

Commentary on News Media Quality Issues in Fairfax/NZME Proposed Acquisition

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1. I am the James Parker Hall Distinguished Service Professor of Law and the Ludwig & Hilde Wolf Teaching Scholar at the University of Chicago Law School and Senior Fellow at the Computation Institute of the University of Chicago and Argonne National Laboratory.¹ At the Law School, I currently teach classes, depending on the year, in Antitrust, Copyright, Network Industries and Secured Transactions, as well as a seminar in technology policy. I also teach The Legal Infrastructure of Business at the University of Chicago Booth School of Business. Finally, I have an online course, Internet Giants: The Law and Economics of Media Platforms available through the Coursera platform.² I was engaged in this matter to provide analysis to the parties described below on their contemplated merger.

2. On May 27, 2016, Fairfax New Zealand Limited (“Fairfax”) and Wilson & Horton Limited (“NZME”) filed a joint Notice Seeking Authorisation or Clearance of a Business Acquisition Pursuant to S 67(1) of the Commerce Act 1986 (the “joint notice”). I have been asked to consider the likely effect of the transaction proposed in the joint notice on news media quality. Quality is not a simple notion, but I do think that there are a number of relevant considerations. I want to focus my analysis on the consequences for quality and diversity of one-sided payments in two-sided markets and then on the free-riding issues associated with the production of news stories with public-good characteristics. Before addressing those two particular issues, I sketch out how I see the current state of the newspaper business and then the relevant markets for media competition in New Zealand.

I. The State of the Newspaper Business

3. On September 7, 2016, the Newspaper Association of America, founded in 1887 as the organization representing the collective interests of newspapers in the United States, changed its name to the News Media Alliance. As the press release put it, “the announcement is the culmination of a larger strategic plan to highlight the news media industry’s evolution to multi-platform, digitally savvy businesses and premium

¹ <http://www.law.uchicago.edu/faculty/picker>

² <https://www.coursera.org/learn/internetgiants>.

content providers.”³ An organization built originally around print newspapers was dropping that as its core defining feature given the belief that the printed newspaper itself is an endangered species.⁴ Nothing suggests that news itself is going away or that text has reached an end, but paper – as a delivery medium for news in the form of text – appears to have a meaningfully finite remaining life.⁵

4. The movement away from paper has had and will continue to have dramatic consequences for news media organizations organized around physical newspapers. These organizations have struggled to monetize text news online at anything approaching the scale of revenues associated with physical newspapers, where revenues were usually generated through subscriptions, single-sale copies and advertising.⁶ As traditional newspapers have moved text news online as part of the expected permanent transition from paper, they have struggled to capture much of the value associated with their content. Other organizations, Facebook and Google being the most prominent, are able to monetize news content. Indeed, a proposed European directive on copyright in the digital single market contemplates additional rights for news publications⁷ to address the fact that “[i]n the transition from print to digital, publishers of news publications are facing problems in licensing the online use of their news publications and recouping their investments.”⁸

5. And moving online isn’t static either. The move from the computer desktop to smartphones has important consequences for the type of advertising that can be effective. Adjacent-display advertising – an ad next to or on top of a news story – was the traditional structure of print newspaper advertising and Google replicated that as it built its dominant search business. That seems not to work as well on smartphone display screens. The strong recent rise of social media – first and foremost Facebook and its allied properties – especially among young users means that many people consume news without ever encountering the underlying content or the news organization that produced it.⁹

6. The move to smartphones will probably accelerate the unbundling of the newspaper. Print newspapers are still delivered as a bundle of news stories each day

³ Newspaper Association of America Changes Name to News Media Alliance, Sept. 7, 2016 (online at <https://www.newsmediaalliance.org/naa-name-change-news-media-alliance/>).

⁴ Jim Rutenberg, Yes the News Can Survive the Newspaper, *The New York Times*, Sept 4, 2016.

⁵ This doesn’t seem to be true for books, where the physical paper-based book now seems to be holding its own after an initial rise of ebooks. Indeed, ebook sales are dropping seemingly driven in part by the fact that ebook prices have increased relative to the prices of physical books. Alexandra Alter, Audiobooks Turn More Readers Into Listeners as E-Books Slip, *The New York Times*, Sept. 23, 2016 (online at <http://www.nytimes.com/2016/09/23/business/media/audiobooks-turn-more-readers-into-listeners-as-e-books-slip.html>).

⁶ See Mark Thompson, CEO, *New York Times*, *The Challenging New Economics of Journalism*, in Reuters Institute Digital News Report 2016.

⁷ European Commission, Proposal for a Directive of the European Parliament and of the Council on copyright in the Digital Single Market, 14 Sept. 2016, at Article 11.

⁸ *Id.* at (31).

⁹ Nic Newman, Overview and Key Findings, Reuters Institute Digital News Report 2016.

they are delivered. National news grouped with other stories of national interest, sports with sports and so on. Bundled within a grouping and then bundled together as a single print newspaper. Online newspapers delivered on desktop computers to a web browser retained at least some of that look and feel (and the corresponding design). But content consumed on a smartphone, perhaps through a link received on social media, means that each story is consumed on its own. Every story on its own bottom as it were. The cross-subsidization of harder content with lighter content that was sustainable with bundled content delivery – print newspapers – is much harder to accomplish when the smartphone is the tool of choice for reading the content.

7. There is a separate problem embedded in the transition from paper to digital and from the desktop computer to the smartphone. For advertising to work as a financing mechanism for online content, ads need to be delivered in a reliable way. Ads delivered on paper in print newspapers were sure to be delivered, but ad blockers reduce the usefulness of ads in a simple, direct way. Ad blockers vary in the extent of use across countries but once a user adopts an ad blocker, they use it regularly.¹⁰ And a recent report, based on a survey in the U.S., makes clear that young people (aged 18-24) are extensive users of ad blockers.¹¹

8. And there is an additional competitive angle here that almost certainly works to the detriment of traditional news media. When content was consumed through standard web browsers, such as Internet Explorer, Firefox, Chrome or Safari, consumers could indeed install ad blockers to block ads but that would at least operate neutrally across all types of ads. As content delivery exits a traditional browser and more content is delivered through apps and social media, more control shifts in favor of the platform owner or app producer. Platform owners like Facebook and Apple are making platform design decisions to give them more control over how advertising is delivered.¹²

9. Print newspapers used to have full control over whether the advertising they sold to advertisers was actually printed in their newspapers and delivered to their readers. When online content was delivered through browsers, all content competed for advertising on the same platform – the internet – and while ad blockers would reduce the effectiveness of advertising, their existence wouldn't tilt the competition for advertising in favor of one type of content over another. But as more online content is

¹⁰ Id.

¹¹ Anatomy Media, Inc., Millennials at the Gate, Fall, 2016 p6. (64% of surveyed consumers have used an ad blocker).

¹² Mike Isaac, Facebook Blocks Ad Blockers, but It Strives to Make Ads More Relevant, The New York Times, Aug. 9, 2016 (online at http://www.nytimes.com/2016/08/10/technology/facebook-ad-blockers.html?_r=0); Roy Rosenfeld, Facebook isn't just fighting ad blockers, it's fighting the underlying causes of blocking, TechCrunch.com, Sept. 10, 2016 (online at <https://techcrunch.com/2016/09/10/facebook-isnt-just-fighting-ad-blockers-its-fighting-the-underlying-causes-of-blocking/>); Alex Hern, A proxy war: Apple ad-blocking software scares publishers but rival Google is target, The Guardian, Jan 1, 2016 (online at <https://www.theguardian.com/technology/2016/jan/01/publishers-apple-ad-blockers-target-google>).

delivered outside of a browser, traditional media are losing more and more control over their ability to deliver advertising in a reliable way.

10. As all of this should suggest, the newspaper business is in the middle of an epic transition. That transition is away from paper to online even as paper is for now a critical, if shrinking, legacy source of revenues for newspaper firms. Market share definitions or market share calculations that ignore this dynamic transition almost certainly offer a false guide to how competition will operate over the next few years. Efforts such as those in Europe to change underlying laws to channel more revenues to news media organizations reflect an understanding that news media cannot undertake their traditional role in democracies if they can't survive financially.

11. The Commission's own analysis appears to reflect these changes. As the Commission has recognized, the movement away from physical newspapers has been ongoing for some time.¹³ At an earlier time, the Commission has seen print newspapers and online media content as being complements rather than substitutes.¹⁴ But as the online world has changed, especially with an increasing fraction of New Zealanders having smartphones within constant arm's reach, the Commission's own analysis has evolved to reflect the reality of increased direct competition between print content and online content.¹⁵

12. And it appears that other antitrust agencies are reaching the same conclusion and are starting to reflect this stark reality for traditional news media in their decision-making. On September 15, 2016, the Australian Competition & Consumer Commission announced that it would not oppose the proposed acquisition of *The Sunday Times* and the online news site perthnow.com.au by Seven West Media even though the print newspapers in issue were "close competitors" and each of their news websites competed directly.¹⁶ The ACCC noted the decline in the amount of newspaper advertising revenue and concluded that advertisers would have other alternatives, such as online, radio and TV, after the proposed acquisition. And the ACCC believed that consumers would continue to have many news media choices, again pointing to online, radio and TV, even if their print newspaper choices were reduced. Finally, the ACCC concluded that after the proposed acquisition, Seven West Media would need to

¹³ *Independent Newspapers Limited and The Marlborough Express Newspaper Company Limited*, NZCC Decision 329 (2 October 1998) at [15].

¹⁴ *Wilson and Horton Limited and Power Plant Productions Limited*, NZCC Decision 445 (07 December 2001) at [36] and *Fairfax New Zealand Limited and Times Media Group Limited*, NZCC Decision 561 (14 October 2005) at [78].

¹⁵ *Bauer Media Group (NZ) LP and APN Specialist Publications NZ Limited*, [2014] NZCC 1 (23 January 2014) at [61] ("We have determined that the proposed acquisition is unlikely to substantially lessen competition in this way because if, post-acquisition, Bauer attempted to increase prices, sufficient consumers would switch to other substitutes, including in particular online provision of similar content.").

¹⁶ Australian Competition & Consumer Commission, *Seven West Media - proposed acquisition of The Sunday Times publication and website from News Limited* (online at <http://registers.accc.gov.au/content/index.phtml/itemId/1198464/fromItemId/751046>).

maintain the quality of their publications and online sites to continue to compete successfully for advertising.

II. Competition in Media Markets in New Zealand

A. Media Markets as Two-Sided Markets

13. We should start with some basic ideas about media markets. Traditionally, the bulk of newspaper revenues have come from two sources: advertising fees paid by firms to place ads in a newspaper and fees paid by readers to buy the newspaper (either in the form of subscription fees or per-copy fees at the newsstand). Newspapers think of both sets of customers in making decisions about what content to place in a paper newspaper or on a website. And these customers might have opposing interests: readers might prefer a newspaper with smaller, less intrusive ads while advertisers want attention even if that distracts from the newspaper stories themselves, so long as actual sales of newspapers don't decline.

14. In modern economic terms, as the Commission recognizes,¹⁷ newspapers are an example of a two-sided market, or put slightly differently, newspapers are platforms. The emergence of the commercial Internet over the last twenty-five years has created firms such as Google and Facebook that share the characteristics of traditional media firms. Content – user-generated content in the case of Facebook – and services – search, mail and more from Google – are provided to consumers and paid for by advertisers seeking to reach those consumers.

15. As is well recognized, there has been a strong drop in newspaper advertising revenues over the last decade if not longer.¹⁸ That drop has occurred simultaneously with the emergence of the Internet as an advertising platform where so much of the content and services of the Internet are advertising-supported. That said, I have not looked in any detail at the advertising side of the market in connection with this proposed transaction.¹⁹

16. Instead, my focus here is on the consumer-facing side of the newspaper market and, in particular, on the question of how competition in that market affects the quality of the content that newspaper firms will produce, but, as should become clear,

¹⁷ See New Zealand Commerce Commission, *Mergers and Acquisitions Guidelines* (July 2013) at [3.44] (“For example, a newspaper acts as a platform for both advertisers and readers. The newspaper creates content. The content is used to attract readers, and readers are used to attract advertisers.”); see also *Fairfax New Zealand Limited and Times Media Group Limited*, NZCC Decision 561 (14 October 2005) at [53].

¹⁸ See Pew Research Center, *State of the News Media 2016*, p. 13 (showing percentages drops in advertising revenue for newspaper companies from 2006, including a 7.8% drop in 2015).

¹⁹ I do note that the Communication Agencies Association of New Zealand (CAANZ), the industry association of the advertisers, believes that changes in the advertising industry have led them to support the proposed merger to increase the likelihood that print will continue to survive and to create an entity that has a sufficiently large data footprint to compete with Google and Facebook in delivering targeted advertising. See Submission to The Commerce Commission on the Proposed Merger of NZME and Fairfax from the Communication Agencies Association of New Zealand (CAANZ), September, 2016.

there are real interactions between the quality offered to consumers and the fact that newspapers operate in two-sided markets.

B. New Zealand Media Markets

17. I have not really been asked to address the question of how to define the market in this transaction, but it is almost impossible to address the quality question without some perspective on the structure of media markets in New Zealand.

18. Try four natural frameworks for understanding this transaction. These will oversimplify undoubtedly but should be useful for the analysis that follows:

1. *Print Newspaper Regional or Local Markets.* One way to see this transaction is to focus on the print newspapers. My understanding is that if one were to focus on the revenues of the merging parties, most of those revenues arise from print newspaper publications. I also understand that, like in many countries, there are important geographic separations between newspapers. That separation means that even large print media firms can merge without meaningfully changing actual competition between them.²⁰ On that framing, the proposed transaction should be cleared or authorised in due course by the NZCC.
2. *Online Media Markets Generally.* A different approach would be to treat print as a legacy shrinking market. Print undoubtedly remains important as a financial engine for newspaper media firms, but on this view, the competitive edge would have moved online, captured perhaps best in the phrase “digital first.”²¹ In this framing, most broadly, online news content competes with a wide variety of content for attention. Facebook – not just Facebook proper but all of its properties – gets 50 minutes per day of attention from each of its users.²² Facebook is advertising supported, as is Google as are a host of other content and service companies on the Internet. But it isn’t just the advertising side of the market where traditional news firms compete with these new Internet giants but also on the consumer side. On this framing of the market, the denominator is presumably quite large and the proposed Fairfax/NZME

²⁰ For example, in the United States, very few consumers would regard *The Chicago Tribune* and *The Los Angeles Times* as good substitutes, even though there are some overlaps in news covered (national and international stories). The Tribune Co. – which recently changed its name to Tronc – purchased the owner of the *L.A. Times* in 2000 in a \$6 billion transaction that received an early termination notice of the investigation from the U.S. Federal Trade Commission. See <https://www.ftc.gov/es/enforcement/premerger-notification-program/early-termination-notices/20002566> and Tribune Gets Antitrust Approval in Times Deal, *The Los Angeles Times*, April 7, 2000 (online at <http://articles.latimes.com/2000/apr/07/business/fi-16965>).

²¹ An economist might say that print is inframarginal in the sense that what is going on in the print market is not having important competitive consequences for the production of news content.

²² James B. Stewart, Facebook Has 50 Minutes of Your Time Each Day. It Wants More., *The New York Times*, May 5, 2016 (online at <http://www.nytimes.com/2016/05/06/business/facebook-bends-the-rules-of-audience-engagement-to-its-advantage.html>).

transaction is correspondingly small potatoes. Again, that would mean that the transaction would be easily approved by the NZCC.

3. *5-4 Transaction in Online News Media Markets.* A narrower approach to online news markets would be to treat the emergence of Facebook, Google and the rest as occurring in a different market from traditional news firms, either on the advertising side of the market or on the consumer side of the market. Again, define the market based on the idea that online is where the competitive edge is even if the existing news firms continue to deliver their content via legacy distribution tools (print for newspapers, radio and TV for other firms).

- My understanding is that there are five substantial firms in the New Zealand news media market: Fairfax, NZME, Radio New Zealand, Television New Zealand and MediaWorks. Each of these firms has moved to distributing content over the Internet and each is pushing into the tools of the others (print firms moving into video and audio and vice versa).
- In that framing, the proposed transaction would move the New Zealand news media market from five firms to four firms. My understanding is that 5-4 mergers are typically approved by the NZCC. That said, as suggested in the first section, it is important not to have too static a conception of these markets. As text moves from paper to digital, it makes it that much easier for news media firms to enter new markets. Both the BBC and the New York Times appear to be entering new markets. The New York Times has announced that it will set up local newsrooms in Canada and Australia.²³ This seems like a natural move: these are organizations that have much content that should already be of interest to readers in other countries and they can better leverage that content if they produce actual local content as well. They have the internal skill set to produce news and they can take advantage of that by hiring local journalists in target markets. Delivering a physical newspaper in a new market might be quite difficult, but online content is just a click away.
- A conception of the market as just online news media markets would need to reflect the likely competition between New Zealand-based media organizations as well as English-language competitors such as the New York Times and the BBC who seem well situated to create New Zealand focused versions of their content augmented with new local content.

4. *2-1 Transaction in Online Newspaper Markets.* Finally, the narrowest online characterization of the market would treat Fairfax and NZME as the only two substantial firms in the online newspaper markets. This framing would treat

²³ New York Times looks to broaden reach with readers in Canada, Australia, Guelph Today, August 24, 2016 (online at <https://www.guelphtoday.com/national-business/new-york-times-looks-to-broaden-reach-with-readers-in-canada-australia-373649>).

the traditional audio- or video-first firms as being in a different market.²⁴ And it would further collapse the geographic separation that exists between Fairfax and NZME in print and would instead treat them as being in the same competitive space. The proposed transaction would then be effectively a 2-1 transaction, ignoring for this purpose, the presence of online sites of print based competitors such as the Otago Daily Times, National Business Review, Sun Media, Bauer and others. And again, the 2-1 framing is quite static as it doesn't grapple at all with possible entry by historically print-based media firms like the New York Times or the presence of New Zealand-based firms historically based in video or audio. Again, the BBC example suggests that non-print media firms can move online successfully.

19. I have not been asked to determine which of these characterizations I think is right and I don't know that I have the information to do that anyhow. The point of this framing is to emphasize that on the first three approaches to market definition, my understanding is that the NZCC will likely approve the merger, while, in contrast, the merger will face the greatest scrutiny by the NZCC if the merger is framed as a static 2-1 merger.

20. The question before me is what would likely happen to news content quality if we assumed that the 2-1 characterization was the right one. I turn to that issue in the next two sections.

II. Diversity and Quality in Two-Sided Markets with One-Sided Payments

21. I want to start with a version of a simple classic example of media markets typically attributed to Steiner.²⁵ Imagine a market in which you have 100 consumers and slots for two traditional over-the-air radio stations. There are two types of consumers: 75 like to listen to country music and 25 would like to listen to classical music. Country-music lovers value the music at \$1, while classical music fans value the music at \$2. Both types of listeners are identical to advertisers who value reaching them at \$1 each.

22. Consider two different fee structures to suggest the issues at stake: (1) advertisers-only pay; and (2) listeners-only pay. Different countries historically

²⁴ The success of the BBC online suggests that there may be good reasons to think there is very little to prevent powerful offline video or audio firms from moving their operations online. See Ofcom, News consumption in the UK: research report, Figure 6.6, websites or apps used for news nowadays, 15 December 2015 (online at http://stakeholders.ofcom.org.uk/binaries/research/tv-research/news/2015/News_consumption_in_the_UK_2015_report.pdf). The same appears to be true in Canada where the CBC has moved its historic position in television and radio into the leading online presence among Canadian speakers of English. See Colette Brin, Canada, Digital News Report 2016, Reuters Institute for the Study of Journalism, p.80-81. And incumbent firms should be able to attract capital to boost their presence in these markets if there are attractive entry opportunities.

²⁵ P. Steiner, Program Patterns and Preferences and the Workability of Competition in Radio Broadcasting, 66 Quarterly J. Econ. 194 (1952).

approached radio in varied ways. The advertiser-only pays model matches the history of the United States and, of course, also matches much of the modern Internet.

A. Advertisers Pay

23. When only advertisers pay, what type of music will be broadcast and how does that depend on the structure of competition between the two radio stations? If the stations are separately owned, each station will play country music. On average, each would get half of the available listeners or 37.5 listeners. No station would play classical music as the station would recognize that its listening audience would drop from 37.5 to 25. If the radio stations were able to extract the full value to advertisers of reaching these listeners, each radio station would earn \$37.50. Note that classical music listeners are left out of the market.

24. But if both of the stations were owned by the same firm, the firm would play country music on one station and classical music on the second. The monopolist would know that it would get 75 country music fans on the one station and 25 classical listeners on the second and that would result in revenues of \$100. In this example, switching from competition to monopoly would boost program diversity and increase output.

25. As this example makes clear and as some of the filings recognize,²⁶ there is no simple relationship between the competitive structure of media and the range of content that the media will produce. In this example, moving from competition to monopoly would improve the types of content available to listeners.

B. Readers/Listeners Pay

26. In some ways that seems surprising and the result is driven in part by the assumption that only advertisers can pay. Switch instead and assume that only listeners can pay and that there is a way to exclude users who don't pay. In the U.S., cable TV is paid for by consumers and consumers who don't pay don't have access to it. And of course this is how paywalls work more generally.

27. If each station plays classical music, it gets half of that market and would get revenues of \$25.²⁷ If each plays country, each again gets half of the market and each would get revenues of \$37.50. But if the firms separate, each would do better: the sole country firm would get \$75 – 75 listeners who each value at \$1 – while the sole classical firm would get \$50 (25 listeners who value at \$2). Each of course would rather be the country firm but neither can switch formats given the choice of the other firm and do better.²⁸

²⁶ See E tū Submission, Application for Authorisation of a Merger between NZME and Fairfax Media, p.6.

²⁷ That assumes, again, that the radio station can obtain the full value of each consumer, here \$2, and that each station would get half of the available classical music listeners if both stations played classical music (i.e. each earns \$2 x 12.5).

²⁸ This is the standard definition of a Nash equilibrium, a conventional solution in noncooperative game theory.

28. Step back and see the big picture here: in this example, how payments are organized in this market has big consequences for the content produced. We can get the full range of content produced with either one firm or competing firms, but we can't do that here if only advertisers can be charged. The introduction of paywalls would create a second way of funding the content in this example and would improve social welfare.²⁹

C. Quality and One-Sided Payments

29. But there is a second point that is important and it relates directly to the question of quality. When only one side of a market can be charged, the only quality that matters is the quality valued by that side of the market. Return to the example where only advertisers can be charged for access to the platform. If the content producer had a way of making better country music so that the value to listeners would increase from \$1 to \$2 but that wouldn't make those listeners any more valuable to advertisers, the content producer would have no reason to increase the quality of its product.³⁰ In a two-sided market, changes in the quality of the product have to be considered as to what they mean for both sides of the market and it matters a great deal whether only one side of the market is paying for the platform.

30. Unsurprisingly, content is shaped by the way in which content is paid for.³¹ Print newspapers have traditionally been supported with two revenue streams – direct payments by readers and payments by advertisers – but online content is predominantly paid for by advertisers. As the model just considered makes clear, when only advertisers pay, from a pure economic perspective, it is only the interest of advertisers that we should expect to be considered. In that world, quality journalism doesn't matter directly but only matters in the way in which it shapes the readers available to advertisers.³²

²⁹ It is worth noting that there doesn't appear to be any current, strong move in favor of paywalls, especially in English-speaking countries. In the United States, the percentage of news users paying for any online news dropped from 11% to 9% in 2015 and there is no English-speaking country in the Reuters Institute for the Study of Journalism survey where the figure is above 10%. See Reuters Institute Digital News Report, pp. 24-25. The fact that the corresponding figure in Norway is 27% suggests the powerful effects of competition online throughout the English speaking world. It is easier to sustain online payment in a country that is more linguistically isolated.

³⁰ Do note the simplification here: in a more extended model, better quality would almost certainly attract more listeners and that is valuable in selling to advertisers. And well-placed news media insiders believe that producing quality journalism is ultimately the only real hope to get consumers to pay for content, which is seen as essential for the ongoing health of the industry as all news moves online. See Mark Thompson, CEO, New York Times, *The Challenging New Economics of Journalism*, pp. 108-09 in Reuters Institute Digital News Report 2016.

³¹ C. Edwin Baker, *Advertising and a Democratic Press* (Princeton Univ. Press 1994).

³² I understand that the parties' perspective is that professional editorial staff are also motivated to produce quality content by virtue of their own professional standards and adherence to editorial charters that each business maintains. And I don't doubt that, but I also see four physical newspapers a day – *The Chicago Tribune*, *The New York Times*, *The Wall Street Journal* and *The Financial Times* – and there are entire sections of those newspapers that seem explicable only because of the advertising that can be sold in them. The emergence and then expansion of the *How To Spend It* glossy magazine in *The Financial*

D. Paywalls

31. My understanding is that in the current media landscape, the incumbent media firms believe that it would be difficult to introduce meaningful paywalls online.³³ As some of the submissions recognize,³⁴ paywalls actually can have substantial social advantages. It would be natural to read what I have just said as saying that paywalls are good. I think that is right, but in some sense, the more important point is the way the payment mechanism shapes the production of content and then the further point about how the organization of content competition also influences the content that is produced.³⁵

32. When only advertisers pay, the content that is produced reflects their interests. In that setting, from a purely economic perspective high-quality content that readers/listeners might value highly won't be produced if that doesn't translate into value to advertisers. And, again, when only advertisers are paying, we may get more diverse content with fewer competitors.³⁶

E. Monopoly Power with One-Sided Payment

33. That sounds like a free lunch from a monopoly and we need to be careful about generalizing from that result. Ask a slightly different question: in this framework, how would the monopolist exercise monopoly power? And the answer here is that, if

Times and the corresponding equivalents in *The New York Times* and *The Wall Street Journal* offer advertisers an attractive format with ads guaranteed to be separated from hard-news stories. See Kate Abnett, How Newspaper Supplements Took on Fashion Magazines, BOF Intelligence, February 17, 2016 (online at <https://www.businessoffashion.com/articles/intelligence/how-newspaper-supplements-are-beating-fashion-magazines-at-their-own-game>).

³³ The submission by the Coalition for Better Broadcasting makes this point as well at p. 8. That said, a number of submissions point towards some experimentation with paywalls in the New Zealand regional market. See the submission by the New Zealand Political Studies Association.

³⁴ See Coalition for Better Broadcasting, Submission to the Commerce Commission on Wilson & Horton Limited and Fairfax New Zealand Limited – Application for authorisation of a business acquisition, p. 8.

³⁵ It is also worth noting that paywalls create a barrier to social discovery of content. As consumers increasing access news media content through social media like Facebook, it is hard to see why consumers would link to content blocked behind a paywall. The whole point of a link is to make it possible for a reader to get to the original story but that won't work if the story is quarantined behind a paywall. Consumers distributing links through social media will have strong reasons to prefer links to content that isn't paywalled.

³⁶ Notwithstanding these virtues of paywalls, my understanding is that the parties believe that there is no meaningful chance that they could profitably introduce paywalls over the relevant time horizon. That view may reflect a few key brute facts. There is no question that there are important differences between a zero cash price and *any* positive cash price and that that would operate as a barrier to the introduction of a paywall. Actual payments would require consumers to enter into payment transactions with the online media firms and that would require the collection of credit card information and more data. There is actually an important separation in the so-called GAFA – Google, Apple, Facebook and Amazon – between those that hold transactional information (generally Apple and Amazon) and those that do not (Google and Facebook). Beyond the transactional point, the behavioral economics literature emphasizes the substantial behavioral differences between a price of zero and a positive cash price. See Dan Ariely, *Predictably Irrational*, p49-65 (HarperCollins, 2008).

there were no other competing providers of digital news,³⁷ we should expect the monopolist to increase the number of ads it ran beyond the number we would see in competition. The monopolist would be trading off the additional revenues from having more ads against the potential loss of readers put off by more ads.³⁸ There may also be a producer benefit in increasing the output of ads in a market.³⁹

34. Nothing in this example says anything about whether the monopolist held market power on the advertising side of the market. And of course it need not: there is no reason in theory or in reality why a firm would need to have monopoly power on both sides of the market. A firm could have market power as to advertising without having any market power over listeners (think of being outside as being a perfect substitute for listening to the radio) or could have market power over listeners without having any market power over advertisers (there could be any number of places to advertise (billboards and other locations) but radio might be a distinctive type of entertainment (meaning that a monopolist could play more ads without losing too many listeners).

35. Note the trade-offs in this type of framework. With consumers not paying cash for the content, they pay only through attention and their exposure to advertising. A content creator “charges” more to the consumer by changing the mix of content and ads over a broadcast period. In the Steiner setting, a monopolist would broadcast a wider range of content and would thereby boost diversity but it would come at the cost of more ads being played or displayed. A government authority that especially prized a wide range of content might very well find that an acceptable tradeoff and see that as a basis for supporting a media merger.⁴⁰

³⁷ This would only be possible if there are no other close substitutes for the news / information that the parties produce and distribute online. As noted above, I understand that there are a number of providers of digital news and information in New Zealand that consumers can switch to with a click of a mouse.

³⁸ And note that this treats ads as a bad thing rather than something that consumers welcome. The reality is almost certainly much more complex. One way to assess this is the growing interest in ad-blocking software. There are important cross-country differences in the use of ad blocking software ranging, in one survey of users in 26 countries from a high of 38% in Poland to a low of 10% in Japan (the surveyed question was about the use of ad-blocking software on any personal device. See Reuters Institute Digital News Report 2016, pp.22-23). More troubling – at least from the perspective of news media firms given the shift in favor of smartphones – is that one-third of surveyed users in Germany, the US and the UK planned to install an ad-blocker in the next year. *Id.* That probably reflects views regarding the ads themselves as well as the fact that ads use data that consumers pay for.

³⁹ As is often the case, economics models with different assumptions might reach alternative outcomes. The idea of advertising congestion focuses on the fact that consumer attention spans are limited and that competing platforms don’t take into account that if they each run many ads, they may reduce the effectiveness of all of those ads. A media monopolist will internalize that congestion effect and might reduce the number of ads compared to a competitive outcome. See Anderson et al, Media market concentration, advertising levels, and ad prices, 40 *Int’l J Indus Org* 321 (2012).

⁴⁰ A number of submissions address the question of whether a combined firm would engage in predatory pricing. At least in the United States, the number of litigated cases of actual predatory pricing is vanishingly small. And of course antitrust agencies can address possible predatory pricing directly.

36. And, to map the Steiner framework more directly into text-based news media, the most natural way to think of this are situations in which competing news media organizations expend substantial resources covering the same stories. These are typically not the subjects of investigative journalism where there is no assurance that competing organizations will be looking at the same issues but instead are more routinized news situations (such, perhaps, as coverage of New Zealand Fashion Week). The duplicative coverage of competing organizations adds value but not necessarily so much that those journalists wouldn't be better deployed to cover other stories if not driven by competitive pressures to cover more mainstream content. In those circumstances, it could easily be the case that there would be net expansion of news coverage after this type of merger even if the sheer number of journalists employed by the merged firm was reduced.⁴¹

37. To summarize the analysis in this section, news media firms, like other firms, can't do everything. They can't cover every possible story and have to make decisions about how they allocate their journalists. The choices they make about which stories to cover are influenced by the competition they face. The point of the simple (but extended) numerical example is to suggest the idea that how that competition operates depends on how content is paid for. When readers pay directly, the value that they attach to content will be taken into account in producing that content. When only advertisers pay – historically, radio in the United States and much of the Internet today (and almost all of the news online) – economic theory would say that only the value that advertisers attach to content will be considered when that content is created.

⁴¹ It is worth noting that the Steiner model is hardly the last word on how to use economic models to capture competition effects in media markets. Anderson & Jullien, The advertising-financed business model in two-sided media markets, Toulouse School of Economics, Working Paper No. TSE-632 (March, 2016) provides a good summary of the wide variety of models in the literature. Models, of course, are always creatures of their assumptions and different assumptions will lead to models with different results. To try one posed by Anderson et al (2012) *op. cit.*, suppose that advertisers want to make sure that they don't "waste" ads by reaching consumers more than once (the assumption here, starkly put, is that they want to reach them only once and that any additional ad impression beyond that is wasted). If consumers multi-home – if consumers consume multiple types of content at the same time – then there is a greater chance of wasted ads. How to solve that? Provide unique content, as if you are the only content producer making that content, you can guarantee to advertisers that none of your readers/users are being exposed to their ads elsewhere. The authors note that this opposes the Steiner model, but the desire for increased exclusive viewers (and therefore increased diversity of content) should still be relevant to a platform even after a merger.

Again, this is very much like the earlier discussion of ad blocking and Facebook, where the key issue was the ability of Facebook to guarantee that ads were actually being delivered. Here unique, highly diverse content is the tool to ensure that duplicative, wasted ads are avoided. The Steiner model predicts content clustering, which is reduced through a merger, a focus on ad waste and ad duplication pushes towards separated content. And the multi-homing issue is just one example of an additional consideration that can alter outcomes. Given all of that, it is hardly surprising one recent analysis of the empirical literature on media mergers and advertising, concluded that "[m]ost studies indicate mixed evidence or no clear-cut result in one or the other direction." See Anderson et al, Media market concentration, advertising levels, and ad prices, 40 *Int'l J Indus Org* 321 (2012).

38. When only advertisers pay, media firms will create content that generates lots of eyeballs – clickbait in the phrase of the day – and media firms will compete to do just that, even if that means that important stories that are less likely to produce lots of traffic are not covered. Competition can of course produce better news content just as competition can do that elsewhere in the economy, but the analysis here suggests when only advertisers pay we are likely to see too much competition to produce clickbait and too little production of diverse content.

III. First-Mover Content and Public-Goods Content

39. There is a second way to get at that idea and that takes us to two competing visions of what counts as quality in media. There seem to be two competing senses of quality that appear in the submissions. A standard conception of quality seen in many antitrust cases is that we judge quality based upon the revealed behavior of consumers. If two restaurants open at the same time and one succeeds while the second fails, the first one was of higher quality in the most basic sense: consumers were willing to fork over cash to sustain the business. This is a vision of quality that implicitly takes into account the cost of producing the good consumed. An expensive foodie restaurant might be of higher “quality” than a more basic diner, but customers will really tell us which is better through their purchasing decisions. In the online media context, if consumers click on it, that makes it high quality, whether that is a story about New Zealand rugby, Kim Kardashian or the search for the Higgs boson.

40. Some submissions⁴² clearly have a different or second conception of quality and this is a reasonably accessible idea. Think award-winning journalism, meaning in the United States, say the stories honored with Pulitzer Prizes or Peabody Awards, and in New Zealand, say Canon Media Awards. To make that slightly more concrete, Matt Nippert of *The New Zealand Herald* won the 2016 reporter of the year award for his story on a Whakapakari Youth Trust camp. These are the type of stories that are about as far away from clickbait as one might imagine. Good journalists almost certainly care about quality of this sort. They want to be read but they most want to be read for the right reasons. And serious news media organizations try to install a respect for journalistic ethics throughout their organizations and often will adopt editorial codes of ethics to make those values concrete in an accessible way.

41. Media firms need to monetize content or they aren’t sustainable. Some content has a very short shelf-life and the desire of readers to have the information *now* means that simply making the content available is the best way to monetize that, whether that is done in print sold to consumers for a fee or online, where the content is matched with paid-for advertising. Much of the content classified as clickbait is content that has only a very brief life to be replaced quite quickly with something new. It isn’t clear exactly how important law is for protecting this content.

⁴² See, e.g., the Coalition for Better Broadcasting submission as well as that of Molineaux et al, Submission on the merger authorisation application by Fairfax NZ Ltd and Wilson & Horton Ltd.

42. But some content is more durable and the award-winning content that clearly matches one version of quality journalism almost certainly has that characteristic. This is content that will have value over time and where the legal system might play some role in protecting that content and that in turn will influence whether a media firm can monetize that content.

43. I don't know the applicable New Zealand law here, but my understanding is that it parallels U.S. law. There are some fundamental aspects of U.S. copyright law that limit the ability of media firms to capture value from the content that they produce. The most basic notion separates ideas and facts from the expression of those in something we term the idea-expression dichotomy. Authors cannot control ideas through copyright; they can only control the expression of those ideas.⁴³ Under U.S. law, authors also don't have a copyright in facts.⁴⁴ That reflects the idea that facts are in some fundamental sense not authored at all, but instead simply exist independent of the act of authorship. Again, a particular expression of facts can be copyrighted but not the facts themselves.⁴⁵

44. That should make clear, I hope, why U.S. copyright law is often seen as providing "thin" protection for much of the content produced by news media, especially newspapers. It is much harder to near-copy audio and video news content, but text can be near-copied quite easily. (All I mean by near-copy is to not copy the content literally but to come close to copying it while still complying with applicable law.)

45. This means that a second publisher can derive value from news content published by a first publisher. If that content has a short-shelf life, there may not be enough time for the second publisher to capture value, but for durable content, the second publisher can compete with the first publisher without having to invest in the original costs of creating that content.⁴⁶

46. This makes this type of high-quality content a type of public good, as economists use that term. We should be concerned that second-moving publishers will seek to free-ride on the efforts of a first publisher and that the ability of later publishers

⁴³ 17 U.S.C. 102(b) provides that: "In no case does copyright protection for an original work of authorship extend to any idea, procedure, process, system, method of operation, concept, principle, or discovery, regardless of the form in which it is described, explained, illustrated, or embodied in such work" (online at <https://www.law.cornell.edu/uscode/text/17/102>).

⁴⁴ See, e.g., *Feist Publications, Inc. v. Rural Telephone Co.*, 499 U.S. 340 (1991) (online at https://scholar.google.com/scholar_case?q=feist&hl=en&as_sdt=400003&case=1195336269698056315&scilh=0).

⁴⁵ New Zealand law appears to match the general shape of U.S. law in how it applies to ideas and facts. See Ideas – Does copyright protect my ideas? Copyright Council of New Zealand (online at <http://www.copyright.org.nz/viewFAQ.php?faq=354>).

⁴⁶ Given the limitations of U.S. copyright law for news media content, it isn't surprising that there is other relevant law, in particular, the hot-news doctrine and the related law of misappropriation. See, e.g., *International News Service v. The Associated Press*, 248 U.S. 215 (1918). But, I think that it fair to say, this doctrine hasn't altered in substantial ways the ability of a second publisher to work off a first-published work.

to do that limits the ability of first publishers to recover the costs of producing the work in the first place.

47. As I have tried to suggest, how much this dynamic can operate depends on the durability of the content and on the extent of media competition. Competition that has a short-life – classic clickbait – may have lost value before it can be appropriated, but durable content faces the risk of second publisher appropriation. Of course, that is much less of a problem if there aren't other publishers operating in the same market. Monopoly can have real costs but it does mean that a single firm will internalize across its properties these types of public-goods stories.

IV. Conclusion

48. As I noted in the beginning, I have been asked by Fairfax and NZME to consider how their potential merger might matter for “quality” in their news publications. As the submissions recognize, the idea of quality is not simple and there are a number of natural ways to understand that idea.

49. I have not been asked to opine about the relevant markets for the proposed transaction, but it is almost impossible to discuss any of the possible consequences of the transaction without some assessment of the relevant markets. As is well-recognized, media markets of the sort at stake in the proposed transaction are two-sided markets meaning, put simply, that both the interests of readers and the interests of advertisers seeking to reach those readers must be considered. I have not considered the advertising side of the proposed transaction.

50. On the reader side, I think that there are a number of natural ways to characterize the markets in issue in the proposed transaction. My understanding is that if the traditional print business of the firms is considered, there is very little direct competition between the firms given the geographic separation between the publications. If instead the focus is on the online media markets, there is a natural question about exactly which firms are in competition with each other in that space. The enormous growth of firms like Google and Facebook – each of which is predominantly supported by advertising – has had substantial consequences for all other firms receiving advertising dollars, but the competition as to users may be just as fierce. Fifty minutes a day on Facebook has to come from somewhere. My assumption is that the New Zealand Commerce Commission would approve the merger reasonably straightforwardly if it were to conclude that the right definition of the market put Fairfax and NZME in direct competition with firms like Facebook and Google.

51. A narrower conception of online news media competition would focus on the convergence that is taking place as the substantial news firms move to a digital first strategy, even as they continue to distribute content through legacy means. This would put five firms into competition with each other in this version of an online New Zealand news media market: Fairfax, NZME, Radio New Zealand, Television New Zealand and MediaWorks. That would make the transaction a 5-4 merger and my understanding is that the NZCC has typically blessed mergers of that type in the past.

52. The narrowest conception would be to focus on online newspapers and to somehow define Fairfax and NZME as being in their own market. That would make this a 2-1 merger and that is the characterization which presumably would face the greatest scrutiny by the NZCC.

53. I have tried to understand the quality issue in that context. In doing that, I have emphasized two ideas. First, how content is paid for matters for what content is produced. When only advertisers pay for content – as is true of most online media content – the only quality that matters for producing the content is quality seen through the interests of advertisers. That is a stark statement to be sure, but the key point is that we should expect content in those circumstances to be designed with the interests of advertisers in mind. Advertisers will want readers but the types of readers who will buy their products. Paywalls would change that, though paywalls seem to be difficult to sustain in the face of strong direct competition. Limiting competition might boost the sustainability of paywalls and that in turn might make it easier to take into account how users value quality. Beyond that, with only advertisers paying for content, there are good reasons to think that competing media producers will cluster their production around very visible content in an effort to attract lots of readers. A single firm would almost certainly cover a broader range of more diverse content.

54. Second, high-quality journalism of the sort that journalists are appropriately proud of goes far beyond the clickbait of the moment. That type of content has a durability that ephemeral content lacks. But that durability poses its own challenges given the limited legal protection that exists for news media content (especially for text). A second publisher can free ride on a first publisher's efforts and that means that this type of content has a public-good quality to it. Again, more limited competition might make it possible to sustain this type of content.

55. It would be natural to ask for a simple bottom line here, but I don't know that I can really do that. I do think that there are important structural considerations of the sort that I have identified that should make the NZCC more open to the proposed merger than it might typically be if the merger is appropriately characterized as a 2-1 merger. The public-good nature of media markets means that these are not standard markets and that is especially so when only advertisers are paying the vast bulk of the revenues to support the economic sustainability of those markets.

56. A number of submissions appropriately emphasize the critical role of the media in democratic societies. But the Internet has put media firms on the run and media have to be financially sustainable if they are to play their important Fourth Estate role.