely to substantially lessen competition in advertising and reader markets, and that the merger should not therefore be cleared. We also indicated that there was not likely to be sufficient benefit from the merger such that we should authorise the acquisition, taking into account the likely detriments to the public that we identified.

Following the release of the Draft Determination, we sought and considered the opinions of the Applicants, experts and the public, including at a public conference convened to hear submissions (6 and 7 December 2016). Following the Conference, further submissions and evidence were received and considered.

Having now completed our assessment of the evidence, our final views are in most respects unchanged from the Draft Determination. We are not satisfied that a substantial lessening of competition is unlikely, nor that there is likely to be such a benefit to the public that authorisation should be granted.

Our final decision is to decline clearance and authorisation.

Media market challenges

The Commission accepts that the Applicants each operate news media businesses in a challenging and rapidly changing commercial environment. Consumers are increasingly embracing the ‘new media’ methods of accessing news, whether by direct access to the Applicants’ respective websites (nzherald.co.nz and stuff.co.nz) and mobile apps, or via social media channels such as Facebook.

NZME and Fairfax have both responded to these changes by adopting a ‘digital first’, multi-media strategy, where they publish all their news content online free to readers as it is produced. A selection of that content is then placed in daily print newspaper editions that consumers pay a monthly subscription or individual cover price to read.

News media markets are two-sided markets. Their commercial model depends broadly on attracting readers so as to sell advertising and also involves charging readers for some publications. The interdependence of these reader and advertiser markets is important. As readership diminishes, the business-case for advertisers weakens and advertisers may look elsewhere for marketing opportunities.

Advertising revenue is necessary for the production of news as content sales are not generally adequate to cover production costs. This poses a particular challenge online, where Facebook and Google account for the majority of digital advertising revenue and news media providers struggle to generate substantial revenue directly from readers. The rise in news consumption through mobile devices, notably smart
phones, has posed an additional challenge for news producers due to the decreased ability to generate advertising revenue through that channel compared with traditional print publications.

X10. It is important to note that the changing commercial environment NZME and Fairfax face is not due to a reduced demand for their core product. New Zealanders are strong consumers of news. Usage data suggests that, on average each month, 2.4 million New Zealanders visit nzherald.co.nz and stuff.co.nz, spending over 5 million hours on these websites. In print, NZME and Fairfax have a combined daily newspaper circulation of over 370,000 – equivalent to nearly a quarter of all households.

X11. However, the Applicants, like all news media, are in a transition phase. The growth in digital revenues is currently not replacing falling print revenues and they are seeking to transition to a more sustainable business model.

X12. Discussion of these commercial environments and imperatives occupied a great deal of submission and evidence. Our decision reflects that we have focused on the choices that readers and advertisers have, and how their choices impact on the commercial prospects of the Applicants.

X13. NZME and Fairfax submitted in their original application that without the merger they would continue to operate as separate entities in the short term. This would inevitably lead to the rationalisation or closure of some uneconomic print publications. By merging, they said they would be better able to continue to invest in journalism and content while adapting their business to the changing environment.

X14. On 25 November 2016, following the Draft Determination and before the Conference, the Applicants presented the Commission with a significantly altered prediction as to the likely future for each of their businesses without the merger. The details of this submission are confidential, [ ]. In this decision we reject that these are likely scenarios without the merger.

X15. We accept that news media markets are not static and that therefore the status quo is an unlikely assumption for the future without the merger. In our view, both Applicants are likely to be increasingly focused on developing their online news businesses and their print products are likely to continue to diminish in number and comprehensiveness over time.

X16. However, in such uncertain and rapidly changing markets, we are not satisfied that we should assume that [ ]. [ ]. In an article published on 23 March 2017 on the future of the news media industry NZME Managing Editor Shayne Currie said:

We are seeing growth in our print readership and you’re seeing examples overseas where subscriptions are increasing in both print and digital because people are
hankering for that quality content. If we can keep producing quality, relevant journalism, then I see our print products going well into the future.

X17. The rate and rapidity of retrenchment of print change is uncertain, but we consider that each business will continue to offer some combination of online and print products over the five year assessment period for this authorisation.

**Merger would remove closest competitor**

X18. In our Draft Determination we considered that the proposed merger would be likely to substantially lessen competition by increasing prices and/or decreasing quality for readers and/or advertisers in the following markets:

X18.1 premium digital advertising;
X18.2 the provision of online national news;
X18.3 Sunday newspapers; and
X18.4 community newspapers in:
  X18.4.1 Whangarei;
  X18.4.2 Hamilton;
  X18.4.3 Rotorua;
  X18.4.4 Taupo;
  X18.4.5 Napier;
  X18.4.6 Hastings;
  X18.4.7 Stratford;
  X18.4.8 Palmerston North;
  X18.4.9 Horowhenua; and
  X18.4.10 Kapiti.

X19. Of those markets identified, our final views remain unchanged with the exception that the concerns we held about the premium digital advertising market have been resolved.

X20. In assessing the effects of the merger on the above markets, we focused on the closeness of competition between NZME and Fairfax in both advertising and New Zealand news content production. We consider that competition would be removed in relevant markets where NZME and Fairfax currently compete for advertisers and readers. Our view is that this would be likely to lead to price increases and/or reductions in quality.
X21. In terms of advertising markets, the evidence we received indicates that advertisers currently negotiate between NZME and Fairfax in deciding which Sunday newspapers to advertise in. *The Herald on Sunday* and *Sunday Star-Times* are direct competitors in the North Island and both attract advertisers targeting a leisure and lifestyle focused audience. The closest print alternatives that may offer a similar audience are not as effective substitutes because they have different publication dates, format and frequency.

X22. Similarly, we found that where NZME and Fairfax community newspapers overlap advertisers will negotiate between them to get the best price. We do not consider that services such as Facebook, flyers or radio are suitable alternatives for local advertisers. The evidence we received shows that NZME earns [__________]. Removing this competition would likely lead to advertising price increases.

X23. We also considered that there was a real chance that the merged entity would increase subscription and cover prices for Sunday newspapers and introduce a paywall for online news that would be more comprehensive and/or more highly priced than in a competitive market.

X24. We further focused on the potential for the proposed merger to reduce the quality of news produced in online news and print markets. News quality incorporates factors such as the variety and volume of news covered, the choices about what content is produced and the breadth, accuracy and timeliness of coverage.

X25. The Applicants submitted that quality would be enhanced under the merger by reducing duplication of editorial staff and allowing them to invest in better journalistic content, training and investigative resources. They also stated that the two-sided nature of the market meant that the merged entity would have no incentive to reduce the quality of the news content it produced as that would lead to reduced readership and a corresponding drop in advertising revenue. The Applicants suggested their internal code of ethics, editorial independence in newsrooms, and the Press Council would also provide safeguards to ensure quality was maintained.

X26. However, we consider that competition between NZME and Fairfax leads them to produce higher quality content than would exist with the merger. Competition incentivises investment in editorial resources, motivates journalists and editors in their day-to-day work, and ensures diversity of editorial approaches. Competition also leads to greater investment and innovation in the way that content is presented to readers.

X27. Fairfax and NZME compete to be the first to unearth and break news. When they have been beaten to a scoop each works quickly to catch up and look for new angles. Under the proposed merger this rivalry and the benefits it delivers is likely to be removed. In our view this would negatively impact the quality of news and breadth of coverage produced.
X28. We consider that the cost savings of the merger, including reductions in editorial and journalistic staffing, would likely have the effect of reducing the range, volume and variety of New Zealand news produced. There is also likely to be a greater concentration of editorial opinions as to what topics to cover and what angle or perspective to take.

X29. We are not satisfied that the two-sided nature of the market nor existing internal safeguards would be sufficient to constrain the merged entity. We do not consider that TVNZ, MediaWorks, Radio New Zealand or any other news providers could expand their online offerings to the extent that they could provide sufficient competition to replace that lost by the merger. In our view, there is a real chance that the merged entity could undertake price increases or quality-reducing cost reductions without putting a significant amount of advertising revenue at risk.

X30. We considered extensive submissions and evidence as to the competitive constraint presented by social media, blogs and other sources of information and access to news. We treat these as a constraint, but as a significantly lesser constraint than the merging parties are to each other. We remain of the view that social media platforms produce relatively little original New Zealand news content and do not represent a significant constraint on the Applicants’ online news offering.

X31. Overall, we consider the proposed merger would be likely to remove the closest competitor of each Applicant, and that this would be likely to lead to price increases or reductions in quality. We are therefore not satisfied that clearance should be given.

Benefits of the merger

X32. Alternatively, the Applicants submitted that if the Commission declined clearance, then it should authorise the merger as it would result in significant public benefits to New Zealand.

X33. In assessing the public benefit, we balance the negative effects of the proposed merger against any gain to the New Zealand public that would result from the merger. We are required to consider quantifiable and unquantifiable benefits and detriments, and to exercise our judgement as to whether we are satisfied on the evidence that a merger results in such a benefit to the public that it should be permitted.

X34. We have assessed the benefits and detriments over a five year period. Even though we agree that print is retrenching, we consider that NZME and Fairfax will continue to operate their print and digital businesses over this period. However, given that the rate of print retrenchment is uncertain, we assessed two different scenarios in our authorisation assessment. Our approach is intended to take into account the benefits and detriments that are likely to occur as a result of the merger.

X35. The Applicants satisfied us that the quantifiable net public benefit of the proposed merger would be potentially significant – we calculate this could also be anywhere between $40 million to around $200 million over five years. The benefits include
savings related to corporate overhead costs, such as marketing, IT, premises and management costs and editorial and operational cost savings.

X36. We considered unquantifiable benefits that could arise from the merger over five years if the merger prolonged the longevity of various print publications and the overall level of editorial resourcing. However, we note that the merged entity would face the same trend of declining print revenues as the Applicants, so a large proportion of this benefit may be relatively transitory.

**Detriments of the merger – loss of plurality and quality**

X37. The fundamental detriment we described in the Draft Determination – and again here – concerns the likely loss of media plurality. Plurality ensures that there is a diversity of viewpoints available and consumed across and within media enterprises. Plurality helps safeguard against concentrating influence over public opinion and the political agenda. A loss of plurality cannot be quantified in a mathematical sense.

X38. In response to our Draft Determination, the Applicants submitted that the Commission could not consider plurality as a detriment as the “relevant detriments are limited to the economic detriments from harm to the competitive process, in the markets in which any lessening of competition is likely.” They further submitted that Parliament expressly removed plurality as a relevant consideration when it repealed the Commerce Act 1975. Therefore, plurality was a policy goal outside the contemplation of the Act.

X39. We address these submissions in greater detail in the legal framework section of this decision. However, we reject the notion that there is a category of negative consequences of a proposed merger that we are required to ignore. This approach could lead to a situation where we would be obliged to authorise a merger that in our assessment is not in the public interest. However the negative consequences are described (ie, as disbenefits or detriments), it is clear from previous legal cases and common sense that we can and should take all the consequences of the merger – positive and negative – into account.

X40. Plurality considerations are particularly important in New Zealand given that current concentration levels of media ownership are already high by international standards. This merger would consolidate the two largest news media providers in New Zealand, in an already concentrated market.

X41. The merged entity would have direct control of the largest network of journalists in the country, employing more editorial staff than the next three largest mainstream media organisations combined. Its news media business would include nearly 90% of the daily newspaper circulation in New Zealand and an overwhelming majority of traffic to online sources of New Zealand news. Including its radio network, the merged entity would have a monthly reach of 3.7 million New Zealanders.

X42. In New Zealand there are no media ownership restrictions or other mandatory journalistic regulations that would be effective enough, in our view, to materially
constrain the merged entity. Public news broadcasting in New Zealand is unlikely to make up for the loss of plurality from the merger.

X43. We are satisfied that the merger would be likely to reduce ‘external plurality’ – plurality between organisations – through concentrating media ownership and influence to an unprecedented extent for a well-established modern liberal democracy of which we are aware.

X44. NZME and Fairfax currently exert meaningful editorial influence over New Zealand’s news agenda. They compete to identify coverage-worthy news events, locate new sources of information, develop new angles on stories and create new methods of communicating with their readership. A reduction in the vigour of that competition – where two leading news firms become one – may result in editorial or ownership choices as to content, resourcing or coverage that result in important events not being covered, or covered less comprehensively than without the merger.

X45. Given the importance of the news media to a well-functioning democratic society, we consider that any adverse effects from reduced plurality have the potential to be substantial. The large audience reach that the Applicants have would provide the merged entity with the scope to control a large share of the news consumed by a majority of New Zealanders. In our view, this level of influence over the news and political agenda by a single firm creates a real risk of harm to New Zealand’s democracy and to the New Zealand public, including both those who read the Applicants’ news content and those who do not.

X46. The Applicants submitted that with the merger the likely ‘internal plurality’ – diversity of voices within a media company – would be sufficient to outweigh any likely reduction in external plurality. They noted that editorial independence and journalistic ethics provide protection against any reduction in the range of internal and external views they publish.

X47. We accept that NZME and Fairfax currently provide a range of views across their online and print publications for at least some stories. However, we are not satisfied there is a real chance that internal plurality will be preserved or increased, particularly in the face of planned cost reductions. The extent of internal plurality is discretionary on the part of the media owner and we do not regard statements that internal plurality will be maintained as a sufficient safeguard on the future editorial decisions of the merged entity.

X48. We also consider that the proposed merger would be likely to cause a loss of quality. This loss is also unquantifiable. However, the Commission considers that there would be a reduction in quality in reader markets due to a loss in competition. While we were conscious not to double count plurality and quality detriments in reaching our decision, our view is that quality detriments from the merger would be significant, in particular for consumers of online New Zealand news.
Balancing benefits and detriments

X49. The Commission is not mathematically able to weigh a quantified net benefit against unquantified quality and plurality impacts. In our view, the case-law is clear that we must not prefer or favour the assessment of quantified effects over unquantified effects. The judgment that we must exercise is not so narrow as to exclude consideration of the likely effect on the New Zealand public of this level of reduction in media plurality.

X50. As part of this balancing exercise, we considered what the benefits and detriments of the merger would be in the event that print retrenched even faster without the merger. However, even if this were to happen, we still consider that the loss of quality and plurality to New Zealanders would be significant. We consider that any further decline in print would also be matched by the increased importance of online news.

X51. Therefore, we do not consider that the highest potential net quantified benefit of around $200 million over five years, or any potential increased longevity of some print publications, would be sufficient such that in our overall assessment the New Zealand public would benefit from this merger. Whether or not some larger net benefit would cause us to reach a different conclusion is not a matter that we are required to decide, but in our assessment this conclusion was not finely balanced. We decline to grant authorisation.

Structure of this Determination

X52. This report is divided into six sections:

X52.1 Section 1 outlines the Commission’s Determination and investigation;

X52.2 Section 2 outlines the key parties to this merger, the current state of the media industry, the Applicants’ rationale for the merger, the legal framework for the Commission’s assessment, the with and without the merger scenarios and the relevant markets;

X52.3 Section 3 defines the relevant markets on the advertising side, and considers whether the proposed merger would be likely to result in a substantial lessening of competition in those advertising markets;

X52.4 Section 4 defines the relevant markets on the reader side and considers whether the proposed merger would be likely to result in a substantial lessening of competition in those reader markets;

X52.5 Section 5 considers the potential vertical and competition effects arising out of the proposed merger; and

X52.6 Section 6 assesses and balances the benefits and detriments that are expected to result from the proposed merger.