OFFICE OF FAIR TRADING

Anticipated acquisition by Capital Radio Plc of GWR Group Plc

The OFT's decision on reference under section 33(1) given on 22 December 2004

PARTIES

1. **Capital Radio Plc (Capital)** is a commercial radio group, providing 21 local analogue stations and 58 digital programme stations, including the Capital FM Network, Capital Gold, Century FM, Xfm and Choice FM. Capital owns outright four local digital multiplexes[1], has a 50 per cent holding in three more and minority interests in a further seven. For the financial year to September 2004, Capital's turnover was £119.9m.

2. **GWR Group Plc (GWR)** is a commercial radio group that owns Classic FM and 30 local analogue licences (providing 36 local stations) and 35 digital programme stations. It owns a controlling interest in the national commercial digital multiplex operator, controls 14 local digital multiplexes and has a minority investment in one London multiplex. GWR also has a minority shareholding in **Classic Gold Digital Limited (CGDL),** which owns 18 AM licences and digital services. For the financial year to March 2004, GWR's turnover was £128.7m.

3. Both GWR and Capital Radio have shareholdings in **Independent Radio News Limited (IRN)** (Capital 45.64 per cent and GWR 8.97 per cent) and in **Hit40UK Limited (Hit40UK)** (Capital 38.1 per cent, GWR 34.2 per cent). These organisations, respectively, provide a national news service (**Newslink**) and a music chart show to radio stations of different groups across the UK in return for advertising space, which is currently sold by Capital (as an agent for IRN and Hit40UK).

[1] Multiplexes are essentially a platform for the broadcast of digital radio.

TRANSACTION

4. Capital proposes acquiring the whole of GWR's issued share capital. The parties notified the anticipated transaction to the OFT on 8 November 2004. The administrative deadline for the OFT's decision is 22 December 2004.

JURISDICTION

5. As a result of the transaction, Capital and GWR will cease to be distinct. The transaction will create a relevant merger situation as the turnover test under section 23(1) (b) of the Enterprise Act 2002 (the Act) is met. In addition the merged entity will supply over 25 per cent of national radio advertising in the UK. For completeness, the parties' activities also overlap in relation to the supply of radio broadcasting services and digital radio multiplex services in the UK.

RADIO ADVERTISING

Relevant market

6. Advertising space is sold on analogue and digital commercial radio stations by the merging parties, among others. The parties have argued that, in considering the relevant frame of reference to assess the competitive constraints relevant to this merger, it is important to understand the wider constraints facing radio from other forms of advertising. In particular, Capital and GWR have pointed to their own internal business experience of advertiser churn away from radio to local newspapers and also the comments of the Competition Commission (the CC) in the *Archant/INM* merger inquiry.[2]

7. As to the parties' arguments regarding local advertiser churn away from radio advertising towards local newspapers, it is not clear that examples of local advertisers switching away from radio are evidence of customers switching between media in response to changes to their relative prices. It is possible that those examples are simply evidence of advertisers re-balancing advertising spend across complementary media in response to a change in campaign strategies.

8. In its *Archant/INM* report, the CC alluded to the importance of local radio to local newspaper advertisers, although it concluded that they were not in the same market/frame of reference. However, this was a merger involving two local newspaper groups, so the focus of the analysis in that case was different to this. In particular, it is not necessarily the case that, in a situation the reverse of that considered by the CC, local radio advertising would be constrained by local

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[2] See Competition Commission's report on the acquisition by Archant Limited of the London newspapers of Independent News and Media Limited, 13/10/04.

newspaper advertising. Indeed, previous reviews of radio mergers (see, for example, the recent CC report into the *Galaxy/Vibe* merger[3]) have consistently found that radio advertising is not substitutable for other types of media advertising, citing its complementary nature and the specific characteristics that appeal to an advertiser.

9. As noted below, the OFT contacted a substantial number of third parties in the course of this investigation. Those who responded expressed various views as to the potential substitutability of radio and newspaper advertising. For example, some advertisers in the East Midlands saw local newspapers as a real constraint on radio advertising, others did not. The picture in other areas of the country was broadly similar. As regards national advertising (see below), there was a clearer (although still not conclusive) view that radio advertising was not constrained to a material extent by newspaper advertising.

10. There is clearly some merit in the parties' arguments, especially when considering local advertisers. However, in the context of this investigation, the evidence is inconclusive. While other media may be a close substitute to radio advertising for some customers, it is not clear that they are a substitute for sufficient customers to warrant inclusion in a wider frame of reference. Accordingly, the OFT believes that, while other advertising media are likely to exert a degree of competitive pressure on radio advertising, the appropriate (if perhaps cautious) approach is to treat radio advertising alone as the starting point for this competition analysis.

11. Two categories of radio advertiser need to be considered:

- National radio advertisers are typically large-volume buyers constructing advertising campaigns to cover broad geographic areas.[4] They tend to purchase advertising airtime centrally through suppliers' sales houses, typically via media agencies. Together with the widespread UK coverage of the parties' stations, these demand considerations point to a UK-wide geographic frame of reference for such customers.

- Local advertisers are typically smaller-volume buyers which mainly purchase advertising directly from local radio stations in their chosen locality. Previous OFT and CC inquiries have determined that the geographic reach of radio stations affects their ability to attract advertising and competitively constrain other stations. Accordingly, the geographic frame of reference for

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[3] See Competition Commission's report on Scottish Radio Holdings plc and GWR Group plc and Galaxy Radio Wales and the West Limited, CM5881, 16/05/03.

[4] These advertisers are known in the radio industry as 'national advertisers' although the geographic coverage of their advertising campaigns might not be the entire UK. It might instead be 'multi-region'.

such customers is localised. The scope of that local framework can be measured by Total Survey Area (TSA) or by Measured Coverage Area (MCA).[5] The MCA is adopted as the basis for assessment of competition at a local level for the purposes of this case as revenue information is only available on this basis.

Competition assessment

National advertising

Shares of national advertising revenue

12. Post-merger the parties will have a 40 per cent share of national Net Advertising Revenue for radio (NAR) (increment 20 per cent), and will become the largest commercial radio group. The next largest radio groups will be EMAP/Scottish Radio Holdings (25 per cent of NAR) and Chrysalis (15 per cent). Capital/GWR will also be able to provide advertisers with geographic coverage of a significant proportion of the UK as, although their only national station is owned by GWR (Classic FM), both have extensive packages of local radio stations that are used to build up national advertising campaigns. The extent of the overlap of those local stations is therefore important for national advertisers.

13. The combined shares of NAR might not, however, be a good measure of the extent to which Capital and GWR compete with each other for national advertising business. This is because the merger will not create a significant number of local overlaps in the parties' radio stations. There are only four areas of the UK where material local overlaps might arise (East Midlands, West Midlands, London and the North-West[6]). Even in areas of historic Capital or GWR strength (for example, in London or in East Anglia), the merger results in no or only limited increments to the pre-merger position.

14. In the sense described above, the parties' radio stations may be seen as complements rather than competing alternatives. Whether this is true turns crucially on whether national advertising customers have any strong geographic preference as to the areas in which they advertise.

- If they do have such a preference, then the limited geographic overlap in the parties' stations strongly suggests that they will not be substitutes for each other. Rather, they will primarily be complements. Hence, there will be no (or only a limited) loss of horizontal competition as a result of the merger.

[5] The licensed Total Survey Area is the area from which a radio station obtains its advertising revenue. The Measured Coverage Area is the guaranteed coverage of a particular licence.
[6] Separate competition analysis of these four overlapping areas follows below.

- On the other hand, if advertisers have no strong geographic preferences when constructing a campaign, they may see the packages of stations offered by Capital and GWR as competing alternatives in the sense that they can substitute different geographic areas to construct a campaign: for example, if the price of advertising in East Anglia rose, advertisers might switch coverage from there to the North East. If this is the case, then the merger might affect competition by removing a key negotiating point for national advertisers constructing a campaign.

15. The OFT considered whether the parties' product offerings are complements or competing alternatives. Capital and GWR thought that their advertising customers had no particular geographic preferences.[7] However, media agencies and advertisers universally commented that they did consider the precise geographic areas to be covered when developing an advertising campaign. The strength of this geographic preference was said to depend on both the individual campaign and the particular advertiser, which might at first sight suggest that elements of competition exist between the packages of Capital and GWR radio stations.

16. However, those third parties that expressed concerns did not raise a concern about competition between packages of stations. Rather, they did so by identifying specific parts of the UK where they said they could not substitute an alternative radio station for one owned by Capital or GWR. As explained below, even third parties producing information to the OFT on the availability of competing alternatives did so noting that the alternatives did not always meet their specific geographic requirements. These more localised concerns point to a material focus on geographic areas on the part of media agencies and advertisers, and hence a lack of competition between the general packages of Capital and GWR radio stations.

17. Although the available evidence points to a range of views, the OFT considers that the balance of the evidence before it indicates that Capital's and GWR's stations are complements rather than competing alternatives (substitutes). Nonetheless, because of the mixed evidence (and in the interests of completeness) the OFT does consider below the relevant competition analysis on the hypothesis that national advertisers have no geographic preference and thus regard the Capital and GWR packages as substitutes.

18. On the basis that national advertisers regard the Capital and GWR stations as complements (which the OFT considers to be the better view on the available

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[7] Other factors used in developing the parameters of a campaign are the reach of a station (how may listeners it gets within a given period), the opportunities to hear (how many times a listener will hear an advert within a given period) and the demographic profile of an audience.

evidence), third parties have raised concerns about possible portfolio effects arising from the merger. These concerns are considered fully below.

19. As noted above, there are only limited local areas of the UK where Capital and GWR stations currently compete. The question as to whether the merger gives rise to a risk of a substantial lessening of competition in each of those local areas is also considered below.

Horizontal competition

20. Even if the packages of Capital and GWR stations were to be seen competing alternatives (i.e. substitutes), the OFT does not believe that there would be any realistic prospect of a substantial lessening of competition arising as a result of the merger. This is because post-merger, national advertisers and media agencies will still be able to switch to alternative stations or create a different package with equivalent coverage. Doing so would discipline the commercial conduct of the merged entity (because advertisers would have no strong geographical preference for the area in which they advertise).

21. To assess the possibility and effect of any switching away from the merging parties' stations to alternative radio stations, both Capital/GWR and a number of third parties produced 'buy-around' analyses which purported to assess the ability for national advertisers to switch away from Capital/GWR stations.

- Capital and GWR carried out extensive buy-around analysis. To lessen the possibility of error due to the differing assumptions underlying these models, the parties used two different methodologies: one derived from Neilsen Media Research data and the other based on actual data for campaigns to which they had sold advertising airtime. In both cases, 10 of the largest national campaigns were modelled.[8] The results suggested that customers would be able to switch 50 per cent of their advertising expenditure away from Capital/GWR to alternative stations and achieve the same reach and demographic mix as on Capital/GWR.[9] Capital and GWR argued that the threat of 50 per cent of advertising spend switching to alternative stations was a strong commercial discipline that would deter the merged entity from raising prices.

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[8] The choice of 10 of the largest national campaigns was said to be random, and a sensible (and conservative) guide to the merger's effects. Capital and GWR said that buy-around would, by definition, be hardest to achieve for these campaigns. Accordingly, if buy-around could be achieved for these campaigns, smaller campaigns would also be able to switch away from Capital and GWR to discipline their competitive conduct.

[9] Capital and GWR argued that their analysis also showed that a similar geographic coverage could also be obtained when buying around the merging entity.

- All third party 'buy-around' analysis was based on switching 100 per cent of the radio advertising spend previously placed with Capital and GWR for one campaign. One third party provided buy-around analysis to show this was possible. This accorded with the anecdotal views of several other third parties.

- At a much later stage of the investigation, four other parties provided buy-around analysis. They concluded that it was not possible to achieve the same reach and demographic mix when buying around Capital/GWR, although in some instances the margin of difference between the overall Capital/GWR coverage and the buy-around coverage was narrow. However, in all cases the conclusion was related to specific geographic areas, suggesting these parties do have strong geographic preferences.

22. Analysis of these buy-around models raises a number of questions. First, although the Capital/GWR analysis suggests that switching to alternative stations is technically possible for some proportion of advertising spend, it does not explain whether sufficient revenue would switch (or could reasonably threaten to switch) in response to a sustained and significant price increase so as to make that price increase unprofitable for the parties.[10] Second, third party buy-around analysis considers switching 100 per cent of advertising spend from Capital/GWR, but does not consider whether some lesser proportion of spend could be switched which would be sufficient to discipline the merged entity. Third, the buy-around data provided by third parties seems to be closely focused on particular geographic areas, which substantially undermines its probative value for these purposes.[11]

23. Furthermore, in considering the buy-around data it is important to note that concerns raised by third parties were not, in the main, directed at a price increase arising from a loss of direct competition between the packages of stations (see para 25). This is consistent with both the view that Capital and GWR do not compete on the basis of distinct national packages of stations and also with the view that it would, in any event, be possible to buy-around the merged entity to create an alternative package.

24. In these circumstances, the available evidence points to the conclusion that, even if Capital and GWR compete using packages of station for national radio advertisers which do not have any geographic preference for their advertising,

[10] The parties estimated critical loss (how much revenue would have to be lost in relation to a price increase to render it unprofitable) but were unable to calculate actual loss (how much would actually be lost in response to a given price increase) at this stage.

[11] Note that in this context a non-coordinated effects theory assumes that there is competition between the Capital and GWR packages of radio stations on the basis that radio advertisers have no (or only limited) geographic preference as to where they advertise.

there will remain clear possibilities post-merger for national advertisers to switch away from the merged entity. Accordingly, this evidence, together with the views set out above regarding the prospects for competition between packages of Capital and GWR stations (see para. 17), does not lead the OFT to believe that it is or may be the case that the merger may be expected to result in a substantial lessening of competition (at a national level).

Portfolio effects

25. The main issue raised by third parties concerned possible portfolio effects arising from the merger of the complementary Capital and GWR radio stations. Third parties feared that the merged entity's larger portfolio of stations with greater geographic reach may give it the ability and incentive to tie (i.e., sell conditionally) or bundle (i.e., price at a discount) sales on less desired stations with high-demand stations.[12]

26. Mergers between firms that do not supply directly competing products rarely lead to a substantial lessening of competition solely as a result of their conglomerate effects.[13] Portfolio effects – arising from the combination of the merging parties' services – may be anti-competitive where they directly affect market structure, increase the feasibility of anti-competitive strategies and/or eliminate the competitive constraint imposed by firms in a neighbouring market.[14] The following competitive analysis focuses on the former two effects only.

27. First, as regards changes to market structure, portfolio effects are generally pro-competitive since they tend to lower customers' buying costs (as customers can now buy the same range of services by dealing with fewer suppliers). However, a merger may substantially lessen competition if competitors unable to offer the same portfolio of products cannot provide a sufficient competitive constraint on the merged parties.[15] In this regard the prospect that the combination of Capital's and GWR's respective packages of stations would provide a compelling 'one-stop shop' for radio advertisers is remote. Given the relatively limited number of radio groups that currently exist, the merger would be a small change for national advertisers that would not materially affect their transaction costs. Indeed, the available evidence indicates that national radio advertisers select the best available stations from the range of alternatives to meet the campaign's objectives. This already involves dealing with most of the radio groups. Moreover, this was not a concern raised by third parties.

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[12] Some third parties were concerned that the Capital/GWR would be able to increase the price of GWR stations post-merger by tying the GWR stations to Capital.

[13] See OFT publication, *Mergers – substantive assessment guidance*, OFT516, May 2003, para. 6.1.

[14] See *Mergers – substantive assessment guidance*, para. 6.2.

[15] See *Mergers – substantive assessment guidance*, para. 6.3.

28. Second, a merger may also give rise to a substantial lessening of competition if the merged firm controls complementary products and is able to engage in tying or bundling behaviour so as to require or encourage customers to purchase a range of products from the merged firm when they would not otherwise buy the full range. Such conduct is likely to result in adverse effects, however, only if it would be difficult for rivals or new entrants to provide competing bundles better tailored to customers needs.[16]

29. There are real doubts that the merged Capital/GWR would have the ability to engage in these sorts of tying/bundling strategies.

- No third party has identified an individual 'must-buy' radio station where customers had no alternative. Even Capital FM, oft cited by third parties as the key station, has lost significant audience and NAR share in recent years.

- Some third parties felt there were no regions where they have to deal with the merged entity. Those that felt such regions existed cited a limited number of them and, in some such cases, the ability to buy-around them was constrained only by a narrow margin of difference between the overall Capital/GWR coverage and the alternative buy-around coverage.

- The only area of material overlap is in the East Midlands. This particular area is discussed in more detail below.

- Some third parties pointed to Capital's and GWR's ownership of shares in IRN and HIT40 UK as a further avenue via which the merger might enhance the bargaining power of Capital/GWR. However, this does depend on Capital/GWR having a clear ability to change the way in which IRN and HIT40 UK operate. Even after the merger it is clear that Capital/GWR will not have the ability unilaterally to change the strategic direction or operation of either IRN or HIT40 UK as they do not have a controlling interest.

30. There is no real prospect that Capital/GWR would have the incentive to engage in such strategies.

- Since there is no material overlap in the parties' radio stations (save in the East Midlands[17]), any area in which the merged Capital/GWR would be a 'must-buy' would exist already. In other words, if there were a well-founded concern here about the ability and incentive to engage in conditional selling

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[16] See *Mergers – substantive assessment guidance*, para. 6.4.

[17] The situation in the East Midlands is discussed below. As explained there, the direct overlap in Capital's and GWR's activities in that local area gives rise to competition concerns.

strategies (or tying) then it would also exist pre-merger. There is however no evidence that either Capital or GWR currently engages in conditional selling. Indeed, some third parties made a specific point of saying that the parties did not do this.

- Even taking account of the reservations expressed above about the various buy-around analyses presented to the OFT, national advertising customers may be able to buy-around the merged entity and could use this ability to discipline it.

- As a matter of economic reasoning, it would seem more attractive to Capital/GWR to extract maximum revenue from its 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.

- There is no substantive evidence to suggest that a tying or bundling strategy engaged in by Capital/GWR would succeed in foreclosing competitors to the extent that Capital/GWR would be able to raise prices to its national advertising customers.

- National advertising customers, such as media agencies, are large and sophisticated purchasers. The top five media agencies account for 50 per cent of all national radio advertising revenue. These agencies can retaliate against individual radio groups. Media buyers agreed that, with the ability to switch 100 per cent of their purchases to other stations, they enjoyed buyer power. The loss of a bargaining point may reduce that buyer power slightly, but it is not clear that the loss is sufficient to amount a substantial lessening of competition.

<u>Conclusion</u>

31. The OFT undertook extensive (over 180) third party enquiries. We asked questions of those with concerns so as to understand how they thought the merger would lead to price increase or foreclosure and to ensure they were given the opportunity to put forward evidence related to such concerns.

32. Although the theories advanced may be more than fanciful, overall there is little substantive evidence supporting the case that the portfolio effects arising from this merger may lead to foreclosure concerns, or that the merger significantly increases the ability and incentive to do so. In the absence of such evidence, the

OFT does not believe that a merged Capital/GWR would have either the ability or the incentive to engage in the sorts of anti-competitive conduct described above, and therefore substantially lessen competition in national radio advertising.

Local advertising

33. As noted above, there are limited overlaps in the parties' commercial radio activities. These arise only in the East and West Midlands, London and the North West.

34. In the latter three areas, irrespective of the measures used, the merged entity would not appear to have substantial market power.

- In the West Midlands, Capital's 96.4 BRMB overlaps on its periphery with 3 GWR stations and 2 Classic Gold stations. The degree of geographic overlap between the parties' stations is limited, with GWR stations focusing on different core areas. NMR data indicates that very few local advertisers and no national advertisers use both the parties' stations. Churn data provided by the parties suggests it is uncommon for advertisers to switch between Capital and GWR stations. Third party evidence suggests that the combined group will continue to face competition from other regional FM licences. No third parties raised particular competition concerns about the West Midlands area.

- In London, there is only a very limited overlap between the 5 Capital stations and 7 GWR stations (which operate around the periphery of Greater London) and 2 Classic Gold stations. Other strong competitors exist in London and the parties point to the fact that Capital FM's shares of audience and NAR have significantly declined, while those of its competitors have grown. One competitor was concerned that customers could not buy around in London but did not provide any evidence to substantiate its claim. Few local advertisers use both parties' stations in the London area. Only one local advertiser raised concerns about competition in the London Orbital area.

- In the North West, Capital's 105.4 Century FM overlaps on its periphery with 3 GWR stations and 1 Classic Gold station. Capital and GWR stations focus on different core areas and are of a different scale. The degree of overlap between the parties' stations is limited. NMR data indicates that there are very few common advertisers between the parties' stations and churn data provided by the parties suggests that there is not significant switching between Capital and GWR stations in the area. Third party evidence suggests that the combined group will face competition from other radio groups. No local advertisers have raised competition concerns about the North West area.

East Midlands

35. In relation to the fourth area, the East Midlands, Capital's Century 106 FM overlaps with 5 GWR stations and 4 Classic Gold stations. Post merger, the parties will hold [45-55] per cent (increment [15-25] per cent)[18] of local NAR within Century's MCA. This measure of local concentration raises potential issues requiring further investigation.

36. In the East Midlands, the extent of competition between the stations is unclear. Capital's station has a wider geographic coverage than the GWR stations and there appear to be only a limited number of common advertisers between the two radio groups in this area. On the other hand, the East Midlands was identified as an area of potential concern by both national and local advertisers.

37. In order to consider the availability of competing alternative stations in the East Midlands, Capital and GWR conducted further buy-around analysis. This analysis did not cover customers using Century and GWR's Trent station as the parties assumed that buy-around in this context was not possible. In respect of overlaps with other GWR stations, the analysis showed that for certain audience demographic profiles in the East Midlands area there were no alternatives. The only alternative station is Saga, which targets a different demographic group to the parties' stations. As noted above, there were some local advertisers in this area which considered local newspapers to be a competitive alternative to local radio. However, views on this point were very mixed among local advertisers, and national advertising customers did not consider local newspapers to be a realistic alternative when building their national strategies.

38. The possibilities for new entry in the East Midlands to compete with the merged Capital/GWR are remote. Although there is likely to be a growing constraint from digital radio and from the issue of 30 new FM licences due to be awarded shortly by Ofcom, both of these factors are currently too uncertain for the OFT to rely on as being sufficient in time, scope and likelihood to deter or defeat any attempt by the merged entity to exploit the reduction in rivalry flowing from the merger.

39. Finally, the competitive pressure represented by buyer power is slight in the East Midlands. First, small local advertisers wield limited bargaining power. Second, given the views expressed above that, for certain key demographics, Capital/GWR will be the only post-merger choice, buyer power for national advertisers is

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[18] Text amended at the request of the parties as containing commercially confidential information.

unlikely to be a material competitive constraint on the merging parties' commercial conduct in the East Midlands.

Conclusion

40. Third party concerns and buy-around analyses conducted for the East Midlands region support the case that switching to an alternative (non Capital/GWR) station in this area would be difficult. As such the removal of Century 106 FM as the closest competitor to GWR's stations will substantially lessen competition for local radio advertising in the area.

DIGITAL SERVICES

Relevant market

41. A multiplex is essentially a platform for digital radio. Multiplexes are local, regional or national in scope.[19] Ofcom has to date licensed and regulates 46 multiplexes in the UK. Ofcom also licences the Digital Sound Programme Service Providers (DSPSP) that the multiplex operator must contract with to provide programming.

42. Most multiplex capacity is contracted to DSPSPs by the multiplex operator at the time of the application by the operator for a multiplex licence. (Only small, local multiplexes tend to have spare capacity at the time of launch.) Ofcom's regulatory framework for digital radio multiplexes is that any single firm cannot own interests in overlapping local multiplexes. [GWR already owns the only commercial national multiplex].

43. The multiplex operator does not have any control over the format of a DSPSP's programming once it has been agreed with Ofcom. Nor does it have any control over the advertising or programming of the stations. Multiplex licences typically last for 12 years and multiplex operators prefer to agree contracts with DSPSPs for a similar period. No party may have more than four DSPSPs operating in a local radio multiplex area.

44. Capital and GWR both have digital radio interests. In particular, Capital owns outright four local digital multiplexes, has a 50 per cent holding in three more and minority interests in a further seven. GWR owns a controlling interest in the national commercial digital multiplex operator, controls 14 local digital multiplexes and has a minority investment in one London multiplex.

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[19] Regional multiplexes refers to larger local multiplexes.

Competitive assessment

45. Third party concerns may be summarised in two ways: first, that the merger will substantially reduce bidding competition for any new multiplex capacity being auctioned by Ofcom; and second, that the merger will give the parties the ability to increase prices to other users of multiplex capacity and thereby foreclose them from the growing digital radio sector. For the reasons explained below, the OFT does not consider there to be any realistic prospect of this merger resulting in a substantial lessening of competition on either basis.

46. First, as to bidding competition for new multiplex licences, Ofcom is unconcerned about any reduction in bidding competition for multiplexes. As the body charged with auctioning any new capacity the fact that it considers there to be sufficient alternative bidders for multiplex licences carries some weight. In any case many bids for the initial multiplexes were uncontested.

47. Second, as to possible foreclosure from multiplex capacity, since the merged entity would either own outright or hold shares in 28 of the 46 multiplex licenses currently available (including the only national multiplex), third parties fear that rival radio stations could face higher costs or barriers to entry at a time when digital radio becomes more important. This prospect seems remote for the following three reasons.

- Since contracts between multiplex operators and DSPSPs tends to be for the full duration of a multiplex licence and typically include prescriptive pricing terms covering the full duration of the contract, there is little scope for any price increases over the lifetime of existing contracts.

- Ofcom's regulatory framework requires multiplex operators to offer non-discriminatory access terms and conditions to all DSPSPs. Capital and GWR noted that the current situation of digital multiplex over-capacity means that there is no scope to increase prices in any event to a new DSPSP.

- To the extent that Ofcom considered there to be a concern here related to access prices or capacity restrictions, it could release more multiplex capacity that would discipline the merged entity.

THIRD PARTY VIEWS

48. The OFT contacted some 180 competitors and customers. Only a small proportion of those responded. Views were mixed, with media buyers far more concerned than national advertisers.

49. Ofcom undertook extensive analysis of the merger as part of its licensing remit. Where this analysis allowed for competitive assessment, Ofcom only identified competition issues in the East Midlands. This reflected the comments it was hearing from the industry. It saw buyer power as the main constraint on the merged entity's position in national radio advertising.

ASSESSMENT

50. Capital and GWR are both commercial radio groups active in the UK. They broadcast radio programming to listeners, provide national and local advertising airtime to advertisers, and provide digital multiplex services to digital sound programming services providers.

51. Although Capital and GWR will together account for some 40 per cent of UK net advertising revenue from radio, this gives a poor measure of the extent to which they do compete with each other. Capital's and GWR's respective radio stations cover largely different parts of the UK. While some customers see Capital's and GWR's stations as substitutable, the balance of evidence suggests that the parties' stations are really complements: this is because the specific geographic area targeted is a consideration in planning all advertising campaigns, hence substitution across geographic areas (and between radio stations in different areas) is difficult. In any event, even if there were some degree of competition between Capital's and GWR's packages of radio stations, the available evidence leads the OFT to believe that there will be clear possibilities post-merger for national advertisers to switch away from the merged entity to alternative stations when building a package of stations for a national campaign.

52. The majority of third party concern has focused on the merger's claimed portfolio effects. However, the OFT believes that the prospects of a combination of Capital's and GWR's respective packages of stations providing a compelling 'one-stop shop' for radio advertisers are remote. As regards the possibility that the merger might change Capital's and GWR's incentives to engage in tying or bundling strategies to anti-competitive effect, although the theories advanced may be more than fanciful, overall there is little evidence supporting the case that the merger significantly increases the ability and incentive of Capital and GWR to engage in such strategies. In both cases national customers will retain significant buyer power which, although reduced by the merger, is still considerable.

53. In relation to local advertising the limited overlaps of local radio stations are not significant outside of the East Midlands. In this locality, the parties will hold a significant post-merger position that raised both national and local advertiser concerns. Here, the parties' own buy-around analysis indicated real difficulties in achieving the same East Midlands reach with the same demographic profile using

alternative stations. The prospects for sufficient countervailing competition from other media (such as local newspapers) or new FM or digital radio entry are not sufficiently strong to remove the belief that there may be a substantial lessening of competition as a result of the merger.

54. Finally, as regards digital radio, there is no realistic prospect of a substantial lessening of competition. Ofcom's control over the bidding process for new multiplex licences would address any putative concern about intensity of bidding competition. In addition, the regulatory framework for multiplex operator licences, existing long-term contracts and the availability of new multiplex capacity will discipline the merged entity's operation of its digital multiplex interests.

55. Consequently, the OFT believes that it is or may be the case that the merger may be expected to result in a substantial lessening of competition within a market or markets in the United Kingdom, specifically in the supply of radio advertising airtime in the East Midlands.

UNDERTAKINGS IN LIEU OF REFERENCE

56. Where the duty to make a reference under section 33(1) of the Act is met, pursuant to section 73(2) of the Act the OFT may, instead of making such a reference, accept from such of the parties concerned as it considers appropriate undertakings to take such action as it considers appropriate for the purpose of remedying, mitigating or preventing the substantial lessening of competition concerned or any adverse effect which may be expected to result from it.

57. The OFT has therefore considered whether there might be undertakings in lieu of reference which would address the competition concerns outlined above. The OFT's guidance on undertakings in lieu of reference state that, 'undertakings in lieu of reference are appropriate only where the competition concerns raised by the merger and the remedies proposed to address them are clear cut.'[20]

58. In lieu of reference to the Competition Commission, the parties have offered to divest the Capital Radio station in the East Midlands, Century 106 FM. The OFT considers that this proposed undertaking will clearly address the local advertising concern identified above in relation to the East Midlands. This remedy is also capable of ready implementation since the assets required to carry on the Century 106 FM business can be readily identified.

59. It should also be noted that, since the East Midlands was one of the areas in respect of which national advertisers raised concerns about inability to buy-around the merging parties, this proposed divestment also mitigates those concerns.

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

DECISION

61. The OFT is not referring the anticipated acquisition by Capital Radio plc of GWR Group plc to the Competition Commission on the information currently available to it because it is considering whether, instead of making a reference, to accept appropriate undertakings from Capital Radio plc to address the competition concerns arising from the merger.

[20] See *Mergers – substantive assessment guidance*, para. 8.3.