

## FACEBOOK INC / GIPHY INC

### Summary of Provisional Findings

**Notified: 12 August 2021**

#### Overview of our findings

1. The Competition and Markets Authority (**CMA**) has provisionally found that the merger between Facebook, Inc. (**Facebook**) and GIPHY, Inc. (**GIPHY – together, the Parties**) (the **Merger**) has resulted or would result in a substantial lessening of competition (**SLC**) in social media and display advertising, harming social media users and businesses in the UK.
2. The report and its appendices, which will be published shortly after this summary, constitute the CMA's **Provisional Findings**. We invite any interested parties to make representations on these provisional findings by no later than **2 September 2021**. Interested parties should refer to the notice of provisional findings for details of how to do this.
3. Facebook completed the acquisition of GIPHY on 15 May 2020, but has been required to hold the businesses separate since 9 June 2020, when the CMA imposed an Initial Enforcement Order. In our notice of possible remedies published alongside our Provisional Findings, we have set out our initial view that the only effective way to address the competition issues that we have identified is for Facebook to sell GIPHY, in its entirety, to a suitable buyer. We also invite submissions from interested parties on these initial views by **25 August 2021**.

#### Who are the businesses and what services do they provide?

***Facebook is by far the largest provider of social media and messaging services in the UK***

4. The Facebook group offers various online products and services to customers in the UK. This includes popular social media and messaging platforms such as the Facebook app, Instagram, Messenger and WhatsApp. Facebook is by far the largest provider of social media and messaging services in the UK, by

number of users. Indeed over 80% of UK internet users access at least one Facebook site per month. Such platforms are generally provided to users for no monetary cost. However, Facebook's platforms (alongside many other social media platforms) are multi-sided in nature, meaning that they supply services to two or more distinct, but related, customer groups. In Facebook's case, in addition to serving users, who use Facebook's social media and messaging platforms to connect with their friends and family, it also serves advertisers, who use Facebook's platforms to market their products to users, and in return, pay Facebook a fee.

5. Multi-sided platforms such as Facebook are often characterised by network effects, in that the value of the product for users on one side of the platform depends on the number of users either on the same side of the platform, or on the other side. For example, in Facebook's case, having a large user-base on its social media platform makes it more attractive to advertisers. Facebook's business model, and the business model of other social media platforms, therefore relies on attracting and retaining users' attention (and gathering data about them), which they then use to sell advertising.
6. An important way of attracting users' attention is by offering engaging content and features. Social media platforms, including Facebook and its rivals (eg Snapchat, TikTok, Twitter), therefore compete to offer users interesting content and features to keep them engaged on their platform for longer. Some of these features and content are provided by the social media platforms and some of it is provided by external providers, or the users themselves (eg photo-sharing on Instagram).
7. A popular feature on social media and messaging platforms are GIFs and GIF stickers, such as those provided by GIPHY.

***GIPHY is the world's leading provider of free GIFs and GIF stickers***

8. GIPHY provides an online database and search engine that allows users to search and share GIFs and GIF stickers. A GIF (or video GIF) is a digital file that displays a short, looping, soundless video, while a GIF sticker displays an animated image comprised of a transparent (or semi-transparent) background which is placed over images or text (such as a Story on Instagram or Snapchat). We use the term 'GIF' to refer to both video GIFs and GIF stickers).
9. While the GIF file format was invented in the 1980s, the onset of social media provided an opportunity to reimagine the GIF as a part of modern internet culture. The main GIF libraries that are used today were launched less than

ten years ago, and the popularity of GIFs has grown enormously since then. Every day, millions of users in the UK post content that includes a GIF.

10. GIPHY describes itself as the world's largest library of free GIFs and stickers. GIPHY offers its GIFs and GIF stickers to UK users both on its own website and app, and via Application Programming Interfaces (**APIs**) or Software Development Kits (**SDKs**) that allow apps (eg Snapchat, TikTok, Facebook, Instagram) to integrate GIPHY's GIF and GIF sticker databases. These integrations allow GIPHY to reach a wide audience, making it the second largest search engine after Google by number of searches.
11. Like Facebook, GIPHY's products are offered free of charge to users and companies using its APIs and SDKs, as well as on GIPHY's own website and app. While GIPHY's API partners do not pay for access to GIPHY's products, these products are important to some API partners as a tool for enhancing user engagement. Until May 2020, GIPHY generated revenues in the United States by offering brand partners a 'Paid Alignment' service to align their GIFs with popular search terms (so that users see them first when searching for a GIF), or to insert them into GIPHY's trending feed, in exchange for payment. In the context of its acquisition of GIPHY, Facebook required the termination of all Paid Alignment activities.

## **Our assessment**

### ***Why are we examining this Merger?***

12. The CMA's primary duty is to seek to promote competition, both within and outside the UK, for the benefit of UK consumers. Following an initial 'phase 1' investigation, the Merger was referred for a more in-depth 'phase 2' investigation on 1 April 2021. At phase 2, the CMA considers whether:
  - (a) there is a 'relevant merger situation' for the purposes of the Enterprise Act 2002,
  - (b) that relevant merger situation has resulted, or may be expected to result, in a substantial lessening of competition (**SLC**) within any market or markets in the UK for goods or services, and
  - (c) if so, whether remedial action should be taken, and if so, what action and by whom.
13. While both Facebook and GIPHY are US-based entities (and prior to the Merger, GIPHY's revenue-generating activities were limited to the US), the important question for the CMA is whether the Merger may have an impact on

competition in the UK. This link to the UK is established by meeting one of two jurisdiction tests: (i) the turnover test (based on the target's turnover in the UK), and (ii) the share of supply test (requiring that the Parties together supply at least 25% of a particular good or service supplied in the UK, and there is an increment to the share of supply).

14. Facebook and GIPHY are both active in the UK, and provide services to UK users. In this case, we provisionally conclude that the Merger has resulted in the creation of a relevant merger situation on the basis of the share of supply test, as the Parties overlap in the supply of:
  - (a) apps and/or websites that allow UK users to search for and share GIFs, in which the Parties have a combined share (by average monthly searches) of [50-60]% with an increment of [0-5]%; and
  - (b) searchable libraries of animated stickers (including both GIF and non-GIF stickers), provided direct to users in the UK, in which the Parties have a combined share (by sticker library size) of [80-90]% with an increment of [0-5]%.

#### ***How have we examined this Merger?***

15. In deciding whether a Merger has resulted, or may be expected to result, in an SLC, the CMA must apply a 'balance of probabilities' standard. This means that the CMA must decide whether it is *more likely than not* that a Merger will result in an SLC.
16. To determine whether this is the case, we have gathered information from a wide variety of sources, using our statutory powers to ensure that we have as complete a picture as possible under the constraints of the statutory timetable to understand the implications of this Merger on competition. The evidence we have gathered has been tested rigorously, and the context in which the evidence was produced has been considered when deciding how much weight to give it.
17. At phase 2, we have focused on two ways in which the Merger could give rise to an SLC. Both of these 'theories of harm' relate to the two-sided market for social media services and display advertising:
  - (a) horizontal unilateral effects resulting from loss of potential competition in display advertising; and
  - (b) vertical effects resulting from input foreclosure in relation to the supply of social media.

18. We provisionally conclude that the Merger is more likely than not to give rise to an SLC on both counts. This is discussed in further detail below.

***What evidence have we looked at?***

19. In assessing this Merger, we looked at a wide range of evidence that we considered in the round to reach our provisional decision.
20. We examined the Parties' own internal documents which show how they run their businesses and how they view their partners and their rivals in the ordinary course of business. Such internal documents can also be helpful in understanding the Parties' plans for the future of their businesses. We undertook a widescale review having collected over 280,000 internal documents from the Parties.
21. We spoke to and gathered evidence from other market participants in the industry to understand better the competitive landscape for the provision of GIF libraries, including the GIF advertising model, and to get their views on the impact of the Merger. In particular, we spoke to the following four categories of market players:
  - (a) social media and messaging platforms and providers of keyboard apps;
  - (b) GIF providers;
  - (c) investors and potential investors in GIPHY; and
  - (d) advertising companies and brands familiar with GIPHY's Paid Alignment advertising services.
22. We also considered the internal documents of certain social media and messaging platforms, and those of GIPHY's key investors, in order to determine how others viewed the GIPHY business prior to the Merger and GIFs more generally, and how they reacted to the Merger.
23. We also calculated market shares. However, in markets such as the ones in which Facebook and GIPHY operate, where there is a wide range of different products and offerings, and where new features and products are introduced regularly, it can be difficult to define the precise boundaries of a 'market'. In these circumstances, when assessing the impact of the merger on competition, the CMA will consider evidence on market shares, if helpful, alongside evidence on how closely the merging parties compete (either currently or in the future). As well as the size of the Parties' market shares, our assessment of the extent to which Facebook and GIPHY have market power also took into account the stability of the relevant market shares, the

strength of competitive constraints on the Parties, and the extent of past entry and exit from the relevant markets.

24. Finally, as well as looking at how competition works currently (and the Parties' current shares of the relevant markets), we recognise that markets, and in particular markets for digital products and services such as those offered by the Parties, change over time. Our assessment is therefore forward-looking and considers the Parties' plans for their businesses in future.

### ***What did this evidence tell us...?***

#### *... about market power?*

25. Market power is typically used to refer to firms who have such strength in a particular market that they are able to influence the price of the goods or services that they sell (eg charging higher prices than they would be able to if an industry was more competitive). This could also be the case in relation to non-price factors such as quality of a good or service, or level of innovation. We therefore considered the relative strength of the Parties in the markets in which they operate. For GIPHY, this is searchable GIF libraries, while for Facebook, this is social media and display advertising. In assessing this relative strength, we considered the other options available to the Parties' customers or users and whether they offer a good alternative to the Parties.
26. In relation to **searchable GIF libraries**, we have provisionally found that social media and messaging platforms have very limited choice of alternatives to GIPHY. Tenor (owned by Google) is GIPHY's only close competitor. GIPHY has a number of distinctive features that may make it particularly attractive to social media platforms, for example, the quality of its content, its reach among distribution partners and the fact that, at the time of the Merger, GIPHY was the only significant provider of GIF-based advertising services. All of this points towards GIPHY having market power in the supply of searchable GIF libraries.
27. In relation to the supply of **social media**, our investigation has provisionally found that Facebook has significant market power. In particular, we considered the fact that the Facebook platforms make up by far the highest share of user time spent on social media in the UK and that other platforms tend to be accessed in addition to the Facebook platforms, rather than as an alternative to them. These provisional findings are also consistent with the findings of the CMA's Online Platforms and Digital Advertising Market Study (the **Market Study**) in 2020, which found that Facebook's platforms had a combined share of 73% of time spent on social media.

28. Finally, in relation to **display advertising**, our provisional view is that Facebook also has significant market power in display advertising in the UK. Display advertising is a form of digital advertising where advertisers pay online companies such as social media platforms to display their advertising on their web pages or mobile apps. This is in contrast to search advertising where advertisers pay online companies to link their company website to a specific search word or phrase. Display advertising is an important industry in the UK, worth over GBP 5.5 billion in 2019. Our analysis shows that the Facebook platforms currently have a combined market share of around [40-50]%. Again, this is largely consistent with the findings of the Market Study.

*...about what would have happened had the Merger not taken place?*

29. In order to provide a comparator and determine the impact that the Merger may have on competition, we have considered what would have happened had the Merger not taken place. This is known as the counterfactual.
30. The Parties told us that it was likely that GIPHY would have become a significantly weakened business had it not been bought by Facebook. Our provisional view is that, had the Merger not gone ahead, GIPHY would have continued to supply GIFs to social media platforms (including Facebook), as it had done before the Merger, and would have continued to innovate, develop its products and services, generate revenue and explore (with the financial and commercial support of investors) various options to further monetise its products. This would have been the case regardless of GIPHY's ownership (ie whether it were to operate independently, as it did before the Merger, or in the hands of an alternative purchaser). We consider that GIPHY had a number of possible options for ensuring the ongoing funding of its business in the short and medium term, including generating revenue through its Paid Alignment model, agreeing a fee for using its services on major social media platforms, obtaining additional funding from existing investors, or sale to an alternative purchaser.
31. We also noted the short-term impact that Coronavirus (COVID-19) had on GIPHY's business prior to the Merger. However, we have not seen any evidence to demonstrate that Coronavirus (COVID-19) would have had a long-term, structural impact on GIPHY's ability to innovate and generate revenue had the Merger not taken place.
32. We also considered what Facebook would have done had the Merger not taken place. As noted above, GIFs are an important driver of user engagement on social media and messaging platforms, including Facebook's platforms, and Facebook told us that a key part of its rationale for acquiring GIPHY was to ensure its continued access to a supply of GIFs in future. We

have therefore assessed the alternative options available to Facebook to ensure continued availability of high-quality GIFs had the Merger not gone ahead, namely: (i) paying some form of platform fee or licence fee to GIPHY, (ii) relying more heavily on other GIF providers (eg Tenor), or (iii) building its own GIF library.

33. Following an assessment of the Parties' internal documents which discussed these options in some detail, our provisional view is that it was likely that Facebook would have continued to procure GIFs from GIPHY had the Merger not taken place, rather than choosing one of the alternative options set out above. We also consider that if Facebook were to develop its own GIF library, this would have been in the longer term and it would have continued to rely on GIPHY in the interim.
34. Our assessment of the effects of the Merger is therefore considered in comparison to a scenario in which, had the Merger not gone ahead, GIPHY would have continued to supply GIFs, innovate, develop its products and services, generate revenue and explore various options to further monetise its products, and Facebook would have continued to procure GIFs from GIPHY, at least in the short to medium term.

*...about any horizontal effects of the Merger?*

35. One of the potential concerns that we have investigated is whether the Merger could lead to horizontal unilateral effects as a result of loss of potential competition. What we mean by this is the possibility that the Merger could remove from the market a business that was competing, or had the potential to compete, with Facebook. In this case we are particularly interested in whether GIPHY could have competed with Facebook in relation to display advertising in the UK. We describe this as 'horizontal' effects because, in this respect, Facebook and GIPHY would both be active at the same level of the supply chain (ie offering display advertising). We consider that GIPHY's Paid Alignment model competes closely with display advertising, such as that offered on Facebook's platforms, in particular because GIPHY's advertising model is typically used to raise brand awareness (as with display advertising), rather than to drive purchases of specific products or services (as with search advertising).
36. In some sectors, including fast-moving technology markets such as the one in which Facebook and GIPHY operate, an important aspect of how firms compete involves efforts or investments aimed at protecting or expanding their profits in the future.

37. One of GIPHY's key innovations was its Paid Alignment advertising proposition, which it first offered in 2017 in the US and which it was making efforts to expand. Under this model, GIPHY obtained payment from advertisers in exchange for advertising. GIPHY had also entered into revenue-sharing agreements with certain social media partners in the US, under which GIPHY would give partners a share of its advertising revenues in exchange for the partners allowing GIPHY to run its Paid Alignment advertising on these partners' platforms. Paid Alignment was used by a number of leading international consumer brands, including Pepsi and Dunkin' Donuts, and was increasingly growing, both in revenue and number of advertisers using the service, until the Merger in May 2020. In the context of the Merger, Facebook required the termination of all Paid Alignment activities.
38. The Parties told us that GIPHY's advertising model was flawed for a number of reasons, including because GIPHY's user base was largely achieved through API integrations with social media platforms, it could not provide brands with helpful audience data and metrics, and it could not offer 'direct response' ads (where the user clicks on the ad to buy the product).
39. However, most of the advertisers that we spoke to were positive about their experience of working with GIPHY, and some of them told us that they had been able to monitor the effectiveness of their advertising with GIPHY to a level that they were satisfied with. This is also reflected in GIPHY's internal documents. Our investigation also found that there were a number of potential advantages to GIPHY's Paid Alignment model which may have outweighed its disadvantages – for example:
- (a) The advertising has been specifically selected by the user to express a particular idea or emotion to the recipient, which has the potential to make the ad very personal and impactful.
  - (b) Similarly, advertising through private messaging, such as Paid Alignments, provides an air of credibility to the advertising, as it is shared by someone that you trust in a private forum.
  - (c) We also heard that an advantage of advertising using GIFs was the fact that they operate on a loop, meaning that one GIF might be seen by users a number of times.
  - (d) Finally, we note that messaging has historically been a difficult format for providers to use to generate revenue, as most forms of advertising significantly worsen the user experience. However, due to its GIF format, the Paid Alignment model of advertising is subtle and intrinsic to the message, rather than interrupting it. This is reflected in GIPHY's internal

documents. Facebook's internal documents also discuss the importance of monetising messaging.

40. We also note from GIPHY's internal documents that GIPHY hoped to develop its Paid Alignments product and expand its offering internationally, including into the UK. Prior to the Coronavirus (COVID-19) pandemic, GIPHY was considering how to respond to significant interest from advertisers regarding international expansion.
41. Despite these plans for expansion, GIPHY's forecasts did not envisage becoming anything like the size or scale of Facebook in the medium term. However, given Facebook's significant market power in display advertising (as discussed above), the acquisition by Facebook of a potential entrant may be concerning, even if that potential entrant is expected to be small.
42. By removing GIPHY from the market, we consider that the Merger has removed a firm with pre-Merger activities that we consider were likely to be valuable in driving other companies' (including Facebook's) efforts in display advertising. GIPHY's efforts to innovate and monetise its services prior to the Merger were valuable, as they increased the likelihood of new innovations and products being made available in future, even allowing for the possibility that GIPHY's Paid Alignment model ultimately might not have been successful. This is the case both for those products and innovations that GIPHY had already begun to develop itself or may have developed in future, but also for any developments that may have been made by Facebook in response to the possibility of competition from GIPHY, or from other social media platforms in partnership with GIPHY. By removing GIPHY, the Merger has eliminated this form of 'dynamic' competition.
43. We consider that the loss of GIPHY as a potential competitor in display advertising is substantial in the light of:
  - (a) Facebook's significant market power in display advertising (as discussed above);
  - (b) GIPHY's strong position as a leading provider of an important social media engagement tool;
  - (c) GIPHY's efforts in recent years to monetise its services, using an innovative advertising model, which had the potential to compete against Facebook for display advertising revenues;
  - (d) Evidence that Facebook and other market participants were also interested in monetising the same or similar social media features;

- (e) The fact that successful expansion into a multi-sided market such as display advertising can be magnified by network effects (eg GIPHY's Paid Alignment model could have generated additional revenues for Facebook's rival social media platforms, leading them to invest more in attracting new users; while if Facebook owns and controls GIPHY, it will be able to reinforce its strong position in this space); and
  - (f) The high barriers to entry in display advertising, demonstrated by very limited successful entry in the market since Facebook became market leader. GIPHY has already developed a large user base and begun to grow its advertising revenue, despite a number of challenges. Another potential competitor may face even more challenges in a world in which the two largest GIF providers, GIPHY and Tenor, are owned by two of the largest tech companies, Facebook and Google.
44. On the basis of the evidence we have seen to date, we therefore consider that the Merger will result in an SLC as a result of horizontal effects, in the form of a loss of potential competition.

*...about any vertical effects of the Merger?*

45. As set out above, GIPHY allows apps (eg social media platforms such as Snapchat, TikTok, Facebook, Instagram) to integrate GIPHY's GIF and GIF sticker databases into their own platforms via an API or SDK free of charge. One of the potential concerns that we have investigated is whether Facebook could disadvantage its rivals in social media by limiting their access to GIPHY in some way, either by preventing them from accessing GIPHY at all, or allowing them to access GIPHY but on worse terms than they did before the Merger. This is known as foreclosure. We describe this as 'vertical' effects because, in this respect, Facebook and GIPHY are operating at different levels of the supply chain (ie GIPHY is acting as an input into Facebook's, and its rivals', products).
46. Our assessment has focused on whether Facebook would have the **ability** and **incentive** to limit access to GIPHY in this way, and whether this 'foreclosure' would have an **effect** on the ability of rival apps to compete with Facebook in social media. We also specifically assessed whether Facebook would be able to disadvantage its rivals by reprioritising innovation and development of GIPHY's services towards the requirements of Facebook's own platforms rather than those of other social media platforms, or by requiring rival platforms to provide more data (eg on individual or aggregate user behaviour) in order to access GIPHY.

47. As discussed above, our assessment has shown that GIPHY has a number of distinctive qualities which mean that many social media platforms rely on it to facilitate user expression. Our assessment of the Parties' internal documents and our discussions with other players in the industry suggest that GIFs are an important feature for social media platforms (including Facebook), particularly in relation to encouraging user engagement. As noted above, GIFs are a popular feature of social media platforms, with the proportion of users posting content that included a GIF being over 25% on some platforms. We also found that there was only one other GIF provider offering a comparable service to GIPHY: Tenor, which is owned by Google. On this basis we consider that following the Merger, Facebook does have the ability to foreclose its rivals.
48. In determining whether Facebook has the incentive to foreclose, we have assessed the costs and benefits of this strategy for Facebook. We have provisionally found that there would be direct benefits of foreclosure to Facebook, in that reducing the engaging features available on a rival social media platform may mean that users switch at least a proportion of their time to other platforms and that, due to Facebook's high share of the market, this is likely to be to a Facebook platform; this in turn may encourage their friends and followers to switch too. We have also considered whether there would be a cost to Facebook of foreclosure, as by limiting access to GIPHY, Facebook would lose (at least partly) the benefit to GIPHY in having a wide pool of users (which makes it more attractive to content creators and to advertising partners). However, we have provisionally found that even if GIPHY were removed from all other platforms, the large user base of Facebook's platforms would mean that it would still be an attractive proposition to partners and creators. A foreclosure strategy targeting one or more specific rival platforms would have even fewer costs. On this basis we consider that Facebook would also have an incentive to foreclose its rivals from access to GIPHY.
49. Our provisional view is that this strategy would have the effect of strengthening Facebook's existing significant market power in social media, and reducing the competition that it faces from others. On the basis of the evidence we have seen to date, we therefore provisionally conclude that the Merger will result an SLC as a result of vertical effects, in the form of input foreclosure.

*...about any countervailing factors?*

50. Once we have decided that a Merger could give rise to an SLC, we also consider whether there are any factors that might prevent or mitigate against that SLC from arising. These are known as countervailing factors. In this case,

we focused on whether there could be any new entrants to the supply of searchable GIF libraries that could prevent an SLC from arising.

51. The evidence that we have collected shows that there are five main barriers to entering or expanding in relation to searchable GIF libraries, and on this basis a new entrant or an existing small provider would face considerable challenges in trying to grow or compete at scale:
  - (a) A large, high-quality content library;
  - (b) A sophisticated search engine;
  - (c) Scale and brand;
  - (d) A viable monetisation model; and
  - (e) Capital.
52. As described above, recent new entrants and smaller GIF providers have not to date been able to reach the same size and quality as GIPHY and Tenor.
53. Our assessment has provisionally concluded that it is not likely that entry or expansion of sufficient scale would occur in a timely manner in order to prevent or reduce the impact of an SLC from arising as a result of this Merger.

## **Provisional conclusions**

54. As a result of our investigation and our assessment, we have provisionally concluded that the completed acquisition by Facebook of GIPHY has resulted or would result in the creation of a relevant merger situation.
55. We have also provisionally concluded that the Merger has resulted or may be expected to result in an SLC:
  - (a) in the supply of display advertising in the UK due to horizontal unilateral effects arising from a loss of dynamic competition, and
  - (b) in the supply of social media services worldwide (including in the UK) due to vertical effects resulting from input foreclosure.
56. Due to the multi-sided nature of the markets in which the Parties operate, a lessening of competition in the supply of social media services also has effects on competition in the supply of display advertising. The vertical effects resulting in a loss of competition in social media that we have highlighted above therefore exacerbate the effects on competition in display advertising arising from the elimination of a potential competitor.