dot·econ

A framework to approach benefits to consumers in Local Media Assessments

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Executive Summary

i. The Office of Fair Trading (OFT) has announced that it will request Ofcom's views on future local media mergers that raise prima facie competition concerns. Where so requested, Ofcom will provide a Local Media Assessment (LMA) that may inform the OFT's decision as to whether to refer the merger to the Competition Commission.

ii. An LMA may include Ofcom's views on various aspects of the merger assessment, such as the scope of the relevant markets, the competitive effect of the proposed merger, the likely market developments in the absence of the merger (including the question whether the merger candidates might remain viable competitors in that case), and whether the proposed merger could be expected to lead to benefits for media users such as higher quality or greater choice, which might be weighed against a lessening of competition.

iii. As part of its preparation for providing LMAs, Ofcom commissioned DotEcon to suggest a framework for examining potential benefits to local media consumers (readers, listeners or viewers). This framework could be drawn on in preparing an LMA within the short deadline dictated by the timeframe for the OFT's decision and using the types of information that parties may be able to provide. Of course, any analysis in relation to a particular merger will be highly case-specific and may include issues that fall outside this general framework.

iv. Our report is addressed to Ofcom and should not be taken as a statement of the types of information that merging parties or their advisors will, as a matter of course, be expected to provide to Ofcom and/or the OFT or of the analysis that Ofcom will necessarily choose to undertake in a given LMA. Rather it is intended to provide Ofcom with a potential framework for addressing this set of issues should they be relevant to the merger in question.

v. **Chapters 1 and 2** consider the context of LMAs and the underlying economic concepts related to the notion of benefits to media users. Within the framework of the Enterprise Act 2002, 'relevant customer benefits' may take the form of lower prices, higher quality, greater choice or greater innovation, but they must be rooted in the private value that media users in their role as consumers place on the provision of local media products. Based on economic principles explained in the report, the OFT is not mandated to consider wider public interest objectives in its competition assessments, and Ofcom instead has a separate statutory role in assessing the public interest considerations of a media merger, should it be called upon to do so by the Secretary of State.

vi. Therefore, the underlying notion of consumer benefits in an LMA is tied to the concept of consumer surplus – the difference between the willingness of media users to pay for the services they receive, and the actual prices they have to pay – and does not extend to aspects of societal welfare that are not reflected in consumers' purchasing and consumption decisions.

vii. The characteristics making media more or less appealing to consumers are multifarious and intangible, and measurable attributes are difficult to find. For this reason, and because local media are usually distributed free or at a price that reflects the value of audiences to advertisers (rather than purely the valuation of consumers), there will often be no good evidence about notional 'willingness to pay' for local media, and little data that would allow one to estimate a relationship between willingness to pay and certain underlying characteristics.

viii. In some circumstances it may be helpful to consider consumers' total time expenditure on media consumption as a proxy for the value they derive from it. Clearly, time expenditure cannot meaningfully be aggregated or compared across different forms of media consumption, such as reading and listening. Within a particular local market and medium, however, looking at movements in time expenditure in conjunction with other measures of demand such as audience reach or circulation numbers can provide additional insights into potential consumer benefits that might be associated with a merger, because it often more closely reflects the *intensity* of consumer use and presumably enjoyment.

ix. A merger could in principle affect consumer surplus by changing prices, quality and the positioning of the product offering in relation to consumers' preferences, where quality refers to the characteristics that make the product more attractive to *all* consumers (so-called vertical differentiation), and positioning refers to the characteristics that determine its appeal to different consumers (e.g. the content type or geographic coverage – so-called horizontal differentiation).

x. In order to assist in the identification of suitable metrics and the assessment of arguments and evidence presented by the merging firms, **Chapter 3** considers various mechanisms through which a merger between two local media outlets may provide benefits to consumers even if it lessens competition with respect to the firms' advertising customers. In particular:

   a. the ability of the merged entity to discriminate prices among its advertising customers might improve, or else the loss of competition could (in theory) be much stronger on the advertising than on the consumer side, in which case higher advertising margins would sharpen the incentives for attracting audiences and thus make the merging firms invest more in quality or reduce their prices;

   b. post-merger re-positioning decisions might lead to an increase in consumer surplus as product variety increases – this phenomenon is especially relevant to radio and has been analysed in relation to US markets; and

   c. the cost of attracting audiences, in particular the fixed costs of content creation, may fall as a result of synergies that can be exploited by the merged firm, making it profitable to provide a higher quality of output.

xi. **Chapter 4** develops a set of indicators that reflect the volume of use, in particular in relation to the amount of time spent on using particular media, and various measures of quality and positioning as described above, supported where possible by evidence of their relevance to consumers. A summary overview of these indicators and their interpretation is presented in the table below.

Table: Overview of indicators

Type	Metric/ Indicator	Interpretation	Comment
Volume	Total time expenditure of consumers	Increase in time expenditure as a result of merger suggests potential consumer benefits. Predicted reduction suggests that consumer benefits are less likely, and that other quality indicators would need to be shown to improve substantially in order to sustain consumer benefits	Used as initial screen in order to assess the likelihood of consumer benefits
Vertical - quality of content	Journalist time engaged in original newsgathering and story creation, expressed as a ratio to coverage population (all media)	Input measure linked to quality - more effort spent on creating original content should improve quality (for content types such as news where consumers value local specificity)	Time engagement measure preferable to any cost measure
	Ratio of originated to syndicated content, for subject-matter of local relevance	Output measure - more original content should increase value to consumers (for local subject matter)	
Vertical - advertising	Advertising pagination, column inches or count (newspapers)	Based on assumption that local newspaper advertising is more likely to be informative than persuasive, and readers are ad-loving at the margin, an increase in advertising would improve quality	May be necessary to consider any shift in the relative weight of informative and persuasive advertising in addition to the pure volume change
	Advertising minutes (radio)	Based on the conclusion listeners are ad-averse at the margin, an increase in advertising minutes would reduce quality for consumers	
Vertical - price	Cover price (paid newspapers)	Increase in price/introduction of charging unambiguously reduces consumer surplus (all else equal)	
	Online access charges		
Vertical - size	Pages, column inches (press)	Presumption that 'more is better'	Might need to be compared with changes in advertising - if size increase is purely due to increased advertising, consumer benefits would only arise to the extent that the additional advertising is valued

Type	Metric/ Indicator	Interpretation	Comment
	Programming hours (broadcast)		But most radio stations already broadcast round the clock
Vertical - frequency	Issue frequency, e.g. daily/weekly (press)	Presumption that 'more frequent is better'	Will generally be accompanied by other changes that need to be evaluated in conjunction
	Frequency of updates of websites/live news feed (online)		
Vertical – intensity of distribution	Number/ubiquity of retail outlets (paid newspapers)	Reduces additional costs (shoe-leather costs) for consumers to access the product - increase in number of retail outlets should make it easier for consumers and thus generate benefits	
	Volume/ubiquity/ intensity of free distribution (free home delivery, drop-distribution, handouts) (free newspapers)	Similar to increased number of retail outlets	
	Parallel online publication or additional content (e.g. online editions, Internet radio or podcasts, streamed or on-demand TV content)	Increase in the number of ways in which content might be accesses should provide consumer benefits	Differentiation in relation to available content might be associated with introduction of charging models or price discrimination; could also be used to segment audiences to support price discrimination amongst advertisers, which could sharpen incentives to grow audiences (see next chapter)
Vertical - physical quality	Colour printing, paper quality (press)	Improved quality should increase consumer surplus	Quality metrics potentially very subjective/difficult to measure and evidence for their importance to consumers relate to other attributes does not exist
	Quality of broadcast signal or equivalent (broadcast media)		
	Website quality and functionality		

Type	Metric/ Indicator	Interpretation	Comment
Horizontal - extent of distribution	Potential closures?	Closure will reduce consumer benefits as previously used product will no longer be available	Will have to be considered in combination with the likely impact of cost savings on other indicators (e.g. improved content quality)
	Will there be a wider/smaller/different area of distribution for all or a sub-set of the papers?	Increased geographic distribution would increase reach and attract additional customers whose valuation increases consumer surplus	Will have to be considered in conjunction with number/ubiquity of retail outlets and – more importantly – potential impact on 'localness' of content, which may be diluted
Horizontal - content positioning	Content positioning in terms of content volumes (for press), mix (for radio) of different genres	Improved match between product attributes and listener profiles should lead to consumer benefits. Repositioning plans in response to a merger might need to be looked at in terms of both positioning and incentives for the investment in vertical dimensions of quality. Repositioning may benefit consumers through increased variety, but formal or de facto amalgamation (e.g. content sharing) for cost-efficiency reasons may reduce it (cf. closures, above)	
	Demographic profiles of readers/listeners/viewers		Can provide some indication of pre-merger 'closeness' of merging firms and thus the likely implications on post-merger competition incentives
Online innovation		Can broaden appeal, extend range of content and broaden distribution, and could thus have considerable consumer benefits. Could also improve segmentation and price discrimination over advertisers, providing sharper incentives to grow and satisfy audiences.	But online channel currently still small and may not be a determining factor in assessment of effects with an immediate horizon.

1 Background and scope

1.1 The changing local and regional media landscape and the OFT's review of the local and regional merger regime

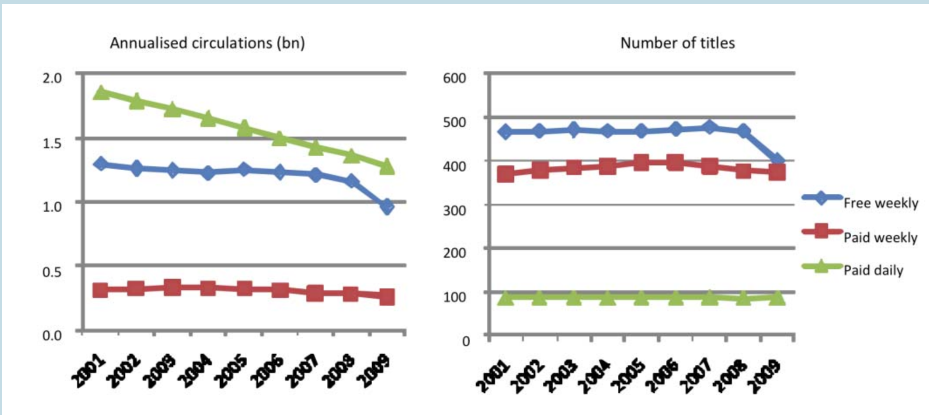
1. The Office of Fair Trading (OFT) recently conducted a review of the UK's local and regional media merger regime (OFT1091, 2009). The review was prompted by the Government's Digital Britain Interim Report, which reported concerns on the part of local media groups that the media merger regime was preventing or deterring consolidation viewed as necessary because of the changing economic and technological environment of local media.

2. Box 1.1 describes developments in relation to local newspapers and local radio and the potential for intra- and cross-media mergers in these sectors.

Box 1.1: Potential local media merger scenarios

Intra-media newspaper mergers

Newspaper publishers, whose sector was the focus of the OFT's review, argued that consolidation is required in order to ensure sustainability in the face of declining advertising revenues, and to respond to the threats and opportunities of the digital medium, delivering efficiencies and benefiting consumers. The local and regional newspaper industry is indeed in the midst of structural change due to an accelerating decline in advertising revenue and readerships linked to the rise of the internet, above all the loss of classified advertising to online search and listings sites.



Source: JICREG, DotEcon analysis. (Based on half-yearly data to May of each year. Paid includes part-paid, part-free. Titles refer to media buying points and include some grouped titles or editions.)

Despite falling circulations, as shown in the diagram above, the number of titles in fact appears to have been fairly stable in the first decade of the century until a sharp dip in the number of weekly freesheets beginning in late 2008. Ofcom's Local and Regional Media in the UK (September 2009) states that closures have generally occurred in highly competitive markets. Free advertising titles are likely to have been particularly hard hit by the economic downturn and collapse of the housing market.

There is broad agreement that industry restructuring will be driven by the need to respond to the threats and opportunities presented by the online medium. The recent (2010) House of Commons Select Committee report on the future of local media in the UK concluded that local newspapers should attempt to capitalise on their positions as longstanding local content providers by diversifying their online presence, converging to multi-platform news journalism (i.e. video footage etc.), as well as forming advertising websites.

Still, there appears to be significant uncertainty about what the digital business model will look like. Development of the online medium is still relatively embryonic: internet readership accounts for around five per cent of the daily audience and less than three per cent of consumption time, while providing less than six per cent of revenue in 2008. Paywalls for local newspaper content have yet to appear. According to Currah (2009), publishers lack a "clear projection and valuation of the digital market."

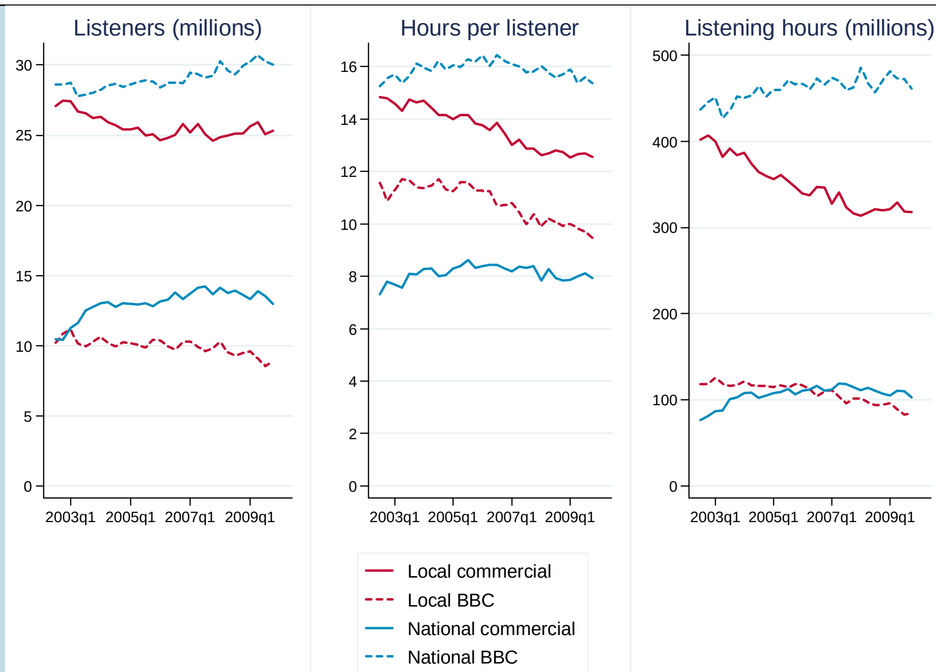
Some, e.g. Chisholm (2009), suggest that local and regional newspapers can adapt to the role of curating user-generated local content while attracting advertisers through their ability to provide targeted advertising and marketing at local level, and point to the success of some Scandinavian newspaper groups in building strong web presences and reverse-publishing such content in print editions. Graham and Hill (2010) conclude that in the long term "[n]ewspapers will probably survive if they supply an 'elite' service to a leadership news audience. This will be in the form of 'hybrid' content: analysis, interpretation and investigative reporting in a print product that appears less than daily combined with constant updating and reader interaction on the Web."

These trends are likely to reinforce a much longer established trend, going on since at least the 1990s, towards a regional 'rationalisation' of newspaper groups' holdings, driven by technological changes whereby production and to some extent content generation are centralised in regional hubs while printing is increasingly outsourced.

Intra-media radio mergers

The number of local and regional commercial radio licences has increased steadily from 172 in 1995 to 317 in 2008 while BBC local and nations stations have been constant at around 46[1] (see Ofcom (2009), LRMUK, Figure 9). Over the second half of this period, however, local radio listening – and in particular listening to commercial local radio stations – has been falling, while national listening figures have held up or even increased, though there is an indication of a recent decline in national commercial listening, as shown in the charts below.

[1] Commercial stations have very varying footprints (measured by Total Survey Area (TSA) or Measured Coverage Area (MCA)) which may be much wider or smaller than those of local BBC services. BBC local radio tends to have a higher ratio of speech content and to employ a higher number of journalists to conduct primary newsgathering.



Source: RAJAR, DotEcon analysis; Notes: 'Local BBC' includes BBC local and regional stations. Basis for calculation changed in 2007

There has been consolidation in recent years driven by economies of scale in back office, group overheads, investments in online, and advertising sales (see Ofcom (2009), LRMUK, paras. 3.51-3.52).

Ofcom has recently[2] made changes to the regulatory regime for analogue local radio aimed at helping stations, especially smaller local stations, to secure commercial scale and financial viability while safeguarding local news and programming. Under the new arrangements FM stations will normally be able, from June 2010, to co-locate and share all programming within relatively wide approved areas or 'mini-regions', thereby effectively forming a larger station with wider coverage. This measure is also intended to facilitate migration to DAB.

Likewise, DAB multiplex operators will be able to merge and extend local multiplexes, including by sharing frequencies (if possible), within wider approved areas. Localness guidelines have also been revised so that FM stations can reduce the amount of locally made programming they are obliged to air in exchange for more regular local news broadcasts. AM stations will be able to apply to be relieved of their locally-made programming obligations.

Ofcom is also proposing to lift the '2+1' restriction on commercial radio licences whereby there must be at least two commercial stations owned by different operators in addition to BBC services in a local area. This change will also facilitate consolidation.

These measures will presumably create additional incentives for radio stations to merge in order to take advantage of the easier conditions for co-location and

[2] Ofcom, 'Statement on commercial radio localness regulation', 15 April 2010. Additional measures to encourage UK-wide services and expansion of digital services are not discussed here

programme sharing and the reduced need for locally based programme making.

Cross-media mergers

Cross-media mergers will be facilitated if Ofcom's proposal to relax local cross media ownership rules are accepted. Under the proposal, the only restriction that would remain would be that a single operator could not own all three of: i) local newspapers with a local market share of over 50 per cent, ii) a local radio station and iii) a regional Channel 3 TV licence.

A widespread view reflected to us in conversations with industry participants is that the commercial case for cross-media mergers is typically weak. In work for Ofcom, Oliver & Ohlbaum[3] conclude that although both radio stations and newspapers output local news and undertake newsgathering, the benefits from consolidation are minimal because news programming accounts for only 5-10 per cent of total radio costs, not all of which would be saved anyway because of the need for radio presenters and reporters, and because advertising revenue synergies are also limited.

However, the recent changes to radio localness regulations, whereby stations can increase their news output in exchange for reduced local programming obligations, could presumably strengthen the business case for a merger between a wide-area local radio operator and a regional newspaper group at least somewhat, especially if the latter already delivers real-time and breaking news via the internet.

1.2 The requirement for local media assessments (LMAs) from Ofcom in future merger cases

3. The OFT concluded that the media merger regime in force since 2003 was sufficiently flexible and evidence-based to allow decisional practice to respond to changing market conditions without legislative amendment. It further announced, however, that it would turn to Ofcom to provide views on relevant issues in the event of future local or regional media mergers that raise a prima facie competition concern.

4. This intention was confirmed in the OFT's 'Mergers – Jurisdictional and procedural guidance' (OFT517, June 2009), which stated that in cases where local or regional media mergers raised prima facie competition concerns, the OFT would ask Ofcom for a local media assessment (LMA) to inform its decisions on the reference test and on the application of any available exceptions to the duty to refer the merger to the Competition Commission (CC).

5. Specifically, an LMA *"would be likely to include Ofcom's views on:*

- *the relevant counterfactual to the merger (including the risk of the asset or business in question failing)*
- *the scope of relevant product and geographic markets*
- *the competitive effects of the merger, and*

[3] Oliver & Ohlbaum, 'A macroeconomic review of the UK local media sector - A report prepared for Ofcom', published alongside 'Local and Regional Media in the UK', 22 September 2009.

- *exceptions to the duty to refer, and in particular Ofcom's views on whether the markets are of insufficient importance (de minimis) to warrant reference and whether there are 'relevant customer benefits' – such as higher quality (which, in the context of newspapers, could for example reflect the range and quality of news reporting) or greater choice of products – which might be weighed against an identified substantial lessening of competition."* (OFT517, para. 6.15)

6. Formal decision-making responsibilities remain unchanged, however, and lie solely with the OFT. Ofcom's role is purely of advisory nature and the decision of how to treat views from third parties rests with the OFT.

1.3 The scope of this report: potential benefits of local media mergers to consumers

7. As part of its preparation for the role of providing LMAs to the OFT – not least in light of the short timeframes of an OFT Phase 1 merger assessment – Ofcom has commissioned DotEcon to suggest a framework for examining potential benefits to local media consumers (readers, listeners or viewers). The identification of such benefits would form part of any LMA that Ofcom would provide.

8. OFT practice in considering local media mergers, reaffirmed in its 2009 review and its recent clearance of Trinity Mirror's acquisition of regional newspaper titles of Guardian Media Group[4], is to examine whether a significant lessening of competition might arise in the relevant market or markets for advertising and, if so, to take account of other factors that may mitigate or outweigh these effects, before deciding whether to refer the case to the CC.

9. 'Relevant customer benefits' to local media consumers, if they can be demonstrated to exist in a particular case, are one such set of factors. Under the 2002 Enterprise Act, such benefits can take the form of:

   - lower prices;
   - higher quality;
   - greater choice; or
   - greater innovation.

10. Within the framework of the Enterprise Act, these benefits must be linked to the private value that consumers place on media goods, rather a wider public value notion. The OFT is not mandated to consider public interest objectives in its competition assessments, and Ofcom has a separate and statutory role in assessing the implications of a media merger for 'citizens' rather than 'consumers'. In view of the fundamental importance of observing this

[4] OFT, 'Acquisition by Trinity Mirror plc of the regional newspaper titles of Guardian Media Company plc', published 24 May 2010. The OFT notes in the text of the decision that it did not consider that a formal LMA was required from Ofcom in this case.

distinction in relation to the nature and source of benefits in undertaking LMAs, we devote the first part of our report to clarifying these concepts and the underlying economic rationale for their separation in the first phase of the UK media merger regime.

11. Our report concentrates on local newspaper and radio mergers, both intra-media and cross-media. Local TV (as distinct from the regional Channel 3 licences) is scarcely represented in the UK, but if a merger situation did arise involving local TV, the principles set out in this report could be adapted to suit. There are also no pure online local media of major importance operating on a commercial basis (distinct from national listings, classified and paid search services that can be searched down to local level). Online offerings in a local or regional setting are in most cases provided by companion sites of traditional media outlets, and we have therefore dealt with online as an adjunct medium.

1.4 Challenges

12. The goal of this report is to establish principles and metrics that can be used by Ofcom for assessing the impact of local media mergers on the private welfare of readers, listeners or viewers. In particular, in view of the 'advertisers-first' approach to media merger assessment, we provide a framework for examining whether there might be *benefits* to consumers in mergers that raise competition *concerns* in relation to advertisers.

13. Even when limiting attention to the effects of local media mergers on private welfare, consistent with the scope of competition policy, assessing the quality implications of a local media merger is a complex task. The OECD's 2003 Policy Roundtable on media mergers concluded that:

> *"[The] effects of a media merger on both advertisers and consumers cannot properly be assessed without considering how the merger might affect quality and diversity* [i.e. consumer choice in a private value sense[5]]. *One might agree with that statement and opt, however, to put very little emphasis, if any, on quality and diversity when reviewing media mergers. This is because these attributes are inherently difficult to measure and the effect of a media merger on them is highly complex."* (OECD 2003)

14. There are several reasons for this complexity:

- The characteristics of media products that make them more or less appealing to consumers are multifarious and intangible, involving informational and aesthetic qualities that are difficult to boil down to a few measurable attributes, and which matter very differently to different consumers.

[5] Diversity is used in the OECD report in the same sense as consumer choice or variety, viz. "Diversity, as the term is used here, refers to the variety of available content, whereas pluralism is reserved for describing the number and nature of independent providers of media services on the market."

- Empirically assessing their contributions and trade-offs within consumers' overall willingness to pay is made still harder by the fact that media products are often distributed for free, providing little price data that one might use in order to estimate consumers' willingness to pay as a function of those characteristics.

- Economic theory offers no sharp predictions of the consequences of media mergers for consumer welfare because of the complexity of the markets involved: media outlets compete for consumers on price (sometimes), 'vertical' quality attributes and 'horizontal' positioning simultaneously, all in the context of a two-sided market in which they act as platforms bringing together consumers and advertisers and reconciling the interests that each of these two sets of customers have in the presence or absence of the other.

- As explained in more detail below, the merging parties may have an incentive to adjust product characteristics post-merger, so that analysis cannot necessarily be based entirely on their pre-merger attributes. In other words, counterfactual analysis must extend to product (re)positioning.

15. These difficulties are compounded by a lack of complex case precedents, especially in newspapers, as noted in the OFT's review, and those assessments that have been conducted have made little more than passing reference to impacts on consumers. The OFT itself concluded its review by stating that there is "little value to be gained from 'blue' skies' work, carried out without any particular merger in mind" and that future assessment practice is likely to be shaped by the experience of future enquiries. At the same time, such assessments will have to be undertaken to a very challenging timetable, leaving little time for an attempt to capture systematically the factors that would allow one to identify consumer benefits flowing from an increase in concentration in local media markets. It is this challenge that this report is intended to help to meet.

1.5 Plan of this report

16. Our report is set out as follows:

- Chapter 2 sets out the economic concept of 'consumer benefit' that is relevant to local media merger assessments from a competition policy perspective and distinguishes it from other notions of media quality and social benefit that apply to public media policy and media discourse more generally. It also sets out a conceptual framework for the rest of the report.

- Chapter 3 emphasises the forward-looking nature of merger assessments and surveys economic arguments that could be relevant in examining the effects on consumers that might be expected to flow from a proposed concentration and assessing the credibility of plans and claims presented by the merging parties. It also surveys existing evidence on the effects of local media mergers on consumers.

- Chapter 4 proposes metrics for assessing the potential impacts of a local media merger on consumers within the timeframes of an LMA and supports them with a range of evidence (where it exists) for their likely relevance.

1.6 Acknowledgments

17. We would like to thank the following individuals and organisations for discussions that informed this report:

- Jim Chisholm (newspaper and media consultant and analyst)
- Media Standards Trust
- Newspaper Society
- Ofcom
- OFT
- Society of Editors

18. We also thank the Ofcom team for facilitating these contacts and for their discussions and comments on earlier drafts.

2 Concepts

2.1 The meanings of 'quality' and 'choice'

19. The terms 'quality' and 'choice' (or 'diversity' or 'variety') have specific connotations in competition economics, and these connotations may be rather different from other notions of quality and diversity that are often applied in a public policy context, in particular in discussions relating to sectors of such social and cultural significance as the media. Because an LMA is tasked with informing a decision in a competition policy context, it is important to ensure that any notion of consumer benefits from better quality or increased choice matches the one used in competition economics.

20. At root, competition policy is concerned with those aspects of consumer welfare that well-functioning markets promote. It therefore focuses on the benefit directly perceived by consumers of media goods because it is this benefit that is reflected in their purchasing and consumption decisions and that therefore influences firm behaviour. The presumption, widely supported by theory and observation, is that in a broad range of circumstances competition tends to benefit consumers by forcing firms to provide attractive products and cater to a range of tastes at prices that are no higher than necessary to fund market rates of compensation for labour and other inputs and provide owners with normal risk-adjusted rates of return. In *this* context, 'quality' is whatever makes a product more attractive to consumers, while the importance of 'choice' is an acknowledgment that consumers will generally differ in what they prefer – and thus that a wider range of products will generally provide consumers with something that is closer to their most preferred variant than a single standard product would be. These notions of quality and choice apply to media as they do to many other industries in which they do not have other, more contentious meanings.

21. Public value conceptions of media standards and plurality, on the other hand, are based on a recognition that the role of media in serving the public interest is broader than just providing a service to immediate consumers and catering to their private tastes. 'Quality' in this sense can refer to the level of coverage and standards of accuracy on issues that make for informed participation in society, while a plurality of providers and viewpoints is valued for its contribution to maintaining democr*atic d*ebate. Of course, particular groups within society also have their own notions of media quality which they are often inclined to advocate for the public benefit.

22. These public interest considerations arise as a distinct objective from those of competition policy precisely because markets – even competitive ones – might fail to yield the level and type of media provision that is considered optimal for society. The reason is that consumers themselves do not fully reflect these benefits in their purchasing and consumption decisions, and so from a social point of view may not adequately reward media enterprises for providing them, or penalise them for not doing so. Competition, and hence competition policy, cannot be relied on to meet these objectives.

23. The distinction between private consumer welfare and the wider public interest is reflected in a division of responsibilities at the first phase of a media

merger assessment under the system in place in the UK since 2003. The OFT as the specialist first-phase competition authority is responsible for decisions purely on competition aspects of the merger. Separately, the Secretary of State has the power to intervene on public interest grounds, in which case he or she will require Ofcom to provide advice and recommendations on the issues involved. Based on Ofcom's advice on the public interest considerations and the OFT's decision on the competition aspects of the merger, the Secretary of State then decides whether to refer the merger to the CC.

24. In providing LMAs to the OFT (as distinct from advising the Secretary of State in public interest interventions), Ofcom's assessment of consumer benefits must be based on the competition policy-related, private value conceptions of quality and choice, and it is these that we therefore develop in this report.

2.2 Consumer benefit

2.2.1 Consumer surplus

25. The welfare concept on which competition policy is focused is the simple notion of 'consumer surplus', defined as the difference between the maximum amount that each individual who purchases the product would be willing to pay and the price they actually pay, aggregated over all purchasers. Consumer surplus differs from the much wider notion of *social* welfare, which even competitive markets may not be guaranteed to promote (e.g. in the case of so-called external effects – welfare impacts that are not mediated through a pricing mechanism), and which may include extraneous considerations (e.g. notions of merit goods).

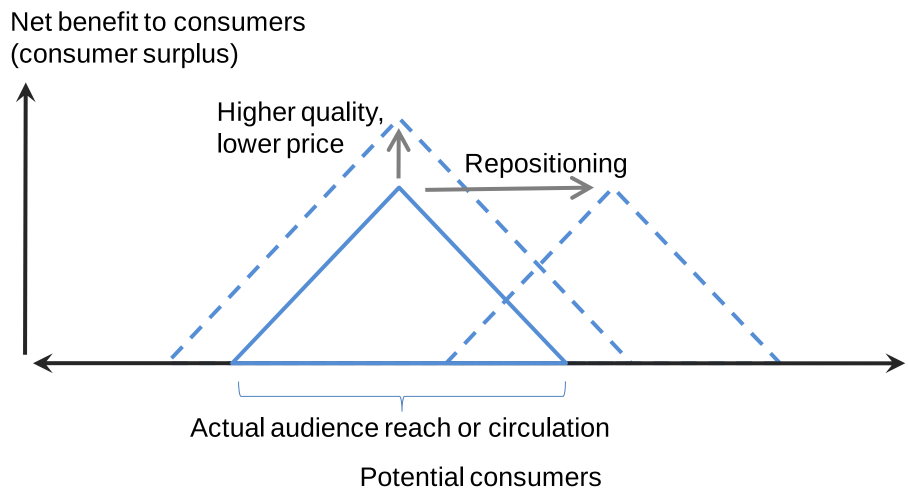
26. The most common concern in relation to mergers between firms competing in the same consumer market is that a lessening of competition can lead to an increase in prices, reducing consumer surplus in part by transferring it to owners or shareholders of firms, and in part by deterring some consumers from purchasing at all (a pure or 'deadweight' loss). Obviously, a reduction in quality following a merger would have similar effects on consumer surplus to an increase in price, whilst the impact of a potential reduction in variety is perhaps more ambiguous: the loss of product variety may mean that some customers no longer can purchase their most preferred variant, but it may also lead to cost savings that, if passed on to consumers to a sufficient extent in the form of lower prices, can outweigh the reduction in valuation as a result of having to purchase products that do not match some customers' preferences as closely as those that were originally available.

27. While the practice of the UK competition authorities in local media merger assessments is to focus on purchasers of advertising, the same principle should ideally govern the assessment of 'consumers' in the terminology of this report, i.e. readers, listeners or viewers.

2.2.2 Consumer surplus as a function of price, quality and positioning

28. As a motif for the rest of the report Figure 2.1 introduces a simple graphical device that will help link consideration of the economics of media mergers with the practical business of gathering metrics of possible merger effects.

Figure 2.1: Strategic variables of commercial media outlets and their effect on consumers



29. Given a population of potential consumers, their incomes, diverse preferences and so on, consumer surplus can be thought of as a function of three things:

- the *price* of the product;
- its *quality*;
- and its *positioning* in relation to their preferences.

30. In the figure, consumers are spread out along the horizontal axis while the benefit that each consumer gains from consuming the product is shown in the vertical dimension. Total consumer surplus is equivalent to the area of the triangle, and depends on price, quality and positioning as set by the media outlet. Quality and positioning are referred to in economics as 'vertical' and 'horizontal' attributes respectively, as suggested by the figure and explained below.

31. Positioning refers to the characteristics of the product that determine its differing appeal to different consumers. In the simplest case, consumers themselves can be thought of as being spread out uniformly along some axis that measures their taste. Willingness to pay, and therefore consumer surplus (represented by the vertical axis) at any given price, is highest among those for whom the product is 'positioned' closest to their preference, and tails off on either side, falling to zero for those who prefer not to purchase or accept the product at all. Thus, the audience of consumers who purchase or accept the media product is the base of the triangle in the diagram, and their total

consumer surplus is its area. (The representation used is intended heuristically and the geometry should not be taken literally.[6])

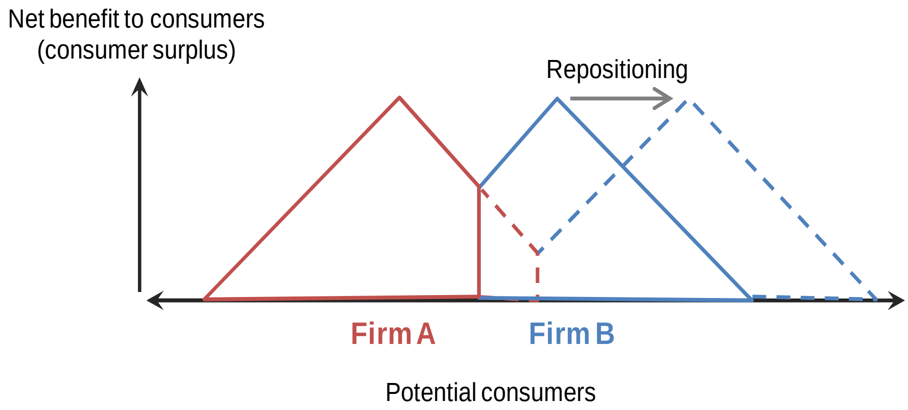
32. The most obvious example of positioning is geographical location. A newspaper focusing on a certain town will, on average, appeal much more strongly to those who live there than to those who live in peripheral areas or are otherwise only partly connected with it, and may have next to no value to those who live outside the area covered by its reporting. However, the same principle can be applied to the 'location' of the product in many other dimensions, such as the programming mix of a radio station among different genres.

33. 'Quality' on the other hand refers to characteristics of the product that make it more attractive to *all* consumers, even if to different extents. For a given positioning (such as the content mix), quality attributes such as the standard of newsgathering or production or overall volume of pages in press, or the quality of broadcast signal in radio, have the same direction of effect on all readers or listeners. Cover prices can also be thought of as a 'vertical' characteristic inasmuch as lower prices can be thought of as unambiguously beneficial to all consumers, even if they differ in their price sensitivity.

34. Price, quality and product characteristics are of course variables controlled by the suppliers, and affected by competition between them. Mergers may therefore have an impact on any of these variables, and thus on consumer surplus. In relation to media products whose provision is funded by supplying audiences to advertisers, and that are offered to consumers for free at the point of use, the main changes in response to a merger will of course happen in relation to product quality and positioning. For example, a merger might result in an increase in consumer surplus if the merging parties were to increase differentiation between their products, moving them further apart along the spectrum of consumer preferences, as shown in Figure 2.2. The additional consumer surplus gained on the right as firm B moves away from firm A outweighs the loss of surplus on the left because the consumers will be able to migrate to Firm A and retain some of their surplus (the region contained by the red dotted line). In other words, the total area covered by the two triangles increases as they are shifted apart.

[6] Economists will recognise this representation as a kind of Hotelling diagram with linear 'transportation' costs. It will be used in this report only in a heuristic way to illustrate the principles of vertical and horizontal differentiation and the impacts of mergers on consumers. Formal models of strategic competition in differentiated product markets are notoriously fragile (and may not have stable equilibria) and are difficult to calibrate realistically to real-world markets. In practice, customer preferences and product characteristics will have many dimensions, and may be linked in complex ways.

Figure 2.2: Consumer surplus effect of an increase in product differentiation



2.2.3 Measuring consumer surplus

35. Merger analysis in respect of consumers involves assessing the direction and if possible the magnitude of the *change* in consumer surplus that a merger might bring about.

36. Consumer surplus is an unobservable construct but effects on it may be inferred by estimating demand functions for the products affected. Demand functions relate the number of consumers who are willing to pay a certain price to the characteristics of the product and competitors' products. Histories of prices, volumes and product characteristics provide data on willingness to pay that can be analysed in this way. Ideally, one would gather a history of prices and other vertical and horizontal characteristics, and based on this information estimate a money-metric consumer value function, or family of functions for different types of consumer, relating their total private willingness to pay to the characteristics of the media product via a set of known parameters.

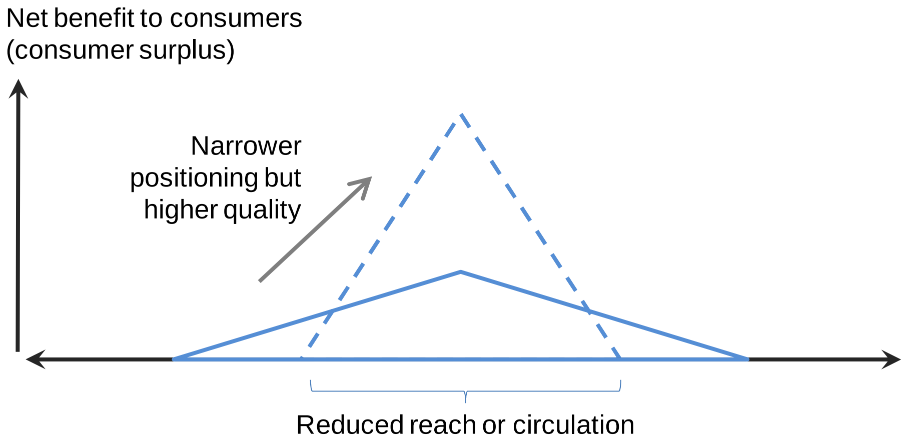
37. Local media, however, are usually provided free or at a subsidised price to consumers, and financed from other sources. Terrestrial radio is necessarily free-to-air[7] and around half of local newspapers are distributed free of charge. Even where price data exist, there may be little historic variation, and the effects of price changes must be separated from background trends in consumption, which in local media are significant. Often, therefore, there will simply be no good evidence about notional 'willingness to pay' for local media, and no data that would allow one to estimate a relationship between willingness to pay and certain underlying characteristics.

38. While changes in the volume of demand are often related to changes in consumer surplus, this is not necessarily the case. For example, it may be the case that a change in the characteristics of a product will increase its value to some customers who already consumed the product, while narrowing its

[7] Satellite radio on an advertising-free subscription model, requiring special receiver equipment, is available in the US.

appeal more widely. In this case, reduced demand – in the sense of a smaller reach or circulation – can be accompanied by an increase in aggregate consumer surplus, as shown in Figure 2.3.

Figure 2.3: Reduced volume of demand may mask an increase in consumer surplus



39. This observation may be especially pertinent to newspapers, which – unlike linear media such as radio – offer an array of varied content, not all of which interests a given consumer.[8] Thus, a newspaper that sacrifices some of the breadth its content in exchange for greater depth may reduce its circulation while generating a greater consumer surplus than before.

40. While willingness to *pay* cannot be observed, willingness to expend time and attention sometimes can, and may provide additional insight into the changes in consumer surplus that might be associated with a merger. Since time is costly to consumers, merger-induced changes in total hours of viewing, listening or reading are likely to be correlated with impacts on consumer surplus. Looking at time expenditure in conjunction with other measures of demand such as audience reach or circulation numbers can provide additional insights into potential consumer benefits that might be associated with a merger, because it additionally reflects the *intensity* of consumer use and presumably enjoyment.

41. Where feasible, Ofcom may therefore wish to consider consumers' time expenditure on media consumption as a proxy for the value they derive from it, at least within one and the same medium and content type. As a practical matter, the history of consumers' pre-merger time expenditures for TV and radio is straightforward to obtain in the form of viewing or listening hours but it is also available to some extent for press and online, thanks to measurement systems and surveys designed to provide this information to advertisers wishing to understand the quality of attention that their ads are likely to receive. Although the difficulty in understanding how time expenditure is

[8] Newspaper readers are reported to read only a quarter of the content of each issue on average.

related to product attributes and projecting how it could be affected by a merger remains, time expenditure nevertheless provides a practical lens for examining the parties' plans and considering possible merger effects, as explained in the next two chapters.

3 Theory and evidence

42. Merger analysis is forward-looking and therefore an inherently predictive exercise. Hence, merger assessments to which LMAs will contribute inevitably involve projections of the effects that might be expected to flow from a proposed concentration, including an assessment of the credibility of the plans presented by the merging parties.

43. In order to assess the credibility of particular developments predicted by the merging parties and to motivate the use of the metrics presented in Chapter 4, it is therefore helpful to consider the mechanisms through which mergers between competing media outlets might affect consumers.

44. Although any such assessment will need to be based on the specifics of the case at hand, prior economic arguments can be helpful in looking at the incentives facing the merging firms and their competitors, and the effects that could result – not least in order to help in identifying areas where detailed information will be needed.

45. This chapter considers, in a relatively informal way, what economic theory suggests about the potential effects of local media mergers on consumers. It looks at the impact that a proposed concentration can be expected to have on the choice of the strategic variables available to media platforms – price, quality and positioning – and thus on consumer benefits. The discussion of these effects is intended to support Ofcom in considering the most relevant source of potential consumer benefits in particular cases, and focus on the most appropriate metrics.

46. Where available, we include empirical evidence concerning the effects of local media mergers (in newspapers and radio) on consumers. Unfortunately, no UK-specific studies of this issue exist to the best of our knowledge, and the evidence is therefore international, drawn mainly from the US. Although the findings cannot be translated to the UK generally (still less to a presumption about the outcome of a particular local media merger in the UK), these studies are useful in suggesting sources of consumer benefit that may be worth exploring in a particular case.

47. We start by setting out a brief description of how one of the key characteristics of media, namely their two-sided role in bringing together the demands of two groups of customers (advertisers and consumers), affects the potential source of consumer benefits. We then explore a number of mechanisms through which a lessening of competition in the provision of advertising impacts might conceivably be accompanied by benefits to consumers.

3.1 Local media as two-sided businesses, and the implications for merger benefits

48. Commercial media, including local media, are examples of two-sided markets[9], in which a single firm or 'platform' serves two sets of demands, and where the demand of the users on one or both sides is affected by the number and characteristics of those served on the other. In the case of local media, the interdependent demands are:

- consumers' demand for content and advertising (or potentially for a lack of advertising, as discussed in more detail in the next chapter); and
- advertisers' demand for consumers' attention.

49. Media users are of course attracted by the content provided in newspapers or radio broadcasts. They may also be interested in informative advertising – which in the context of local newspapers means mainly classifieds. On the other side, advertisers value consumers' attention rather than content per se, although there may be halo effects from placing advertising in proximity to certain types of content (as with spot advertising or sponsorship and promotion). Thus, their primary concern is to reach target numbers of relevant consumers. Explicitly in radio and TV, but implicitly also in press, advertisers pay for a volume of exposure to their target consumers. They may also be concerned with reach (i.e. reaching a wide number of consumers rather than duplicating exposures to one and the same consumers) and immediacy (i.e. achieving their targets within a short timeframe).

50. It is this interdependence of demand that distinguishes multi-sided businesses from other multi-product firms, and requires the firm to reconcile the interests that its two sets of customers have in each other in pursuing its commercial objectives, which are assumed to be long-term profit maximisation. The terms offered to each side are influenced by their effect on the value of demand from the other side, and the challenge facing two-sided businesses is to set terms to both of their customer groups that recognise these feedback effects as well as the competitive constraints imposed by rivals.

51. This interdependence helps explain why prices to consumers of local media may be below cost, or even zero. Most local media (all commercial radio for technological reasons, and many newspapers by choice) are distributed free, and even paid titles generate only 20-25 per cent of their revenues from copy sales. If advertisers place a large value on being able to reach consumers, and consumers would respond very strongly to higher prices for media products, it

[9] Other examples of two-sided markets often quoted in the literature include payment systems (acquiring and issuing banks), estate agents, brokers, or dating and matching services (including nightclubs). The theory of two-sided markets has given rise to an active literature in the last decade. This research has yielded some important insights, but it is still incomplete. A recent synthesis by Weyl (forthcoming), while extending the work of Rochet and Tirole (2003, 2006) and Armstrong (2006), concludes that the literature is at an "early stage". The models throw up some surprising results, which can vary sensitively according to the details of the assumptions made.

is commercially attractive for media outlets to fund the cost of content creation, production and distribution to a substantial extent, or exclusively, by charging advertisers – particularly when consumers are averse to advertising. Being able to rely exclusively on advertising revenues makes possible the commercial provision of services over platforms such as terrestrial broadcast transmission that, for technological reasons, historically did not even allow broadcasters to charge listeners or viewers.

52. The two-sidedness of (local) media markets has important implications for the analysis of potential consumer benefits.[10]

- In 'normal', one-sided markets, the direct impact of a change in competitive conditions falls on only one group of customers. In order to establish whether consumers are better or worse off as a result of a merger, it is sufficient to establish the impact that an increase in concentration will have on prices and product characteristics, and weigh the detrimental effects of any increase in prices against potential benefits from improved quality, if they arise. Often, the direction of the effect of a significant lessening of competition will be similar for prices and quality: a merger that reduces competition can often be expected to result in higher prices and/or lower quality – unless the merger will create efficiencies for the merging parties that will be passed on to consumers to a substantial extent.

- The two-sided nature of the (local) media business opens up the possibility that, in response to a change in competitive conditions, the balance of costs and benefits for the two groups of customers might change. For example, a lessening of competition in relation to advertisers that leads to an increase in advertising prices and advertising revenues might lead to increased investment in content and might thus benefit consumers.

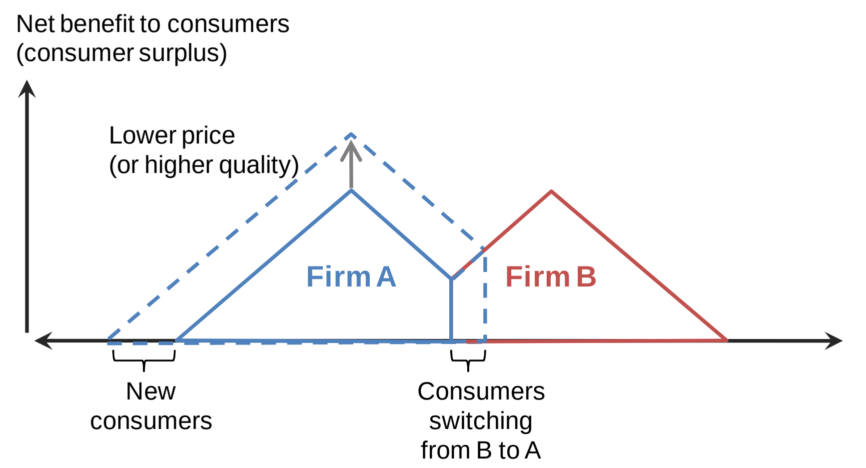
53. Of course, it is not necessarily the case that an increase in prices to advertisers will benefit media customers making up the advertisers' audience (other than in the sense that a reduction in advertising as a result of increased prices might reduce the nuisance costs faced by media users). In general, consumers may be vulnerable to a similar lessening of competition as advertisers when media outlets in the same geographical market merge. While the effect may not always manifest itself in a price increase (since many local media are provided for free), it could do so in the other vertical dimensions, leading to higher profits through cost savings by 'skimping' on quality of content or convenience of distribution to a now more captive audience or readership. It could even lead to the closure of titles or stations, thus reducing choice and variety.

54. A simple illustration of the fact that a merger might cause competitive harm not only on the advertiser side, but also for consumers, is provided in Box 3.1.

[10] More generally, several papers have emphasised the need for a distinctive approach to merger analysis in two- or multi-sided markets (see, for example, e.g. Evans (2003), Evans and Noel (2008)).

Box 3.1: Competitive harm to media consumers

By reducing its price, or increasing the quality of its offerings to consumers, a media outlet can increase its audience size. In the diagram below, an increase in the quality of Firm A's offer (or a reduction in the price charged to readers) will result in an increase in its audience consisting of both of consumers who currently were not served at all plus consumers who previously chose Firm B's offering because it provided them with a greater surplus. The first group of consumers represents new additions, the second group represents consumers won from rival firm B.



If A and B were to merge, they would have a clear incentive to mitigate pre-merger competition, which would amount to cannibalisation of the merged firm's own business post-merger. The incentives to invest in quality in order to win a larger audience will be reduced. As a result, the quality set by the merged firm will tend to be lower, resulting in reduced consumer surplus. Media users may suffer competitive harm from a merger, not necessarily in the form of higher prices, but through lower quality.

It is worth noting, however, that this logic may be reversed if advertisers are polarised in terms of their target demographic.[11] A recent model of the newspaper market allows advertisers' valuations to vary not only with the number but also the characteristics of readers and finds circumstances in which a merger to monopoly can theoretically lead to lower prices to consumers as a result. While the empirical relevance of this model is uncertain, it does at least suggest that attention should be paid to differences in the relative value of different consumers to advertisers. The gist of their model is that, unlike the standard case presented above, the 'switchers'

[11] To facilitate the analysis of an extremely complicated subject, economic models of media markets tend to assume that advertisers value consumers indiscriminately, but this is a simplification. In reality, advertisers target particular audience niches, and contracts for advertising on broadcast media, where audience composition can be monitored (via RAJAR and BARB), are usually struck explicitly in terms of a volume of impacts 'against' required demographic groups. Thus, in radio for example, "the selection of individual stations within a radio schedule is determined principally by calculations of cost-efficiency against the advertisers' targeted demographics" (see Change Agency (2009), 'Future of UK Commercial Radio – Advertiser and Agency Research' (Ofcom, 'Radio: the implications of Digital Britain for localness regulation', July 2009, Annex 7).

between the titles are on average *lossmaking*, and this sends the above logic into reverse.[12]

The reason is that advertisers target groups who are more 'concentrated' towards the poles of the spectrum. For concreteness, suppose that advertisements target either women or men (but not both simultaneously) and that the tastes of each gender are correlated with the horizontal distribution of consumers so that women are concentrated towards one end and men towards the other. Then the average reader in the middle of the axis is less valuable to any given advertiser than the average reader towards the poles, who is more likely to be of a specific type, and their marginal contributions to advertising revenues also differ.[13]

Pre-merger, each newspaper sets its price (and/or quality) such that marginal revenue equals marginal cost. The impact on cost and on copy sale revenue is the same for all marginal consumers, but their contributions to advertising revenue differ. Thus, when the marginal profit from a price cut is zero (as it must be if profits are at a maximum), then this must be an average across profitable additional readers located towards the extremes of the axis lossmaking additional readers located in the centre. Yet the latter are precisely those who are attracted from the rival title, which would therefore benefit from offloading some of its lossmaking consumers if the first title were to cut its price. Post-merger, this benefit is internalised by the merged entity and the price cut (or quality increase) is profitable overall.[14]

55. The overall balance between reductions in the incentives to compete for customers and potential benefits from an increased incentive to invest in quality or change positioning depends on the specifics of the case, but it is important to recognise that, unlike in the case of one-sided markets, media outlets perform a balancing exercise when choosing their strategic variables. More generally, the incentives on merging parties to alter provision to consumers must be viewed at least partly (and in radio wholly) in terms of the effect on advertising revenue, while taking account of the feedback of more or less advertising on consumers.

[12] See Chandra and Collard-Wexler (2009). In the empirical part of their paper, they look at prices both to readers and to advertisers in Canadian newspapers between 1995 and 2002, during which three major acquisitions in the industry were approved by the Canadian Competition Authority. They find no evidence of an impact on prices to either group. Merging and non-merging titles followed similar trends, and if anything the titles that changed ownership actually saw smaller price increases or greater price declines than those that did not.

[13] To make this clear, imagine that one type of advertiser is willing to pay £100 to reach 1000 female readers and another type is willing to pay £100 to reach 1000 male readers. Then adding 1000 readers who are split 50/50 between women and men adds only £50 in advertising revenue (per ad) whereas adding 100 readers who are split 80/20 towards either women or men adds £80.

[14] A feature of this and many of the models surveyed is that they abstract from the details of the advertising market by assuming that advertisers have a constant willingness to pay per consumer, which in this case is the same for all advertisers. If this were so, then platforms would always charge this value, and extract the entire surplus from advertisers. ('Surplus' here means the total benefit that advertisers derive from advertising on the merging platforms less their total advertising expenditure.) It would thus be impossible to motivate a theory of harm as no more 'harm' could be inflicted on the advertisers. This model also assumes readers are indifferent to advertising, and is therefore not truly two-sided. However, this type of simplification is necessary in order to illuminate the main issue under study.

56. OFT practice in local media merger situations is to consider whether there is a potential significant lessening of competition (SLC) from the point of view of advertisers and, if so, to take account of other factors including possible benefits to consumers that may offset its adverse effects.[15] In line with this 'advertisers-first' approach to merger assessments in local media, the question that we need to consider now is for what reasons competitive harm to advertisers (in the form of higher charges) might be offset by potential benefits to consumers, which – owing to the fact that media users generally pay relatively little, and often nothing – are most likely to result from changes in quality and positioning.

3.2 Higher advertising margins may improve the incentives to attract consumers through lower prices or higher quality

57. As noted above, free titles account for roughly half of all local and regional newspapers by circulation, and even among paid titles, copy sales account for only 20 to 25 per cent of revenue.[16] Commercial radio is entirely free-to-air as it would not be feasible or cost-effective to monitor and bill listening. A distinguishing characteristic of commercial, advertising-funded local media enterprises is that their 'treatment' of consumers is heavily influenced by their value as sources of advertising revenue.

58. What matters for merger assessment is how changes in the competitive conditions following a merger affect both sets of customers. An explicit general model of competition and mergers in two-sided markets, even under price-only competition, has not yet been proposed. However, in a monopoly model Rochet and Tirole (2006) derive a result they refer to as the 'see-saw' principle, whereby "a factor that is conducive to a high price on one side, to the extent that it raises the platform's margins on that side, tends also to call for a low price on the other side as attracting members on that other side becomes more profitable". 'Price' here refers to a price per interaction (i.e. a charge to each side for every encounter with the other side), which is not how consumers pay for media. Weyl (forthcoming) reformulates this principle as

[15] In its review of the local media merger regime the OFT states that: "In practice [...] media mergers are more usually found to raise concerns on the advertiser side (that is, if concerns arise at all) […] Advertising is a key input to the competitive process in other markets, and so if advertising rates increase, then the increase in costs will tend to be passed on by the advertisers to their customers. As such, harm to advertisers will typically also generate harm to end-consumers in those other markets" (OFT1091, June 2009, para. 4.14. The decision in the 2008 Global/GCap radio merger also notes that a focus on harm to advertisers, with possible benefits to consumers being treated as efficiencies requiring stringent demonstration, is consistent with previous merger enforcement cases in the UK and other jurisdictions. The analytical framework for the assessment of consumer benefits that may outweigh the effects of a SLC in a merger situation, as well as efficiency benefits to consumers that may prevent a SLC from arising, is set out in the draft OFT/CC merger assessment guidelines (OFT/CC, April 2009, "Merger assessment guidelines: consultation document").

[16] OFT1091 (2009), p. 32.

meaning that factors that cause a platform to choose a lower number of participants on one side cause it to choose a higher number on the other.[17]

59. The general insight is that profit-maximising platforms in choosing their strategic variables take account of the effects that increasing the number of customers on one side will have on their attractiveness to customers on the other side. This, together with the relative price elasticity of the two customer groups, affects the balance of prices (and, one would expect, the choice of other strategic variables such as product quality that affect demand).

60. This suggests that a merger between local media outlets that results in competitive harm to advertisers may result in benefits to consumers if the relative price elasticities of these two groups change, e.g. because the merging parties were closer competitors from the perspective of advertisers than from the perspective of media users.[18] In this case, the merger will tend to reduce the price elasticity of advertising demand facing the firm by more than it will reduce the elasticity on the consumer side. This might lead advertising charges to increase by more than would be expected purely as a result of the increase in market power, and to a consequent reduction in the charges to media users – or a corresponding increase in quality. Thus, the applicability of the 'see-saw' argument is perhaps strongest in cases where the merging entities compete more strongly with each other on the advertising side than on the consumer side. Admittedly, it is not easy to imagine circumstances in which this might hold, although ultimately this will depend on the facts of the case.

61. Another mechanism by which competitive harm to advertisers might be combined with benefits to consumers is linked to the difference between marginal and average benefits enjoyed by advertisers, and the possibility that a merger may give the combined entity greater leeway to price discriminate among its advertising customers. This is because in setting their terms and conditions to the two sides of the market, profit-maximising media outlets will only take account of the extent to which their profits depend on becoming

[17] However, Weyl (forthcoming) also shows that the see-saw principle is not entirely general to all model specifications.

[18] We should note that this question is distinct from whether the boundaries of the relevant market are different when assessed in relation to advertisers and to consumers respectively. There are good arguments to suggest that in two-sided markets, as a matter of principle, the boundaries of the relevant market must be the same for both groups of customers. Even though customers on one side may appear not to switch readily between different providers, whereas those on the other side transact with all, these decisions are endogenous (see Gabszewicz and Wauthy, 2004) and do not imply that different platforms are not a substitute for one group of customers, but for the other. Because advertisers are concerned with reaching consumers and are largely indifferent to content per se, it may however well be the case that two different media outlets are close substitutes for advertisers, though not necessarily for consumers. Also local businesses focused on a target audience in a narrow catchment area may be more restricted in terms of substitution possibilities as advertising over a wider area involves paying to reach irrelevant consumers and is therefore unlikely to be cost-effective. To the extent that media firms with market power can discriminate and charge higher prices for such captive advertisers, this too would raise the value of local audiences and might provide an increased incentive to invest in quality where the growth in audience comes largely at the expense of regional or national media.

more attractive to customers on both sides. For example, a media outlet setting a uniform price for its advertising impacts, in choosing its price to media consumers (or setting its quality), will take account of the fact that increasing its audience will allow it to increase advertising rates, but the extent to which this is possible will depend on the increase in the willingness to pay of the marginal advertiser. This may mean that too little is spent on increasing audience size if the benefit of doing so is greater on average across all advertisers than for the marginal advertiser.[19] Since advertisers do not derive any independent value from advertising in the absence of an audience it must be the case that those who are only just willing to pay the price charged have a lower valuation for each consumer's attention than those who would be willing to pay more. Therefore, if the merged firm were in a position to discriminate better amongst advertisers and thus extract a greater proportion of their surplus, it would invest more in attracting audiences by either lowering price or increasing quality.[20]

62. Whether any of these effects dominates the potential harm to consumers as a result of a reduced incentive to compete in practice is clearly an empirical matter. However, it is quite possible that the increased value of audiences to the media firm as a result of higher advertising prices, and perhaps greater scope for price discrimination, could provide incentives to increase quality in order to grow the audience. Thus, a merger of already free newspapers or of free-to-air radio stations (even absent efficiencies, considered later) that enables greater surplus to be extracted from advertisers could benefit consumers by providing incentives to increase the attractiveness of content,

[19] Similar considerations are relevant on the consumer side. To the extent that the loss of readership of local newspapers is partly associated with the move of classified advertising from the printed medium to online – arguably the major source of current structural change in the local press industry – this suggests that those readers who are leaving are those who are most interested in informative and classified advertising content, i.e. those who are relatively more 'ad-loving' (and less content-oriented) compared with the readership as a whole. If so, local newspapers have an offsetting and growing incentive to keep advertising prices low to retain advertisers and hence maintain their readership, which could be weighed against any increase in market power over advertisers arising from a merger. Put intuitively, increased competition for ad-loving readers gives platforms an incentive to ensure the supply of the local advertising content they value, even if they have market power over advertisers. In free-to-air broadcast media such as local radio the situation may be the other way round. Here it is more plausible to assume that listeners are ad-averse, as discussed in the previous chapter, and it is possible that the marginal consumers at any given level of advertising airtime will be more ad-averse than the average. Intuitively, radio stations may worry 'too much' about exposing marginal listeners to advertising, and provide too little advertising airtime (at too high prices) as a result.

[20] Roson (2008) takes into account that the advertising price depends on a number of factors that had been neglected in previous work, including expected audience composition (noting that advertisers and viewers are not homogeneous, as in Chandra and Collard-Wexler (2009)), and that there is a correlation between program type and audience composition) and the amount of price discrimination feasible across different advertisers. Roson then looks at different market structures (i.e. monopoly, and oligopoly under various sequential structures as well as with different numbers of channels) and finds that for several of these structures, the ability to price discriminate amongst advertisers raises the level of quality to consumers. This is because price discrimination allows the operator to scale advertising prices in response to changes in quality.

the effectiveness and convenience of distribution, or other vertical characteristics such as those set out in the next chapter.

63. Understanding the mechanism through which consumer benefits arise will allow one, however, to identify what factual information should be sought from the merging parties. The incentive to reduce investment in attracting audiences is stronger the larger the overlap between the two titles in terms of their audience. Equally, the impact on the price elasticity (or the 'quality elasticity') on the consumer side is likely to be smaller in cases where there has been less overlap prior to the merger. Where there is historic evidence that one paper has been able to grow its circulation without taking away too many readers from the other paper, one might expect the increased incentive to invest in further audience growth as a result of the improved ability to turn audience size into advertising revenue to dominate. By contrast, evidence that the products were substitutes in consumers' eyes (e.g. that any gain in readership of one paper came largely at the expense of the other) would suggest that such an effect might be negated by a temptation for the merged firm to 'skimp' on quality once competition is removed. (Alternatively, however, the merged firm may reposition the products so that they no longer compete so strongly for the same consumers, actually benefiting consumers by providing greater choice and variety. This possibility is discussed in the next section.)

64. Similarly, where a merger is likely to increase the ability of the merged entity to discriminate between different types of advertiser, and thus extract a greater proportion of any surplus that advertisers might enjoy, an increase in quality and thus consumer benefits are more likely. One way in which this price discrimination could come about is through an extension of a local newspaper's online presence. Offering two versions of the product, offline and online, could separate the 'readership' into those with a greater propensity to use online services (typically younger consumers, as discussed in the next chapter) and those who are more attached to traditional formats (typically older). To the extent that advertisers have different valuations for reaching these two groups of consumers, and can choose to advertise on one or other platform, this separation increases a media owner's ability to extract their willingness to pay, relative to a counterfactual in which it has a weaker online presence.[21]

65. Finally, consumers are directly affected by the quantity of advertising carried – on the whole positively in the case of local newspapers (holding fixed the volume of non-advertising content) and negatively in the case of radio (see the next chapter for a discussion of consumer attitudes towards advertising in local media). In past radio merger cases the competition authorities have noted that a reduction in advertising (due to higher prices being charged to advertisers post-merger) will have an offsetting benefit to consumers by

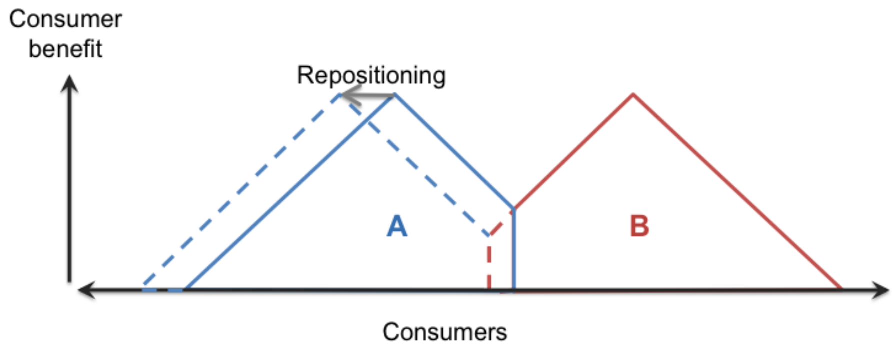
[21] This is along the lines of the discussion in footnote 20 above, as Roson (2008) concludes that "[b]ecause new technology for delivering advertising will arguably increase the ability of broadcasters to discriminate on advertising prices, [… the fact that this may lead to an increase in quality] is an important result."

exposing them to fewer commercials. However, this is only a first-order effect, and raises the question why the merged stations might not then find it optimal to reduce expenditure on the quality of content, while maintaining their audience. The above arguments suggest that, in certain circumstances, they may not wish to do so.

3.3 Post-merger product repositioning can increase variety and create a better match of products to consumers' differing tastes

66. A further source of potential offsetting benefits to consumers following a media merger concerns the scope and incentive for horizontal repositioning. Positioning is particularly relevant to radio, where stations tend to have a relatively clear-cut programming niche and identity. By contrast, because newspapers can offer a 'broad front' of content, and because local newspapers in particular are differentiated by geography rather than political viewpoint, they are less constrained to adopt a narrow positioning. Nevertheless, positioning decisions such as the content mix (as well as look, style and tone) can be important in newspapers also.

Figure 3.1: Post-merger repositioning



67. The intuition behind post-merger repositioning is that the merged entity can resolve the pre-merger competitive overlap between the two products by separating them in product (or indeed geographical) space. In Figure 3.1 we can think of firms A and B as radio stations, each seeking to maximise total listening hours, which we equate with the areas of the triangles on the assumption that consumers' time expenditure and benefit are closely correlated (see previous chapter). Before the merger, their equilibrium positions are such that neither has an incentive to move closer to or further away from the other. If station A repositions away from the centre, it gains listening hours on the 'outside' but loses the same volume of listening on the 'inside', including a portion of listening that switches to station B. Post-merger, that portion is recaptured by the merged entity and the repositioning is worthwhile. Therefore the common owner has an incentive to reposition the two stations further away from each other and total hours (and hence consumer benefit) are increased.

68. Again, however, this is only a first-order effect and it must be checked whether this benefit would not be offset by an incentive to reduce quality (or perhaps, in the case of paid newspapers, to increase price). Gandhi et al. (2005) use

simulations of competition on both price and product positioning, on the one hand, compared with price-only competition on the other, to investigate the overall impact on consumers of the (beneficial) increase in product variety and the (adverse) potential for higher prices. They find that "[i]f the merging products initially are close to each other, the merger is less anticompetitive in the price-location model than in the price-only model, because the merger causes the merging products to separate, thereby reducing the incentives to raise prices. Conversely, if the merging products initially are far apart, the merger is more anticompetitive in the price-location model than in a price-only model, because there is a general softening of price competition as products spread out post merger."

69. This paper was cited in the OFT's investigation of the Global/GCap merger, albeit with respect to advertisers, although substantially the same point holds for listeners. Although the model is illustrative and cannot be calibrated to real-world situations, it implies that competitive harm is less likely in situations in which, pre-merger, the merging products are relatively close in positioning. In the Global/GCap case, the OFT lent greater weight to repositioning benefits in the case of the Midlands, where the merging parties' stations were relatively close in their demographic profile, than in London, where they were already relatively differentiated.

70. There have been several studies of radio station repositioning, specifically format switching, following a wave of consolidation in the US radio industry that followed the relaxation of ownership rules in the 1996 Telecommunications Act (see Box 3.2). The empirical literature therefore focuses on variety (horizontal differentiation), but does not address quality (vertical differentiation). We are not aware of studies specifically examining the impact of UK radio mergers.

Box 3.2: Effects of ownership concentration on variety in local radio markets

Berry and Waldfogel (2001) find that concentration reduced entry while maintaining or perhaps even increasing variety, measured by the number of formats represented. Stations presumably have production cost economies of broadcasting in one and the same format, and indeed, stations in different areas that are jointly owned are less diverse than those that have different owners. But stations that are jointly owned within *one and the same* area show more diversity than those that are jointly owned but in different areas. The authors speculate that these results may be due to consolidated radio station owners pre-empting entry (at least in effect, if not necessarily in intent) by 'fanning out' the positioning of their stations in a local market. They also find that the 'spacing' of jointly owned stations is narrower in large markets, and attribute this to the greater ease of entry in such markets. These findings would appear to be equally consistent with joint owners avoiding competition amongst their radio stations, as per our discussion in the last chapter. The authors note that variety increases consumer welfare but unfortunately do not analyse the causal impact of consolidation on total listening within each market, which could be taken as an indication of total consumer enjoyment.

Romeo and Dick (2005) find that format changes frequently enable stations to improve their performance, and their analysis supports the notion that this is more difficult if the format space is already ‘crowded’. They also find that format changes by smaller station groups may counter the potential exercise of market power by larger groups that acquire a larger audience demographic through a merger.

Jeziorskiy (2009) estimates that total advertising was higher (by around one per cent) as a result of industry consolidation due to post-merger repositioning, even though advertising rates were 10 per cent higher than they would otherwise have been. But he finds listeners to be highly ad-averse, so that the increase in advertising negated the benefit of increased diversity of formats.

Sweeting (2010) goes a step further than Berry and Waldfogel (2001) by examining US radio mergers between close competitors within one and the same format (and in the same local market) by examining playlist overlaps. He contests the finding that post-merger repositioning necessarily leads to increased variety as the merged stations seek to reduce cannibalisation. He finds, empirically, that merging stations do indeed differentiate themselves in this way, but that they also position themselves closer to competitors rather than occupying less crowded parts of the playlist spectrum. The net result is that mergers increase the share of the merging entities but the total format audience, and variety within the format, is unchanged. He also finds that there is no significant change, and specifically no reduction, in advertising airtime ('commercial loads'), and argues that this is consistent with Department of Justice practice in blocking local radio mergers where it believes there may be an increase in market power over advertisers.

Several other studies of the US radio merger wave are not directly relevant to consumer impacts but may be of wider interest as background to LMAs. Brown and Williams (2002) found that local concentration caused advertising rates to national and local advertising agencies (their data did not include direct advertisers) to be 3-4 per cent higher in 2001 than they would have been otherwise. Sweeting (2007) infers repositioning costs while Smith and O'Gorman (2008) do so for cost efficiencies of consolidation, which they find to be substantial.

71. Although not strictly in relation to mergers, there is also empirical evidence of repositioning in response to substitution towards online media. An implication of this evidence for our purposes is that repositioning may be an important secondary effect in assessing local newspaper mergers that are likely to result in a greater separation of the online and offline readership for the purpose of enabling the merged firm to price-discriminate more effectively.

Box 3.3: Content repositioning in response to online substitution

George's (2008) study of the impact of the internet on the US newspaper market contains interesting evidence about repositioning in the newspaper industry in response to the changing composition of the residual offline readership: in areas where internet penetration is strongest (and desertion by younger and more educated readers most intense) a greater fraction of reporting resources is being devoted to local topics such as education and crime, and topics of particular interest to Hispanics and blacks, such as immigration and diversity. She also finds a greater emphasis on investigative reporting.

Similar evidence, this time from the impact of the aggressive expansion of the New York Times after 1996 (rather than mergers), is provided by George and Waldfogel (2006). They find that local penetration of the New York Times reduces interest in local papers among more educated consumers and increases it among less educated groups. They trace the latter effect to the fact that local newspapers have changed their targeting as a result of the Times' expansion, reducing national and international coverage and increasing local content.

72. As discussed above, merging firms have an incentive to mitigate pre-merger competition (post-merger cannibalisation) not necessarily by raising prices or lowering quality, but by separating their products in terms of quality or positioning.

73. Alternatively, however, in pursuing this strategy merging firms may actually find it optimal to close down one or more of the products altogether (see e.g. Norman et al., 2005; Berry & Waldfogel, 2001), and this possibility should be examined in the context of an LMA. Particularly in newspapers, 'closure' can take various shades, such as ceasing distribution of one the titles in areas where it competes most fiercely with another title involved in the merger. A joint owner may also wish to integrate the titles in to a single vehicle.

74. Again, however, economic theory does not offer a firm prediction about the direction of the overall welfare effects on consumers. For example, Zacharias (2009) shows that it is theoretically possible (but by no means necessarily the case) that consumer welfare is actually higher under a monopoly than under a horizontally differentiated duopoly, since the benefit of greater variety can be more than offset by an incentive to raise prices above the monopoly level.[22]

3.4 Cost efficiencies and synergies in content generation can lead to a higher quality of product

75. A merger or acquisition, besides reducing the overall elasticity of demand facing the merging entities and hence increasing their joint market power, may also reduce costs due to efficiencies or synergies. To benefit consumers, and hence to be taken into account in a competition assessment, this reduction must be passed through to them in some way, whether as lower prices or a higher quality of product or service, or in the form of beneficial innovation. All of these effects could potentially arise in the case of local media mergers, although perhaps to different extents.

76. Pass-through is more likely where the cost efficiencies bring down marginal costs, as economic theory suggests these costs affect pricing decisions, while reductions in pure fixed costs may simply be passed on to owners and shareholders.

77. Classic marginal cost efficiencies involve a lower cost of serving additional customers. Such efficiency arguments are inapplicable to radio as the marginal cost to a station of an additional listener tuning in is zero. In newspapers, such efficiencies could result, for example, if the physical

[22] Zacharias (2009) employs a standard Hotelling model to compare consumer surplus under a monopoly (situated in the centre of the product space) and a duopoly in which two firms choose positioning and then price. Under certain conditions the loss of consumers from a rise in price when the firms optimally locate close to the end-point of the interval is relatively small and results in each of the two firms charging a price sufficiently higher than the monopoly price to negate the benefits of increased variety.

production and distribution of a title previously carried out using a relatively inefficient process is folded into the more efficient processes of the merger partner.

78. However, theory suggests that the size of the reduction in marginal costs must be very sizeable in order to offset the consequences of a significant increase in market power and (to our knowledge) supply-side efficiencies have yet to be a decisive factor in the acceptance of a merger without remedies in the UK.

79. On the other hand, a large portion of media business costs is linked to content generation. These costs can be considered fixed from a technological point of view, in the sense that they do not vary with *exogenous* fluctuations in demand at the margin (the number of copies produced and distributed or the number of listeners tuning in). However, in economic terms they are part of the variable costs of attracting consumers to the title or station. Thus mergers that create economies of scope across titles or stations in generating or managing content could justify quality improvements and/or price reductions to consumers that would not be profitable to either party absent the merger.

80. In considering the effects of synergies in content-generation on consumers, however, it may be important to distinguish between operational economies of scope in generating different forms of content (such as the use of content management systems or technology that frees up journalist time) and economies of scale that arise from content-*sharing* across merging titles or stations. If consumers value the volume of content specific to their local area (in a 'vertical' sense), or if consumers in one area served by two titles benefit from the choice of content (in a 'horizontal' sense), a homogenisation of content across two partially overlapping areas could adversely affect the quality and variety available to them.

81. As discussed in Chapter 4, take-up of online services of local media outlets is currently still limited. It may therefore be that immediate merger-specific efficiencies or innovation benefits related to the development of online companion platforms are not yet clearly enough established to play a decisive role in the assessment of a merger of local media in a relevant geographic market.

3.5 Summary

82. In this chapter, we have considered various mechanisms, based on insights from economic theory, through which a merger between two local media outlets may provide benefits to consumers even if, at the same time, it results in a reduction of competition with respect to the firms' advertising customers. The reason for exploring these mechanisms, is that Ofcom, in undertaking an LMA, is likely to have to rely to a substantial degree on information provided by the merging parties or potentially third parties (such as competitors, suppliers or industry bodies) who wish to submit information. Understanding the mechanisms that link changes in competitive conditions to the factors that affect consumer surplus will be helpful in assessing the relative merits of the arguments made by the merging firms based on the evidence available.

83. Our starting point was the fact that (local) media businesses operated in a two-sided manner, bringing together the demand from consumers for media

content, and the demand from advertisers for audiences, and doing so in competition with each other. This immediately raises the question why a reduction of competition between media firms that affects the advertising side would not also result in reduced competition for readers, listeners and viewers, resulting in higher prices or – more likely in the context of local media – lower quality. At the same time, the two-sided nature of local media businesses draws attention to the fact that one needs to consider the full range of terms and conditions to both sets of customers when looking at the impact of reduced competition, and that conceivably, as prices on one side go up, those on the other may go down (or quality may improve).

84. We have identified a number of reasons why reduced competition between local media outlets that unambiguously harms advertisers might nevertheless be accompanied by benefits to consumers. To the extent that it is available, we have also provided evidence from empirical studies in relation to three mechanisms.

85. These mechanisms are:

- a potential change in the relative sensitivity of the two sets of customers to changes in prices or quality following a merger, or the improved ability of the merged entity to discriminate prices among its advertising customers, which would sharpen the incentives for attracting audiences;
- post-merger repositioning decisions that might lead to an increase in consumer surplus as product variety increases; and
- a reduction in the cost of attracting audiences as a result of synergies that can be exploited by the merged firm.

86. While there are no clear-cut and unambiguous results that would allow one to postulate particular effects from a merger, and therefore the assessment of potential consumer benefits needs to be case-specific, an understanding of the basic transmission mechanisms can help Ofcom make more effective use of information gathered in the context of an LMA.

4 Metrics

87. On receiving a request for a local media assessment (LMA) from the OFT, Ofcom will have a very short window in which to gather, synthesise and assess case-specific information. This chapter recommends areas that Ofcom might wish to focus on in assessing potential impacts on consumers, and the types of information it could seek for that purpose. As throughout this report, we are concerned only with the impacts on consumers rather than the full range of issues on which Ofcom may be called on to report.

88. We have been asked by Ofcom to identify metrics for the assessment of consumer impacts that are:

- demonstrably strong indicators of quality;
- applicable to print and broadcast media and to different geographical areas; and
- readily measurable within the timeframes of merger assessment, without requiring lengthy primary research.

89. The task of identifying metrics that will provide a reliable gauge of future consumer impacts needs to be approached realistically. Merger assessments are inherently forward-looking and so rely on qualitative economic reasoning as much as on quantitative data that describe the pre-merger scenario. Retrospective studies can in principle make use of a much wider range of indicators based on actual outcomes. However, even in the case of completed mergers, the post-merger history is typically too short to permit this kind of 'before and after' analysis. Also, the timeframe of two to three weeks within which Ofcom will have to deliver its report will not permit original data-gathering, predictive modelling or simulations.

90. This chapter emphasises a relatively small set of indicators that meet the above criteria, and organises them by economic theme using the framework established at the end of Chapter 2. The intention is that Ofcom will be able to cross-reference potential economic arguments such as those presented in Chapter 3 with the types of indicator that could be sought to assess their relevance in a given case, by looking at the history of the merging parties and their products in the run-up to the merger and critically evaluating their stated merger plans.

4.1 Sources of metrics and information

4.1.1 Indicators of consumer impacts

91. We have drawn on three sources of information on the importance of different attributes of local media provision for consumers:

- empirical studies on media demand, focusing in particular on the variables used in specifications of consumer demand or utility functions;
- the journalism literature relating to issues of media 'quality', and
- industry sources.

92. A literature exists on the identification and measurement of quality in media, with notable contributions being Merrill (1968), Merrill and Lowenstein (1971) and Bogart (1989). Meyer and Kim (2003) provide a useful review and agenda for future research in quantifying the quality of newspapers. In particular, they summarise and propose quantitative metrics for the evaluation of 'quality', down to e.g. Flesch measures of readability (based on word length and sentence length), number of letters to the editor per issue, number of library subscriptions etc.

93. However, the notion of quality that this literature seeks to operationalise is not clearly defined and is of the 'you know it when you see it' type (as in the title of the Meyer and Kim (2003) paper). The measures are canvassed from editors' value judgments, and reduced via statistical factor analysis to five dimensions, namely ease of use, localism, editorial vigour, news quantity and interpretation. The authors conclude that further work is required to examine the link between these attributes and measures of performance. To date only limited work has been done to correlate these measures with outcomes (e.g. circulation numbers)[23], but is not convincing of causality or magnitude. Thus, this literature, while suggestive of possible metrics, is of only limited relevance in justifying which determinants of value to consumers are most important.

94. Another strand of literature discusses more explicitly the nature of value to consumers, but is of limited operational use for our purposes. For example, Gleich (2005) presents a range of studies on quality of media and cites findings that consumers' trust of media outlets is related to the latter's economic success. While trust and accuracy were emphasised by the industry experts we spoke to as important attributes of news coverage to consumers, it is clearly difficult to make these concepts operational in a merger assessment.

4.1.2 Information sources for LMAs

95. Ofcom will be able to draw on two main sources of data in preparing LMAs:

- audience or readership information from industry data sources to which Ofcom has subscription access;
- information supplied by the parties and data made available to Ofcom by the OFT.

Off-the-shelf subscription data

96. Ofcom can routinely draw on audience or readership information from JICREG (for local newspapers), RAJAR (for radio) and BARB (for television) for information such as[24]:

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[23] For example, Lacy and Fico (1990) found that the 25% of the variance in circulation sizes of a sample of newspapers was explained by newspaper quality as defined by the ratio of staff-written to external content.

[24] Worked examples for a metropolitan area were provided to Ofcom separately from this report.

- the range and type of local media outlets in a given area, and their basic product characteristics; in particular, coverage areas and population; programming genre and format (for radio), pagination, advertising and editorial volumes, frequency and whether paid or free (newspapers);
- consumption patterns, i.e. audience reach and listening/viewing hours (for radio or TV), and circulation and (where it has been researched) readers per copy and time spent reading per reader, and hence total reading time (for newspapers); and
- demographic breakdowns of consumption patterns by age, gender and social grade.

97. As well as their relevance to understanding the pre-merger status quo for the purpose of assessing impacts on consumers, these tools have a role to play in the other areas that are likely to figure in an LMA but which are outside the scope of this report, such as:

- determining geographic overlaps among the merging outlets and the potential areas within which competitive effects might arise (which could extend to abutting titles or stations owned by the parties);
- examining the counterfactual for the merger through the analysis of consumption trends; and
- characterising overall local media provision within the affected areas, casting a wide view of potential product substitutability.

Data from parties

98. Given the limitations associated with off-the-shelf data, the merging parties themselves may be in a better position to provide information that would assist Ofcom in establishing the quality impact of a proposed merger. Most of the work in assessing consumer impacts may come down to examining the content of the merger plans, assessing their economic credibility, and identifying the differences in provision with and without the merger that are most likely to affect consumers. Merger plans and the kinds of supporting information that Ofcom and the OFT will find valuable will of course be merger-specific, and the merging parties should be encouraged to provide this information to Ofcom and to the OFT. Ofcom may also wish to consider information provided by parties other than the merging firms.

99. The following discussion is intended to provide some indication as to as to the type of information that could inform Ofcom's analysis and, potentially, substantiate claimed benefits to consumers (as well as other arguments relevant to the scope of an LMA). Of course, in practice only limited data might be available for a number of local media mergers, and some of the information discussed below may not be relevant in the context of a specific merger. Whilst the remainder of this chapter also sets out areas of information that are likely to be capable of informing an analysis of consumer benefits and, where possible, the types of information that might be requested or welcomed that is not available off-the-shelf or from industry sources, but might be provided by the merging parties, it should not create the expectation that all (or even most)

of the data discussed will need to be provided by the merging parties, and assessed by Ofcom, for each local media merger.

100. Also, it is worth stressing that even though the following discussion focuses on the possibility of using quantitative measures (such as, for example, information on content volumes and splits and on journalist numbers and their assignments, for the merging companies and potentially their competitors) both quantitative and qualitative evidence will have to be considered. Ofcom will inevitably have to take a pragmatic approach, and the parties may wish to provide other data or information that might help Ofcom in its task.[25]

4.2 Anticipated impact on time expenditure as an initial indicator of likely consumer benefits

101. As pointed out in Chapter 2, evidence of consumers' willingness to pay for (local) media products and its determinants will generally be lacking, but consumption volumes, particularly if they can be measured in a time expenditure metric, can provide a reasonable proxy for total consumer enjoyment that is at least comparable within one and the same content type and medium, albeit not across different media (such as between press and radio).

102. This suggests that the anticipated impact of an intra-media merger on consumers' total time expenditure could be used as an initial screen: to the extent that merger plans foresee a reduction in consumers' aggregate time expenditure relative to the no-merger scenario, other compelling arguments for benefits to consumers that are not reflected in time spend would seem to be required in order to support a case for offsetting consumer benefits in the face of shrinking volume predictions.

103. Reviewing the parties' projections for total consumption (readership, readers per copy and time spent reading for press, and audience reach and listening hours for radio) and the assumptions used to justify them is therefore a potential starting point for Ofcom's analysis of possible consumer impacts of a local media merger.

104. As a practical matter, obtaining data on the history of consumers' pre-merger time expenditures for radio and TV is straightforward as they are measured by RAJAR and BARB in the form of viewing and listening hours, respectively. Audience reach, i.e. the number of households or individuals who tune into a certain channel or station within a given period, is also available.

105. The usual consumption metric for newspapers, for practical reasons, is observed circulation, i.e. the number of copies sold or distributed free of charge. Circulation reveals the extent or reach of consumption but not its intensity, and changes in circulation may therefore be a misleading indicator of

[25] For instance, prizes and industry awards for content or production have been used in some studies of quality, e.g. Berry and Waldfogel (2004), Logan and Sutter (2004), Taylor (2003), and could be adduced by parties where relevant. We have not attempted to list or assess these here.

effects on total consumer surplus. Reading time, by analogy with listening or viewing hours in broadcast media, is likely to be a better proxy if it is available.

106. Many titles do in fact conduct periodic research into readers per copy (RPC) and time spent reading (TSR) per reader, from which average issue readership (AIR) and the total reading time generated by each circulated copy can be calculated. This research is conducted by third party research agencies to standards set down by JICREG, which publishes the figures. These measurement practices exist in order to provide advertisers with information about the volume of attention that media products attract, which informs their valuation of advertising opportunities.[26]

[26] This might suggest that advertising expenditures themselves could be used as indicators of consumers' total enjoyment of media. However, consumers with the same demand for the media content may have different value to advertisers, and advertising prices and expenditures reflect competitive conditions. Thus, eliding the analysis of impacts on consumer welfare with advertising volumes or expenditures is not appropriate, and also defeats the object of looking at consumer impacts as a distinct and potentially offsetting factor in a merger case.

107. Similarly, tracking of online use increasingly incorporates metrics based on time spent at each website in addition to page views and visits, although no consistent methodology for this has yet emerged, and different web analytics companies adopt different measurement approaches.

Box 4.1: Circulation, readership and time expenditure in local press

Characteristics and consumption metrics for a sample of local and regional newspapers

Means	Free weekly	Paid weekly	Paid daily
Marketing area population (000s)	142.8	267.0	794.2
Editorial pages	15.0	41.1	40.6
Advertising pages	50.9	58.0	22.3
Readers per copy (RPC)	1.6	3.1	2.7
Time spent reading (TSR) (mins)	17.8	30.1	29.6
Reading time per copy (mins)	28.9	90.6	79.1
Circulation (000s)	52.8	17.9	42.2
Average issue readership (AIR) (000s)	83.0	54.7	112.5
Total issue reading time (000s of hours)	25.4	28.8	58.8

Source: JICREG, DotEcon analysis. (Means for 185 free weeklies, 142 paid weeklies and 57 paid dailies in 2008.)

To illustrate, the table above summarises JICREG data for titles in 2008 for which such information is available. Total reading time per copy is over three times higher for paid weeklies than for free weeklies (roughly 1.5 hours as opposed to 0.5), and almost as high for paid dailies, as a function of both a higher number of readers per copy and higher time spent reading by each reader. As a result, total issue reading time is actually higher for paid weeklies than for free weeklies (28,800 hours as against 25,400 hours on average), despite paid weeklies having a much smaller average circulation (17,900 copies as against 52,800).

This is not to say that total issue reading time provides a basis for comparing consumers' utility across titles, because of differences in the user contexts in which, for example, free and paid titles are distributed and consumed. However, changes in time spent reading for one and the same title, especially if they can be related to changes in the volumes of different content or other characteristics, are potentially informative about the determinants of total consumer 'enjoyment' in a particular case and how it might be affected under the plans of the merging parties.[27]

108. Total consumption, preferably in a time metric, would certainly seem to be an obvious outcome variable in ex post studies of the impact of local media mergers on consumers (although in fact the studies of merger episodes in the

[27] An illustrative analysis of this type based on the panel of titles in the JICREG historical reports and their characteristics was presented to Ofcom in the course of this report.

US referenced in the next chapter, with one exception, do not seem to have done this). Operationalising this concept in an ex ante setting without outcome data is of course much harder, and would in theory require predictive structural models of the kind that are far beyond the time and resources available for an LMA.

109. The concept of time expenditure does, however, provide a practical lens through which to examine the parties' plans. As part of their business case for integrating, would-be merger partners may have created projections of expected advertising volumes, driven in turn by expectations of the audience or readership post-merger as compared with a no-merger scenario, and where such projections exist, they could form a useful source of information. In radio, these projections will certainly involve listener hours rather than just audience reach, as advertising revenues are explicitly traded on the basis of volumes of impacts. Although press advertising is sold as space, advertisers likewise implicitly value exposures, which are a function not only of circulation but also of the amount of consumer attention that a given circulation delivers. It is therefore possible that parties to a newspaper merger will have formed some indicative predictions of readers per copy and time spent reading as well as circulations.

4.3 Indicators of quality impacts

110. Assuming that the parties project that total consumption will increase relative to the counterfactual, then the specific plans and business case assumptions need to be critically evaluated. Most of the work in assessing consumer impacts in an LMA will come down to examining the content of the merger plans, assessing their economic credibility, and identifying the differences in provision with and without the merger that are most likely to affect consumers.

111. The discussion that follows is divided into two sections, corresponding to the division between vertical and horizontal (quality and positioning) attributes introduced in previous chapters. The indicators are presented along the lines of the 'characteristics approach' to the economic analysis of differentiated products, which consists of enumerating attributes that, taken individually, are believed to affect the value to consumers positively or negatively (to different extents and, in the case of 'horizontal' attributes, in different directions for different consumers). We suggest that examination of the consumer effects of a particular merger should focus on how provision may change in these respects. However, it is unlikely that Ofcom will find it necessary or feasible to assess all of these indicators in any particular case, and equally it may wish to consider others that are not listed here in response to the specific circumstances of the case.

112. It must be recognised, however, that aggregating the effects of these changes on overall consumer welfare is inescapably problematic. Our conclusion from an extensive review of the economic and media literature and consultation with industry experts is that little or no publicly available research exists concerning the relative contributions of these different aspects of provision to consumers' willingness to pay (or willingness to expend time and attention). This means that they can only indicate the direction of effects on consumers.

Where these directions differ, evaluating the tradeoffs between them appears to be an unavoidable challenge, unless the parties themselves can provide research or evidence to assist.

113. They are presented in a relatively generic way rather than as specific 'evaluation criteria' of the kind that might apply to a regulatory compliance exercise. Information from the merging parties may be useful in demonstrating the relevance (or potentially, the inapplicability) of these factors for consumers. For example, early access to consumer and marketing research that may have been carried out by the parties, could be valuable to Ofcom in producing an LMA, in particular where this covers a period of a few years leading up to the merger,

4.3.1 Vertical quality indicators

114. Table 4.1 summarises the main vertical quality dimensions of provision to consumers that could be affected by a merger. The presented order is not meant as a presumption of their relative importance. These attributes are discussed in turn in the sections that follow.

Table 4.1: Checklist of attributes and potential indicators - 'vertical' product dimensions

Change in attribute (sign of effect)	Possible indicators (and applicability to different media)
Quality of content (+)	• journalist time engaged in original newsgathering and story creation, expressed as a ratio to coverage population (all media) • ratio of originated to syndicated content, for subject-matter of local relevance
Newspaper advertising (+), broadcast advertising (-)	• advertising pagination, column inches or count (newspapers) • advertising minutes (radio)
Price (-)	• cover price (paid newspapers) • online access charges
Size (+)	• pages, column inches (press) • programming hours if not already 24/7 (broadcast)
Frequency (+)	• issue frequency, e.g. daily/weekly (press) • frequency of updates of websites/live news feed (online)
Distribution (+)	• number/ubiquity of retail outlets (paid newspapers)

	• volume/ubiquity of free distribution (free home delivery, drop-distribution, handouts) (free newspapers) • parallel online publication or additional content (e.g. online editions, Internet radio or podcasts, streamed or on-demand TV content)
Physical quality (+)	• colour printing, paper quality (press) • quality of broadcast signal or equivalent (broadcast media) • website quality and functionality

Quality of content

115. Given the fundamental importance of local newspapers to consumers as originators and publishers of local news, discussed in Box 4.2 and unanimously confirmed to us in discussions with stakeholders, the most relevant metrics of content quality concern the capacity to generate original news and reporting.

116. In principle this can be measured in terms of cost inputs (expenditures), physical inputs or outputs. Expenditures are the most problematic of the three as cost allocations may be imperfect and expected cost efficiencies following a merger can obscure the measurement of underlying inputs and outputs.

117. Output measures, if they can be supplied by the parties, such as the volume in column inches of originated as opposed to syndicated news content in the years leading up the merger, are useful in characterising the pre-merger situation and trends and provide a more direct measure of the product that actually reaches consumers, but may be more difficult to project in the post-merger scenario.

118. An alternative measure is the labour input[28] to original newsgathering and story creation. The simplest such measure is the pre- and post-merger (planned) headcount of full-time equivalent reporting staff serving the areas jointly affected by the merger. A more refined measure, however, should take account of the proportion of their time that is or will be spent engaged in actual newsgathering (as opposed to, for example, design and layout) and the extent to which operational efficiencies might lead to a more intensive use of journalists in frontline activity.

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[28] A recent unpublished analysis of UK national newspapers by Jim Chisholm shows that there is no *cross-sectional* correlation between editorial staff numbers (inputs) and editorial pagination (outputs) because of differences in the nature of the output produced by publications as different as, for example, the tabloids and the Financial Times. However, we would still expect an increase in editorial staff input of an *individual title and genre* (here, local news) to increase the volume and/or quality of the output, particularly if the input is measured in terms of journalist time engaged in newsgathering (and assuming that the quality of the journalist staff is the same).

119. Especially where merger plans involve changes in the coverage area of the titles involved, attention should be paid to how the 'density' of local newsgathering effort will be affected, for example by comparing the ratio of newsgathering hours or originated news content with the population addressed by the merging titles.

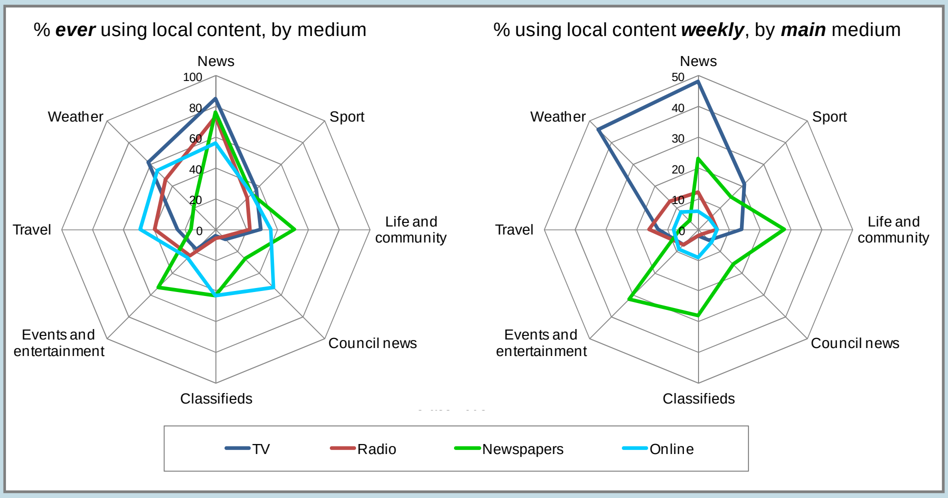
120. Similar metrics to those suggested for newspapers could be applied to radio news content, although given the secondary importance of radio as a medium for local news (many fewer consumers rely on local radio as their main source of news despite it having similar reach to local and regional newspapers; see Box 4.2 below) and the much smaller scale of local radio newsrooms,[29] this issue may not be very influential in an analysis of consumer benefits.

121. 'Quality' as opposed to genre of output is arguably less of an issue in radio as very little of a station's output is originated by the broadcaster itself. Depth of catalogue and breadth of playlists is a possible measure, although analysis at this level of detail hardly seems realistic in the timeframe of an LMA unless evidence is brought forward by the parties. Other factors such as the popularity of presenters or DJs are similarly hard to discuss in general terms but could prove relevant in a particular case.

[29] According to O&O (2009) research for Ofcom, producing local news requires between two and five reporters and presenters while producing national and international news is much cheaper (because they are provided by one of two major UK radio groups like Sky News and IRN). Our understanding is that much of the story material for local radio news is researched from local newspapers, although radio stations will also report live and breaking news before it appears in print.

Box 4.2: Content and medium choice in local media

Consumption of local content by medium



Source: Ofcom Local and Regional Media research (April-May 2009), DotEcon analysis

The charts above, based on Ofcom consumer research, show total and frequent use of local content by medium. The analysis, which was conducted for Ofcom's public research into media localness, does not include non-local content, such as music aired by local or regional commercial radio stations.

Local or regional news is the most heavily consumed content category, accessed on a weekly basis by 89 per cent of adults – with 48 per cent of adults relying mainly on regional BBC and ITV news bulletins and 23 per cent relying on regional or local newspapers.

Use of other content types reflects the characteristics of each medium: broadcast media are used particularly for real-time weather and travel information, while print is used for more extensive and browsable content such as community stories and local government information, listings and classifieds. While the presence or absence of overlaps is not conclusive, the findings suggest there may be relatively limited substitutability between broadcast and print media from consumers' point of view.[30]

Online, which in the Ofcom research refers to companion sites to traditional media outlets, has the most even distribution of use, reflecting its mixed characteristics as a medium, capable of supporting both browsable text content, similar to print, and real-time information and, increasingly, video and audio, similar to broadcast media. Although it is the main source of weekly information for fewer than ten per cent of adults in any one category of local content (right-hand chart), a much higher percentage of adults have used local media sites at some stage (left-hand chart), and presumably many do so regularly as a secondary source. If other kinds of website were included, such as geographically searchable classified and listings services, there may be a much higher degree of overlap with press in those categories.

[30] Where there is overlap, such as in news, sport and local stories, the different characteristics of the media (immediacy for broadcast media, depth and breadth in print) and the different geographic scope of coverage (regional or relatively wide-area for TV and radio, and more local for press) suggest that they may not be effective substitutes for most consumers.

> Newspaper groups cite competitive pressure from such services as a major reason for the current decline in advertising and circulations.
>
> Overall, the Ofcom survey found that 92 per cent of adults consume some form of local or regional media each week, a statistic that is driven by near-universal viewing of regional TV news bulletins. Local or regional radio is listened to weekly by around 55 per cent of adults[31], while weekly reading of local or regional newspapers is 54 per cent for free titles and 41 per cent for paid titles[32]. Companion websites to local and regional commercial media are visited weekly by over 20 per cent of adults. Other local media are used to smaller extents.[33]

Advertising

122. Economic accounts of media markets often assume that viewers, listeners and readers are averse to advertising. This conventional wisdom has strong empirical support from studies of commercial network television, but may not apply to print media, in which advertising content and supplements can be skipped.[34] It is especially questionable in local media, where advertising tends to be informative rather than persuasive.[35]

123. For local newspapers, an assumption that readers are generally averse to advertising is certainly misplaced. As Box 4.2 above shows, almost a quarter of adults in the UK actively turn to the local press as their main source for classified advertising. Industry sources confirmed to us that display advertising

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[31] This figure is broadly in line with RAJAR figures for the weekly reach of BBC and commercial local and regional stations.

[32] Since both types of publication circulate in many areas, especially densely populated ones, the combined reach of local newspapers is likely to be higher than for radio.

[33] Among local or regional magazines, free titles are read at least weekly by 11 per cent of adults, paid-for titles by six per cent and council newspapers or magazines by five per cent.

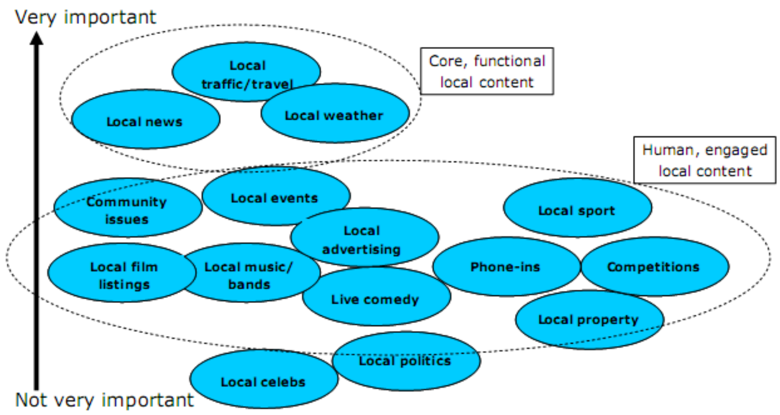
[34] Studies by the GfK Institute in the 1990s, cited in Gabszewicz et al. (2002), found different attitudes towards advertising in different EC countries, with a particularly high rate of ad-skipping by UK newspaper readers despite lower resistance to media advertising among UK consumers overall. However, ad-skipping does not necessarily imply a disutility from the presence of advertising, and the findings may relate to national titles, which contain more brand-building advertising than regional or local titles. Kaiser (2007), using quarterly panel data on 105 magazines in the German market from 1973 to 2004, concludes that readers are ad-loving in more cases than they are ad-averse. He uses an instrumental variables technique due to Hausman (1997) to control for the possibility that the causation runs from circulation to volume of advertising or that the two are affected by omitted variables (and similarly for cover prices and non-advertising content).

[35] Advertising is often characterised as being either persuasive or informative. Persuasive advertising is designed to alter consumers' brand preferences, while informative advertising is designed to alert them to the existence or characteristics of a product or service. Local press advertising, display as well as classified, is essentially informative, and plays an important role in reducing search costs for properties, vehicles, jobs, or other goods and services, and in promoting local businesses. Classified advertising accounts for over two-thirds of local newspapers' advertising revenues (see OFT1091 (2009), p.12). Radio commercials are also largely informative but include some brand advertising. For instance, some national advertisers will use local and regional radio in constructing nationwide campaigns.

in local titles is primarily informative rather than brand-building, alerting readers to local store promotions and discounts, for example.

124. It may be helpful to think of newspaper readers as varying according to whether they are *content-seeking* (and relatively indifferent to advertising) or actively *ad-seeking* (and relatively indifferent to content). The former group may consist of regular consumers of local news and information, while the latter may be those who (perhaps temporarily) are in the market for a job, partner, car, property or service. This distinction is potentially important in thinking through the effects of a local press merger, as the two types of reader could be affected differently by a repositioning of the content mix. For example, a change in the volume or localness of editorial content will affect the first type, while the quantity and type of classified advertising will affect the second.[36]

Figure 4.1: Relative importance of local content types delivered by local radio



Source: Essential Research (2007) for Ofcom[37]

125. Local and regional radio advertising also plays an informative role and evidence from survey work for Ofcom (see Figure 4.1) suggests that listeners treat advertising as similarly important to other forms of local information, while confirming that local news, weather and especially travel information are the most valued forms of (local) content on radio.

126. However, what matters for the welfare analysis of mergers or policy innovations is the effect of *changes* in advertising levels *at the margin*. Because radio is broadcast in a linear stream, one type of content displaces another, and it seems safe to assume that there is a level at which there is too much advertising for most listeners' tastes. It is therefore possible for listeners to value the presence of advertising on the whole while still benefiting from a reduction in advertising airtime at its given level.

[36] Cross-media substitution possibilities are also likely to be different for each type. In particular, it may well be ad-seekers who are disproportionately deserting local newspapers or at least their print versions for the internet.

[37] Ofcom, 'Radio: the implications of Digital Britain for localness regulation', July 2009 (Figure 6).

127. Empirical evidence supports this view. Jeziorskiy (2009), for example, finds a significant negative effect of advertising on choice of station in US local radio at prevailing levels, while Romeo and Dick (2005), also for US stations, find that a one per cent increase in ad time generates a 2.5 per cent decrease in listening share. While we are not aware of published UK-specific research that examines the taste or distaste for advertising on local and regional commercial radio stations, in the OFT's decision on the Global Radio/GCap Media merger in 2008 "the parties submitted that their radio stations broadcast no more than 13 minutes of adverts per hour because this is the tolerance band of listeners – too many listeners switch off if the proportion of adverts increases beyond this to make extra advertising profitable".[38]

128. These indications that local radio audiences are on the whole advertising-averse at the margin are also consistent with broadcasters' commercial incentives – if a station's commercial airtime were at such a low level that listeners wanted more, a radio station would have an incentive to increase it (unless advertisers' demand were already inelastic at that level of airtime and audience, in which case advertising revenues would fall).

129. It therefore seems highly likely that local radio listeners can be considered advertising-averse over the relevant increment of commercial airtime that might be affected by a merger, and thus that less radio advertising would improve listener welfare. Internal research by the merging stations into the relationship of listening hours to advertising airtime would help gauge the likely increase in listening hours of possible reductions in advertising airtime.

130. The fact that some online services offer users advertising-free versions of their content for a price or as a benefit from subscribing to full access is evidence that online advertising is a nuisance to users at least in some contexts.[39] Casual inspection of local and regional newspaper websites suggests, however, that classified and other informative advertising (such as coupons and promotions) are featured alongside news and other editorial material as a form of valuable content to users and that intrusive brand advertising or click-throughs are not prevalent, at least currently, either on these or on radio station companion sites.

Price

131. As discussed in previous chapters, price plays a limited role in local media, being restricted to paid newspapers, although there have been exploratory attempts to charge for online access to local newspaper content, as is currently being planned for national titles. In mergers involving paid titles, price histories could be gathered and attention should be given to plans or possible incentives for the parties to alter pricing strategies post-merger.

132. Any increase in the price of access to local media, or a move from free to paid-for provision, would obviously reduce consumer benefits in the first instance

[38] OFT, 'Completed acquisition by Global Radio UK Limited of GCap Media plc', 27 August 2008

[39] For examples and a theoretical model see Tåg (2007).

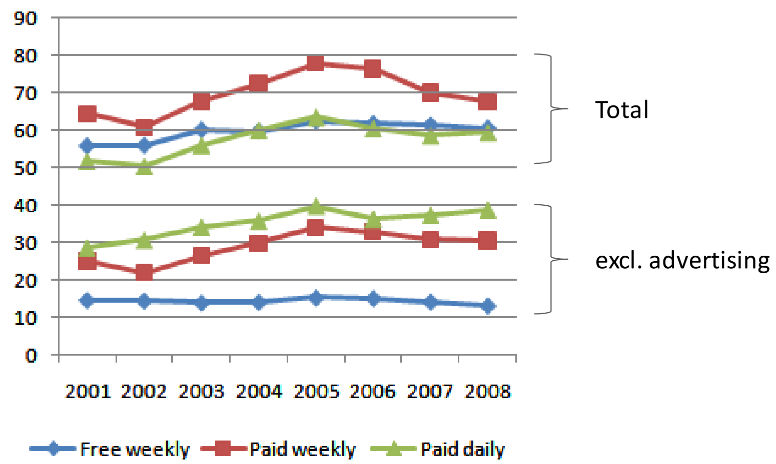
(assuming these developments would not happen anyway). In order to compensate for this, there would have to be substantial improvements in product quality.

133. It is also worth noting that some titles, such as the Manchester Evening News, have adopted hybrid pricing and distribution strategies whereby the same edition has a paid-for circulation and is distributed free of charge in some areas (the city centre) and at certain times.

Size

134. Product dimensions are relevant to press because pagination is extensible. All else being equal (in particular, the content mix), consumers can be expected to prefer a larger product to a smaller one, at least over reasonable ranges. Data on newspaper pagination[40] (adjusted for format, i.e. whether tabloid or broadsheet) are available from JICREG.

Figure 4.2: Trends in average pagination of local newspapers



Source: JICREG, DotEcon analysis (based on constant sample of 192 free weeklies, 200 paid weeklies and 56 paid dailies)

135. Figure 4.2 illustrates the variation in average advertising and editorial pagination among different types of local newspaper over time. Page counts and the inclusion of supplements have generally grown over time due to improvements in production technology. However, this trend appears to have reversed in recent years. This underlines the general importance of assessing merger plans against an appropriate counterfactual that captures background trends.

136. For radio, an extension of broadcast hours, e.g. through the night, can also be considered as a benefit to consumers, although possibly a relatively marginal one. In practice, however, the majority of local radio stations already broadcast round the clock.

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[40] Berry and Waldfogel (2004) use pagination as a metric for newspaper quality in a study of the relationship between quality and market size.

137. As a more general observation, since the 'dimensions' of a print product are extensible in a way that radio broadcast hours are not, content analysis of newspapers should be done in terms of absolute volumes rather than the content mix. This point is illustrated in the later section on content positioning (see Box 4.3).

Frequency

138. Changes in the frequency of issue (typically to less frequent publication) are currently being observed in the local newspaper market and this is one of the variables that could be affected by a merger. All else being equal, consumers might be expected to prefer more frequent publication, although in reality a change in frequency, especially a move from daily to weekly, is likely to be accompanied by other changes such as an adjustment of pagination or a repositioning of the content mix.

139. A merger could potentially lead to a title maintaining a more regular frequency than it otherwise would, or else, perhaps as part of a repositioning among the merging titles, could result in a title being published on a different frequency as part of a product differentiation strategy.

Intensity of distribution

140. The intensity of a title's distribution within its circulation area (as opposed to changes in the distribution area, covered in the next section) can be considered as a quality dimension in the sense that it affects the accessibility of the product to all consumers and will drive overall consumption.

141. Synergies and/or a greater ability to command advertising revenue could result in more effective distribution via retail outlets (for paid titles) or a more aggressive and ubiquitous distribution of free titles whether by home delivery, at drop locations or by handout.

Physical quality

142. Major innovations in production technology beginning in the 1980s included the increasingly widespread use of colour printing and improved systems for design and layout. However, this transition is essentially complete. We have not been able to identify evidence as to the importance of physical production attributes to consumers.

143. In relation to local radio available over DAB, this may create the opportunity for a more efficient use of multiplex capacity and thus an increase in bitrates, potentially leading to improved audio quality. Again, there is no evidence in relation to the impact that such an improvement in quality might have on consumers. Our presumption would be that the change would have to result in a substantial and audible change in the quality of the broadcast in order to affect consumer valuation.

144. Mergers in which such benefits to consumers are claimed would need to be supported not only by evidence for the types of improvement from a technological point of view, but also ideally research substantiating the impact on consumers.

4.3.2 Horizontal attributes

145. 'Horizontal' attributes, as explained in Chapter 2, refer to characteristics of media products that may have positive or negative effects on different consumers, because of differences in taste across the potential consumer base. As Chapter 3 discussed, merging parties may have strong economic incentives to reposition one or both of the merging products that overlap in a geographical market in order to alleviate cannibalisation between them and discriminate more effectively amongst consumers and advertisers. Table 4.2 summarises the main areas in which changes in horizontal attributes should be considered, which concern the geographical distribution areas of the merging titles or stations and potential repositioning of content.

Table 4.2: Checklist of attributes and potential indicators - 'horizontal' product dimensions

Change in attribute	Possible indicators (and applicability to different media)
Extent of distribution	• Potential closures? • Potential consolidations of individual titles? • Wider/smaller/different area of distribution for all or a sub-set of the papers?
Content positioning	• Content positioning in terms of content volumes (for press), mix (for radio) of different genres • Demographic profiles of readers/listeners/viewers

Extent of distribution

146. Changes in coverage areas are a possible consequence of a merger and could take a variety of forms, such as extensions (e.g. filling-in of areas in the case of radio station mergers under the changes in localness regulations recently announced by Ofcom), consolidation of merging newspaper titles into a single title (or localised editions of a single title), separation of coverage areas (e.g. through the curtailment of distribution of one merging title where it overlaps with another), or even, in the extreme, closures.

147. Extensions and contractions of coverage areas could be expected, to a first order, to improve and reduce consumer welfare respectively, but must be considered in tandem with other effects, such as a potential dilution or concentration of reporting resources. These effects and their analysis are likely to be highly merger-specific.

148. Economies of scale and scope in jointly producing two local media vehicles may permit new forms of content, although they may also lead to content-pooling among the merging titles. There is a continuum of possibilities ranging from a degree of shared content to the titles becoming editionalised variations or being merged outright.

149. Whether consumers benefit or suffer from a pooling of content is likely to depend on the subject matter that is primarily of interest to them. Diluting the

localness of news content will reduce the attractiveness of the product, while the quality of other, less local content, such as culture or business, or wide-area classified or listings information, could actually benefit from a concentration of resources.

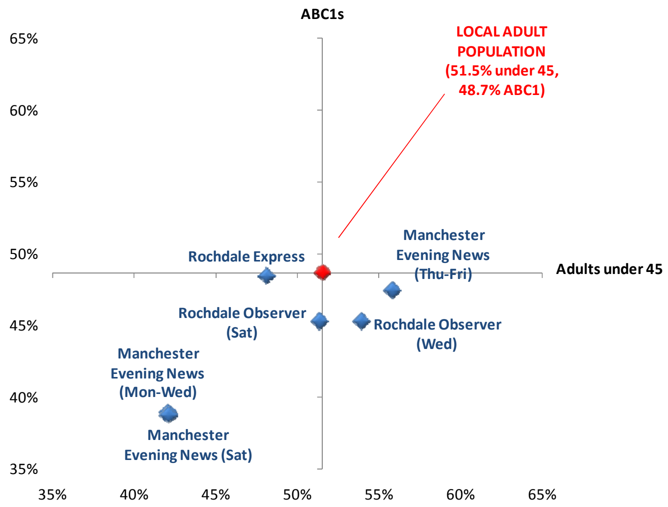
Content positioning

150. Consumers are highly diverse in their preferences for different kinds of content – some might prefer news and sport, others might attach particular preference to music and entertainment, for example. This is particularly pertinent to radio, which reaches the consumer as a single linear stream of content rather than a broad front of parallel content from which they can choose. Thus, radio stations have well-defined station 'formats' (administered by Ofcom) based on relatively narrow genres (usually categories of music) and target demographics (primarily age-based). There is also scope for them to alter the emphasis of their content within their given format, through their choice of playlists, for example.

151. As was discussed in Chapter 3, the incentives for, and effects of, post-merger repositioning depend on the degree of pre-merger similarity of the products involved, which should therefore be examined as part of an LMA. Stated plans for product repositioning or shifts in coverage should of course also be assessed. Broadly speaking, benefits of increased variety are more likely to arise in situations where the products are positioned relatively closely to each other pre-merger.

152. Similarity can be assessed on the basis of both the consumer base and product characteristics. In the first instance, demographic profiles of the readership or listenership of the merging products and others in the market (based on age group, gender and social grade) can easily be created from the standard industry sources and supplemented by internal research made available by the parties. Competitor analyses dating from before the merger may help reveal the main dimensions on which the merging products previously competed most intensely, which in turn are the dimensions that are most likely to be separated in any repositioning of the products following the merger. They may also contain information on the degree and type of competition from third parties, where relevant.

Figure 4.3: Illustration of demographic positioning (local newspapers in Rochdale)



153. Figure 4.3 illustrates a readership profile for titles in a JICREG area based on two demographic dimensions. Similar analyses were provided to the OFT by the parties in the Global/GCap radio merger and used in its consideration of the incentives for repositioning and possible benefits to advertisers from access to more focused target audiences. However, similarity in audience or readership demographics is a less reliable indicator of product 'closeness' and substitutability for consumers than it is for advertisers, since advertisers largely value exposure to demographic segments irrespective of content, while individual consumers within those segments may in fact view media products quite differently.

154. For this reason content profiles, namely the volume (for press) and mix (for radio) of different categories of content should be analysed to the extent that data can be sourced from the parties.

Table 4.3: Programme formats of radio stations operated by Global and GMG in Greater Manchester

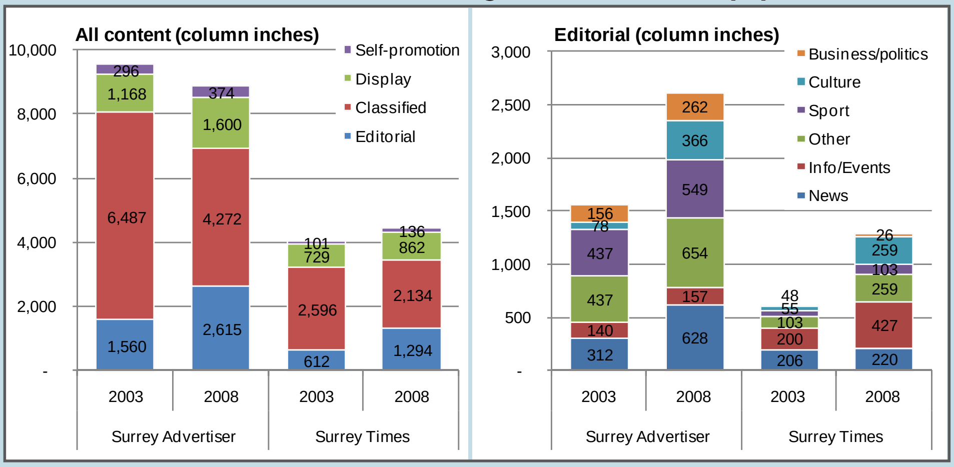
	Contemporary		Classic	
	Mainstream	**Niche / alternative**	**Mainstream**	**Niche / alternative**
Global		Galaxy XFM	Gold	
GMG	Real Radio			106.1 Rock Radio Smooth Radio

155. An illustration of a high-level classification of the formats of radio stations owned by two groups in the Greater Manchester area is shown in Table 4.3. Using genre-level data supplied by the relevant companies, more in-depth content analysis could be undertaken of potential station complementarities.

156. An example for press, based on a content analysis conducted by Oliver & Ohlbaum for Ofcom's 2009 study of Local and Regional Media in the UK (but re-presented in absolute volume terms rather than proportions), is given in Box 4.3.

Box 4.3: Content volume analysis for local newspapers

Content volumes before and after an integration of local newspaper titles



Source: Oliver & Ohlbaum for Ofcom[41], DotEcon calculations

As with radio, no studies or ex post merger analyses to our knowledge have addressed market outcomes following local or regional newspaper mergers in the UK. The nearest we have found to a case study is in a content analysis of local newspapers in a selection of areas of the UK at 2003 and 2008 carried out by O&O as part of Ofcom's study of Local and Regional Media in the UK. These area studies include Guildford, where three titles were integrated between those dates to form the Surrey Times, a free weekly. The data are presented in the charts above, where we have recalculated the absolute volumes of content (rather than the proportional mix) from the original report, leading to somewhat different conclusions. While classified advertising declined, editorial space doubled (and display advertising space also increased). The increase was in subjects such as listings or culture, which the O&O authors note may be syndicated, while the volume of news remained constant. Figures for the sister paper, the Surrey Advertiser (a paid weekly broadsheet distributed over a wider area), are also shown. It likewise grew its editorial space between the two years, but in particular, doubled its news content. For both titles, the increase in editorial space is well above the average trend in Figure 4.2.

4.4 Online innovation

157. Almost all traditional media platforms now operate online content. Online can be viewed as a combination of 'quality' dimensions (e.g. improved

[41] Ofcom (2009), 'An analysis of the content of local and regional newspapers – a report by Oliver & Ohlbaum'.

accessibility) and positioning effects (e.g. appealing to different set of platform preferences), but is more convenient dealt with in a distinct section.

158. Regional press titles offer companion websites containing video content in addition to simply reproducing textual and photographic content from print editions. They also feature additional, user-generated content which may be more local (and carried on local subsites). They emphasise online classified advertising services, including jobs and dating sites, operated by the parent group.

159. However, although a major preoccupation of newspaper industry, the online audience in the UK is currently small: internet readership accounts for around five per cent of the daily local newspaper audience and less than three per cent of consumption time, while providing less than six per cent of revenue in 2008.[42]

160. Online strategies of radio groups are broadly analogous to those of the local and regional press. The internet provides an alternative delivery mechanism for content carried on the traditional platform (including both streamed Internet radio and time-shifted content such as podcasts or other non-live audio), as well as acting as portals to additional content, some of it user-generated.

161. There are no “volume” metrics akin to pagination for newspapers or hours of programming for TV or radio that can readily be specified for online services. However, online audience and demographic information is available for newspaper sites via JICREG.

Box 4.4: Online/offline migration and substitution by consumers

The move to digital content is a major preoccupation of the local newspaper industry in particular and is a potential source of merger synergies in view of the common fixed and variable costs of online publication of multiple titles, which could have consumer impacts.

By extension, differences in consumers' propensity to use the internet may well cause mergers to affect them differentially. There is abundant evidence that younger and/or higher-income groups have the highest rates of internet use in most countries. In the UK, while more than 80 per cent of under-55s have an internet connection at home, the proportion falls sharply among higher age groups and is also significantly lower for C2DEs.[43]

In an important study of the US newspaper market, George (2008) finds strong evidence that the internet disproportionately attracts younger, educated, urban individuals away from daily newspapers and that the composition of the offline readership is changing as a result. (She also finds that traditional newspapers have shifted coverage in response. Product repositioning, which may benefit the 'residual'

[42] Jim Chisholm (2009), 'UK newspapers: The road forward. A discussion document on the future of the UK regional press,' December 2009.

[43] Ofcom, 'Accessing the internet at home – A quantitative and qualitative study among people without the internet at home by Ipsos Mori', June 2009.

readership, is considered in the next chapter.)

The analysis in George (2008) does not address whether those who are substituting away from traditional newspapers are switching to online versions of the same outlets or to alternative sources. Gentzkow (2007), based on data from 2000-2003, finds that the online version of the Washington Post has acted as a substitute for the print edition. His estimation results show that the propensity to choose the online edition is again higher for younger and more educated individuals, and for those who are in full-time employment, especially if they have online access at work.

Kaiser (2005) has considered whether companion websites are substitutes or complements for the print version of newspapers based on circulation and click data for eight national and 85 local German newspapers between 1998 and 2005. He finds that online versions detract from print circulation in the case of national titles but increase it in the case of local ones, although the effects in each case appear to be small. The analysis does not take account of changes in the quality of online versions or distribution strategies.

There appears to be no firm view in the UK local and regional newspaper industry as to whether online versions on the whole cannibalise or encourage print sales. In any case it appears that newspapers view the internet not so much as a tool for promoting print circulations but as a means of recapturing classified advertising that is anyway migrating to the internet and of attracting a new readership among younger consumers, perhaps ultimately with a view to charging for online content (although the viability of this model has not yet been demonstrated).

4.5 Summary

162. Table 4.4 provides a synoptic overview of the various indicators discussed in this chapter. A number of general conclusions can be drawn:

- Most obviously, the merging entities and other interested parties will be a prime source of information that could potentially inform Ofcom's assessment of consumer benefits. Having to rely on such sources of information to a substantial extent implies that it is important for Ofcom to be able to evaluate the likelihood and credibility of the effects anticipated by the parties. The discussion of mechanisms through which mergers in the local media sector might lead to consumer benefits from a theoretical perspective presented in the next chapter can be of help in this regard.
- Mergers may affect many of the factors set out above simultaneously, and it is therefore important to consider the effects of various changes in conjunction. This can be complicated by the fact that trade-offs exist, which inevitably require some attempt to be made to aggregate and consolidate the effects.

Table 4.4: Summary overview of indicators

Type	Metric/ Indicator	Interpretation	Comment
Volume	Total time expenditure of consumers	Increase in time expenditure as a result of merger suggests potential consumer benefits. Predicted reduction suggests	Used as initial screen in order to assess the likelihood of consumer

Type	Metric/ Indicator	Interpretation	Comment
		that consumer benefits are less likely, and that other quality indicators would need to be shown to improve substantially in order to sustain consumer benefits	benefits
Vertical - quality of content	Journalist time engaged in original newsgathering and story creation, expressed as a ratio to coverage population (all media)	Input measure linked to quality - more effort spent on creating original content should improve quality (for content types such as news where consumers value local specificity)	Time engagement measure preferable to any cost measure
	Ratio of originated to syndicated content, for subject-matter of local relevance	Output measure - more original content should increase value to consumers (for local subject matter)	
Vertical - advertising	Advertising pagination, column inches or count (newspapers)	Based on assumption that local newspaper advertising is more likely to be informative than persuasive, and readers are ad-loving at the margin, an increase in advertising would improve quality	May be necessary to consider any shift in the relative weight of informative and persuasive advertising in addition to the pure volume change
	Advertising minutes (radio)	Based on the conclusion listeners are ad-averse at the margin, an increase in advertising minutes would reduce quality for consumers	
Vertical - price	Cover price (paid newspapers)	Increase in price/introduction of charging unambiguously reduces consumer surplus (all else equal)	
	Online access charges		
Vertical - size	Pages, column inches (press)	Presumption that 'more is better'	Might need to be compared with changes in advertising - if size increase is purely due to increased advertising, consumer benefits would only arise to the extent that the additional advertising is valued
	Programming hours (broadcast)		But most radio stations already broadcast round the clock
Vertical -	Issue frequency, e.g. daily/weekly	Presumption that 'more	Will generally be accompanied by other

Type	Metric/ Indicator	Interpretation	Comment
frequency	(press)	frequent is better'	changes that need to be evaluated in conjunction
	Frequency of updates of websites/live news feed (online)		
Vertical – intensity of distribution	Number/ubiquity of retail outlets (paid newspapers)	Reduces additional costs (shoe-leather costs) for consumers to access the product - increase in number of retail outlets should make it easier for consumers and thus generate benefits	
	Volume/ubiquity/ intensity of free distribution (free home delivery, drop-distribution, handouts) (free newspapers)	Similar to increased number of retail outlets	
	Parallel online publication or additional content (e.g. online editions, Internet radio or podcasts, streamed or on-demand TV content)	Increase in the number of ways in which content might be accesses should provide consumer benefits	Differentiation in relation to available content might be associated with introduction of charging models or price discrimination; could also be used to segment audiences to support price discrimination amongst advertisers, which could sharpen incentives to grow audiences (see next chapter)
Vertical - physical quality	Colour printing, paper quality (press)	Improved quality should increase consumer surplus	Quality metrics potentially very subjective/difficult to measure and evidence for their importance to consumers relate to other attributes does not exist
	Quality of broadcast signal or equivalent (broadcast media)		
	Website quality and functionality		
Horizontal - extent of distribution	Potential closures?	Closure will reduce consumer benefits as previously used product will no longer be available	Will have to be considered in combination with the likely impact of cost savings on other indicators (e.g. improved

Type	Metric/ Indicator	Interpretation	Comment
			content quality)
	Will there be a wider/smaller/different area of distribution for all or a sub-set of the papers?	Increased geographic distribution would increase reach and attract additional customers whose valuation increases consumer surplus	Will have to be considered in conjunction with number/ubiquity of retail outlets and – more importantly – potential impact on 'localness' of content, which may be diluted
Horizontal - content positioning	Content positioning in terms of content volumes (for press), mix (for radio) of different genres	Improved match between product attributes and listener profiles should lead to consumer benefits. Repositioning plans in response to a merger might need to be looked at in terms of both positioning and incentives for the investment in vertical dimensions of quality. Repositioning may benefit consumers through increased variety, but formal or de facto amalgamation (e.g. content sharing) for cost-efficiency reasons may reduce it (cf. closures, above)	
	Demographic profiles of readers/listeners/viewers		Can provide some indication of pre-merger 'closeness' of merging firms and thus the likely implications on post-merger competition incentives
Online innovation		Can broaden appeal, extend range of content and broaden distribution, and could thus have considerable consumer benefits. Could also improve segmentation and price discrimination over advertisers, providing sharper incentives to grow and satisfy audiences.	But online channel currently still small and may not be a determining factor in assessment of effects with an immediate horizon.

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