



Completed acquisition by Global Radio UK Limited of GCap Media plc

ME/3638/08

The OFT's decision on reference under section 22(1) given on 8 August 2008. Full text of decision published on 27 August 2008.

Please note that square brackets indicate figures or text which have been deleted or replaced at the request of the parties for reasons of commercial confidentiality.

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PARTIES

1. **Global Radio UK Limited** (Global) is a privately-owned UK based commercial radio group, the activities of which comprise nine local radio analogue stations grouped under three principal brands (Heart, Galaxy and LBC). These stations are also broadcast on DAB digital radio. Global's stations are essentially limited to London, the Midlands and the North of England. Global owns one digital-only station (The Arrow) and has a [] per cent stake in MXR Limited which itself owns 5 multiplex licences. For the financial year 2007, Global's turnover was approximately £[]. Global accounted in 2007 for approximately 10 per cent of all UK commercial radio revenues.
2. **GCap Media plc** (GCap) is a public company listed on the London Stock Exchange. It was formed by the merger of Capital Radio plc and GWR plc in May 2005 and owns a portfolio of 71 local analogue radio licences across the UK, as well as the Classic FM national station. Many of these stations are also broadcast on DAB digital radio. GCap owns one digital-only station, and 22 digital multiplex licences, four of which have not yet been launched. It has interests in 10 further multiplex licences in conjunction with third parties such as Bauer, Arqiva and Global. For the financial year 2007, its turnover was some £200 million. GCap accounted in 2007 for approximately a third of all UK commercial radio revenues. In addition, GCap Media Services Limited is appointed as GMG Radio Holding Limited's exclusive agent in relation to the sale of GMG's airtime to national advertisers.

TRANSACTION

3. On 31 March 2008, a wholly owned subsidiary of Global announced that it had reached an agreement to acquire the entire share capital of GCap for approximately £375 million (225 pence per share in cash).
4. The transaction was completed on 6 June 2008. The OFT accepted initial undertakings from Global on 6 June 2008. The OFT's statutory deadline in this case is 6 October 2008. The parties submitted an informal merger notification on 23 May 2008. The OFT's extended administrative deadline expired on 31 July 2008.

JURISDICTION

5. As a result of this transaction Global and GCap have ceased to be distinct. The UK turnover of GCap exceeds £70 million, so the turnover test in section 23(1)(b) of the Enterprise Act 2002 (the Act) is satisfied. The OFT therefore believes that it is or may be the case that a relevant merger situation has been created.

EXECUTIVE SUMMARY

A) Introduction

6. The OFT's decision in this case is to suspend its duty to refer in order to consider Globals proposed remedies to divest certain assets to an up-front buyer(s). These remedies appear, in principle, to be clear-cut in that they restore pre-merger competition for customers running regional radio advertising campaigns to reach listeners in the East and West Midlands.
7. The transaction largely combines complementary assets. Globals prime assets include relatively new and strong radio brands in Heart and Galaxy, and the corporate know-how, common programming format and consistent audience demographic associated with them, its comparative disadvantage is a lack of geographic coverage. GCaps prime assets consist of an extensive radio network, largely of heritage local radio stations, across the UK, comprising 71 local broadcasting licenses, as well as one national license (Classic FM), its relative disadvantage is the lack of a unified and recognizable brand proposition – that is, a common programming format to attract a particular audience demographic, and a unified brand proposition to advertisers targeting that audience in a national campaign. The primary value proposition of the transaction is the combination of Globals brands and GCaps UK-wide station

network, Global also intends to refresh certain GCap stations that will remain locally-focused brand propositions.

8. As noted, Global has limited national coverage, being present in only London and the Midlands, where its activities overlap geographically with GCap, and the North of England. Outside of the Midlands and in London, the transaction is best characterised as a conglomerate merger. Both parties stations are sold as complementary products to the same class of advertising buying agencies who purchase airtime on bundles of stations, assembled to achieve broad coverage in radio and multi-media advertising campaigns run on a national, that is, UK-wide basis.

B) The Midlands – anti-competitive effects require remedies to restore competition

9. The OFT's evidence, including customer concerns, suggests that the parties are the top two competitive choices for a very substantial proportion of advertising customers running regional radio advertising campaigns in the East and the West Midlands, respectively – Global can offer a single regional play, Heart, in both areas (as well as Galaxy in West Midlands) while in each region GCap sells a regional bundle of some or all of its local stations. In light of evidence that this competition eliminated by the merger will not be replicated by remaining or new rival radio stations or other media sources, the OFT believes there is a realistic prospect of a substantial lessening of competition for regional radio advertising campaigns in each of the East and West Midlands.
10. For the sake of completeness, the OFT then drew inferences on the scope of the market - if Global could likely raise price post-merger, with a post-merger share of regional advertising campaign revenue of between [60-70] per cent in both areas, then it should follow that a hypothetical monopolist could do likewise. Accordingly, the OFT backed into market definition, concluding that two relevant markets affected by the merger were the supply of radio airtime for regional campaigns in the East and West Midlands, respectively. The OFT's approach to the Midlands demonstrates that market definition did not contribute to the critical findings underpinning intervention (in this case, a duty to refer and consideration of first-phase remedies) based on unilateral effects in a merger of differentiated products. At the same time, the analytical value of market definition for other purposes - as a screening device, as a tool in testing other theories of harm, and for *de minimis* purposes - is brought out elsewhere in the decision.
11. In the Midlands, the OFT was not presented with sufficiently compelling evidence that the prospect of anti-competitive harmful effects on advertisers

for regional campaigns would be outweighed by pro-competitive efficiencies benefiting listeners and advertisers in those same areas, nor that merger-wide benefits accruing elsewhere would outweigh such harm such that the OFT would rely on customer benefits exception to reference under section 22(2)(b) of the Act.

12. Where market self-correction cannot be expected to restore a substantial loss of competition, intervention by way of remedies may do so. In this case, the OFT ruled out the so-called *de minimis* exception to reference, on the grounds that the case was a clear-cut candidate for first-phase merger remedies which would protect customers without incurring the costs of a reference. When considering the actual undertakings in lieu offered by Global, for the OFT to be satisfied that a remedy was clear-cut, those offered remedies needed to restore pre-merger competition to supply airtime to regional radio advertising campaigns. In both cases, the remedies are clear-cut, amounting to a divestiture of the total overlap and, as far as regional customers are concerned, an unwinding of the transaction and its effects in the Midlands.
13. In the East Midlands, this will in principle be achieved by divesting the overlap, in the form of Globals Heart station, to an up-front buyer. Subject to consultation, the new purchaser will either re-brand the station or license the Heart brand and national programming format while exercising wholly independent control over local programming content and advertising sales. In the West Midlands, the new purchaser will acquire all four GCap stations, allowing that player to bundle all possible combinations of these stations and thus compete on the same regional basis against Global and others as did GCap pre-merger.

C) London – pro-competitive efficiencies outweigh the risk of anti-competitive effects

14. Although the merger is horizontal in London, because the parties products are substitutes, they are nevertheless not close substitutes. In fact, the parties products are purchased as complementary parts of a London package, because they offer customers different London audience demographics. In an important sense, then, certain key efficiency benefits of the merger that the OFT recognizes in London – notably the elimination of the double mark-up or Cournot effect that arises when two complementary products are sold at a lower combined price by a common owner – are those associated with vertical or conglomerate mergers, not horizontal ones.
15. The prospect that the merger substantially reduces rivalry is much weaker than in the Midlands, where the parties are the top two competitive choices for regional campaigns. For London campaigns, Bauers Magic and Kiss brands

makes it a more direct competitor to each party, and arguably GMGs Smooth, as well as Virgin Radio, are equally close substitutes to either merging party as the parties are to each other. For a substantial proportion of radio advertising revenue booked on London stations, that revenue derives from national multi-media advertising campaigns, where the purchasing agencies have significant leverage to adjust radio spend, though this demand-side constraint does not appear to apply to customers running London-wide campaigns only. Ignoring efficiencies, it is a finely balanced question as to whether supply-side constraints alone are sufficient to rule out even a realistic prospect of a substantial lessening of competition, that is, a loss of competition that entails customer harm.

16. This makes London a marginal case, where efficiencies were merely required to tip the balance to be decisive, rather than needing to carry the burden of a counterweight or trump against, say, a compelling presumptive case of very substantial anti-competitive effects (for example, a merger to monopoly in a market with no entry prospects). In this case, the merger-specific efficiencies are two-fold and, in the OFT's judgment, comfortably clear the hurdle of tipping the balance in London.
17. First, there is compelling evidence that Global will have the profit incentive to bundle together former GCap and Global stations at a lower package price than the equivalent mix-and-match bundled price pre-merger, when the stations were not commonly-owned. The price-lowering incentive counteracts any price-increasing incentive gained from internalising competition between the parties stations. Unlike certain other types of efficiency, this does not require pressure from rivals to ensure pass-on to customers, it is profit-maximising for the merged firm to lower prices of bundles independent of any rivalry.
18. Second, Global will reposition its now commonly-owned stations to attract listeners, in a way designed to increase total audience size for all stations combined, and increase the demographic focus of the respective station audiences. While directly benefiting end-consumers – who are at no risk of price effects – advertisers also benefit: not only from the ability to reach a greater audience, but also to better target their advertising towards more focused demographics (because many product advertisements are targeted, to greater or lesser degree, towards certain age, gender and income groups), which means less wastage of the message and better value-for-money for the advertising customer. Both types of efficiencies, if realized, will improve the Global/GCap station offer to listeners and advertisers. The driver of this efficiencies analysis is the net impact of the transaction on customer welfare, the OFT's overall belief is that the parties London customers will be better off

as a result of the merger, and in any event there is no realistic prospect that the parties customers will end up worse off.

19. Moreover, London radio rivals like Bauer, Virgin and GMG will be obliged to respond if they wish to retain and grow both classes of customer. These efficiencies can properly be characterised as rivalry-enhancing because rivals remain in the market who will need to match or better respond to the merged firms improved offer if they are to win and retain customers made better off by the merger, and the net effect of the merger is that it will enhance - or in any event not substantially reduce – overall rivalry notwithstanding the loss of rivalry between the parties themselves.
20. Consequently, there is no realistic prospect of customer harm, by the same token, any lessening of competition is not substantial, and the duty to refer is not met.

D) There are no residual competition issues at national level

21. The OFT finally considered whether any national issues arose over and above those generated by the Midlands overlaps, which are subject to divestiture (or else the entire transaction will be referred). The OFT was able to rule out the residual prospect of unilateral, coordinated and non-horizontal effects at the national level for reasons detailed in full below.

BACKGROUND ISSUES

A) Commercial radio as a two-sided market

22. Fundamental to the success of a commercial radio station is its ability to attract listeners. Radio stations compete for audience (i) by developing and promoting a recognisable and attractive station brand and (ii) by broadcasting programmes according to the targeted demographics in the relevant geographic area. The better the quality of the programmes and the offer made to the audience as a whole, the more attractive a radio station becomes for listeners and, in turn, the more attractive it becomes for advertisers seeking to reach them.
23. Commercial radio stations earn their revenues principally from the sale of advertising. They compete for advertisers through the size of their total audience, the demographic profile of their listeners, the strength of their brand and through price negotiations.

24. Although most radio stations have advertising rate cards, they typically do not have standard pricing, as discounts and negotiations are commonplace. Pricing of radio advertising is generally based on the basis of a given cost per thousand (CPT) adults reached by a spot campaign. The capital cost of advertising campaigns varies according to (i) the number of listeners a radio station has and how long they listen for – the larger the audience the greater the spot costs, (ii) the type of audience reached by the station, and how finely targeted the stations audience is, (iii) the number of spots required, and (iv) the period of time the campaign is to run.
25. Radio is sometimes used on its own, as a stand alone advertising campaign (notably, on occasions where it is used to deliver a specific local message). However, most of the time, it is used as part of a mixed media message to supplement and reinforce advertising messages delivered primarily by other media (such as television).

B) Merger analysis in the commercial radio sector

26. As summarized by the Canadian Competition Bureau, [a]dvertisers pay radio stations in order for listeners to hear their commercials and ultimately to increase sales, and listeners purchase radio broadcasting content by listening to the commercials (and, at least some, responding to them).¹
27. The OFTs analysis in this case primarily focuses on whether, as a result of the merger, advertisers will pay more to reach listeners and/or receive reduced value for the money they spend on adverts.
28. While it is self-evident that listeners would not experience a direct adverse price effect in the way advertisers might, a merger could also result in listeners being obliged to pay more for the broadcasting content they seek by being obliged to listen to incrementally more advertising - which can be considered an adverse effect based on the reasonable assumption that listeners do not listen to the radio primarily to hear adverts. In respect of audience tolerance of total advertising relative to music, talk, news and other broadcasting content, 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.
29. Alternatively, adverse effects are possible on listeners to the extent that reduced competition may mean that listeners may be faced with lower-quality

¹ Canadian Competition Bureau, *Ex Post Merger Review: An Evaluation of Three Competition Bureau Merger Assessments* 1 August 2007, Ch. 6.2.1 available at www.competitionbureau.gc.ca/epic/sitre/cb-bc.nsf/en/O2453e.html.

programming or innovation levels, for example, less investment in paying for top DJs, presenters, research into play-lists and listeners tastes, and so forth.

30. In fact, the potential direct adverse effects (for example, price) felt by advertisers and the potential indirect adverse effects (for example, programming) felt by listeners are inter-related because of the two-sided nature of radio. For example, if listeners switch off because they do not like programming (or there are too many ads) then radio is also likely to be less valuable to advertisers, because their message reaches fewer listeners simultaneously. Conversely, the brand repositioning efficiencies in London discussed below work in the opposite direction: programming improves so more listeners tune in, therefore advertisers are able to reach more listeners and radio is more valuable to them. In both these examples, the competitive effect of a merger on either sides of the market is mutually reinforcing.
31. However, in some respects, the competitive effects may be inversely related: that is, an increase in prices that harms the advertiser side of the market may actually benefit the listener side of the market if it restricts advertising output (total airtime), to the extent that listeners do not listen to the radio primarily to hear adverts.
32. In the latter case, the inverse relationship between the competitive effects on either side of the market is countervailing and adverse effects on one side of the market are balanced by benefits on the other to some extent. Nevertheless, the OFT considers it appropriate primarily to consider the competitive effects of the merger on advertisers and treat any countervailing benefits to listeners as part of the efficiencies analysis subject to appropriate evidentiary rigour. A priori, it is unclear to the OFT how much—if at all—listeners value each incremental reduction in advertising below the 13 minute-per-hour threshold, nor does the OFT know the curvature of the relationship between price and total airtime demanded by advertisers for each relevant station affected by the merger.
33. Absent compelling evidence on efficiencies, therefore, the OFT proceeds on the basis that (i) it is advertisers who will primarily and most directly feel any adverse effects arising from a commercial radio merger and (ii) any possible countervailing effect on this from the listeners side of the market, while theoretically plausible, must meet stringent efficiency evidence requirements rather than merely be assumed to be sufficient. The OFT notes that a focus on harm to advertisers is consistent with previous merger enforcement in radio cases in at least the UK, Ireland, Canada and the United States. In this case, the parties did not seek to argue that prices rises to advertisers would benefit listeners in any relevant market.

C) Relevant customer classes and geographies

a) Distinctions based on the geographic scope of the radio advertising campaign

34. For present purposes, it is appropriate to conceive of radio advertising campaigns in the UK taking place at the national (UK-wide), regional and local levels, respectively, reflecting the geographic coverage sought by the client in question.
35. National campaigns are usually run by large advertisers, typically of retail consumer goods and services, seeking to deliver a common message nationwide to a large proportion of the UK population. For such customers, radio is often a supplementary medium to reinforce over the air the message that potential customers of the relevant advertised product have seen on commercial television or in other media (newspapers, billboards, the internet, and so forth). Such customers, with few exceptions, usually operate via an advertising agency that will help draw up an advertising strategy and negotiate with commercial radio groups on the advertisers behalf and leverage bundled demand of multiple clients in price negotiations. Almost all national campaign revenue is actually generated via agencies and dealt with by way of annual contract negotiations (see further below).
36. Regional campaigns are run by advertisers for whom the campaign in question is only designed to reach listeners within a certain region (for example, because it relates to regional services within the catchment areas of certain retail commercial outlets or relates to public service messages specific to a region). Examples relevant to this merger are regional campaigns in the East Midlands, West Midlands, and Greater London. As discussed in detail below, such customers can choose to purchase spots on a regional station and, in some areas at least, can also elect to purchase several spots across several local stations sold as a region-wide bundle.
37. Local campaigns are run by advertisers whose geographic focus is narrower still, limited to a local area and therefore in principle limited to the local radio station or stations that broadcast in that area. Examples relevant to this merger are advertisers based in a city in the East Midlands – say, Nottingham, Derby or Trent – seeking to reach only that municipal radio audience, for example. The extent to which a regional station is a cost-effective substitute to a local station is considered further below.

b) Distinctions based on how the advertising airtime is purchased

Direct and indirect (agency channel) purchases

38. As set out in the 2006 report issued by Ofcom on the radio advertising sector,² (the Ofcom report) and in accordance with the OFT's Capital/GWR decision,³ purchasing channels in radio advertising may be segmented between direct and indirect advertisers.
- Direct advertisers buy directly from a specific radio station on a campaign-by-campaign basis (referred to as direct corporate customers), these can be large corporates negotiating their own national advertising strategy at one extreme, and local advertisers dealing with their local station for a local campaign at the other.
 - Indirect advertisers purchase advertising through media buying or advertising agencies. Agencies are commissioned by advertisers in order both to assist them in developing a media plan that will meet given campaign objectives and to advise them on the most cost-effective means of implementing that plan.
39. The revenue share of direct advertisers for a given commercial radio group is substantially smaller, in general, than that for indirect advertisers. Within the category of indirect advertisers, the parties submit that a further distinction should be made between contracted and non-contracted advertisers, because spend by agencies under an annual contract has become an increasingly important proportion of spend in recent years. Accordingly, the parties submit that the present analysis should distinguish between indirect purchases made under an annually negotiated contract (referred to as contracted) and indirect purchases made on a campaign-by-campaign basis (referred to as non-contracted).
- Contracted purchases typically cover all stations in the UK sold by the commercial radio group in question. These stations are sold as a package but with individual prices per station. Advertisers derive the benefit of lower prices in exchange for committing a certain percentage of their radio expenditure with the commercial group in question. Commercial groups seek to attract revenues based on all stations in their portfolio, to maximise their overall revenues, rather than seeking to attract revenues for specific radio stations. The annual contracts typically include additional discounts for early booking and overnight advertising, on the one hand, and additional premium prices for peak periods (morning and evening rush hours) and late bookings, on the other.

² Report on market definition in the commercial radio sector published by Ofcom on 19 October 2006, conducted outside the scope of a specific case review.

³ *Anticipated acquisition by Capital Radio plc of GWR Group plc*, 22 December 2004.

The parties therefore submit that contracted advertising is national in scope. Although prices per station are negotiated individually during the annual negotiation and vary depending on a number of factors (including the historic rates and the attractiveness of the stations demographic), the radio groups objective is to maximise the overall revenue that it generates on a nationwide basis, that is, to maximise its percentage share of overall spend that the agency commits. Agencies seek to negotiate a deal for the entire portion of their client base that advertises nationwide, not for any one client with specific geographic interest.

- Non-contracted advertising is typically purchased bespoke on a station-by-station basis to reflect a campaign-by-campaign approach, which might well be for a regional campaign, where the advantages of using an agency become significant, but could also include local campaigns, and in both cases encompass negotiations with the target station and those other stations that purchasers would consider to be competing alternatives.

Approach to measuring concentration in supply of airtime for various campaigns

40. On the basis of the above, contracted advertising revenue data is used as the best available proxy for supply of radio airtime for use in national campaigns.
41. Both non-contracted and direct advertising revenue data are used as the best available proxies for supply of radio airtime for regional and local campaigns. As it is not safe to generalise that non-contracted agency revenues all represent regional campaign revenue and direct revenues all represent local campaign revenue, the OFT has had regard to both data in tandem in evaluating the mergers impact on regional campaign prices and other terms in the East Midlands, West Midlands, and Greater London.

c) Substitutability between regional and local stations in this merger

42. As noted, customers running regional campaigns, instead of purchasing airtime on a regional station, may alternatively buy a bundle of various local radio stations that cover the regional area they are looking to advertise in. In that context various local stations sold as a bundle may constitute an effective substitute to a regional station.
43. Conversely, however, a regional station is less likely to offer a suitable alternative solution to only one local station: buying airtime on a regional station is economically not rational for an advertiser looking to reach a

targeted local population.⁴ The OFT has considered that, in theory, a regional station seeking to optimise spare capacity might be willing to sell advertising airtime at lower prices to local advertisers, however the OFT has seen no indication that the regional radio stations involved in the present case implement this type of practice.

44. In addition, the parties submit that using spare capacity to broadcast local adverts on a regional radio station would be perceived as clutter that worsens the quality standard of that station, and therefore risks losing regional advertisers. This is reflected in the fact that data, provided by third parties and corroborated by third party evidence, show that neither Global nor GCap are currently including the accepted maximum of 13 minutes of advertising per hour, in other words, they are not seeking to fill their capacity with proportionately cheaper airtime offered for obviously local campaigns.
45. Given the above, the OFT considers for the purpose of the East and West Midlands in this case, where Globals regional stations overlap with various GCap local stations, the competition between the two merging parties is limited at the local level – Heart, being a regional station, is not a cost-effective economic substitute for GCaps smaller local stations. To the extent that advertisers sought to reach a specific local area to advertise a local business, it would not appear efficient for them to advertise on Heart given the wastage entailed as they reach (and pay for) a large proportion of listeners who they would not regard as potential customers for their business. Accordingly, this decision focuses on the loss of competition between the parties in respect of the supply of airtime for regional campaigns in the East and West Midlands, respectively, and the loss of any potential local competition in the Midlands is not considered further.

D) Rationale for the transaction

46. In the context of commercial radio currently facing major challenges and given GCaps particular declining situation (for example group listening hours, and more generally in terms of group revenue), the parties submit that the merger

⁴ To demonstrate the high cost of wastage implicit in switching to Heart 100.7 for a local customer, take the following example. The average CPT for BRMB, which has a reach of more than 400,000, was approximately £[] in 2007. The average CPT for Heart 100.7 West Midlands, which has a reach of more than 800,000, is approximately £[]. As a result theoretically, a spot on BRMB would cost £[] and a spot on Heart 100.7 would cost £[] (CPT x thousands of listeners). However, the BRMB advertiser who switched to Heart 100.7 but wanted to target only listeners living in the BRMB TSA would be paying an 'actual' CPT of approximately £[] (£[] divided by the reach of BRMB), because the campaign would be covering significant numbers of listeners outside the advertiser's target area (to whom the advertising campaign would be irrelevant).

will enable them to create a better radio product for advertisers and listeners in an attempt to increase the popularity of radio.

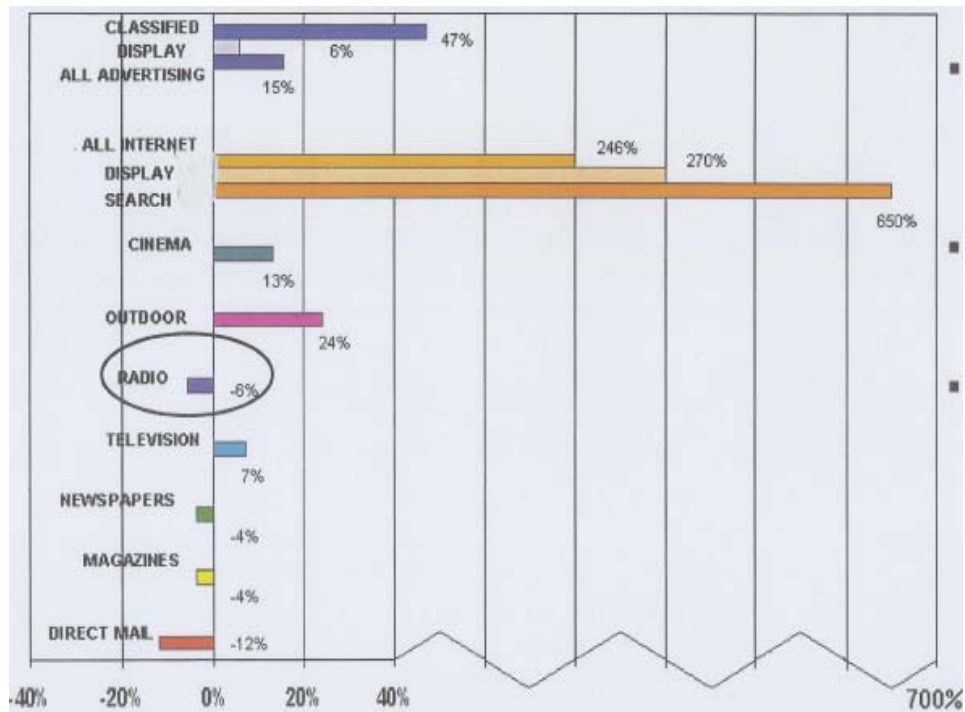
a) Commercial radio facing major challenges

47. A major argument put forward by the parties to explain the rationale for the transaction relates to the challenges which, they submit, commercial radio is currently facing:

(i) Radio advertising is in decline in comparison with other media.

The parties refer to the Ofcom report, which showed that while some 40 per cent of UK businesses use advertising, radio is used by only 4 per cent of businesses in the UK, largely for local and regional advertising campaigns. In addition, the parties claim that the large majority of negotiations are carried out by agencies on behalf of corporate clients and that radio is not regarded as a 'must have' product by these agencies. As demonstrated by share figures of advertising expenditures between 2003 and 2007 set out in the table below, radio has notably lost out to internet and outdoor advertising in recent years, while TV and press remain by far the preferred display advertising platforms in the UK.

Figure 1
Relative growth of advertising by media



Source: Parties (WARC – percentage since 2003)

As a result, radio is one of the least important media in the UK and has seen its importance diminish over the last five years. More specifically, commercial radio revenues are also in decline: although total revenues (including sponsorship and promotion) have increased from £594.6 million to £598.2 million between 2000 and 2007, this represents a fall in real terms of approximately 17 per cent.⁵

(ii) Commercial radio is losing listening share to the BBC

As can be seen from Figure 1 below, the BBC has been increasing listening shares at the expense of commercial radio in recent years, causing the commercial radio sector to lose revenues: competition from the BBC makes it harder for commercial radio to win commercial listeners. The BBC is in a sense a single-sided market, or closer to it,⁶ because it simply seeks to attract listeners without having to incorporate advertising airtime to generate revenue. In the two-sided context of commercial radio, meanwhile, in losing listeners, commercial groups

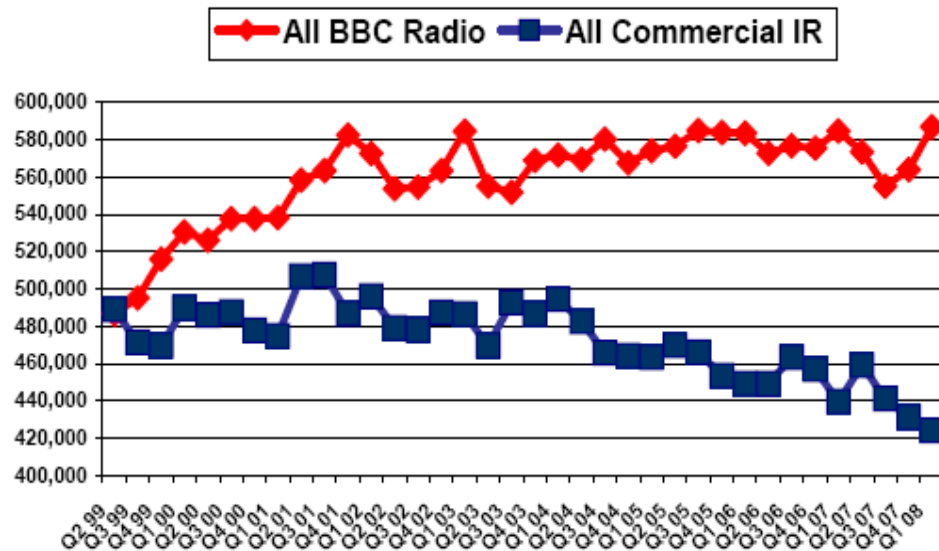
⁵ RAB (Radio Advertising Bureau)/Ofcom revenue data.

⁶ The BBC must of course justify its spending as a taxpayer-funded public service organisation, so it does 'face' another 'market', but a very different one than commercial radio faces when it seeks to generate revenue from advertisers.

have also become less attractive to advertisers and accordingly, generated less revenue and, assuming costs have not declined proportionately, lower profits.

Figure 2

Listening hours for BBC and Commercial Radio on a quarterly basis from Quarter 1 2000



Source: Rajar

According to industry data, commercial radios UK share of listening has fallen between 1999 and 2008 from 50 per cent to 41 per cent while BBC Radios share of listening across the country has grown from 50 per cent to 57 per cent over the same period.

b) GCap is in particular need of restructuring

48. According to the parties submission, total listening hours for the GCap group dropped by 18 per cent between 2005 and 2008, compared to 8 per cent for commercial radio as a whole. GCaps total revenues have fallen by more than [20-30] per cent in real terms over the same period of time. Furthermore, the parties observe that [], they argue that the restructuring plans for GCap, as foreseen in the context of the present transaction, are even more urgent.

c) Parties plan underlying the transaction in the present context

49. The parties plan to undertake the following:

(i) Marry Globals brands and GCaps geographic scope

Globals strategy is to develop near-national coverage for its Heart brand as well as greater coverage for the Galaxy brand. GCaps well known stations are associated with a particular area and therefore are not appropriate to develop a national brand. Global intends to use cost savings achieved through the merger to re-brand the majority of GCaps heritage stations, refocusing those stations towards the standard Heart/Galaxy demographic. The parties submit that this operation will result in a better offering for both listeners – who will be able to listen to Heart throughout the South of England and the Midlands, and for advertisers – who will be able to advertise across the whole or part of the Heart/Galaxy network, with a better understanding of the product and the audience demographic across the network.

(ii) Refresh and refocus GCap core city stations

Certain of GCaps stations, in particular those that are located in large cities which have the capability of supporting a truly local station, will not be re-branded. Instead, Global intends to refocus these core assets towards more targeted demographics. Again, the parties submit that this will benefit listeners and advertisers, both of whom will have a better understanding of what to expect from the station.

(iii) Set up national network programming with quality presenters and at the same time, retain the local character

Global intends to broadcast the same programme across its entire network of stations Endnote 1, leading to costs savings on production and higher quality product and presenters. At the same time, Global will ensure that the local character of the re-branded stations is retained, in order to preserve the loyalty of the local audience and provide a platform for local advertisers. Local features such as news, weather and traffic will be retained, as well as some local programming.

50. The plan described above is to be carried out by Globals management team which, the parties submit, has significant experience in the media markets in general and in radio more specifically, and can show impressive track records, having successfully led similar operations in the past. According to the parties, the re-branding of GCaps network and the revitalisation of the core city stations would not be possible without this team. These points are developed further in the London efficiencies analysis, below.

SECTION II — REGIONAL ANALYSES OF MERGER EFFECTS

REGIONAL CAMPAIGNS IN THE MIDLANDS

A) The role of market definition

51. As the OFT's Substantive Assessment Guidance for mergers makes clear, market definition is a means to an end and not an end in itself.⁷ That end is the assessment of the competitive effects of a merger. In this context, market definition may provide a framework for analysing the direct competitive pressures faced by the merged firm by considering its market share relative to the shares of other suppliers active in the market. However, in markets such as radio where products are differentiated, being branded and/or of differing actual or perceived quality, share data based on a chosen market definition may be a poor indicator of the likelihood of unilateral effects.
52. In differentiated products markets, then, the OFT considers that a low combined market share for the merging parties on the narrowest plausible candidate market definition would be sufficient to rule out concerns.⁸ As the OFT's Substantive Assessment Guidance for mergers makes clear, the narrowest candidate market comprises the merging parties products immediately affected by the merger.⁹
53. However, when products are differentiated, if the merging parties combined share of supply is high on a narrow plausible candidate definition, then the OFT considers that it may be more probative to test the validity of unilateral effects theories of harm by considering real world evidence relating to the direct competitive constraint actually exercised by one party on the other, and removed by the merger, rather than embark upon an analytical exercise featuring hypothetical monopolists in an effort precisely to define what may be fuzzy market boundaries through conventional SSNIP-test analysis.¹⁰

⁷ See paragraph 3.11.

⁸ This is not to be confused with the broad description of the term 'supply' used in the context of the share of supply test for jurisdiction, under which—to ascertain whether it has jurisdiction—the OFT may calculate shares of supply which, while based on a reasonable description of goods or services, may be too narrow to be plausible candidate markets.

⁹ See paragraph 3.17.

¹⁰ Whether approached indirectly by way of market definition or directly by competitive effects, the critical issue that is common is analytical or evidentiary rigour in approaching questions of demand- and supply-side substitution, among others. To the extent market definition acts as a materiality check in merger control, materiality concerns are quite explicitly dealt with in the *de minimis* assessment.

54. Consequently, in this case, the OFT's analysis has focused on the geographic areas in which there is an overlap between the parties activities in radio advertising and where those overlaps generate high post-merger candidate market shares.

B) Candidate market shares as a screen

55. Considering supply of radio airtime to advertisers as a plausible candidate product market, and the advertising campaigns at national level, and at relevant regional levels reflecting horizontal overlaps between the parties – namely in the East Midlands, in the West Midlands and in London – as candidate geographic markets, post-merger the parties have the highest combined share of advertising for each of (i) contracted agency, (ii) non-contracted agency (NCA) and (iii) direct customers (DC) in each of these four candidate markets. The remainder of this Section focuses on regional issues in the Midlands and London, residual national issues are dealt with thereafter.

C) Unilateral effects in regional East Midlands campaigns

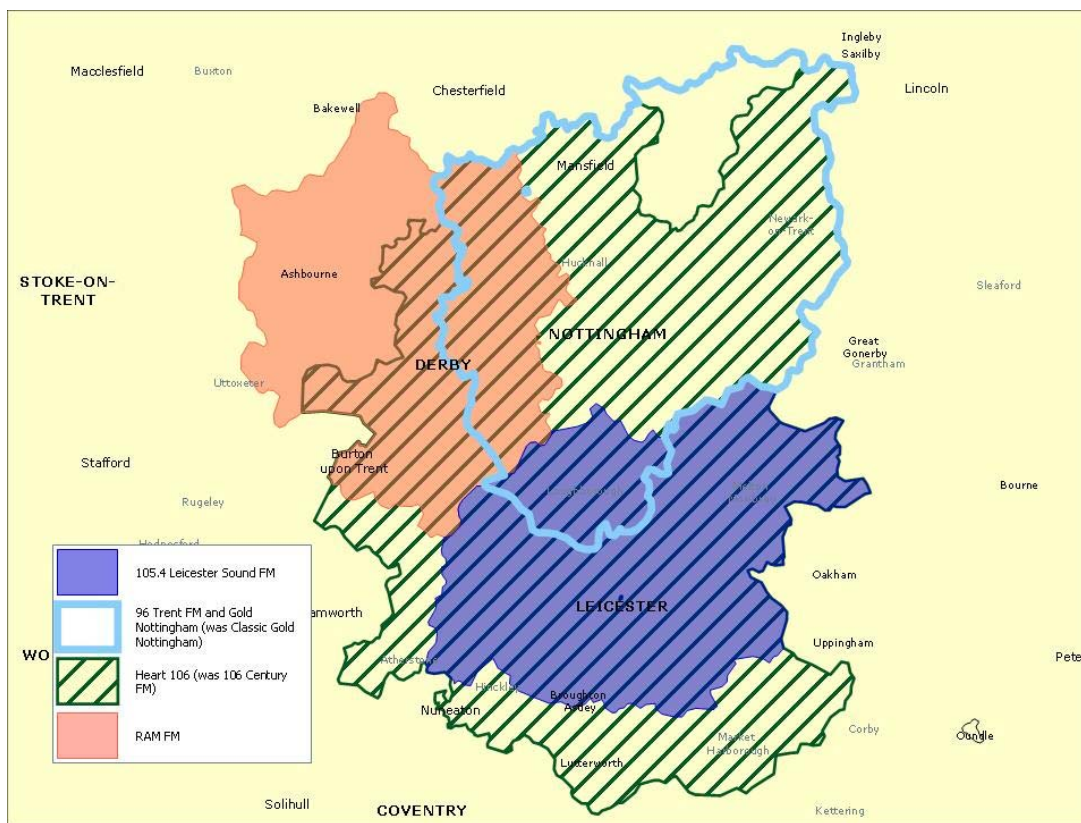
a) Candidate shares are too high to rule out competition concerns

56. The overlap in the East Midlands arises between Globals Heart 106 regional station and GCaps Ram, Trent and Leicester Sound local stations. In this region, the merged entity is by far the largest radio group with [60-70] per cent of non-contracted agency (NCA) expenditure and [70-80] per cent of direct customer (DC) expenditure respectively. The next largest radio group is GMG (owner of Smooth) with [20-30] per cent and [0-10] per cent shares of NCA and DC revenue, respectively.

b) The parties stations overlap heavily in geographic and demographic reach

57. Globals station, Heart 106s, covers most of the East Midlands region, including the major centres of Leicester, Nottingham and Derby. Each GCap radio station has a local coverage within the East Midlands region: Trent FM broadcasts across the Nottingham area which includes the towns of Mansfield and Loughborough, Ram FM broadcasts across Derby and Derbyshire, Leicester Sound broadcasts to the Leicester area. Map 1 set out below shows the geographical location of the Global and GCap radio stations in the West Midlands.

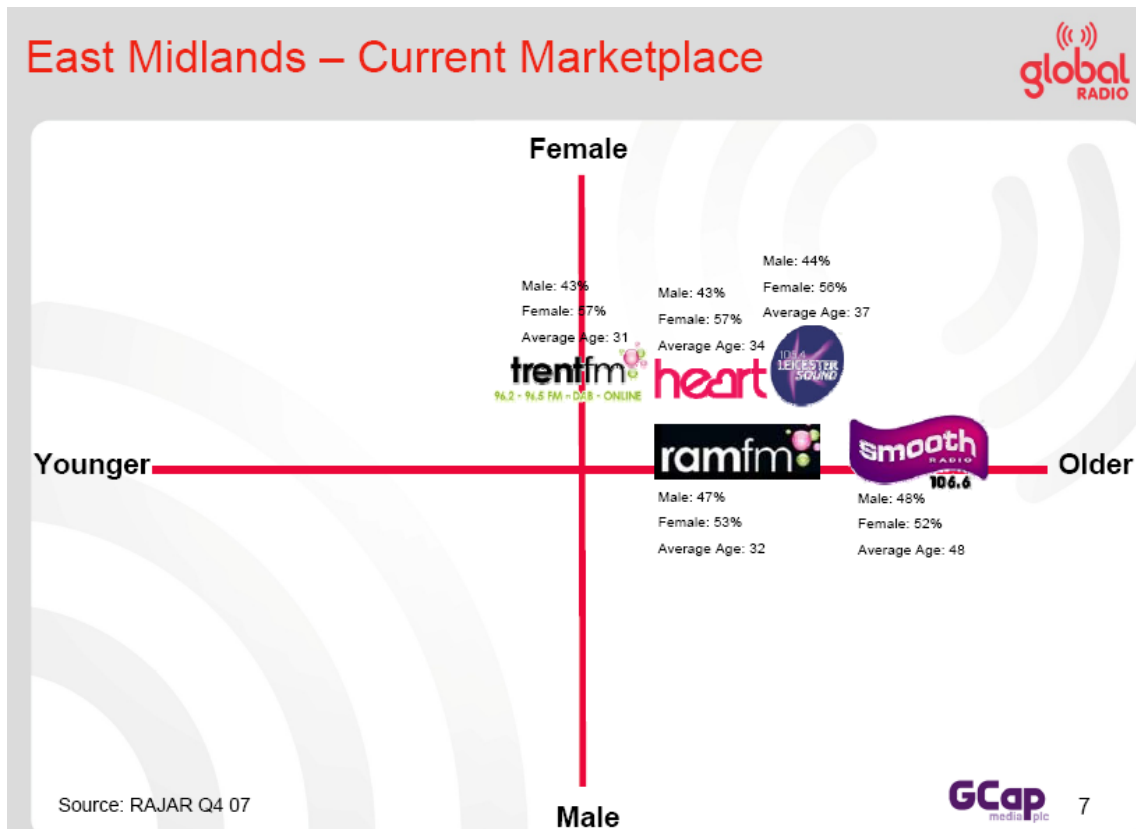
Map 1
Global Radio and GCap stations in the East Midlands



58. Given this geographical configuration, the OFT considers that, for customers seeking regional campaigns, it is reasonable to conclude that there was competition between the parties for such customers pre-merger – Heart by offering straightforward regional coverage, GCap by being able to provide a bundle of local stations that would then (as evident from Map 1 above) provide geographic coverage analogous to that of a single regional station. The OFT has therefore examined evidence pertaining to the degree of competition that existed between the parties pre-merger and the extent to which there was (and will remain) competition from other sources. As discussed below, the survey evidence suggests that GMG (Smooth) and the remaining other competing radio stations would be unlikely to provide effective rivalry to the new entity at the regional level. This was confirmed by customers who argued that they will not have the ability to switch to other stations of equal branding and equal importance and thus will be worse off.
59. Furthermore, there is only a relatively small number of radio stations in the East Midland region, such that all the stations lean towards competing for the middle ground in terms of demographics in order to maximise their respective

coverage. As can be seen from Figure 2, the parties appear to be sufficiently close in terms of targeted profiles so as to be considered close competitors from a demographic perspective as well.

Figure 3
Brand map of commercial radio stations: East Midlands



60. The parties have provided a customer overlap analysis (discussed further below) which, the OFT finds, in fact corroborates the proposition that the parties are indeed close competitors at the regional level.

c) Evidence suggests high margins and high diversion ratios between the parties

61. By focusing on direct competitive effects rather than market definition at first instance, analysis of potential unilateral effects avoids the distraction of the binary fallacy in which products are treated as either exerting no constraint, being outside the market, or all differentiated products in the market exerting equal constraint, and thus treating differentiated products essentially as commodity products. In many differentiated product cases, there is a spectrum of constraints of varying closeness - that is, immediacy and intensity

- operating on a merging party's products. Where one supplier faces close competition from another supplier's product (or store, or radio station) and acquires those products, prima facie unilateral effects concerns arise, because the internalisation of that constraint, and the recoupment of sales formerly lost to the rival if it raised price – are the prima facie basis for a unilateral ability and incentive to raise prices profitably post-merger.

62. When available, diversion ratio data is perhaps the best measure of closeness of competition between merging firms, as it will show what proportion of sales lost in the event of a price rise on one firm's products would be lost to a competitor pre-merger, but recouped post-merger. Absent historical natural experiments showing actual customer switching behaviour when relative prices rose (so-called revealed preferences of customers), the stated preference of customers – that is, their stated reaction to price rises - are one of the best-available proxies for what would happen to prices or other variables post-merger.
63. In *LoveFilm/Amazon* and *Homebase/Focus*, both 2008 unilateral effects cases involving differentiated products subject to close OFT scrutiny, the OFT has explicitly applied a presumption that the combination of high margins and high diversion ratios established a rebuttal presumption of unilateral effects.¹¹
64. In this case, margins are high. The parties submitted that margins on incremental sales of radio advertising are in the order of [] per cent, and the concerns set out below would arise even if margins were substantially lower than this. As far as diversion ratio evidence is concerned, the parties have provided two customer surveys carried out by the British Marketing Research Board (BMRB), providing evidence, based on customers' stated responses, on the diversion ratio from one party to the other among all alternative switching destinations in the event of a 10 per cent price increase by one of the merging parties. The survey results are illustrated in the following table.

¹¹ See *Anticipated acquisition by LoveFilm of the online DVD rental business of Amazon*, decision of 15 April 2008, para 25 onwards and *Completed acquisition by Home Retail Group plc of 27 stores from Focus (DIY) Ltd*, decision of 15 April 2008, para 61 onwards.

Table 1
Diversion ratios (per cent) for non-contracted agency (NCA) and direct customers (DC)

10 per cent Price rise on Global	Switch to Global		Switch to GCap		Switch to GMG		Switch to other*	
	NCA	DC	NCA	DC	NCA	DC	NCA	DC
Global			100 (60)	14 (14)	0 (0)	14 (14)	0 (40)	71 (71)
GCap	22 (18)	14 (13)			0 (0)	14 (13)	78 (82)	71 (74)

Notes:

*Other radio and other media.

Figures are for those customers who believe they know to whom they would switch business, figures in parentheses are diversion ratios that include customers giving don't know answers.

65. Based on these survey results, the diversion ratio going from Global to GCap is particularly striking – 100 per cent of NCA customers who knew which source they would turn to in the event of a 10 per cent price increase for advertising on Heart, and 60 per cent even including all don't know responses, in the reverse direction, the figure of 22 per cent (18 per cent) is still significant though much lower, interestingly, no NCA customers identified GMG as a second choice. The diversion ratios for direct customers is both directions, in contrast, is overall relatively modest at around 14 per cent, about the same as switching to GMG.
66. Overall, these figures, taken in isolation, give rise to concerns, particularly in relation to the constraint that GCap, as a whole, would appear to place on pricing of regional radio advertising on Globals Heart 106.
67. The parties submit that the OFT should be cautious about placing weight on the survey results given the small sample size relied upon. The OFT acknowledges the small size of the sample and the evidentiary implications that flow from such small sample sizes, indeed, in light of this, the evidence in this case suggesting a combination of high margins and high diversion ratios creates a weaker presumption of unilateral effects in this case. However, the OFT considers that the prima facie unilateral effects concerns in the East Midlands arising from the diversion ratio data from the survey are strengthened by additional evidence gathered in the course of the investigation, discussed below.

d) The parties customers overlap and have expressed concern

68. Customers have expressed concerns about the impact of the merger in the East Midlands – principally non-contracted agencies relating to a lack of competitive choices potentially arising as a result of the merger. They fear that in the event of a price increase post-merger, customers will lack the ability to switch to other stations given the absence of an equivalent alternative offer in the East Midlands region.
69. Some agencies have provided concrete examples of situations where they were able to play off Globals Heart station against GCaps stations in order to counter attempted price increases, or obtain better prices than they would otherwise be able to. These agencies submit that, post-merger, any diversion between the parties will be internalised such that the merged entity will be in a position to raise price or reduce quality. One customer provided an example of playing off Heart against the GCap stations to enable this customer to achieve more favourable rates with Heart than it would otherwise have been able to do.
70. These customer concerns are corroborated by customer overlap analysis. Although the parties submit that there are very few customer overlaps between Heart East Midlands and the GCap stations, the following shows that:
- Customer overlaps between Heart East Midlands and the GCap stations are material: of [60-70] NCA customers on Heart, [20-30] also advertised on one or more of GCaps stations, and of [60-70] DC customers on Heart, [20-30] also advertised on one of Trent, Ram or Leicester Sound.
 - A significant proportion of GCap customers are regional as opposed to local-only advertisers – by comparing Leicester Sound and Trent which the parties submitted would represent the best overlap with Heart East Midlands: [30-40] of [80-90] NCA customers advertising on Trent also advertised on Leicester Sound and [30-40] of [60-70] NCA customers advertising on Leicester Sound have also advertised on Trent in 2007, and [0-10] of [120-130] Trent DC and [0-10] of [100-110] Leicester Sound DC have advertised on both stations in 2007.
71. Despite the parties arguments, the customer overlap analysis provided by the parties for the East Midlands region shows that a material number of Global customers also advertise on GCap stations. In addition, a significant proportion of non-contracted agency customers buy various GCap stations as a package, whose geographical coverage overlaps with Globals Heart station. The parties did not provide the OFT with complete information on the actual bundles of

GCap stations that were being purchased by customers, but provided customer overlap data on the basis of a Leicester Sound and Trent combination. Nonetheless, the number of customers purchasing this combination is already material (approximately [0-10] per cent of each stations total advertisers for direct customers and up to [50-60] per cent of non-contracted agency customers) such that it may be that additional numbers of customers are purchasing alternative bundles. For these reasons, the OFT does not rule out concerns deriving from the combination of the above evidence simply on the basis that there are too few overlaps between the parties to raise competition concerns.

e) Despite buy-around analysis, other radio stations do not dispel concerns

72. The parties submit that there is significant competition from other radio stations in the East Midlands. They refer to Smooth as a key regional player in the region with a non-contracted agency share of [20-30] per cent and a direct share of [0-10] per cent, indicating that Smooth currently has an older listener base but is attempting to reposition its offer and drive average age down to the 35-54 range. A tail of remaining smaller stations in the region such as Oak FM Hinckley, Radio Mansfield, Sabras FM, []¹² will, according to the parties, provide additional competitive pressure on the merged entity.
73. In order to support their submission, the parties provided a buy around analysis¹³ conducted in the East Midlands, which they claim demonstrate that purchasers would have the ability to switch a significant proportion of any advertising campaign away from the Global and/or GCap stations to a combination of Smooth and other smaller stations referred to above. More specifically, they submit that non-contracted advertisers will be able to buy around the merged company in the event of any attempted price increase – they argued that customers would be able to switch some 50 per cent of revenues away from the combined group and that this degree of switching would be sufficient to make any price increase unprofitable.

¹² []

¹³ Buy around analysis shows the ability of an advertiser to switch a particular campaign away from one or more specified stations, whilst achieving similar reach and 'opportunities to hear' (OTH). It can reflect a switch of total spend away from the station concerned, or of a proportion, for example 75 per cent or 50 per cent of spend. Buy around analysis is intended to demonstrate that there are effective substitutes to the station concerned that are able to deliver a broadly comparable product in terms of frequency, geography, demographics and reach.

74. The OFT has found however, that most of the modelled campaigns, which use third party stations as an alternative to the original merged entity's campaign, appear to produce better value for the advertisers than the original campaign itself on Heart for example (both in terms of revenue and in terms of impact). Given that it is clear that, despite these theoretical benefits, customers do in fact contract to purchase regional campaigns from Heart and GCap (on a bundled basis) and only 14 per cent of Global's customers and 21 per cent of GCap's customers stated in the second BRMB survey that they would switch to Smooth in the event of a 10 per cent price increase, this casts significant doubt on the reliability of the buy around analysis carried out by the parties. This highlights a generic potential weakness of buy-around analysis: it purports to show what customers could do in the event of a price increase, but is not necessarily probative of what they would do. The OFT gives substantially greater weight to the survey data where customers themselves predict what they would do.
75. In any event, a number of third parties have expressed reservations about an advertiser's ability, post-merger, to buy round the merged entity in the local areas as they say it will not be possible to achieve sufficient coverage by using the smaller remaining stations.
76. Evidence provided by third parties indicates that some customers consider the parties' stations as the only two alternatives for advertisers seeking to operate regional campaigns. From the radio stations in the post merger market, the local alternatives for customers are Radio Mansfield, Lincs FM, Gold Notts and Sabras. On the basis of the survey evidence and third party comments, the OFT does not consider these small radio stations will be able to reposition and/or expand audience such as to provide realistic discipline on Global's post-merger pricing in respect of regional advertising campaigns.

f) Other media will not replicate the constraint lost by the merger

77. The parties argued that they are sufficiently constrained in the East Midlands by other media, and provided a number of customer switching examples to support this argument. While this evidence was potentially probative of the constraint of other media, in particular local press, on local radio advertising, the OFT considered that the evidence was limited in relation to the potential constraint of other media on regional radio advertising campaigns.
78. This relative lack of evidence of a constraint from other media on regional radio advertising campaigns is corroborated by the survey results which showed that the diversion ratio from Global to other media was zero percent

for NCA customers who knew their preferences (but up to 40 per cent including don't knows). Even assuming an asymmetric constraint lost – that is, that GCap constrains Globals Heart 106 but not vice versa, the diversion ratio evidence, coupled with customer concerns, and lack of evidence of Global customers switching to other media, leads the OFT to retain competition concerns that the merger may facilitate higher advertising airtime prices for regional campaign customers on Heart.

79. In particular, critical loss analysis based on the aggregate diversion ratios in Table 1 above suggests a market no wider than only radio advertising.¹⁴ The aggregate diversion ratio from Global of non-contracted agency customers to other radio stations (GCap, GMG and others) is 100 per cent, and of direct customers is 29 per cent. The aggregate diversion ratio from GCap of non-contracted agency customers to other radio stations (Global, GMG and others) is 33 per cent, and of direct customers also is 33 per cent. A hypothetical radio-advertising monopolist raising prices by 10 per cent to each of Globals non-contracted agency customers, Globals direct customers, GCaps non-contracted agency customers or GCaps direct customers therefore retains this fraction of business that diverts to other radio advertising.
80. The fraction of business that diverts to non-radio advertising is therefore 100 per cent less this fraction: for Globals non-contracted agency customers this is 0 per cent (that is 100 per cent less 100 per cent), for Globals direct customers this is 71 per cent (that is 100 per cent less 29 per cent), for GCaps non-contracted agency customers this is 67 per cent (that is 100 per cent less 33 per cent), and for GCaps direct customers this also is 67 per cent. Given the parties high incremental gross margins (that is between [...] per cent) the hypothetical monopolists actual loss in response to a 10 per cent price increase is therefore between [...] and [...] per cent (depending on the incremental gross margin assumed, from [...] per cent) for Globals direct customers, between [...] and [...] for Globals non-contracted agency customers, between [...] and [...] per cent for GCaps non-contracted agency customers and between [...] and [...] per cent for GCaps direct customers.¹⁵
81. These estimates of the hypothetical monopolists actual loss based on the aggregate diversion ratios in Table 1 do not exceed estimates of the critical loss, which vary between [...] and [...] per cent (depending on the incremental

¹⁴ Based on a uniform 10 per cent price increase, to each class of customer, by a hypothetical monopolist of radio advertising. For a critical discussion of such traditional hypothetical monopolist test-based critical loss analysis, see section A. Market definition in National Analysis in Section III.

¹⁵ See footnote 51 below for details of the calculation used. The same results apply (that is a relevant market no wider than only radio advertising) if the aggregate diversion ratios including 'don't know' answers are used.

gross margin assumed, from [] per cent).¹⁶ Consequently, on the basis of the high margins and diversion ratios that generate the OFT's prima facie concerns regarding unilateral effects, the relevant product market in the East Midlands appears no wider than only radio advertising, such that other media will not impose a sufficient constraint on the parties.

g) Other countervailing factors are unpersuasive

Countervailing buyer power

82. The evidence of buyer power on the part of customers running regional campaigns in the East Midlands is weak. Total aggregated NCA and DC revenue account for the minority of the parties revenues, and it is unclear what leverage individual customers behind these figures could exercise in light of the evidence discussed above.
83. A substantial majority of the parties business in the East Midlands ([50-60] per cent for GCap and [60-70] per cent for Global) and in the West Midlands ([50-60] per cent for GCap and [70-80] per cent for Global) may be conducted under annually-negotiated contracts with the major advertising agencies, and this volume of business may plausibly be subject to countervailing buyer power.¹⁷ However, that argument would depend on the existence of an umbrella effect that would protect other classes of customer.
84. As far as umbrella effects are concerned, the argument according to which buyer power of big customers protects smaller ones, may be relevant in a market with uniform posted prices, but is not relevant in a market characterised by individually-negotiated (bilateral) prices and therefore price discrimination.¹⁸
85. There is a further argument in this case, namely that smaller agency or direct customers can arbitrage by actually switching or threatening to switch their volume to be negotiated through a large agency, and benefit from that agency's leverage, and also be immune from price discrimination because their

¹⁶ See footnote 50 below for details of the calculation used.

¹⁷ The parties submitted that, nationally, the top five contracted agencies (alphabetically, Aegis, Group M, Magna, Opera and Publicis) accounted for [50-60] per cent of GCap's airtime revenues in 2007 and [60-70] per cent of Global's, whereas the parties accounted for only a tiny fraction of the top five agencies total revenues (that is radio plus other media). The issue of buyer power would still turn, however, on the degree of substitution (spending adjustments if not total switching away) such customers would engage in and leverage to discipline radio groups negotiating annual sales of airtimes, including for relevant stations at the regional level.

¹⁸ To the extent that it is argued that the number of unprotected customers is small, this is an issue for the *de minimis* exception. However, it is not relevant to the existence of the substantial lessening of competition.

campaign would be protected by the aggregated anonymity of the larger agency. However, the OFT has seen no evidence of such switching or threat thereof being exercised, and the proposition has not been validated by the affected customers. Accordingly, a possible argument in principle is unsubstantiated in this case and is therefore insufficient to resolve the concerns identified above.

Countervailing supply-side constraints – repositioning, expansion, entry

86. As noted, for lack of evidence, the OFT does not consider that any brand repositioning by any of the very limited number of very small alternative radio stations established in the East Midlands would be sufficient to address the OFT's regional concerns.
87. As regards *de novo* entry, new entrants require a broadcasting licence. The limited number of licences suggests barriers to entry are currently significant. In both Capital/GWR and the Vibe/Galaxy cases,¹⁹ the OFT and CC did not credit entry as being timely, likely or sufficient to resolve concerns, in Capital/GWR, the concern related to the overlap featuring Century 106, which is now Globals Heart 106. The OFT has not received any information during the course of its investigation to warrant it taking a different view on *de novo* entry in this case.

h) Efficiencies in the East Midlands

88. The parties argued that the OFT should take account of efficiencies that they claimed will arise from the merger in the East Midlands. Specifically, they claimed that the merger will result in Cournot effect efficiencies, brand-repositioning, synergies and improved inter-media competition. They argued that these benefits would outweigh any adverse effects that the OFT might find in relation to the East Midlands.
89. The OFT explains these types of efficiencies in detail, as well as the evidentiary standards and methodology it uses when assessing both so-called rivalry-enhancing and customer benefit efficiencies, in the section of the decision addressing the competitive effects of the merger in London.
90. In relation to the East Midlands, the OFT considers that the parties have not met the compelling evidence standard in relation to the efficiency benefits of the merger for this region. Specifically:

¹⁹ Vibe Radio services limited / Galaxy Radio Wales and the West Ltd: a report on the merger situation, 14 April 2003.

- Cournot effect efficiencies – the conditions under which Cournot demand-side efficiencies arise are discussed in detail in the London section below. In brief, in the East Midlands, the OFT does not believe that they will arise given that the merger combines closely substitutable propositions for customers, rather than complementary ones, thus depriving the argument of most of its logical force – in other words, regional campaign customers purchasing GCap station bundles already benefit both from the bundled price and the one-stop-shop regional offer from Heart, while local campaign customers, by definition, are unlikely to wish to purchase a merger-specific bundle featuring a local GCap station and Heart,
- Brand re-positioning efficiencies – the OFT does not rule out the possibility of brand re-positioning efficiencies arising from the merger in the East Midlands, in fact, the clustering of brands around the demographic middle ground in principle suggests powerful repositioning possibilities towards more focused demographics. (The section below in on Campaigns in Greater London contains a detailed discussion of brand repositioning as a demand-side efficiency). However, the geographically localised differentiation of the GCap stations (versus the region-wide character of Heart) complicates this argument. Trent, RAM and Leicester Sound are heritage local stations and, in the time available at least, the OFT has not understood why it would be profitable to reposition these stations on a regional basis, when each in fact caters to a local audience: repositioning works as an argument, or works best, when all the stations in questions are in the same geographic market, and where the geographic audience can be teased apart demographically and total listenership expanded: in London, these localised distinctions do not apply as London stations are London-wide.
- Synergies and improved inter-media competition – the principal supply-side synergies claimed are fixed cost savings, which raise questions, compared to variable costs savings, in terms of their pass-on to customers (as discussed under London), and in any event, a very modest proportion of which relate to the East Midlands, finally, the OFT has not been presented with compelling evidence that any benefits arising from inter-media competition would occur.

91. Again, as detailed in the London section below, the above evidence would also need to be compelling so as to resolve the OFT's concerns in the East Midlands, which in relation to regional campaign customers are far more pronounced than were the OFT's prima facie concerns in relation to London.

92. As a result of the above, the OFT does not consider that the parties have presented sufficient evidence in relation to efficiencies arising in the East Midlands to show that any adverse effect on customers in that area would not be substantial. In addition, the OFT notes that its reservations in this respect also apply to the extent that benefits from the merger arising in the East Midlands were to be considered as part of the customer benefits exception to the duty to refer (see below).

i) Conclusion on merger effects in the East Midlands

93. Taking all the above evidence into consideration, the weight of evidence supports a realistic prospect of a substantial lessening of competition in the supply of airtime for regional radio advertising campaigns in the East Midlands. This conclusion derives from (i) high share of supply to NCA and DC customers, (ii) closeness in geographic and demographic reach, high margins and high diversion ratios, at least from Global to GCap stations, (iii) customer concerns, and (iv) a lack of compelling evidence that other radio stations, media, new entry or buyer power would replicate the important competitive constraints lost by the merger.

D) Unilateral effects in regional West Midlands campaigns

a) Candidate market shares are too high to rule out competition concerns

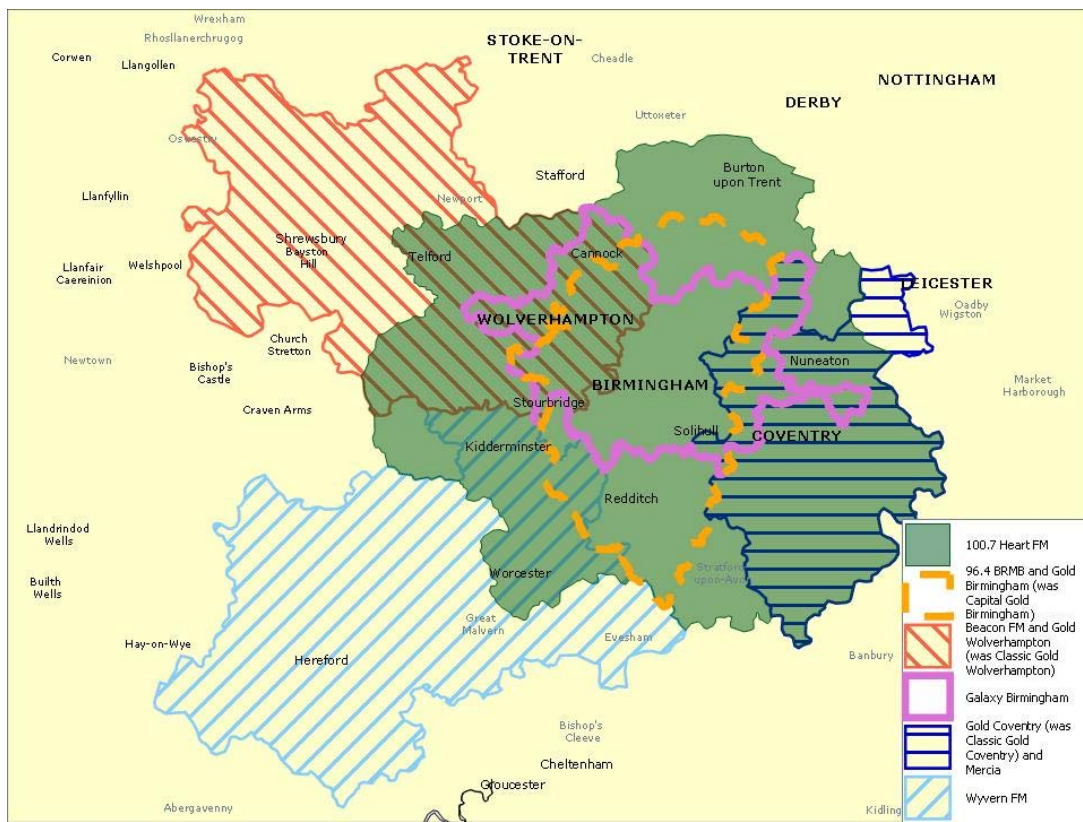
94. The overlap in the West Midlands arises between Globals regional Heart 100.7 and Galaxy stations on the one hand and GCaps local BRMB, Mercia, Beacon, Wyvern and Gold stations on the other hand. In this region, the merged entity is by far the largest radio group with [60-70] per cent and [70-80] per cent of non-contracted agency expenditure and direct customer spend respectively. The next largest radio group is GMG (Smooth) with [10-20] per cent of NCA and [10-20] per cent of DC. Bauer is also present in this region with [0-10] per cent of NCA and [10-20] per cent of DC.

b) The parties stations overlap heavily in geographic and demographic reach

95. The coverage area of Globals Heart 100.7 extends to most of the West Midlands region, including notably Birmingham, Wolverhampton, and Coventry. Galaxy broadcasts to a wide area within the West Midlands region centred on Birmingham. GCaps radio stations have local coverage within the West Midlands region: BRMB broadcasts in the Birmingham area. It can also

be received in parts of Wolverhampton. Beacon broadcasts to the North-West section of the region encompassing Wolverhampton and reaching as far as Oswestry. Wyvern broadcasts to the south west of the region, covering Kidderminster and Worcester. Mercia broadcasts to the Coventry area which is south east of the region. Map 2 set out below shows the geographical location of the Global and GCap radio stations in the West Midlands.

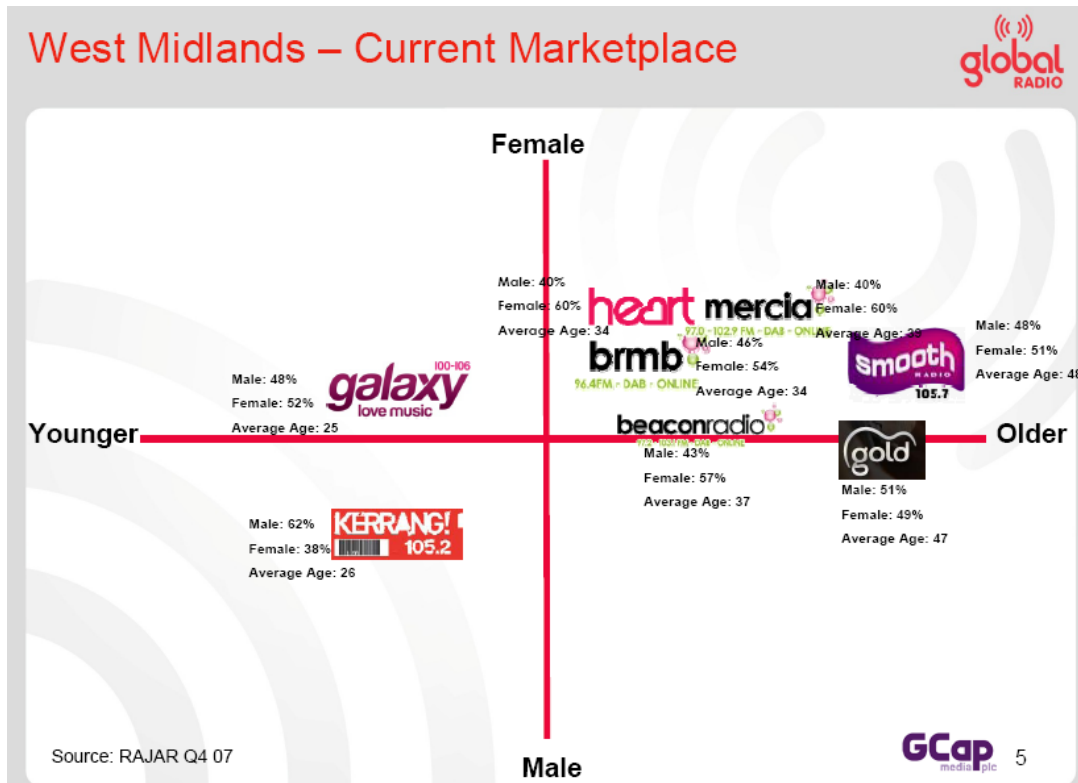
Map 2
Global Radio and GCap stations in the West Midlands



96. For the same reasons as in East Midlands, the OFT considers that, for customers seeking regional campaigns, it is reasonable to conclude that there was competition between the parties for such customers pre-merger. The OFT has therefore examined evidence pertaining to the degree of competition that existed between the parties pre-merger and the extent to which there was and will remain competition from other sources.
97. Finally, as it is the case in the East Midlands area, the parties in the West Midlands appear to be sufficiently close in terms of targeted profiles, as can be seen from Figure 3 below, so as to be considered close competitors from a demographic perspective as well.

Figure 4

Brand map of commercial radio stations: West Midlands



c) Evidence suggests high margins and high diversion ratios between the parties

98. The OFT's analysis, like in the East Midlands, assumes high margins based on the parties submissions. As far as diversion ratios are concerned, the BMRB survey carried out in the West Midlands is illustrated in the following table.

Table 2
Diversion ratios for NCA and DC

10% price rise on	Switch to Global		Switch to GCap		Switch to GMG		Switch to other*	
	NCA	DC	NCA	DC	NCA	DC	NCA	DC
Global			39 (35)	54 (54)	13 (12)	15 (15)	48 (54)	31 (31)
GCap	17 (16)	3 (3)			6 (5)	6 (5)	78 (79)	91 (93)

Notes:

*Other radio and other media.

Figures in parentheses are diversion ratios including don't know answers.

99. Based on these survey results, the diversion ratio to GCap of those Global non-contracted agency customers who knew where they would switch is 39 per cent (and 35 per cent including don't know answers), and of Globals direct customers to GCap is 54 per cent. In the reverse direction, the diversion ratio to Global of those GCap non-contracted agency customers who knew where they would switch is 17 per cent (and 16 per cent including don't know answers), but of GCaps direct customers to Global is just three per cent. This diversion ratio from GCap to Global is low because many of GCaps customers are local advertisers, who would not switch to advertising on Globals regional Heart station (nor to GMGs regional Smooth station or Bauers Kerrang!) but instead would switch to other local radio stations such as The Wolf (UTV) and Touch FM (CN Group). Even though the diversion ratios between the parties in the West Midlands are less balanced than in the East Midlands, taking the results from both of the merging parties shows that the preferred alternative choice for regional advertising customers in aggregate remains the parties radio stations.

100. In addition to the above survey results, which like the East Midlands also rely on small sample sizes, the OFT considers that the prima facie unilateral effect concerns in the West Midlands that arise from the diversion ratio data from the survey are strengthened by additional evidence gathered in the course of the investigation.

d) The parties customers overlap and have expressed concern

101. Third parties have expressed concerns that are similar to those expressed in the East Midlands.

102. Although the parties submit that there are very few customers overlaps between Heart West Midlands and the GCap stations, and further that most of GCaps customers in the West Midlands are local and do not look for regional cover, the following shows that:

- Customer overlaps between Heart and GCap stations are material: of [70-80] non-contracted agency customers on Heart, [30-40] also advertised on one or more of GCaps stations, and of [30-40] direct customers on Heart, [0-10] also advertised on one or more of GCaps stations.
- A significant proportion of GCap customers are regional as opposed to local-only advertisers – comparing Mercia and BRMB which the parties submitted would represent the best overlap with Heart West Midlands: [20-30] of [50-60] non-contracted agency customers advertising on Mercia also advertised on BRMB, and [20-30] of [80-90] non-contracted agency customers advertising on BRMB have also advertised on Mercia in 2007, and [0-10] of [100-110] Mercia direct customers and [0-10] of [100-110] BRMB direct customers have advertised on both stations in 2007.

103. The customer overlap analysis provided by the parties for the West Midlands region shows that a material number of Global customers, in particular non-contracted agencies customers, also advertise on GCap stations. In addition, a significant proportion of non-contracted agency customers buy various GCap stations as a package, whose geographical coverage overlaps with Globals Heart (and to a lesser extent Galaxy) station. As with the East Midlands, the parties did not provide the OFT with complete information on the actual bundles of GCap stations that were being purchased by customers, but provided customer overlap data on the basis of a BRMB and Mercia combination. Nonetheless the number of customers purchasing this combination is already material (approximately [0-10] per cent of each stations total advertisers for direct customers and up to [30-40] per cent of non-contracted agency customers) such that it may be that additional number of customers are purchasing alternative bundles. For these reasons, the OFT does not accept the parties argument that the evidence provided demonstrates a sufficiently immaterial customer overlap between the merging parties for there not to be a realistic prospect of a substantial lessening of competition.

e) Despite buy-around analysis, other radio stations do not dispel concerns

104. The parties submit that there is significant competition from other radio stations in the West Midlands. Smooth is referred to as a key player in the West Midlands as in the East Midlands with a non-contracted agency share of [10-20] per cent and a direct share of [10-20] per cent. In addition, several

other smaller stations are present and in particular Kerrang! owned by Bauer, The Wolf (UTV), Touch FM (CN Group) and Radio XL (independent station).

105. The parties also provided a buy around analysis for the West Midlands, which they claim, demonstrates that purchasers would have the ability to switch a significant proportion of any advertising campaign away from the Global and GCap stations to a combination of Smooth and the other smaller stations referred to above.
106. However, the buy around analysis conducted by the parties for the West Midlands raises the same issues as those arising from the East Midlands analysis (see paragraph 74) and it is therefore not possible for the OFT to place any material weight on the conclusions that the parties claim followed from the buy around analysis.
107. Customers in West Midlands argued that the parties own the main stations in the Midlands. The only alternative option would be GMGs Smooth and Bauers Kerrang!, but their demographic profile are very different to the merging parties radio stations, see Figure 4 above. In particular, one customer argued that it would be extremely harmful to both the industry and to customers if Global were allowed to own Heart and BRMB/ Mercia/Beacon on the basis that there would be no comparable alternative offer, and the negotiating power of local customers would be reduced.

f) Other media will not replicate the constraint lost by the merger

108. Similar to the East Midlands, the parties argued that they are sufficiently constrained in the West Midlands by other media, and provided a number of customer switching examples to support this argument. While this evidence was potentially probative of the constraint of other media, in particular local press, on local radio advertising, the OFT considered that the evidence was limited in relation to the potential constraint of other media on regional radio advertising campaigns.
109. In particular, critical loss analysis based on the aggregate diversion ratios in Table 2 above suggests a market no wider than only radio advertising.²⁰ The aggregate diversion ratio from Global of non-contracted agency customers to other radio stations (GCap, GMG and others) is 57 per cent, and of direct customers is 85 per cent. The aggregate diversion ratio from GCap of non-contracted agency customers to other radio stations (Global, GMG and others)

²⁰ Based on a uniform 10 per cent price increase to each class of customers by a hypothetical monopolist of radio advertising. For a critical discussion of such traditional hypothetical monopolist test-based critical loss analysis, see section A. Market definition in National Analysis in Section III.

is 39 per cent, and of direct customers is 21 per cent. A hypothetical radio-advertising monopolist raising prices by 10 per cent to each of Globals non-contracted agency customers, Globals direct customers, GCaps non-contracted agency customers or GCaps direct customers therefore retains this fraction of business that diverts to other radio advertising.

110. The fraction of business that diverts to non-radio advertising is therefore 100 per cent less this fraction: for Globals non-contracted agency customers this is 43 per cent (that is 100 per cent less 57 per cent), for Globals direct customers this is 15 per cent (that is 100 per cent less 85 per cent), for GCaps non-contracted agency customers this is 61 per cent (that is 100 per cent less 39 per cent), and for GCaps direct customers this is 79 per cent. Given the parties high incremental gross margins (that is between [] per cent) the hypothetical monopolists actual loss in response to a 10 per cent price increase is therefore between [] and [] per cent for Globals non-contracted agency customers (depending on the incremental gross margin assumed, from [] per cent), is between [] and [] per cent for Globals direct customers, is between [] and [] per cent for GCaps non-contracted agency customers and also is between [] and [] per cent for GCaps direct customers.²¹

111. These estimates of the hypothetical monopolists actual loss based on the aggregate diversion ratios in Table 2 do not exceed estimates of the critical loss, which vary between [] and [] per cent (depending on the incremental gross margin assumed, from [] per cent).²² Consequently, on the basis of the high margins and diversion ratios that generate the OFT's prima facie concerns over unilateral effects, the relevant product market in the West Midlands appears no wider than only radio advertising such that other media will not impose a sufficient constraint on the parties.

g) Other countervailing factors are unpersuasive

112. The parties arguments and the OFT's evaluation of them are substantially the same as in the East Midlands.

h) Efficiencies in the West Midlands

113. The parties arguments and the OFT's evaluation of them are substantially the same as in the East Midlands.

²¹ See footnote 51 below for details of the calculation used. The same results apply (that is a relevant market no wider than only radio advertising) if the aggregate diversion ratios including 'don't know' answers are used.

²² See footnote 50 below for details of the calculation used.

i) Conclusion on the mergers effect in the West Midlands

114. Similar to the East Midlands, taking all the above evidence into consideration, the weight of evidence supports a realistic prospect of a substantial lessening of competition in the supply of airtime for regional radio advertising campaigns in the West Midlands. This conclusion derives from (i) high share of supply to NCA and DC customers, (ii) closeness in geographic and demographic reach, high margins and high diversion ratios, at least from Global to GCap stations, (iii) customer concerns, and (iv) a lack of compelling evidence that other radio stations, media, new entry or buyer power would replicate the important competitive constraints lost by the merger.

E) Coordinated effects in the East and West Midlands

115. The OFT does not need to consider whether the merger gives rise to coordinated effects in the East and West Midlands areas on the basis that the remedies offered by the parties and on which the OFT has decided to suspend its duty to refer, will restore the pre-merger situation for regional advertisers in both regions.

CAMPAIGNS IN GREATER LONDON

A) Risk of anti-competitive effects

a) Prima facie indicators of unilateral effects concerns

116. The transaction raises prima facie concerns in Greater London (London) based on the following cumulative considerations:

- High combined shares and increments. As was the case in East and West Midlands, as a simple screening device, candidate market shares based on shares of advertising revenue are too high to rule out competitive concerns. As noted above, for advertisers, the parties share of non-contracted agency and direct customer revenue are the best-available proxy for candidate market shares. The parties combined share of contracted agency advertising in London is [50-60] per cent (increment [20-30] per cent), of non-contracted agency advertising is [40-50] per cent (increment [20-30] per cent) and of direct advertising is [30-40] per cent (increment [10-20] per cent)
- Supply-side constraints. As was the case in East and West Midlands, there is no evidence that post-merger entry by new firms or repositioning

or expansion by existing competitors would be timely, likely and sufficient to eliminate any concerns

- Demand-side constraints. While countervailing buyer power may well apply in respect of certain customers, typically national agencies under annual contracts, who assemble national advertising campaigns of which London stations form a material part, there is no compelling reason to conclude that such protection would extend to those customers running London-wide advertising campaigns only (this being the equivalent of regional campaigns in the East and West Midlands), and against whom London radio suppliers can price discriminate.
- Customer concerns. Two customers using the parties London radio stations to advertise were concerned about the merger:
 - One argued the concentration of revenue share between the Global, GCap and GMG Groups represents an unacceptably large concentration of selling power,²³ and
 - Another one argued that the merger may reduce their negotiating power and their ability to switch stations. While in the short term it may well withdraw advertising, over the longer term clients will feel the need to return to the most popular stations owned by the new group.

117. In respect of London, based merely on the above indicators, the merger raises prima facie unilateral effects concerns warranting closer consideration. As set out in detail below, the OFT therefore examined whether the parties were close competitors prior to the merger, existing pre-merger competition from other rivals absent any specific response to the merger (such as repositioning or expansion), and the presence of merger-specific efficiencies. As set out below, taken together, this evidence was sufficient in aggregate to remove the prima facie concerns raised by the above factors.

b) The parties are not close competitors compared to rival stations

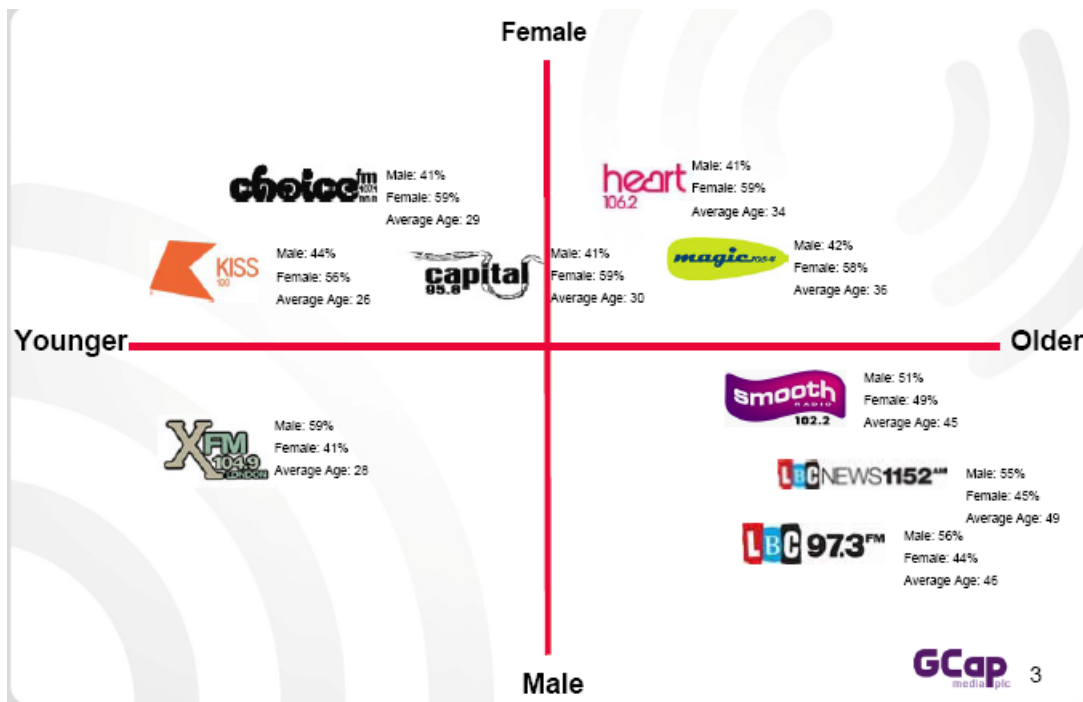
118. A valid unilateral effects theory relies, among other things, upon the parties products being close competitors, in other words, the merger combines the first and next-best choices for a substantial proportion of customers. Internalisation of this competition – the recoupment of sales lost to the other merging firm – provides the ability and incentive to raise price or reduce

²³ Global sells national radio advertising on behalf of GMG but does not sell London-wide advertising, and therefore GMG's share in London should not be included in the competitive assessment of the merged entity at the local London level.

quality profitably post-merger. Critically, however, the evidence in respect of London suggests that the parties are not close competitors and that the greater competitive constraint on each party pre-merger is derived from Bauer.

119. This finding is supported by customer views, discussed below, and evidence on the product positioning of Global and GCap stations relative to rival stations and each other. To illustrate this point, the brand map below (Figure 5) identifies the parties radio stations in London (Heart and LBC for Global, and Capital, Choice and XFM for GCap) and those of their competitors (Bauers Magic and Kiss, and GMGs Smooth), which shows that the listener demographics of the parties stations do not overlap with each other but do with the listener demographics of their competitors stations. This distinction in demographic coverage between the merging parties contrasts with the East and West Midlands areas where the merging parties stations overlap much more significantly in terms of demographic profiles (see Figures 3 and 4).

Figure 5
Brand map of commercial radio stations: London



Source: the parties

120. Virgin radio, not featured above, targets 25-44 year old listeners. It has a slight male ABC1 bias, with a core listenership of 35-44 year olds. As such, it would fit into the demographics chart between Smooth and LBC News on the vertical axis, and parallel with Magic on the horizontal axis.

121. In addition to these commercial stations, the BBC is the prime listening competitor in London (as it is nationally), with each of its five primary stations targeting different demographic profiles: BBC Radio 1 focuses on a 'young' audience, competing most closely with Capital, Kiss and Galaxy. BBC Radio 2 is focused on 'old' audience and is closer to Heart and Magic. BBC Radio 3 is closer to Classic and BBC Radio 4 and 5 are 'speech only' stations. The position of the BBC and commercial radio players in London in respect of audience shares is set out below.

Table 3: Audience Hours – London radio

Supplier	Hours 000	Share Per cent
BBC	70,119	46
Global	22,563	15
GCap	18,012	12
Global + GCap	40,575	26
Bauer	22,019	14
Virgin	6,119	4
GMG	3,732	2
Other	5,653	4
Total	153,434	100

Source: Parties, based on RAJAR Dec 2007

122. Direct customer evidence also points to Bauer being a closer competitor to either of the parties than they are to each other, and to GMG being no less close a competitor to the parties than they are to each other. In particular, in the second BMRB customer survey:

- of six respondents in London who said they would switch some or all of their radio advertising business away from Global in the event of Global increasing its prices by 10 per cent price, four chose Bauer stations (three Magic and one Kiss) to switch to and two chose GMGs Smooth, whereas just one chose GCaps Capital,²⁴ and
- of nine respondents in London who said they would switch some or all of their radio advertising business away from GCap in the event of GCap increasing its prices by 10 per cent price, five chose Bauer stations (three

²⁴ These choices are not mutually exclusive, that is respondents may have chosen more than one alternative to Global.

Kiss and two Magic) to switch to and two chose GMGs Smooth, whereas just one chose Globals LBC.²⁵

123. The OFT notes the relatively small number of responses to the survey in numerical terms. However, of the 31 respondents to the BMRB survey in London, 42 per cent reported advertising budgets of over £1 million, of which 43 per cent on average was spent on radio. Although the absolute numbers of potential switchers appears low, the total amount of money potentially switched appears significant. Consequently, the OFT considers the evidence of potential switching in London from the second BMRB survey as probative of the relative lack of close of competition between Global and GCap.

c) No coordinated effects concerns arise

Horizontal coordinated effects between substitutes

124. The transaction does not combine close substitutes for unilateral effects purposes, but it does reduce the number of major commercial radio competitors in London from three to two, leaving the post-merger Global and Bauer as the two principal commercial players (although Virgin and GMGs Smooth are also significant). Moreover, the survey evidence suggests that non-radio alternatives are not effective substitutes for customers running London radio advertising campaigns, the OFT believes that price discrimination may be possible against such customers purchasing such campaigns, buyer power does not appear in respect of such campaigns, and de novo entry is unrealistic. Accordingly, the OFT considered the possibility that the merger would create or enhance coordination between a duopoly of Global and Bauer post-merger.

125. The OFT considers that in theory radio groups/stations could coordinate around price in three ways. First, radio groups/stations could charge a single CPT to all advertisers, second, they could charge a CPT dependent on the type of advertiser or the total spend of the advertiser and finally, the stations/ groups could tacitly coordinate with respect to each customer on a customer by customer basis.

126. Transparency and simplicity of pricing is vital to the successful collusion of firms in the three ways discussed above. The OFT has examined the transparency of the actual CPT rates charged by the parties and their competitors. It is clear from the investigation that although CPT rates are published, they are not transparent. The main reason for this is that the

²⁵ These choices are not mutually exclusive, that is respondents may have chosen more than one alternative to GCap.

published CPT rates are used as a starting point in negotiations and because the fact that each customer, or agency, negotiates on an individual basis means the actual price paid by each customer will be different and will be unknown to other customers and competitors. The parties submit that there are approximately five features that affect the level of CPT paid by each customer. The features are: brand recognition, how established the radio station is, historical factors, the audience, and, the reach of the station. It is apparent from this list that these features will be different for each radio station. Different customers will also place different weights on these features and so will be willing to pay different CPTs. It is clear from this that pricing is not simple and so it would be difficult for tacit coordination to be focused around charging the same CPT to all advertisers or to different groups of advertisers.

127. It may be easier for radio stations and/or radio groups to coordinate their behaviour if the product or service is homogenous. However, the OFT has found that advertising in radio stations is heterogeneous. The content of the radio stations is different, which reflects the differing audience compositions and sizes. This heterogeneous nature of radio stations is not conducive to coordination across large radio groups with many differing radio stations targeting different audiences. In addition, the post-merger market in London is asymmetric with the merged entity having a significantly different market share than the second biggest firm in the market. Thus, the incentives for coordination are different for the resulting duopoly.

128. In light of the above, and as will be further explained in the analysis of coordinated effects at the national level, the OFT does not consider that this merger will increase the incentive or the ability of radio stations and/or radio groups to tacitly (or explicitly) collude to increase prices.

Coordinated effects from a conglomerate merger

129. Although on the basis of the discussion above, traditional coordinated effects appear unlikely, coordinated effects can still arise from a conglomerate merger such as this in two ways.

130. First, a conglomerate merger might give rise to multi-market contact, which makes coordination easier by making it easier to reach an agreement—by making firms more symmetric and increasing the extent of their interaction—and/or by making enforcement more effective (by allowing for more severe punishments over several markets or by enhancing detection of deviation from the coordinated outcome).

131. Second, the acquisition of complements by merger changes bundling opportunities and, by doing so, may change the sustainability of coordination. That is, if bundling has a negative impact on the profits of a rival then it

makes credible punishment for deviation from a coordinated outcome more severe.

132. However, as with traditional coordinated effects theories, the issue for conglomerate coordination is the extent to which a merger makes a difference to whether coordination will be enhanced in either of these ways. In this regard, the merger does appear to increase multi-market contact between the parties and Bauer: put simply in terms of Figure 5 above, pre-merger GCaps Capital and Choice radio stations are in the top left quarter of the brand map with Bauers Kiss, and Globals Heart is in the top right quarter of the brand map with Bauers Magic, post-merger, then, both Global/GCap and Bauer are in the top left and right quarters of Figure 5. A necessary criterion for this theory of harm is that the merger would make the parties and Bauers market position more symmetric. Table 4 below shows the shares of NCA and DC revenues in London.

Table 4
Shares of non-contracted agency and direct customer revenue in London

Group	Station	Share (per cent)
Global	Heart	[10-20]
Global	LBC	[10-20]
	Total Global	[20-30]
GCap	Capital	[10-20]
GCap	Choice	[0-10]
GCap	XFM	[0-10]
GCap	Gold London	[0-10]
	Total GCap	[20-30]
	Total Global/GCap	[40-50]
Bauer	Magic	[20-30]
Bauer	Kiss	[10-20]
	Total Bauer	[30-40]
SMG	Virgin	[0-10]
GMG	Smooth	[0-10]
	Others	[10-20]

133. However, the multi-market contact arising from the merger does not make the merged Global/GCap and Bauer more symmetric (see Table 4). Consequently, consideration of whether bundling may change the sustainability of coordination by increasing the severity of punishment appears a moot point.

d) No portfolio power concerns arise

134. A unilateral effects theory considers whether a merger creates market power in respect of the merged firm's customers, or significantly enhances it. It does not focus directly on the degree to which pre-merger market power is exercised, which is grandfathered into the analysis: in other words, the focus of the analysis is whether the merger makes things substantially worse for customers, not the degree to which the merging firms in particular enjoy any degree of pre-merger market power. Such power is a question of degree, and in a differentiated product market is related to the brand strength and other measures of customer loyalty and willingness to pay for that firm's product,²⁶ due to actual or perceived quality differences between that and the other products on offer.
135. At the more extreme end, if one or more of the parties stations had such a degree of market power that it qualified as an essential or must have station that customers could not entirely substitute away from at all – the OFT would need to consider the market power that the merged firm might exercise by leveraging that market power across a bundle of stations, whereby customers are incentivised (or at the extreme, in the case of formal tying, obliged) to purchase an optional (or tied) station because they must purchase the essential (or tying) station. This portfolio power theory is discussed in more detail in the conglomerate effect section of the OFT Substantive Assessment Guidance.
136. In London, however, the OFT notes that GCaps Capital station is in decline, having lost [80-90] per cent of its advertising revenue in real terms since 2000. Even if it may historically have been a must have station, it was not viewed by respondents to the two BMRB customer surveys as a must have radio station, which is consistent with its decline in advertising revenues. Similarly, the BMRB surveys reveal that no other Global or GCap radio station in London is considered to be must have. As the survey evidence shows that Bauers Magic and Kiss brands are close substitutes for Global and GCap stations, this further calls into question the must-have or essential character of any of the parties stations – inherent in the concept of must have-market power is that there are no close substitutes to turn to instead. Other evidence corroborates this, pointing to the parties radio stations being more complementary (for example in terms of demographics) than substitutable, but not to them being must have complements. A third party noted that London's commercial radio market is known to be particularly fiercely competitive due to the fact that many stations compete in this area. When discussing London,

²⁶ For example in an end-consumer retail market, geographic proximity to home or workplace will be a factor relevant to pre-merger market power, and in some cases location of the retail outlet may be the primary factor.

another third party stated that whilst theoretically this could be an area of concern, the medium of radio is vulnerable because of its size and lack of importance and therefore it believes any opportunity for monopolistic behaviour is rather unrealistic. As this necessary (but not sufficient) condition for anti-competitive conglomerate or portfolio power effects does not appear to be met, the issue of foreclosure of competing radio stations and resulting harm to customers is unlikely.

137. Consequently, the OFT does not believe that anti-competitive conglomerate effects are an issue in London.

e) Interim conclusion on competitive effects in London

138. On the basis of the above, prima facie concerns arise in London on the basis of unilateral effects, but not coordinated or conglomerate effects. As to the evaluation of the unilateral effects concerns based on the above considerations, there is no doubt that these are above fanciful, which is the minimum standard of belief required to justify a duty to refer, but the question of whether the OFT judges there to be a realistic prospect of a substantial lessening of competition is finely balanced. In the event, it is unnecessary to resolve this essentially interim question, because the evidence on efficiencies is sufficient to tip the balance and ultimately allow the OFT comfortably to rule out concerns that customers would be worse off as a result of the merger, and thus comfortably rule out that any lessening of competition in London would be substantial.

B) Assessment of pro-competitive efficiencies

a) Criteria for efficiencies claims under the Act

139. As the OFT's Substantive Assessment Guidance for mergers make clear, a merger may be expected to lead to a substantial lessening of competition when it is expected to weaken rivalry to such an extent that customers would be harmed. This may come about, for example, through reduced product choice, or because prices could be raised profitably, output could be reduced and/or product quality or innovation could be reduced.²⁷ That is, it is adverse effects on customers that differentiate a substantial lessening of competition, warranting a reference or remedies, from a mere lessening of competition, which requires no further investigation or intervention.

²⁷ See paragraph 3.7.

140. As the Substantive Assessment Guidance further makes clear, the Act allows the OFT to take efficiency gains from a merger into account at two separate points in the analytical framework:

- where they avert the adverse effects of a substantial lessening of competition by enhancing rivalry, and
- where they do not avert a substantial lessening of competition but will nonetheless be passed on after the merger in the form of customer benefits that countervail the adverse effects that would arise from the substantial lessening of competition.

141. Consistent with other agency guidelines, the Substantive Assessment Guidance states that efficiencies claims – at either gateway in the OFT's analysis – must meet the following cumulative criteria. They must be:²⁸

- demonstrable (that is be shown to arise clearly and be very likely to arise within a reasonable period of time)
- merger-specific (that is, be attributable to the merger, as a direct consequence of it judged relative to what would happen without the merger), and
- likely to be passed on to customers.

142. The latter point is relevant as it is customer welfare that is at stake in competitive effects analysis, and in the substantiality of any lessening of competition, and not private gains to the merging parties.

b) Evidentiary burdens on efficiencies: a sliding scale approach

143. The OFT's Guidance makes clear that the evidence required in relation to such efficiencies must be compelling if it is to be taken into account: ...where mergers raise possible competition concerns, the OFT is generally sceptical, in the absence of compelling evidence, that efficiency gains will not only arise but will also be passed on to a sufficient extent to customers, especially where there are few remaining competitive constraints on the parties. Accordingly, in these situations, the evidence presented by the parties on efficiencies and their likely impact on rivalry must indeed be compelling.²⁹

²⁸ See paragraph 4.34 (rivalry-enhancing efficiencies) and 7.7-7.8 (customer benefits exception).

²⁹ See paragraph 4.35.

This discussion of evidentiary standards equally applies to efficiencies qualifying as customer benefits.³⁰ Indeed, it would be odd if this were not the case given that the same efficiency claims may fall for consideration in the substantial lessening of competition test and/or subsequently in relation to the customer benefits exception.

144. The importance of setting appropriate evidentiary burdens should not be underestimated, and where claims are potentially self-serving and outcome determinative to the analysis of what would otherwise be an anti-competitive merger, it is appropriate that the competition authority not easily be persuaded by unverified claims. The OFT's long line of cases involving allegedly failing firms, and the evidentiary standards on counterfactuals in such cases, bear this out.³¹ Moreover, it is unarguable that for a claim for which the evidence can only be in the merging parties hands, it is incumbent on those parties to furnish such evidence and meet the burden of persuasion.

145. At the same time, however, it is not appropriate to read this burden in a way that is impossible in practice ever to meet – so as to render the Guidance academic or Parliamentary intent that customer benefits be able to be taken duly into account at first phase be unfulfilled – or be so rigid and immutable as to be unable to vary according to context.

146. When considered at either efficiencies gateway as a countervailing argument to concerns that lost rivalry will translate into adverse effects on customers, the gravity of the OFT's concerns as to anti-competitive effects is relevant to the overall burden such a countervailing argument must meet to overcome such concerns (and that countervailing argument itself comprises both the compelling evidentiary standard that must be met and the magnitude of efficiencies claimed). This position is consistent with the U.S. and EC horizontal merger guidelines: that beyond meeting a suitable minimum threshold of substantiating efficiencies claims with respect to each of above three criteria, evidence on merger-specific and countervailing efficiencies should be judged on a sliding scale. That is, the greater and more powerful the case in favour of anti-competitive effects of the merger, the greater and more powerful the countervailing claims must be to meet and overcome such concerns. As set out in the US Horizontal Merger Guidelines:

³⁰ There is no reason to think the standard would be lower as an exception to a finding of substantial lessening of competition than in considering whether the lessening of competition is substantial in the first place. The same 'clear and compelling' evidentiary standard is cited in the customer benefits exception with specific reference to a 'multi-market trade-off', that is, where predicted customer harm in one market - consistent with a duty to refer and 'SLC finding' – is outweighed by customer benefits in another market(s). However, the evidentiary standard applies equally to customer benefits. See Guidance at 7.9.

³¹ See *Tesco/Kwik Save*, decision of 20 December 2007, citing previous cases.

The greater the potential adverse competitive effects of a merger ... the greater must be cognizable efficiencies in order for the Agency to conclude that the merger will not have an anticompetitive effect ... When the potential adverse competition effect is likely to be particularly large, extraordinarily great cognizable efficiencies would be necessary to prevent the merger from being anticompetitive. In the Agency's experience, efficiencies are most likely to make a difference in marginal cases when the likely adverse competitive effects, absent the efficiencies, are not great. Efficiencies almost never justify a merger to monopoly or near monopoly.³²

147. This clearly captures the unobjectionable notion that very large harmful effects must correspondingly be outweighed by very large countervailing benefits. But the OFT also applies the point in relation to marginal cases in another sense of marginal – not just that the anti-competitive effects are small, but that the probability of adverse effects occurring at all is small.
148. As should be apparent from recent OFT cases, including the *de minimis* line of cases,³³ what matters when considering anti-competitive effects and the welfare of customers under the substantial lessening of competition assessment is not just the size of market (for example £10 million or £1 billion), the magnitude of the mergers price or non-price effect (for example a 3 per cent or 30 per cent price rise), and the durability of that effect (3 months or 3 years). It also matters how likely such adverse effects are to occur at all, in other words, the confidence the OFT has in its prediction that customer harm will result from the merger. The former factors go to the question: how bad is the harm if it actually happens? The latter question is: how likely is the harm to happen at all? It would be disingenuous to ignore the fact that assessment of post-merger outcomes, both welfare-enhancing and

³² U.S. Horizontal Guidelines (1992, efficiencies section revised in 1997), Part 4. Compare the identical point made in the subsequent 2004 EC Horizontal Merger Guidelines: 'The greater the possible negative effects on competition, the more the Commission has to be sure that the claimed efficiencies are substantial, likely to be realized and to be passed on, to a sufficient degree, to the consumer. It is highly unlikely that a merger leading to a market position approaching monopoly or leading to a similar level of market power, can be [cleared] on the grounds that efficiency gains would be sufficient to counteract its potential anti-competitive effects' (para 84).

³³ See in particular the OFT decision in *Anticipated acquisition by BOC Limited of the packaged chlorine business and assets carried on by Ineos Chlor Ltd* 29 May 2008, paragraphs 118-119.

welfare-reducing, is generally an inherently predictive exercise,³⁴ and is based on probabilities, not certainties.³⁵

149. This applies equally to any prediction that lost rivalry is substantial enough to result in customer harm, which explains why the OFT has deliberately taken it into account in its *de minimis* assessment. While at first-phase the reference test is clearly asymmetric, in that the OFT needs only believe in a realistic prospect of a substantial lessening of competition, from realistic prospect to certainty covers a very wide range of probabilities indeed.

150. It is appropriate, therefore, to take this variability on the facts into account not only in the cost/benefit weighing of the OFT's *de minimis* judgment – which applies only after the OFT has found a duty to refer and a realistic prospect of substantial lessening of competition but also in the weighing exercise of considering the evidence supporting a risk of anti-competitive effects and the evidence supporting countervailing efficiencies. Moreover, while some efficiencies can be characterised as rivalry-enhancing and cognizable under the first gateway, and other scenarios would be cognizable only as customer benefits under the second gateway, the essential exercise of weighing evidence and considering probabilities and scale is common to both gateways. Accordingly, this point should not be limited simply to the *de minimis* and customer benefits discretionary exceptions to the duty to refer, but also to rivalry-enhancing efficiencies claims that are weighed as part of the integral assessment of the SLC test itself.

151. Accordingly, in keeping with a sliding scale approach, the OFT might judge efficiencies evidence to be compelling in resolving concerns where those concerns were relatively moderate, say, based on a 25 per cent probability of future harm, but fail to do so when the probability was, say, above 90 per cent.³⁶ This is consistent with the notion that, in practice, efficiencies will almost never justify a merger to monopoly – because irrespective of the scale of harm, the probability of some significant degree of harm in merger to monopoly scenarios, all else equal, tends to be very high, which means that the probability of, say, variable cost savings that overcome the incentive to raise price must also be correspondingly high. In sum, then, provided always

³⁴ Even in the case of completed mergers, given the OFT's statutory time limits to refer such a case and the incentives of merged firms not to raise prices pending the outcome of the OFT's investigation, the analysis is more likely to be predictive than retrospective. That said, actual post-merger prices rises have been observed and taken into account in certain completed merger references under the Act: see for example OFT decision *Completed joint venture between Stagecoach Bus Holdings Limited and Braddell plc in relation to Megabus.com, Motorvator and Scottish Citylink brands*, 15 March 2006.

³⁵ See OFT Substantive Guidance Assessment Note on the IBA Case, OFT 516a.

³⁶ For example, in the case of a completed merger to monopoly where observable prices had in fact gone up post-merger and there were no cost-related or other reasonable alternative explanation for this, save for the elimination of pre-merger competition.

that the evidence presented by the parties on efficiencies is compelling, the OFT will have regard both to the likelihood of the benefits materialising and the magnitude of those benefits in weighing them against the magnitude and likelihood of adverse effects.

152. The OFT considers it relevant that its concerns in London are marginal in the sense of a finely balanced or marginal judgment as to whether there is even a realistic prospect, let alone a likelihood – of anti-competitive effects, even before consideration of efficiencies. Whilst the evidence must be compelling, its weight must be judged in the context of being a tipping factor when all evidence is considered in its totality, and not as a counterweight to an extraordinarily strong theory of harm where all other evidence points clearly towards customer detriment.
153. In the event, as set out below, the OFT has concluded that rivalry-enhancing efficiencies are indeed sufficient to resolve residual doubts about anti-competitive effects resulting from the loss of rivalry between Global and GCap. The prospect of anti-competitive effects in the Midlands, by contrast, is substantially more clear-cut and of higher probability, and the parties efficiencies claims therefore carried a greater burden of persuasion. This burden they did not meet, at least not in the time left available for OFT consideration of these issues.

c) Demand-side efficiencies as rivalry-enhancing efficiencies

154. As set out below, both types of efficiency credited by the OFT in this case are demand-side efficiencies, which directly benefit customers. As rivals remain in the London market, it is appropriate to characterise these efficiencies as rivalry-enhancing. This is because if the Cournot effects and/or repositioning benefits do in fact materialise, they will improve the merged firms offer to customers. In a market characterised by rival suppliers competing for custom, one suppliers gain is another rivals loss. To the extent that rivals such as Bauer, GMG, Virgin and – critically for audience, albeit not for advertising, the BBC – wish to win those customers back, or win new customers in competition with Global, they too will have to respond competitively, having considered ways to improve the attractiveness of their programming, and improve their value for money to advertisers. Accordingly, such efficiencies ought to make rivals try harder to become more efficient and valuable to customers.
155. As the OFT's ultimate conclusion is that customers in London are likely to be overall better off, rather than worse off, the loss of competition is not substantial, because OFT guidance has defined a loss of rivalry leading to customer harm as critical to the substantiality of that lessening of competition.

Put differently, in analysing the question of the overall effects of the merger through the prism of a process of rivalry, the relatively modest reduction in rivalry achieved by merging the two firms is outweighed by the customer benefits that enhance rivalry among remaining suppliers.

d) Demand-side efficiencies: Cournot effects in London radio

156. The parties claimed that the merger will enable them to price bundles of their complementary radio stations in London more efficiently, from the view-point of advertisers, than either party selling advertising on one or more than one of its radio stations independently. Given the parties complementary radio stations are not must have, there appears to be little risk of this bundling foreclosing access to advertisers for their competitors in London: Bauer, GMG and Virgin.
157. These demand-side efficiencies are known as Cournot effects and arise when products are complements such that lowering the price of one product increases demand for it and for other products that are used with (but not instead of) it. To the extent that products are complements, bringing them under common ownership (for example by merger) internalises the positive effect of a fall in the price of one on sales of the others. Without common ownership, the firm that cuts price does not reap the full benefit of the increased sales of the other products. Consequently, internalising this effect through a merger will result in lower prices for all products in the bundle, because it will become profit-maximising for the firm that sells both complements to sell them at a lower combined price than the sum the customer would have paid to assemble the same package on a mix and match basis pre-merger from two different suppliers. This holds true even before taking into account any one stop shop transaction cost savings from buying only once, rather than multiple times with more than one supplier.
158. The Cournot effect occurs because it solves a double-marginalization problem, thus enhancing allocative efficiency. This is analogous reasoning to that which says that vertical mergers are often efficiency-enhancing because they eliminate the double mark up: that is, pre-merger, each firm independently marks up the price of its product over marginal cost without taking into account the fact that this mark-up will adversely affect sales volumes of the complementary product it does not own. This is the converse of the point that the merged firm will reap the benefit of increased sales of the complement it now owns when it lowers price. The current OFT guidelines do not explicitly capture the above points, other than to say the vertical mergers are often

'efficiency-enhancing' (at paragraph 5.1), but the CC guidelines³⁷ and the EC non-horizontal merger guidelines develop the above point in similar terms.³⁸

159. As suggested by the CC guidelines, this pricing efficiency is all the more likely in instances such the present case where the merging firms had been exercising a degree of market power before the merger.³⁹ This holds true because if pre-merger prices were set in a perfectly competitive market – at marginal costs – there is no room for the price to go down post-merger.⁴⁰ Because in many branded goods markets products enjoy a degree of market power, this assume prices set significantly above marginal cost, and thus the scope for the ability and incentive to lower price post-merger.

160. In addition, as noted, bundling is desired by customers because it serves to reduce transactions costs through one-stop shopping.

The Cournot effects in London are demonstrable and merger-specific

161. The second BMRB survey revealed that 52 per cent of respondents in London used a portfolio of London radio stations and that 19 per cent used radio alone. On this basis, the scope for Cournot effects arising from a merger of complementary radio stations appears material, with 10 per cent (that is, 19 per cent of 52 per cent) of advertisers in London seemingly eligible to be directly positively affected.⁴¹

162. As for the magnitude of any such Cournot effects for these 10 per cent of London advertisers, the parties submitted in response to the OFT's Issues Letter, [] examples from June 2004 to October 2007 of Global lowering its price to direct (that is, non-agency) customers for multi-station campaigns in London. The parties stressed that these multi-station discounts were not for increased volume on any one station but instead were pure pricing complementarities. For eight of these examples, the multi-station discount was

³⁷ CC2: Merger References: *Competition Commission Guidelines* (2003), para. 3.71: 'A conglomerate merger might also involve bringing together of products that are complements. In general, the merger should then increase the incentive to lower prices' and para. 4.44.

³⁸ EC Non-horizontal merger guidelines, (2007), para.13.

³⁹ CC2, para 4.44, which refers to elimination of double marginalisation 'when two non integrated firms both have significant market power'. So the third limb of the efficiency argument in paragraph 141—that efficiencies must be likely to be passed on to customers—does not require there to be the same extent of post-merger rivalry within the market such as it may for other rivalry-enhancing efficiencies (see paragraph 4.34 of the OFT's Substantive Assessment Guidance for mergers) since the pass-on of Cournot effects is in some sense 'automatic'.

⁴⁰ This argument rests on prices being linear, that is set on a per-unit-sold basis (or some variant thereof), rather than being non-linear, that is with a fixed component and then some per-unit increment. Prices for radio advertising are linear (that is are CPT).

relative to the price that the advertiser had actually previously paid shortly before to use one or more of the Global radio stations in isolation, not against some national full-price bundle. The average discount in these eight examples for the same radio station used as part of a bundle compared to when it had previously been used in isolation was [10-20] per cent, ranging from [0-10] per cent to [30-40] per cent.

163. The OFT considers the evidence above to be sufficiently compelling to show that that demand-side efficiencies in the form of Cournot effects are demonstrable and given the evidence above, would arise within a reasonable period of time. The OFT also considers the evidence above to be sufficiently compelling to show that that demand-side efficiencies are merger-specific: the parties already offer multi-station campaign discounts for all of their own radio stations, so it is irrefutable logic that further, incremental discounts on a bundle can only come from adding radio stations owned by someone else (absent the merger). In the examples discussed above, the average discount was [10-20] per cent for moving from one to two stations and [10-20] per cent for moving from two to three stations.

The Cournot efficiencies in London will be passed on to customers

164. Lastly, the OFT considers the evidence above to be sufficiently compelling to show that demand-side efficiencies are likely to be passed on to customers given the parties have the economic incentive to do so: it is profit-maximising to lower the bundled price without regard to rivals reactions, and every aspect of the OFT's current analytical framework of merger assessment is predicated on firms behaving in a profit-maximising manner. As this type of efficiency does not commonly arise in a horizontal merger, and because the OFT's rivalry-enhancing efficiencies section is geared toward such mergers, the Guidance's general comment that rivalry is required to ensure pass-on to customers is inapplicable in this particular context. As noted, the efficiency arises in this case because, although the merger is horizontal to a degree, because it involves a merger of players owning London radio stations which are substitutable to some degree for each other, the parties respective stations are more complementary than they are substitutable, in that customers often purchase airtime from multiple London stations as a bundle to ensure maximum coverage of their advertising campaign, this makes this horizontal merger in London more like a conglomerate merger.

⁴¹ Were better prices achieved by one customer also to enable other customers to get better prices then this would be a conservative estimate.

e) Demand-side efficiencies: product repositioning in London radio

Repositioning in radio broadcasting—background

165. A further demand-side merger efficiency in a two-sided market such as radio can occur as a result of post-merger product or brand repositioning. The basic proposition is that by changing radio stations format and/or programming post-merger in a way that benefits listeners (that is, by greater demographic specialisation by individual radio stations), combined radio stations can achieve a larger and more focussed total audience. The resulting airtime is therefore more valuable to advertisers seeking to reach a large, focussed demographic. This is also known as an indirect network effect or externality.⁴² Economic theory supports this argument,⁴³ and this theory has been validated by empirical evidence specifically in relation to the radio broadcasting sector, albeit in a different jurisdiction.⁴⁴ This suffices to rule any out concerns that such claims should in principle be dismissed as not being recognizable as efficiency claims.

⁴² A direct network effect in a classic market means that an individual user gains a greater benefit, the greater the number of other users, the classic example being the telephone network. An indirect network effect is a benefit to users (here to advertisers) the greater the number of users (here, listeners, and in this case, the more focused the demographics of that audience) on the other side of the two-sided market.

⁴³ See Amit Gandhi, Luke Froeb, Steven Tschantz and Gregory Werden 'Post-Merger Product Repositioning', *Journal of Industrial Economics*, March 2008, pages 49–67, who find that the merged firm moves its product varieties away from each other to reduce cannibalization and its competitors move their product varieties between those of the merged firm. Post-merger repositioning therefore benefits customers by increasing product variety. However, they also find that repositioning affects post-merger prices in two countervailing ways: there is upward pressure on all prices as product varieties spread out but the merged firm's incentives to raise price are reduced as its product varieties move away from each other (as there is less competition between them to internalize).

⁴⁴ See Steven Berry and Joel Waldfoegel 'Do Mergers Increase Product Variety? Evidence from Radio Broadcasting', *Quarterly Journal of Economics*, August 2001, pages 1009–1025, who show that the effect of radio mergers after the US Telecommunications Act of 1996—which relaxed radio ownership restrictions to differing extents in different-sized markets, effectively running experiments on consolidation in markets of different sizes—was to increase the amount of programming variety relative to the number of stations. Other academic work suggests the same changes also improved radio stations' performance in the market, implying that format changes by smaller stations may counter the potential exercise of market power by large radio groups that acquire a substantial share of a particular audience demographic through merger. See Charles Romeo and Andrew Dick 'The Effect of Format Changes and Ownership Consolidation on Radio Station Outcomes', *Review of Industrial Organisation*, December 2005, pages 351–386. By way of guidance for future parties: the OFT notes that while the factual UK- and London-specific evidence was and had to be supplied by the parties, the OFT undertook independent research to validate the theoretical basis of product repositioning claims, and took a proactive approach to such questions: the above material was not supplied by the parties. The process of validating efficiencies claims requires early dialogue with the OFT to stand a proper chance of making a contribution to the analysis.

166. In general, it is repositioning of substitutable brands and not complementary brands that can efficiently internalise this indirect network externality but in London, the parties brands are more complementary than substitutable. Nonetheless, in what follows the OFT discusses brand re-positioning as a demand-side efficiency in London in order to provide within this section of its decision a consistent, self-contained narrative on the OFT's treatment of efficiencies in merger control, rather than leaving the reader to piece together such a narrative from isolated discussions at several places elsewhere in this decision. Section C below further provides a comparative overview of the OFT's analysis of efficiencies in London and the Midlands to this end.

Demonstrability of efficiency claims based on post-merger product repositioning

167. Efficiency claims based on post-merger product repositioning are, like any claim, susceptible to the objection that there is no guarantee that such plans will be carried out, and that, even if attempted in good faith, such plans may fail.

168. In addressing the issue of the demonstrability or verifiability of such claims, evidence of industry practice, and in particular efficiencies from previous acquisitions, can be particularly useful in demonstrating that, based on successful and analogous past experiments, efficiencies will be a plausible and potentially likely result of the merger.⁴⁵ While past success is not guarantee of similar future benefits, a track record inspires greater confidence.

169. The parties provided details of peoples track records, now working with Global, of brand repositioning for radio in the UK, which showed their success in segments of the market where GCap had failed, in developing Magic in London and in launching Heart (in the Midlands and London) and Galaxy (in the Midlands). These case studies are discussed in the Annex.

170. The parties plans to reposition their brands in London as shown in Table 2. According to those plans, Heart is not repositioned post-merger but Capital becomes [], whereas Choice becomes []. While these demographic shifts do not appear stark – and not in the order of some of the format changes applicable in the U.S. empirical examples – there is some customer support for the value of such repositioning (see below), and the proposition is that even modest shifts by age and gender mix can attract marginal listeners who will tune in now that the overall programming format of that station caters that degree more to their tastes in music, talk and other content.

⁴⁵ For an equivalent view, see *Prepared Remarks of Dr. Michael A. Salinger, Director, Bureau of Economics, Federal Trade Commission, before the Antitrust Modernization Commission: Treatment of Efficiencies in Merger Enforcement*, 17 November 2005.

Table 5
Parties plans for brand repositioning in London post-merger

Demographics	Heart		Capital		Choice	
	Pre	Post	Pre	Post	Pre	Post
Male (per cent)	41	[]	41	[]	41	[]
Female (per cent)	59	[]	59	[]	59	[]
Average age	34	[]	30	[]	29	[]

171. Unusually in this case, the OFT received customer responses – and the relevant customers are all significant customers of the parties London stations, among others – that were favourable about the merger in general, and some effectively expressed the view that brand re-positioning, among other merger benefits, would be a favourable development:

- According to the Times, a spokesman for media buyer ZenithOptimedia, said: Obviously consolidation does mean a decrease in competition, which we see as an issue, but a stronger radio operator means better funded programming and greater strength to take on the BBC. It will make radio a much better proposition for advertisers.⁴⁶
- One third party stated that the merger will enable a number of changes to be made in the positioning of Globals overall portfolio of brands. This will reduce music overlap between services and enable its portfolio to be more distinctive. As a result, the Global portfolio will have wider appeal to a larger audience. The same third party added that the merger will be beneficial to commercial radio, helping to reverse its declining share of audience against the high budget of the BBC.
- Another third party argued that cost savings resulting from the merger can be used to grow the brand and improve content. In addition, it noted the reduction in the number of sales houses will create time savings for the agency. The same third party further noted that the merger will be rivalry-enhancing, in the sense that it will lead to stronger competition with the BBC.
- Finally, according to another third party, the merger is the finalisation of a process that will lead to two/three radio networks being able to offer a simpler national purchasing process at a more competitive price.

⁴⁶ See Times online, *Global could face competition investigation*, 1 April 2008, at http://business.timesonline.co.uk/tol/business/industry_sectors/media/article3660567.ece

172. The parties submit that these demand-side brand repositioning efficiencies are very likely to arise given:

- the need to revitalise the commercial radio sector, which has seen its share of listening drop at the expense of the BBC from 50 per cent in 1999 to 41 per cent in 2008 causing commercial radio revenues to fall by 17 per cent in real terms,
- GCap is in particular need of restructuring having seen its stations in London and the Midlands figure significantly in this decline with Capital losing [80-90] per cent of its advertising revenue in real terms since 2000 (see Figure 3 above) and with its Midlands stations (Beacon, BRMB, Leicester Sound, Mercia, Ram and Trent) losing between [20-30] and [50-60] per cent of advertising revenue in real terms in the same period. [], and
- the way to deal with the issues above is by brand re-positioning, for which Global has a demonstrable and successful track-record (see paragraph 144 above and Annex).

Repositioning is merger-specific

173. The parties submitted that these demand-side brand re-positioning efficiencies would not be possible absent the merger because, absent the merger, there is an incentive on both parties (separately) to seek to capture as much as demographic space as possible, effectively chasing the middle ground. This phenomenon is underlined by Figures 1 and 2 – the brand maps provided of the East and West Midlands.

174. As a result, it is only upon the bringing of the different stations under common ownership that it would be rational for the owner of those stations commercially to take the decision to differentiate the stations further in terms of demographic space. This claim gains weight, because it is consistent with the U.S. evidence on product repositioning of radio stations format that occurred after a wave of mergers following U.S. deregulation of ownership restrictions, but not before it.

175. Finally, unlike efficiencies based on the combination of complementary physical assets, these product repositioning claims depend substantially more on the value of human capital – skilled staff with know-how that can manage and reposition brands and the programming format and other aspects associated with the station pre- and post-repositioning: in short, knowing what will expand a UK radio audience in a demographically-targeted way, thus driving advertiser value and increasing advertising revenues.

176. Although not mentioned in OFT guidance, a standard and often very valid caution in respect of know-how or managerial efficiencies is that they are not merger-specific, because managers and skilled staff are hardly unique to the merging and in particular the acquiring firm: absent the merger, the target firm could hire new comparable management and/or skilled staff. Yet it seems uncontroversial as a general proposition – outside the narrow context of efficiencies in merger control – to observe that the competitive performance of a firm can vary greatly depending on its management, brand strategy, and so forth and that such skills may be in short supply. It also appears a valid general observation that a good faith motivation for some mergers is indeed that the acquiring managements believe that it has the know-how to improve the target firms proposition to customers relative to the incumbent (and any other alternative team), and in some case, that combining new management with the retention of certain key staff of the target (and their knowledge) may be a vital combination of human capital to realizing improvements in quality, progress on innovations, and so forth.
177. It is therefore inappropriate to conclude that, in principle, managerial and know-how efficiencies are inherently not recognizable for these purposes, although they will be difficult to attest,⁴⁷ and it will be appropriate to apply the overall evidentiary safeguards discussed above in relation to all efficiencies claims: evidence of a mere good faith belief that the acquirers management can do better will not be sufficient: compelling evidence will be required.
178. As to the weight to be attached to such claims, the track record of the individuals and firms they are associated with, and corroboration from customers, can be valuable tools in deciding whether such claims are unduly speculative or should be credited as merger-specific. As noted above, both factors apply in this particular case.

Repositioning benefits will be passed on to customers

179. Unlike in certain other contexts, there is no issue in such efficiencies claims about whether cost savings will be passed on to benefit customers. Inherent to the proposition of improving the product to listeners and advertisers is that both sides of the two-sided market are direct and simultaneous beneficiaries of the strategy. While the merged firm must also stand to benefit from such a strategy, that does not result in a balancing of who appropriates the benefits – rather, all three groups – radio provider, listeners and advertisers are better off if the strategy is successful. The radio provider gains extra revenues, and may even be able to post higher CPTs to reflect the higher value product (more listeners will simultaneously hear that advert) – but if so, that would reflect a

⁴⁷ For an equivalent view, see *ibid.*

more valuable product to advertisers, leaving them better off. (Recall that radio is not a commodity product, it is the quality-adjusted price or value-for-money proposition that matters, not merely the headline price itself).

f) Supply-side efficiencies

180. The OFT has considered whether supply-side efficiencies – notably the cost savings claims made below – should appropriately be considered (only) under the second gateway under the Act, the customer benefits exception, rather than as a rivalry-enhancing efficiency. In the event, it was unnecessary to decide the issue at present as they are not necessary for the assessment of the merger in London. For convenience, and because they supplement the demand-side efficiencies analysis in one respect (see below), they are discussed below.
181. The parties submit that Globals financial model for the integration of the Global and GCap businesses would result in £[30-40] of cost savings in synergies in total. Of this £[30-40], £[0-10] are in the Midlands and the bulk of the remaining £[30-40] are in London. However, many of these savings appear to the OFT to be fixed costs. As the OFT's Substantive Assessment Guidance for mergers makes clear, supply-side rivalry-enhancing efficiencies of this kind are more likely to be taken into account where they impact on marginal or variable costs, as such cost savings tend to stimulate competition and are likely to be passed more directly on to customers in terms of lower prices (because of their importance in short-run price setting behaviour). Generally, savings in fixed costs will not be given such weight as they are not so important in short-run price formation. However, fixed costs may also be important in short-run price formation where, for example, competition takes place via a tendering process and bids reflect both the fixed and variable costs of the tendered service.⁴⁸
182. Although the parties do tender to supply radio advertising by submitting bids to advertisers, the parties submit that bids do not reflect the fixed costs of the tendered radio advertising service to any great extent. Consequently, the OFT in this case does not credit the major, fixed component of the substantial cost savings in London identified by the parties as rivalry-enhancing supply-side efficiencies.
183. In differentiated products markets, the extent of pass through of marginal cost savings into lower prices that benefit customers is determined largely by the curvature of demand and idiosyncratic properties of particular functional forms for demand. Paradoxically, then, demand properties that lead to larger

⁴⁸ See paragraph 4.33, footnote 27.

incentives to raise price from mergers also lead to greater pass through of compensating marginal cost reductions that have the reverse incentive to lower price.⁴⁹ In this regard, the OFT notes that the merger does not appear to increase the parties market power much in any event, so marginal or variable cost savings do not appear more likely to be passed on as a result of the merger.

184. Nonetheless, the OFT accepts that the fixed cost savings in London identified by the parties will be used to help fund the repositioning of their stations post-merger, reinforcing the discussion of demand-side rivalry-enhancing efficiencies above.

C) London and the Midlands: a comparative overview of the OFT's analysis

185. The OFT considers that, on the basis of the above and considering all the evidence in the round, the merger of Global and GCap in London is at worst a lessening of competition but not a substantial one because:

- the parties are not close competitors, and
- there are demonstrable, merger-specific, rivalry-enhancing, demand-side efficiencies in London, principally in the form of Cournot effects, that are likely to be passed on to customers.

186. As the first point made the unilateral effects case finely-balanced, the latter point acted to tip the balance in favour of clearance, and did so comfortably based on the sliding scale approach outlined above.

187. By way of comparison to the Midlands conclusion, the Cournot effects applicable to the combination of complements in London does not apply in the Midlands, where the merger effect is to combine close substitutes – which is also the very reason why the OFT's unilateral effects concerns were pronounced for regional campaigns in these areas. The absence of Cournot effects in the Midlands meant that the countervailing demand-side efficiencies analysis hinged on the repositioning evidence in the Midlands. Given part of the reason post-merger brand repositioning can be pro-competitive is that rivals position their brands between the repositioned brands of the merging parties, some of the potentially pro-competitive impact of brand re-positioning in the Midlands was lost as there are too few competing regional brands to do this.

⁴⁹ See Gregory Werden, Luke Froeb and Steven Tschantz 'The Effects of Merger Efficiencies on Consumers of Differentiated Products', *European Competition Journal*, October 2005.

188. For this reason, this more limited claim of countervailing benefits in London, combined with the greater persuasive burden applicable given the strength of the OFT's concerns in the Midlands, meant that such claims required extraordinary close scrutiny to ensure they were powerful enough to offset concerns, consistent with the sliding scale approach outlined above. While in principle the OFT may have been able to resolve this issue and conduct a robust weighing exercise had further time available, the necessary confines of first-phase merger control meant this was not possible in this particular case. As such, the OFT must resolve doubts in favour of its duty to refer in the East and in the West Midlands.

189. For convenience, the OFT attaches a summary table comparing the efficiencies issues and opposite outcomes in London and the Midlands.

Table 6
Overview of efficiencies claims in London and the Midlands

Issue	London	Midlands
Anti-competitive effect concern (pre-efficiencies claims)	Weak – parties are not close competitors	Strong – parties are 1 st and 2 nd choices for regional advertising campaigns
Cournot effect efficiency claim (merger of complements)	Yes – merger of complements (weak substitutes) for London-wide campaigns	No – merger of close substitutes (for regional campaigns)
Product repositioning efficiency (indirect network effect)	Some credit given – some repositioning will occur given multiple stations in same geographic market (though products already pushed apart (that is, complementary pre-merger))	Prima facie stronger claims (pushing substitutes apart from a former middle-ground cluster, but complicated in that each Midlands area not a single geographic market like London)
Variable cost savings	Not claimed / substantiated	Not claimed / substantiated
Fixed cost savings	Large savings claimed, but not demonstrably passed on	Small savings claimed, not demonstrable passed on

REGIONAL MARKET DEFINITION

190. As discussed above, the OFT takes the view that defining the relevant market is not necessary for the present regional competitive effects analysis, but is of relevance to the de minimis assessment carried out below.

A) East and West Midlands

191. In this context, given the survey evidence and third party comments gathered in the course of the investigation, the OFT believes that the merged entity, with combined candidate market shares of [70-80] and [70-80] per cent in West and East Midlands respectively will be in a position to raise prices in both areas. In turn, it follows from these findings that a hypothetical monopolist would be able to do likewise, consistent with the critical loss analysis in the unilateral effects section above. Therefore, the OFT considers that the two relevant markets affected by the merger are the supply of radio airtime for regional campaigns in the East and West Midlands, respectively.

B) London

192. Evidence gathered in the course of the investigation also points to a separate relevant market for radio advertising in London. Indeed, neither the survey evidence nor third party comments suggest that other advertising media are effective substitutes to radio advertising in London. In any event, given that the merger does not raise competition issues in London, the OFT does not consider it necessary to conclude on market definition in the London area.

SECTION III — NATIONAL AND OTHER OVERLAPS

NATIONAL ANALYSIS

A) Market definition

193. The parties submitted that the relevant market at the national level is wider than only radio advertising and extends to other media such as press and television. In support, the parties pointed to two critical loss analyses based upon the two BMRB surveys, both of which indicated that—in response to a 10 per cent increase in the price of radio advertising—a sufficiently large number of customers would switch all or some of their advertising expenditure away from radio to render such a price increase unprofitable.
194. Product market definition based upon survey work at the national level does not aid the regional competitive effects analysis discussed above. However, product market definition may be important for national unilateral effects analysis and is important for national coordinated effects analysis. This section therefore discusses national product market definition.
195. As described above, the parties approached national product market definition using critical loss analysis (CLA). In CLA the critical loss is the percentage decrease in output that just makes unprofitable a SSNIP by a hypothetical monopolist of some narrow candidate market. The actual loss is the predicted percentage decrease in sales in response to such a SSNIP by the hypothetical monopolist. If the actual loss exceeds the critical loss, then the relevant market appears wider than the narrow candidate market considered.
196. As is conventional in CLA, the parties based estimates of the hypothetical monopolists critical loss on incremental gross margins, which they assumed to be between [] per cent: the parties told us that the increment to which this gross margin applied was an extra minute of radio advertising.

For a SSNIP of 10 per cent, this implied a critical loss of between [] and [] per cent.⁵⁰ That is, depending on the incremental gross margin, a hypothetical monopolist would find a 10 per cent SSNIP unprofitable if, in response, it lost between [] and [] per cent of its sales.

197. The parties estimates of the predicted loss of the hypothetical monopolist in response to a 10 per cent SSNIP (the actual loss) came from the two BMRB surveys. In the first, 67 respondents who were non-contracted agency and direct corporate customers in London and the Midlands were asked inter alia what they would have done had the cost of their last advertising campaign been 10 per cent higher. In response, 14 per cent said that they would switch all of their advertising budget to another medium and a further 26 per cent said that they would switch some of their budget to another medium. The parties took this as an estimate of the actual loss (that is, 14 per cent plus some fraction of 26 per cent) and, because this exceeded the critical loss of between [10-20] and [10-20] per cent (depending on the margin assumed), submitted that the market was wider than only radio advertising.

198. In the second, 154 respondents who were non-contracted agency and direct corporate customers in London and the Midlands were asked inter alia what they would do if the price of advertising on all radio stations increased by 10 per cent. In response, 16 per cent said that they would switch all of their advertising budget to another medium and a further 27 per cent said that they would switch some of their budget to another medium (with most responding that they would switch around half of their budget). The parties took this as an estimate of the actual loss (that is, 16 per cent plus around half of 27 per cent) and, because this exceeded the critical loss, submitted that the market was wider than only radio advertising.

199. The OFT did not consider this analysis persuasive for three reasons. First, the increment of business lost to a SSNIP that the parties used in their estimates of the critical loss was a minute of advertising. However, the evidence submitted by the parties on discounts for multi-station campaigns (discussed above) indicates that when the parties tender to supply an advertising campaign, they do not submit a per-minute price but rather a price for the whole campaign. This suggests that the relevant increment in the incremental margin is an advertising campaign, not a minute of advertising. Because more costs are variable over the course of a campaign than are variable over one minute, the incremental gross margin for a campaign is lower than the

⁵⁰ As is conventional in CLA, the parties calculated the critical loss as the SSNIP divided by the margin plus the SSNIP. For example, for an incremental gross margin of [] per cent and a SSNIP of 10 per cent, the critical loss is $0.1/([]+0.1)=[]$ per cent. For an incremental gross margin of [] per cent and a SSNIP of 10 per cent, the critical loss is $0.1/([]+0.1)=[]$ per cent.

incremental gross margin for one minutes advertising. The impact of using a lower incremental gross margin in the calculation of critical loss is to make the critical loss higher. Consequently, it is not clear to the OFT that the parties estimate of the actual loss would exceed the critical loss.

200. Second, in the first BMRB survey, respondents were asked what they would have done had the price of their last advertising campaign been 10 per cent higher. This is not the same as asking about all radio prices increasing by 10 per cent, which is the traditional implementation of the hypothetical monopolist test. Nonetheless, this question in the first BMRB survey does provide an estimate of the aggregate diversion ratio, that is, the fraction of sales lost by one product (or bundle of products in this case) when its price alone rises by a SSNIP that go to other products (or bundles of products) in the candidate market. This estimate of the aggregate diversion ratio can also be used in CLA to obtain an estimate of the actual loss, however, albeit by applying a different formula to the one used by the parties.⁵¹ Using these estimates of the aggregate diversion ratio from the first BMRB survey gives estimates of the actual loss that do not exceed the parties critical loss estimates, suggesting a market no wider than radio advertising only.⁵²

201. Third, in the second BMRB survey, respondents were asked what they would do were the price of all radio advertising to increase by 10 per cent. However, given the practice of bilaterally negotiating prices, it is not clear that a hypothetical monopolist of all radio stations would increase all prices by 10 per cent. Instead, asking whether such a hypothetical monopolist might profitably implement a price-discriminating SSNIP might be a more sensible—though less traditional—thought experiment for market definition. The second BRMB survey cannot provide an estimate of the actual loss by a price-discriminating hypothetical monopolist. Further, the critical loss for such a

⁵¹ The formula for the actual loss is $(1-a)*(s/m)$ where a =aggregate diversion ratio, s =SSNIP and m =incremental gross margin. See Joseph Farrell and Carl Shapiro 'Improving Critical Loss Analysis', *Antitrust Source*, February 2008, pages 1–17.

⁵² In particular, assuming that the 26 per cent of respondents who would have switched some of their advertising budget would have switched half of it (consistent with the results of the second BMRB survey), then 27 per cent (that is 14 + 13 per cent) of business would have been lost to other media following a 10 per cent price increase. This implies 73 per cent (that is 100 – 27 per cent) of business would have diverted to other radio stations, given no respondents said that they would continue to advertise on radio and pay the extra amount. With this estimate of the aggregate diversion ratio of 73 per cent, the actual loss for a 10 per cent SSNIP assuming a [] per cent incremental gross margin is $(1-0.73)*(0.1/[])= []$ per cent, and the actual loss for a 10 per cent SSNIP assuming a [] per cent incremental gross margin is $(1-0.73)*(0.1/[])= []$ per cent. These estimates of the actual loss are less than the respective estimates of the critical loss of [] and [] per cent respectively, implying a market no wider than radio advertising only.

price-discriminating SSNIP is higher, hence it is not clear that such an estimate of the actual loss would exceed it.⁵³

202. Consequently, to the extent that product market definition matters to the analysis of national competitive effects, then on the basis of the above, the product market appears to be no wider than radio advertising only.
203. Given that the product market at the national level appears to be no wider than radio advertising only, the OFT's analysis next asks whether the parties combined market share is high enough to warrant concerns over unilateral or coordinated effects. The parties combined share of national radio advertising revenues amounts to some [40-50] per cent⁵⁴ and will therefore constitute the biggest commercial radio group in the UK. This is too high to rule out competition concerns.

B) Unilateral effects

204. The merged firms station portfolio combines Globals existing strength of well known and recognised radio brands (Heart / Galaxy) with GCaps wide geographic coverage. In that sense, the merger amounts to a conglomerate, with the exception of London and the East and West Midlands where it creates horizontal overlaps.
205. Self-evidently, any genuinely national advertising campaign must include the Midlands. Therefore, Midlands stations sold as part of a national bundle to contracted agency customers are therefore likely to provide the new entity with significant market power post merger.
206. One customer mentioned that, while GCap currently clearly has a much larger market share and more stations than Global, they are close competitors. Access is required to the major centres of population and the larger stations which these groups both own. Currently they compete for advertisers spend on both national and local campaigns.
207. The parties argued that, faced with the prospect of price increases for national campaigns based on any acquisition of market power in the East and West Midlands, customers would be able to respond by threatening to adjust (and

⁵³ The formula for the critical loss with a price-discriminating SSNIP is simply the SSNIP divided by the incremental gross margin. See Øystein Daljord, Lars Sørgard and Øyvind Thomassen 'Making sense of market delineation with the aggregate diversion ratio', *Journal of Competition Law and Economics*, June 2008, pages 263–270. For example, for an incremental gross margin of [] per cent and a SSNIP of 10 per cent, the price-discriminating critical loss is $0.1/[] = []$ or [] per cent. For an incremental gross margin of [] per cent and a SSNIP of 10 per cent, the price-discriminating critical loss is [] per cent.

actually adjusting) the allocation of their overall advertising spend such that they reduced the radio component and partially substituted part of their overall budget to other advertising media. The OFT accepts that, to the extent that radio advertising is generally used as a secondary or complementary component to an overall advertising package (particularly where national campaigns are concerned), it appears possible for customers to flex the proportion spent on different media. However, the OFT does not have evidence – in particular given the context of a radio-only market – that such flexing would be sufficient to prevent any unilateral effects arising at a national level by reason of the creation of market power in the East and West Midlands.

208. Additionally, the parties submit that discounted prices offered to customers as a result of bundling radio stations complements at the national level is likely to offset the new entity's incentive to increase prices in the Midlands. Finally, the OFT, as outlined above, has come to the conclusion that the merger does not raise concern in London.

209. The OFT has not found it necessary to conclude whether the merger gives rise to a realistic prospect of a substantial lessening of competition at a national level (through the creation of market power in the East and West Midlands). This is because, even if this were the case, the OFT considers that any remedies offered in the East and West Midlands area that are sufficient to address comprehensively the substantial of competition in those regions would alleviate also any issues arising as a result of the merger at the national level.

C) Non-horizontal effects

210. Some third parties have expressed concerns about possible conditional selling whereby the merged firm may tie sales of advertising space on less desirable stations to its most highly demanded or must have stations, thereby providing less value for money to customers, including denying the opportunity to mix-and-match between the parties and other stations, should they wish to do so. Some rivals to the merged entity have also raised foreclosure concerns.

211. However, the OFT is not persuaded that these concerns are valid in the present case, broadly in line with its analysis of similar allegations in *Capital/GWR*.⁵⁵ Principally, the evidence before the OFT does not establish that (absent the East and West Midlands) the parties have stations to which there was no alternative. To the extent that the parties individually had strong positions in any local regions pre-merger, this would not be changed as a

⁵⁴ Note that GCap does not account for all of GMG's airtime sales.

⁵⁵ *Anticipated acquisition by Capital Radio plc of GWR Group plc*, 22 December 2004.

result of the merger, as it was only in the East and West Midlands and London that the merger created horizontal overlaps between the parties.

212. In addition, as noted in Capital/GWR, it would seem more attractive to the parties to extract maximum revenue from their most highly demanded stations without engaging in strategic behaviour (such as tying). Tying tends to reduce value for money to a customer, inducing the customer to reduce purchases of the less heavily demanded station and thereby reducing profit for the firm overall. This would only be a profitable strategy in the long-term if the effect of the conduct is to foreclose competitors, however, there is no substantive evidence available to the OFT to suggest that the parties would successfully be able to foreclose competitors at a national level as a result of the merger.

D) Coordinated effects

213. As discussed above, market definition is important for national coordinated effects analysis. It was found that the product market is for radio advertising only. It is clear that the scope of the product market is crucial to the analysis of coordination and market concentration. Theory suggests that a collusive oligopoly, acting as one, could raise prices. The OFT has examined the effect that this transaction will have on the radio stations and or radio groups ability and incentives to collude either tacitly or explicitly.

214. Third parties have raised two concerns regarding possible tacit collusion in the post-merger market. One of the concerns relates to the merged entity and Bauer coordinating by not competing strongly in each others territory. The second concern relates to a tacit price fixing strategy in the post-merger market.

215. As regards the first concern, the value of contracted and non-contracted/direct advertising emanating from each area where Bauer and the merged entity are active varies significantly. Thus, the incentives of either Bauer or the merged entity to not compete strongly in each others areas are mitigated by the fact that the profitability of these areas varies and thus the incentives to deviate are significant. In addition, the required divestitures in East and West Midlands remove the overlap of the parties and make part of the divestiture available to a competitor. Thus, the market power of the merged entity in these areas is reduced and thus the incentives of Bauer to deviate increase.

216. As regards the second concern, the OFT considers that in theory radio groups/stations could coordinate around price in three ways. Firstly, radio groups/stations could charge a single CPT to all advertisers, secondly, they could charge a CPT dependant on the type of advertiser or the total spend of

the advertiser and finally, the stations/ groups could tacitly coordinate with respect to each customer on a customer by customer basis.

217. Transparency and simplicity of pricing is vital to the successful collusion of firms in the three ways discussed above. The OFT has examined the transparency of the actual CPT rates charged by the parties and their competitors. It is clear from the investigation that although CPT rates are published, they are not transparent. The principal reason for this is that the published CPT rates are used as a starting point in negotiations and, because the fact that each customer or agency negotiates on an individual basis means the actual price paid by each customer will be different and will be unknown to other customers and competitors. The parties submit that there are approximately five features that affect the level of CPT paid by each customer. The features are: brand recognition, how established the radio station is, historical factors, the audience, and, the reach of the station. It is apparent from this list that these features will be different for each radio station. Different customers will also place different weights on these features and so will be willing to pay different CPTs. It is clear from this that pricing not simple and so it would be difficult for tacit coordination to be focused around charging the same CPT to all advertisers or to different groups of advertisers.
218. The OFT has also found that it would not be possible for coordination to be based on charging a CPT rate based on the total spend of the advertiser. This is because many agencies negotiate share deals, which specify the proportion of the total budget that the agency allocates to spend on radio that will be spent with the radio station or radio group. When these negotiations are taking place the radio stations are not aware of the revenue that will be gained from the share deal. Therefore, making coordination on this basis difficult.
219. As regards coordination on a customer-by-customer basis, it may be easier for radio stations and/or radio groups to coordinate their behaviour if the product or service is homogenous. However, the OFT has found that advertising in radio stations is heterogeneous. The content of the radio stations is different, which reflects the differing audience compositions and sizes. This heterogeneous nature of radio stations is not conducive to coordination across large radio groups with many differing radio stations targeting different audiences.
220. As discussed in the OFT's Substantive Assessment Guidance for mergers, the OFT suggests that in order for coordination to be sustainable the market conditions would have to be conducive to tacit coordination so that it isn't disrupted. In this case, as discussed above,

advertising agencies may have countervailing buyer power, which may be enough to destabilise any coordinated behaviour.

221. In light of the above, the OFT does not consider that this merger will increase the incentive or the ability of radio stations and/or radio groups to tacitly (or explicitly) collude to increase prices.

OTHER OVERLAPS

A) DAB multiplex ownership

222. DAB multiplex ownership is restricted by the Communications Act 2003. One person may not control more than one national DAB multiplex. A person who controls a local/regional DAB multiplex may not control a second such multiplex if it overlaps with, or is overlapped by, the first by 50 per cent of more in either direction. Global currently has a [] per cent stake in MXR Limited and GCap a [] per cent stake. As a result of the merger, it will acquire GCap's stake in MXR, giving the merged entity a controlling stake of [] per cent in MXR. MXR owns five regional multiplex licences: North East, North West, Yorkshire, South Wales and the Severn Estuary, and West Midlands. The overlap arising as a result of the transaction covers the West Midlands and the Severn Estuary. The OFT understands that divestments will be required in those areas to deal with the overlaps: Global will be required to divest certain of its digital services following the acquisition of GCap in Nottingham (Gold Nottingham and one of Galaxy, Xfm or Chill) and Swindon & West Wiltshire. Direct and indirect radio advertising should be taken to encompass sale of advertising on digital and analogue stations.

223. Multiplex licences generally last for 12 years and can be renewed once, with the exception of new local multiplex licences issued by Ofcom since 2003 which are not eligible for renewal. Contracts between multiplex owners and digital broadcasters (digital sound programme service providers, or DSPSPs) tend to be entered into for the full duration of a multiplex licence (12 years), and it is unusual for a contract to permit increases in price during the contract term. Overcapacity in digital radio frequencies means that price increases would be unlikely. The issue of over-capacity was acknowledged by the OFT in its decision on Capital Radios acquisition of GWR and by Ofcom in its Review of Media Ownership Rules in 2006.

224. The terms and conditions of contracts entered into with DSPSPs are regulated by Ofcom and must provide for non-discriminatory access. In addition, Ofcom is free to allocate available spectrum between different uses as it sees fit as it is not constrained by any statutory restrictions other than its general duties to

secure the optimal use of spectrum. Additional licences to those already identified by Ofcom may be available if additional frequencies can be found. Alternatively Ofcom could agree a move to DAB + technology which uses spectrum more efficiently than DAB.

225. In summary, the OFT does not consider that the transaction raises any competition concerns in relation to DAB.

B) Manchester area

226. As regards the other areas of overlap, in Manchester the merged entity would be the fourth largest supplier for non-contracted agency customers, with a share of [10-20]per cent, and the third largest player in the direct sector, with a share of [0-10] per cent. There are no grounds for competition concerns in Manchester as a result of this transaction.

C) Yorkshire and the North-East areas

227. As indicated earlier in the present decision, GCap has a national sales agreement with GMG, under which GCap acts as a national sales house for GMG. As part of the agreement GCap is also responsible for selling advertising on all GMG radio stations to agencies based in London.

228. However, GMG retains the control of its direct sales in London and the regions. GMG has sales teams dedicated to advertisers based in each of the North West, Yorkshire, the North East, the Midlands, Scotland and Wales. GMG is also building its own London based sales force. For completeness the local areas where GMG and Global overlap (which are not covered in the unilateral effects section) have been analysed, namely the North East and Yorkshire, but no competition concerns were considered to be realistic, and they will not be analysed further.

SECTION IV – EXCEPTIONS TO THE DUTY TO REFER

DE MINIMIS

A) Introduction – markets of insufficient importance

229. The OFT believes that there is a realistic prospect of a substantial lessening of competition arising in relation to the supply of advertising for regional campaigns in the East Midlands and in the West Midlands. It has also identified the possibility that the test for reference is met in relation to the supply of the East Midlands and West Midlands regional aspects of a bundled national advertising campaign, although it has not found it necessary to conclude on this point for the reasons set out earlier in the national analysis section.
230. The parties argued that the OFT should apply the markets of insufficient importance, or de minimis, exception to the duty to refer, as recently revised.⁵⁶
231. The parties stated that revenues from non-contracted regional customers in each of the East Midlands and the West Midlands are lower than £10 million, they are estimated to be closer to £[0-10] million in the West Midlands and approximately £[0-10] million in the East Midlands.⁵⁷
232. As the OFT makes clear in its published guidance, the £10 million market size threshold for consideration of the de minimis exception is calculated by reference to the aggregate value of the markets in which a realistic prospect of a substantial lessening of competition is found.⁵⁸ Given that the estimated revenues from non-contracted customers in the East and West Midlands is in aggregate greater than £10 million (£[] million), then presumptively the OFT is likely to consider the affected markets to be of sufficient importance to justify a reference. In this case, however, given that the annual value of the affected markets only marginally exceeds the £10 million threshold, the OFT has for the sake of completeness considered whether it would nevertheless be

⁵⁶ OFT 516 b, November 2007.

⁵⁷ The parties based this estimate on the following assumptions: (1) all non-contracted revenues on Heart West Midlands and Heart East Midlands are regional as are those on Smooth and Kerrang! (2) £[] of non-contracted revenues on Galaxy Birmingham are regional (3) [] per cent of non-contracted agency spend on the Midlands GCap stations are regional and (4) [] per cent of direct revenues on the Midlands GCap stations are regional.

⁵⁸ Ibid paragraph 7.6.

appropriate to exercise its discretion not to refer the merger to the Competition Commission.

B) Undertakings in lieu and *de minimis*

233. As stated in the Dunfermline/BRN case,⁵⁹ and as explained further in the BOC/Ineos case,⁶⁰ the OFT believes that it would be proportionate to refer a problematic merger where it is clearly open to the party or parties to offer a clear-cut undertaking in lieu of reference, because the recurring benefits of avoiding consumer harm by means of undertakings in lieu in a given, and all future like cases, outweighs the one-off costs of a reference.

234. As set out in more detail in the Dunfermline/BRN case, the OFT makes this judgment on an objective or in principle basis at the stage of considering whether to invoke the de minimis exception, without regard to whether parties have actually made any such offer, or the content of any such offer, neither of which will in any event be known to the decision maker at the time that application of the de minimis exception is considered.

235. In this case, it was clear to the OFT, based on its objective evaluation of the transaction, that this case was a clear candidate for resolution of any competition concerns by means of undertakings in lieu. As in the Dunfermline/BRN case, this case fits the classical profile of the OFT's undertakings in lieu cases: in other words, a small proportion of a larger benign or even beneficial transaction raises concerns, and those concerns can be addressed structurally by means of a divestiture package.

236. The OFT considers that clear-cut (effective and proportionate) undertakings in lieu are in principle available because it is open to Global to divest either the Heart station and Galaxy in the West Midlands or a package of all of the local GCap stations in each of the East Midlands and the West Midlands, thereby removing the problematic overlap created by the merger. In making this judgment, the OFT has taken account of the fact that divestment of local radio stations has operated as a successful undertaking in lieu in previous transactions in the radio sector.⁶¹

237. The OFT notes that it does not, however, include what would amount to prohibition when considering whether clear-cut undertakings in lieu are available: it is not the role of the undertakings in lieu process effectively to

⁵⁹ OFT *Completed acquisition by Dunfermline Press Limited of the Berkshire Regional Newspapers business from Trinity Mirror plc* 4 February 2008.

⁶⁰ OFT *Anticipated acquisition By BOC Limited of the Packaged Chlorine Business and Assets carried on by Ineos Chlor Limited* 29 May 2008.

⁶¹ OFT *Anticipated merger between Capital Radio and GWR* 22 December 2004.

invite parties to abandon their own transactions. However, this is not the case in this instance. A divestment of the entirety of one of the overlapping businesses in each of the East Midlands and West Midlands would not go to the heart of the transaction. Rather, this structural remedy, which would restore the status quo ante in the affected markets, would fit with the logic of first-phase remedies, namely to resolve competition concerns clearly whilst allowing the transaction, albeit in modified form, to proceed.

238. There appears no reason why as a matter of principle, the main rationale for the transaction (marrying Globals brands with GCaps coverage) would be generally undermined by divestment of one of the partys radio station businesses in each of the East Midlands and West Midlands areas. Further, the second rationale given for the transaction (refreshing GCaps core city stations) would not be undermined outside the East and West Midlands were a structural divestment to be made to resolve competition concerns.
239. In this context, the OFT notes also that GCap owns a portfolio of 71 local analogue radio licenses across the UK, as well as the Classic FM national station, and that divestment of (for example) the GCap local radio stations in the East and West Midlands would mean divestment of seven local stations (Trent, RAM and Leicester Sound in the East Midlands and BRMB, Wyvern, Beacon and Mercia in the West Midlands). It is quite clear, then, that such a divestment would in no way equate in actual or practical terms to prohibition of the transaction.
240. On the basis of all of these factors, in the circumstances of this case, it is therefore appropriate for the OFT to rule out an evaluation of the de minimis exception in this case on the grounds that it would be clearly open to the parties to offer a clear-cut – that is, effective and proportionate – undertaking in lieu.

CUSTOMER BENEFITS

241. As discussed earlier in this decision, the parties argued strongly that the OFT should take account of efficiency gains resulting from the merger that, they stated, would benefit both advertisers and listeners. The parties submitted that, given that regional advertisers in London and the East and West Midlands are likely to obtain quantifiable benefits which far outweigh any possible concerns, the OFT should exercise its discretion not to refer the merger because the customer benefits of the merger outweigh any adverse effects.
242. As discussed in the London efficiencies section above, the OFT has considered the efficiency claims put forward by the parties at two stages of its analysis: first, in determining whether any lessening of competition could be said to be

substantial in each of London and the East and West Midlands, second, below, in determining whether to exercise its discretion not to refer to the merger to the Competition Commission.

243. Section 22(2)(b) provides that the OFT may decide not to make a reference if it believes that any relevant customer benefits in relation to the creation of the relevant merger situation concerned outweigh the substantial lessening of competition concerned and any adverse effects of the substantial lessening of competition concerned.⁶²
244. Customer benefits are defined in the Act as being benefit[s] to relevant customers in the form of – (i) lower prices, higher quality or greater choice of goods or services in any market in the United Kingdom (whether or not the market or markets in which the substantial lessening of competition concerned has, or may have, occurred or (as the case may be) may occur), or (ii) greater innovation in relation to such goods or services (section 30(1)(a)). For those benefits to be counted, the OFT must believe that the benefit has accrued as a result of the creation of the relevant merger situation concerned or may be expected to accrue within a reasonable period as a result of the creation of that situation, and the benefit was, or is, unlikely to accrue without the creation of that situation or a similar lessening of competition (section 30(2)).
245. Section 22(2)(b) provides the OFT with a discretion (may, as opposed to the prohibition on making a reference in the circumstances described in section 22(3) (no reference shall be made)). That discretion (as with the *de minimis*, or markets of insufficient importance, exception in section 22(2)(a)) is whether or not to refer the relevant merger situation: it is not a discretion not to find a substantial lessening of competition in a given market or markets.
246. As a result of the structure of the Act, it is clear that the customer benefits exception to the duty to refer in section 22(2)(b) requires the OFT to consider that any relevant customer benefits in relation to the relevant merger situation concerned outweigh all of the findings of a substantial lessening of competition and any adverse effects resulting from them. It is not possible under the Act for the OFT to exercise its discretion in relation to one particular finding of a substantial lessening of competition (in market X) but then to make a reference in respect of another substantial lessening of competition (in market Y). The OFT refers relevant merger situations to the Competition Commission, not individual markets on which it has found a substantial lessening of competition – and the customer benefits exception must therefore operate in relation to the merger situation as a whole (in the same way that the *de minimis* exception would do).

⁶² An equivalent provision applies in respect of anticipated mergers in section 33(2)(c).

247. As discussed in detail, the OFT has considered carefully the extent to which demand- and supply-side efficiencies arise in each of London, the East Midlands and the West Midlands.
248. It is clear from section 30(1)(a)(i) of the Act, and as stated in the OFT's Substantive Assessment guidance⁶³, that the claimed customer benefits need not necessarily arise in the market(s) where the substantial lessening of competition concerns have arisen. To that extent, it is conceivable that the efficiencies that the OFT considers demonstrated in respect of the merger in London could be sufficient to outweigh the substantial lessening of competition found in the East and West Midlands. However, the OFT does not consider that there is clear and compelling evidence that this is the case.
249. The efficiencies evidenced in London, as discussed in that section, are sufficient in magnitude to tip the balance of the unilateral effects case in London in favour of clearance. However, as far as both the East and West Midlands are concerns, given:
- the strength of the OFT's concerns
 - the absence of demonstrable Cournot effects
 - the fact that efficiencies derived from brand re-positioning in the Midlands have not been demonstrated to be compelling, and
 - the modest fixed and no variable cost savings substantiated.
- the customer benefits of the merger in London are insufficient to outweigh the substantial lessening of competition concerned (and any adverse effects arising from it) in the East and West Midlands.
250. Finally, the OFT notes that the parties have not provided compelling evidence on the existence of benefits from the merger outside London and the East and West Midlands that could tip the balance in favour of the exercise of the discretion.
251. The OFT has therefore decided not to exercise its discretion not to make a reference under section 22(2)(b).

⁶³ Paragraph 7.9.

UNDERTAKINGS IN LIEU

A) Introduction

252. Where the duty to make a reference under section 22(1) of the Act is met, the OFT may, pursuant to section 73(2) of the Act, instead of making such a reference, accept from such of the parties concerned undertakings as it considers appropriate for the purpose of remedying, mitigating or preventing the substantial lessening of competition concerned or any adverse effect which has or may result from it.
253. The OFT's guidance states that in order to accept undertakings in lieu of reference [] the OFT must be confident that the competition concerns identified can be resolved by means of undertakings without the need for further investigation. Undertakings in lieu of reference are therefore appropriate only where the competition concerns raised by the merger and the remedies proposed to address them are clear cut, and those remedies are capable of ready implementation [].⁶⁴
254. The OFT's starting point and preferred remedy is always to seek an outcome that restores competition to pre-merger levels, thereby comprehensively remedying the substantial lessening of competition.⁶⁵ The objective is to ensure that competition following the implementation of the remedy is as effective as pre-merger competition. The most straightforward way of restoring competition to pre-merger levels is to restore the status quo ante, which would normally involve reversing the completed acquisition.⁶⁶ In practical terms, this results in divestment of the entire increment in the relevant market brought about by the merger. However, this is without prejudice in any given case to the ability of the parties to persuade the OFT that a proposed remedy that does not directly restore competition to pre-merger levels nevertheless clearly and comprehensively removes the substantial lessening of competition identified thereby satisfying the requirements of section 73(2) of the Act.
255. As a general rule, the OFT considers that it is appropriate for it to seek to remedy or prevent competition concerns, rather than accepting remedies that simply mitigate concerns. The OFT has not, to date, accepted an undertaking

⁶⁴ See paragraph 8.3 of OFT *Mergers Substantive Assessment Guidance*.

⁶⁵ See *Co-operative Group (CWS) Limited v OFT* [2007] CAT 24, paragraphs 149-151, where the CAT approved the OFT adopting as its starting position the restoration of competition to pre-merger levels.

⁶⁶ The Competition Appeal Tribunal described this in *Somerfield v Competition Commission* [2006] CAT 4, paragraph 99, as 'a simple, direct and easily understandable approach to remedying the [substantial lessening of competition] in question.'

in lieu on the basis that it mitigated the concerns without remedying or preventing them. In all cases, the OFT is mindful that there remains the possibility of a reference at the end of which the Competition Commission enjoys enhanced powers to those of the OFT. For these reasons, the OFT would be extremely cautious before accepting a purely mitigatory remedy, and would be very unlikely to do so save where it was abundantly clear that the Competition Commission (notwithstanding its power actually to prohibit an anticipated merger or to require the full unwinding of a completed merger) would be to no material extent better placed than the OFT to achieve a remedy that would restore the levels of competition that existed pre-merger.

256. In this case, Global offered structural remedies to address a potential situation in which the OFT concluded that the test for reference was met []

257. In relation to each of the East Midlands and the West Midlands, Global offered multiple proposals: a stage 1 remedy offer as a first choice and then additional staged offers as further choices to be considered only if the OFT considered that the previous offer was insufficient to remedy the concerns identified.

B) East Midlands

258. Stage 1 of the parties offer was []

259. The OFT considered whether [] was sufficient to address clearly the identified competition affects in the East Midlands. However, it concluded that the nature of the competition concern identified in this case meant [] would be insufficient to remedy the concerns with the necessary degree of confidence.
[]

260. Given that OFT did not consider stage 1 as a suitable remedy, it considered Globals stage 2 undertaking for the East Midlands. Stage 2 consisted of two separate options. Globals preference was to be able to implement either option by way of ultimate remedy, but it made clear that, should only one of the two options prove acceptable to the OFT, it would offer that specific option.

261. Globals stage 2 option A remedy consisted of a franchise arrangement, whereby the divestment purchaser would own the 106 licence and the physical assets of the station, with a licence of the Heart brand and a right to sell advertising on the station at a regional level. Global would retain the right to sell the station at a contracted/national level, but all revenues (including contracted revenues) would flow through to the new owner. Global/GCap would receive a certain commission from the new owner on all contracted sales made for the East Midlands Heart franchise.

262. Global proposed the following specific provisions for the franchise agreement:

- the franchisee would be required to use the Heart brand, playlists and other content (jingles etc.)
- the franchised Heart station would use Heart national network programming, but would have separate local programming (as with all Heart stations)
- ideally, Global would retain control over the choice of local programming staff, including local presenters (on the basis that this is an important part of a stations image and consistency needs to be maintained at a national level), and
- a certain proportion of the inventory could be prioritised for local/regional non-contracted advertising (as against national contracted advertising).

263. However, Global made it clear that if any of the above four propositions were considered by the OFT to be unacceptable in terms of solving the competition concerns identified in a clear-cut fashion, Global would be willing not to include them in the franchise arrangement.

264. The OFT's concern in the East Midlands related to competition in the supply of regional advertising campaigns. By permitting the divestment purchaser of the 106 licence and assets to licence the Heart brand and sell advertising at the regional level, the effect of the undertaking would be to allow the divestment purchaser to compete on the back of its Heart licence against a package of Global/GCap local stations for regional advertisers. Prima facie, therefore, competition is restored by this merger.

265. The OFT considered whether there was any question as to whether the structure of the option A arrangement meant that the remedy could not be said to be clear-cut in its scope or operation. However, in this regard, the OFT accepts the parties arguments that this structure has been successfully tried and tested in the industry. For example, it is similar to the way GMG currently sells its brands – contracted advertising is sold through Global/GCap and local advertising is sold by the local sales teams. Furthermore, the OFT notes by way of practical consideration that there is already a separation between local and national sales teams within Hearts existing set-up.

266. The OFT considered that allowing Global to retain control over the choice of local (as opposed to national) programming staff, including local presenters, might appear to compromise the independence of the station at a regional level (given that it would be competing against the bundle of retained Global/GCap local stations). However, Globals undertaking in lieu offer was

very clear that this point could fall away to the extent that it risked undermining the clear-cut nature of the remedy. On this basis, the OFT considers that stage 2 option A appeared sufficiently clear-cut in principle for the OFT to be able to suspend its duty to refer, subject always to public consultation on the undertakings prior to acceptance.

267. Global's alternative stage 2 option B remedy for the East Midlands comprised a sale of the 106 FM licence only (without the Heart brand), with the station to be re-branded with a different brand owned by the divestment purchaser. The remedy would not include divestment of the Heart brand given that one of the drivers for the overall transaction was for Global to be able to create a national network based on its Heart brand. However, to the extent that the divestment purchaser were able successfully to use an existing brand or to establish a new brand using the existing 106 licence, the remedy would mean that the divestment purchaser would become a supplier of regional advertising campaigns in place of the existing station in competition with the GCap bundle of local stations.
268. In concluding that this stage 2 option B remedy was, in principle, clear-cut in its operation to remedy competition concerns, the OFT was mindful of the fact that there have been numerous instances of radio station re-branding in recent years such that there was no reason to believe that a suitable divestment purchaser would not be able to compete strongly with the merged firm in the East Midlands region even without use of the previous Heart brand. Indeed, Chrysalis re-branded the Century station to become Heart in 2005 following undertakings in lieu given in the Capital/GWR merger.⁶⁷ On this basis, the OFT considered that stage 2 option B was also sufficiently clear-cut in principle in its scope and operation to enable the OFT to suspend its duty to refer to seek undertakings in lieu in respect of the East Midlands region.
269. Given that both stage 2 option A and option B were sufficient to remedy the OFT's concerns and both appeared in principle to be capable of being clear cut in their scope and operation, the OFT is willing to suspend its duty to refer on the basis that Global has the option of pursuing either option A or option B at this stage.

C) West Midlands

270. The parties offered a wider range of staggered alternatives in relation to the West Midlands. Stages 1 – 4 of the parties offer comprised various alternative possibilities involving divestment of one or more of the GCap local stations in

the West Midlands area, including in at least one case the divestment of the largest local station, BRMB, but in all cases comprising a subset of the existing basket of four GCap stations (BRMB, Beacon, Mercia and Wyvern). In all four stages, the relevant local GCap stations would be accompanied by the accompanying Gold licenses.

271. The parties argued, successively, that divestment of each of these packages of GCap local stations was sufficient to remedy any competition concerns identified by the OFT and that each stage was a proportionate remedy to address those concerns.

- First, the parties argued that the remedy would lead to a reduction in the combined non-contracted share of the combined Global/GCap entity, in stages 1 and 3, this would be to a level slightly above that of GCap pre-merger, in stages 2 and 4, this would be to a level below GCaps pre-merger non-contracted share.
- Second, the parties argued that the reach of these packages would give any potential regional customer significant leverage against a price increase on the combined Global/GCap entity in the West Midlands.
- Third, the parties pointed to the geographic overlap between the relevant divestment package in each case and the existing Heart TSA.
- Fourth, the parties pointed to the fact that the divestment packages would have low levels of contracted spend compared to Hearts reliance on contracted revenue.
- Fifth, the parties argued that the relevant divestment brands were strong in the Midlands.

272. The OFT considered, sequentially, whether divestment of the relevant packages of GCap stations was sufficient to address clearly the identified competition affects in the West Midlands. However, in each case, it concluded that the nature of the competition concern identified in this area meant a divestment of only one or some of the GCap stations – even a remedy involving the largest GCap station in the West Midlands, BRMB – would be insufficient to remedy the concerns with the necessary degree of confidence given the context of undertakings in lieu. It was not clear to the OFT that – even on the most extensive of the remedy packages proposed in stages 1 to 4 – a purchaser of any of these packages would necessarily be able to offer advertising customers seeking regional coverage a sufficiently strong or

⁶⁷ OFT *Anticipated acquisition by Capital Radio Plc of GWR Group Plc* 22 December 2004. The parties provided a large number of other examples of examples of re-branding of stations following acquisition between 1997 and 2008.

flexible bundle of local stations in order to compete against the regional offering provided by Heart in the West Midlands to the same degree as GCap was able to do pre-merger (which amounts to the pre-merger degree of competitive constraint). For this reason, the OFT did not consider that the divestment of any of these packages of a subset of the existing four GCap stations would remedy in a clear-cut fashion the competition concerns identified for advertisers seeking regional coverage in the West Midlands.

273. The OFT accepts the possibility that one or more of these divestment packages might be sufficient in scope for a divestment purchaser to be able to offer some form of bundle to compete against Global/GCaps Heart station for advertisers seeking regional customers. However, in the absence of detailed information showing the precise combination of GCap stations that customers were using, or were threatening Global to use, in order to provide an actual or potential alternative to Heart, it was not possible for the OFT to be confident that a partial remedy involving only a subset of the GCap local stations in the West Midlands would restore competition to pre-merger levels. Indeed, the OFT's conclusion in this regard was strengthened by evidence that a material number of customers were currently actually purchasing all four GCap location stations to create a bundled package giving wide regional coverage. To the extent that these customers considered it necessary or desirable to purchase all four GCap stations pre-merger, it is reasonable for the OFT to consider that divestment of a subset of the GCap stations in the West Midlands would be likely not to have functioned as a clear-cut remedy for at least these GCap customers. For these reasons, the OFT concluded that stages 1 to 4 of the parties undertakings in lieu offer in respect of the West Midlands were insufficient to remedy the concerns identified by the OFT to the requisite clear-cut standard.
274. Stage 5 of the parties offer comprised the divestment of all four GCap West Midlands stations – BRMB, Beacon, Mercia and Wyvern – with the accompanying Gold licenses. By contrast to stages 1 – 4 of the parties offer, stage 5 involved the divestment of all of the GCap stations, thereby effectively removing the increment brought about by the merger in the West Midlands. Divestment of the entirety of GCaps local stations in the West Midlands will place the divestment purchaser in the same position as GCap pre-merger in order to compete for advertisers requiring regional campaigns in the West Midlands. This remedy would therefore act in a clear-cut fashion to restore competition to pre-merger levels in the West Midlands and on this basis the OFT has decided to suspend its duty to refer as regards the West Midlands in order to seek undertakings in lieu from the parties.

275. To the extent that divestment of all four GCap West Midlands stations is a more comprehensive remedy than might ultimately be required at the end of a detailed phase II investigation, this arises from the need for the OFT to be confident that an undertaking in lieu remedy acts in a clear-cut fashion.⁶⁸ The parties are always free at the end of a phase I investigation where the OFT finds that its duty to refer is met not to offer undertakings in lieu but to advance their arguments in more detail before the Competition Commission.

D) Regional aspects of national advertising campaigns

276. The OFT did not find it necessary to conclude whether the merger gave rise to a realistic prospect of a substantial lessening of competition in relation to the East Midlands and West Midlands regional components of a national campaign on the basis that any undertakings in lieu that remedied concerns arising for customers seeking regional campaigns in these areas would also remedy any related concerns arising at national level.

277. To the extent that the OFT ultimately accepts undertakings in lieu on the basis of stage 2 for the East Midlands and stage 5 for the West Midlands (as discussed above) these undertakings will restore the competitive choice that existed as regards East Midlands and West Midlands regional campaigns to pre-merger levels. As a result, any advertiser (or agency) seeking to place a national campaign will benefit from the same degree of competition in the supply of East Midlands and West Midlands regional aspects that they did pre-merger.

E) Preservation of customer benefits

278. Section 73(4) of the Act states that, in accepting undertakings in lieu, the OFT may, in particular, have regard to the effect of any action on any relevant

⁶⁸ See for example OFT *Anticipated acquisition by Boots plc of Alliance UniChem plc 6 February 2006* in which the OFT accepted undertakings in lieu in respect of pharmacies where the merger resulted in a reduction in the number of pharmacies from three to two on the basis of a one-mile overlap even though it took the view that it only 'may be the case' that the merger may be expected to result in a substantial lessening of competition in these areas. In commenting on this decision in subsequent litigation, Simon Pritchard, then Director of the Mergers Branch at the OFT, stated: 'The OFT was therefore obliged to conclude, reluctantly, as a result of the limited number of 3:2 areas that were marginally problematic, its duty to refer applied 'across the board' to every 3:2 area. I say reluctantly because we were aware that, depending on the undertakings in lieu proposals, that this might compel a reference in respect of areas where none was necessary, or result in divestments where none was really necessary. Nevertheless, this issue is consistent with our first-phase role in UK merger control, despite the extensive investigation and experience applied to this particular case' (Celesio v OFT [2006] CAT 9, paragraph 157).

customer benefits in relation to the creation of the relevant merger situation concerned.

279. The OFT's Substantive Assessment Guidance states that it: ... will also seek to agree undertakings that preserve any merger-specific customer benefits. However, the OFT will not accept undertakings in lieu of reference that do not address the identified competition effects but which are designed instead to lock in sufficient customer benefits to outweigh the risks of a substantial lessening of competition arising from such of the parties concerned as it considers appropriate undertakings to take such action as it considers appropriate.
280. The OFT's evaluation of the proposed undertakings in lieu in this case has, in accordance with its obligations under the Act, been driven primarily by the aim of remedying or preventing the substantial lessening of competition identified in the East Midlands and West Midlands. The OFT considers that the stage 2 undertakings in the East Midlands and the stage 5 undertakings in the West Midlands will achieve as comprehensive a solution as is reasonable and practicable to the substantial lessening of competition identified and any adverse effects resulting from them (in accordance with section 73(3) of the Act). By way of secondary consideration, however, the OFT has considered the extent to which these undertakings preserve any merger-specific customer benefits.
281. The stage 2 option A undertakings in the East Midlands (the franchise arrangement) will not undermine any efficiencies brought about by the creation of a national Heart brand or by the reinvigoration of the GCap brands at local level. The stage 2 option B undertakings would preserve the latter benefit but would, as identified by the parties, not allow for the use of the Heart brand in the East Midlands.⁶⁹
282. The stage 5 undertakings in the West Midlands (sale of all four GCap local stations and the Gold licences) will in no way undermine the efficiencies brought about by the creation of a national Heart brand. Whilst it is true that the GCap local stations would no longer be owned by Global/GCap post-merger, the OFT would in any event require that any divestment purchaser would be able to compete effectively with Heart for the purchaser to be approved.
283. The undertakings in lieu offered with respect to the East Midlands and the West Midlands will have no impact on any benefits from the merger in relation to the London stations, nor to any nation-wide benefits, other than as

⁶⁹ The parties stated that it would be too confusing for the local market to re-brand GCap stations to Heart.

discussed above. For this reason, the OFT considers that the stage 2 undertakings in the East Midlands and the stage 5 undertakings in the West Midlands would largely preserve any relevant customer benefits arising from the merger.

F) Need for an up-front buyer

284. The OFT has considered whether it is appropriate in the circumstances of this case to require that the relevant divestments in the East Midlands and West Midlands be made to an up-front buyer or buyers.⁷⁰ An up-front buyer requirement means that the OFT will consult publicly on the suitability of the proposed divestment purchaser, as well as any other aspects of the draft undertakings, during the public consultation period.

285. The OFT will seek an up-front buyer where the risk profile of the remedy requires it, for example where the OFT has reasonable doubts with regard to the ongoing viability of the divestment package and/or there exists only a small number of candidate suitable purchasers.

286. The parties argued in this case that an up-front buyer requirement was unfair and disproportionate. They provided a list of companies that they regarded as realistic potential purchasers for the divestment assets in the undertakings in lieu. However, in line with the OFT's request for specificity on this matter, they made it clear that, should the OFT consider an up-front buyer necessary as a means to ensure the viability of any proposed undertaking, Global would be prepared to accept the need to find an up-front buyer as a requirement of the undertaking, given a reasonable length of time to do so.

287. The OFT, however, considers that the risk profile of the undertakings in this case, in particular in relation to the undertakings offered to remedy competition concerns in the East Midlands, and the limited number of purchasers that would be considered by the OFT to have the necessary expertise, resources and incentives to operate the divested radio businesses as an effective competitor in the market place, mean that it would be proportionate and appropriate in this case to require an up-front buyer. In particular the OFT notes that:

- divestment of the stations should be to a buyer with the necessary expertise, resources and incentives to operate the divested business as an effective competitor in the market place – in the case of the stage 2 undertaking in the East Midlands, this would be most likely to translate

⁷⁰ The OFT requires that the GCap stations in the West Midlands be divested to a single purchaser. However, this does not have to be the same purchaser as in the East Midlands.

into a requirement that the divestment purchaser had sufficient knowledge and experience of the radio market that it would be able to sell advertising on the Heart station at a local level (option A). In the case of option B, the divestment purchaser would also be likely to have to have a sufficiently strong existing brand (or at least a basis for a new brand) that it would be able to re-brand the existing Heart station and compete against GCaps local stations in the East Midlands (Trent, RAM and Leicester Sound), and

- divestment of the stations to the divestment purchaser should remedy, mitigate or prevent the competition concerns identified and should not in itself result in a substantial lessening of competition within any market or markets in the UK – this requirement is most obviously (though not exclusively) met in a clear-cut fashion by a divestment purchaser that is not already present in the relevant market, given that divestment to an existing competitor would inevitably increase concentration and itself raise concerns.

288. The combined operation of the above requirements for the divestment purchaser mean that, in the OFT's view, there is likely to be a relatively small pool of potential purchasers that would be suitable in the circumstances of this case. When combined with the fact that the remedies package, although capable in principle of operating in a clear-cut fashion, is undoubtedly more complicated in the East Midlands than a straightforward divestment of a wholly stand-alone business, the OFT believes that the circumstances of this case mean that an up-front buyer requirement is justified and proportionate.

289. In the West Midlands, for the divestment to restore competition in a clear-cut manner such that the purchaser can compete as GCap did pre-merger against Global and rivals on the basis of a portfolio of the relevant stations, it follows that the portfolio cannot be split-up and sold to various different buyers. Multiple purchasers of individual stations would not be able to compete on a package basis (and GCaps ability to do this pre-merger forms the basis of the duty to refer). Accordingly, the OFT seeks a single purchaser for the package of GCap West Midlands stations. This requirement may also limit the field of potential purchasers, reinforcing that the up-front requirement is both necessary and proportionate.

G) Conclusion on undertakings in lieu

290. Accordingly, the OFT has decided to exercise its discretion under s73(2) of the Act to suspend its duty to refer to consider whether to accept undertakings instead of making a reference to the CC.

DECISION

291. The OFT's duty to refer the completed acquisition by Global of GCap to the Competition Commission pursuant to section 22 of the Act is suspended because the OFT is considering whether to accept undertakings in lieu of reference under section 73 of the Act.

END NOTES

The parties have informed the OFT that in fact, networked programmes will be broadcast only across the Heart network, and separately across the Galaxy network, at certain times of the day.

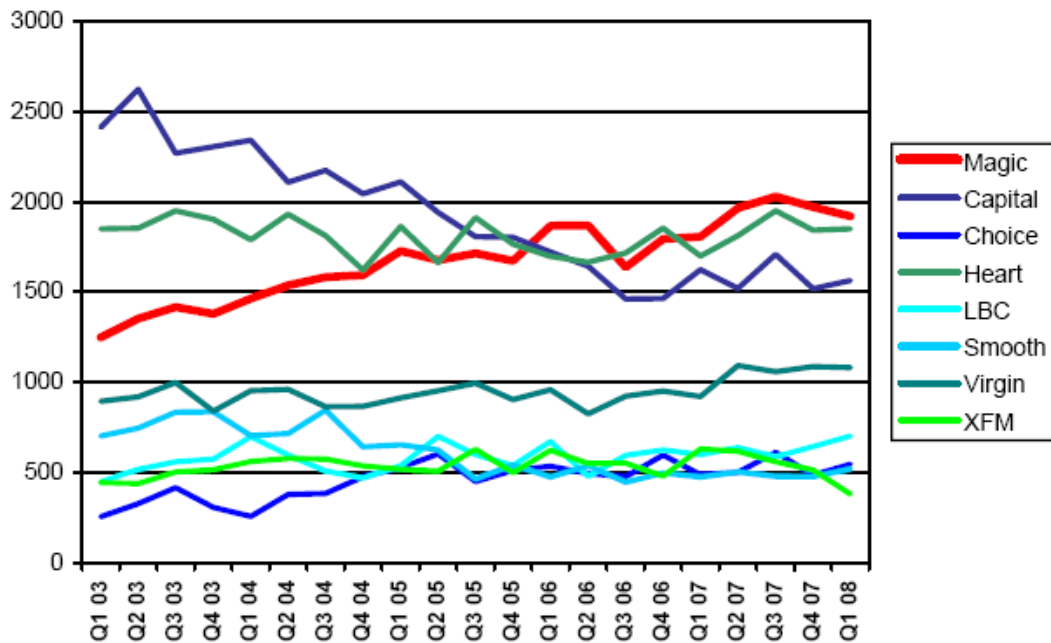
ANNEXE

Case studies of brand repositioning

Magic in London

1. After Richard Park was appointed Programme Director of Magic in 2003 (a position he held until 2007), Magic changed programming under the rubric 'More music, less talk' from easy listening to appeal instead to the 35-44 female demographic. Magic also hired popular DJs. As a result, the parties submitted, almost a million new listeners were added by 2007, by when Magic had become London's most listened to radio station and was the only radio station to show a consistent increase in audience reach over the period (see Figure 1 below).

Annex Figure 1
Reach of London radio stations, 2003Q1 to 2008Q1



Heart in London

2. Globals launch of Heart in London in 1995 was also successful. Copying the sales policies following the success of the launch of Heart in the Midlands in 2004 under Chrysalis (then owner of Heart) Sales Director Don Thomson (currently Chief Operating Officer at Global), Chrysalis carried out research among advertisers to prepare packages for them that included factors such as no more than 3 adverts in one break, no more than 12 adverts per hour and guaranteed category exclusivity. As a result, the parties submitted, Heart gained a reputation as a station that listened to its advertisers and grew from a standing start to become Londons leading radio station by revenue with [20-30] per cent of the market in 2007, overtaking GCaps Capital in 2006 (see Figure 2 below).

Annexe Figure 2 Annual advertising revenue for Heart and Capital in London, 1996 to 2007

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Heart and Galaxy in the Midlands

3. The OFT also considers Globals examples of success in launching Heart and Galaxy in the Midlands as relevant to consideration of efficiencies in London. In the West Midlands, under Don Thomson and pioneering the advertiser-led repositioning outlined above, audiences and revenues grew steadily after Heart launched in 1994 at a time when GCaps stations were declining (see Figure 3 below).

Annexe Figure 3 Annual revenues for Heart, BRMB, Beacon, Wyvern and Mercia in the West Midlands, 1995 to 2004

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4. Century 106 was re-branded as Heart in the East Midlands and was launched in September 2005. The re-branding took 4-6 weeks and followed 4 steps, (i) new on-air slogans for the station such as 'Century, the Heart of the Midlands', (ii) changing play-lists (slowly at first, then gathering pace), (iii) DJs explaining the re-branding to listeners and (iv) a television campaign and other

promotional activities. Since then, the parties submitted that Heart has enjoyed steady revenue growth (by [] per cent from 2005 to 2006) whereas revenues for GCaps stations in the region have declined by between [0-10] and [30-40] per cent (see Figure 4 below).

Annexe Figure 4
Annual change in revenue for Global and GCap stations in the
East Midlands between 2005 and 2005

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5. The parties submitted that the re-brandings (from Kiss) of Galaxy Manchester and Galaxy Yorkshire were managed exactly as for Heart in the East Midlands and increased revenue over threefold from 1998 to 2007. The parties further submitted that the re-branding (from Choice) of Galaxy Birmingham and the launch of Galaxy North East have been similarly successful.