

Anticipated acquisition by Facebook, Inc. of Kustomer, Inc.

Summary of the CMA's decision on relevant merger situation and substantial lessening of competition

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Please note that [X] indicates figures or text which have been deleted or replaced in ranges for reasons of commercial confidentiality

SUMMARY

1. The Competition and Markets Authority (**CMA**) has found that the anticipated acquisition by Facebook, Inc. (**Facebook**) of Kustomer, Inc. (**Kustomer**) does not give rise to a realistic prospect of a substantial lessening of competition (**SLC**) in any market in the UK. Facebook and Kustomer are together referred to as the **Parties**, and for statements referring to the future, as the **Merged Entity**.
2. Facebook agreed to acquire Kustomer on [X] (the **Merger**) for a purchase price of \$[X] million, an amount that represents a very substantial multiple of Kustomer's 2020 global revenues of £[X] million.
3. Facebook is a global technology company offering a range of services to consumers and businesses, including social media platforms, messaging channels (Messenger, WhatsApp and Instagram Messaging), digital advertising and a range of business tools. Facebook's primary revenue-generating activity is offering ads space and related services. Facebook anticipates that it may generate significant revenues in future through its messaging channels.
4. Kustomer was founded in New York in 2015 and offers a software as a service (**SaaS**) customer relationship management (**CRM**) software specialised in customer service and support. This software is designed to help agents in a company's customer service function manage communications with consumers. Kustomer's CRM software integrates with a range of communication channels that can be used for communications between

business and consumers (**B2C**), including phone, email, webchat, SMS, Messenger, WhatsApp, Instagram and Twitter. As part of its CRM software, Kustomer offers a proprietary live webchat communication channel to its CRM customers.

5. The CMA has jurisdiction to review a merger where either (a) the target company generates more than £70 million of turnover in the UK (the turnover test); or (b) the merger results in the Parties having a share of supply of goods or services of any description in the UK of 25% or more (the share of supply test). Kustomer's revenues do not meet the turnover test; however, the CMA has concluded that the Parties together (Facebook's messaging channels and Kustomer's proprietary webchat channel) have a share of more than 25% in the supply of B2C messaging channels. The CMA notes that its analysis is not affected by the relatively small size of the increment resulting from the Merger: Facebook has a very significant share of the B2C messaging segment, and it will typically be the case that the increment resulting from the acquisition of a nascent player will be small. The share of supply test considers the total combined share of the Parties, not the individual share of each merging party.
6. In assessing whether there is a realistic prospect that the Merger would result in a substantial lessening of competition (**SLC**) in any market in the UK, the CMA considered specifically:
 - (a) whether the Merger would raise barriers to entry and expansion by increasing Facebook's data advantage in online display advertising, leading to reduced competition in that market;
 - (b) whether Facebook could harm the competitiveness of other customer service and support CRM software providers by limiting or degrading their access to Facebook's messaging channels;
 - (c) whether Facebook could reduce the competitiveness of other suppliers of B2C messaging services by preventing them from integrating their services with Kustomer; and
 - (d) whether, following the Merger, Facebook could rely on cross subsidisation from its online display advertising business to offer Kustomer on a free or freemium basis making it difficult for other suppliers of CRM services to compete.
7. The CMA has carefully considered how the Merger might affect competition in the markets in which the Parties operate, taking into account current competition in those markets, anticipated future developments, and the

Parties' business strategies. Facebook's acquisition of Kustomer is part of its strategy to grow its B2C messaging business and the CMA considered how the Merger could affect competition in the markets for online display advertising, customer service CRM, and B2C messaging.

8. Where a supplier has significant existing market power, as Facebook does in online display advertising, the CMA's concern about any given level of constraint removed or reduced by a merger will be greater than in a scenario where a supplier does not have market power. The CMA has, therefore, carefully considered how the Merger may affect Facebook's existing significant market power.
9. In the course of its detailed Phase 1 review, the CMA received input from a wide range of third parties, used its compulsory powers for information gathering, and received more than 25,000 internal documents from the merging parties.

Theory of Harm 1: whether the Merger would raise barriers to entry and expansion by increasing Facebook's data advantage in online display advertising, leading to reduced competition in that market

10. The CMA considered whether the Merger would increase Facebook's data advantage in a way that would raise barriers to entry in online display advertising, making it more difficult for other suppliers to compete with Facebook.
11. In its recent Online Platforms and Digital Advertising Market Study, the CMA found that Facebook has significant market power in online display advertising and is by far the largest supplier of online display advertising in the UK, accounting for more than half of online display advertising expenditure. The CMA also found that Facebook's superior access to data gives it a significant competitive advantage in advertising targeting and acts as a barrier to entry and expansion to actual or potential rivals. The evidence gathered by the CMA in the course of its merger investigation supported the conclusions in the market study, both that Facebook has significant market power in online display advertising and that Facebook's access to data gives it a competitive advantage in advertising targeting.
12. Based on a review of Facebook's documents relating to the acquisition of Kustomer and input from third parties, the CMA found that the Merger would increase the data available to Facebook. First, Kustomer's business customers may opt to give Facebook access to the data about their end customers they store in Kustomer's software. Second, Facebook expects that

it will be able to use Kustomer to increase the use of its B2C messaging services and 'click to message' (**CTM**) ads, and Facebook gathers data from both these sources.

13. The CMA notes that B2C messaging is growing and is expected to continue to grow absent the Merger, which will likely increase Facebook's data advantage. In reviewing a merger, the CMA considers only effects that result from the merger itself. The CMA considers that the current size of Kustomer, even considering its future potential growth, means that the additional data Facebook gains as a result of the Merger would not be expected to raise barriers to entry in online display advertising. Furthermore, the CMA found evidence that Facebook's rivals will be able to access some data similar to the data Facebook can obtain through Kustomer, and most advertising competitors did not express concerns about the Merger.
14. As a result, the CMA believes that there is no realistic prospect that the Merger will result in an SLC as a result of raising barriers to entry by increasing Facebook's data advantage in online display advertising.

Theory of Harm 2: whether Facebook could harm the competitiveness of other customer service and support CRM software providers by limiting or degrading their access to Facebook's messaging channels

15. The CMA considered whether, after the Merger, Facebook could foreclose customer service and support CRM suppliers that compete with Kustomer by restricting or degrading their access to Facebook's messaging channels; that is, whether Facebook could make it more difficult for these companies to compete to win business customers. CRM providers rely on Facebook APIs to connect to Facebook's messaging channels and to integrate them into their software. Business customers of the CRM providers then rely on the CRM's software to connect to Facebook's messaging channels. Some CRM suppliers connect directly to Facebook's APIs and others rely on a communication platform as a service (**CPaaS**) supplier that connects them to multiple messaging channels.
16. The CMA first considered whether Facebook would have the ability to restrict or degrade access to Facebook's messaging APIs in order to harm the competitiveness of CRM rivals. While B2C messaging is still at an early stage of adoption, it is growing quickly and Facebook's messaging channels are by far the largest B2C messaging channels in the UK today. CRM suppliers and business customers confirmed to the CMA that access to Facebook's messaging channels is important to businesses, and CRM providers told the CMA that they would likely lose customers if their access to Facebook's

messaging channels was restricted or degraded. The CMA also concluded that it would be possible for Facebook to restrict or degrade access to its APIs using either technological or contractual means: where a CRM connects directly to Facebook's API, Facebook could deny them access or use technological means to degrade their access; where a CRM connects to Facebook's messaging channels through a CPaaS, Facebook could rely on contractual terms with the CPaaS to restrict the CRM's access.

17. The CMA then considered whether Facebook would have the incentive to restrict or degrade access to Facebook's messaging APIs in order to harm the competitiveness of CRM rivals. The CMA considered Facebook's overall business strategy when assessing its incentive. Facebook generates the large majority of its revenues today through its advertising business. Facebook is seeking to grow its B2C messaging business and considers that this could be a significant source of revenue in the future. Facebook anticipates generating limited revenues through CRM licensing fees, but it will further benefit from business customers using its CRM services through increased access to data, expected increased use of Facebook's B2C messaging channels and CTM ads, and keeping businesses in the Facebook ecosystem for a greater range of activities.
18. In assessing Facebook's incentive to restrict or degrade API access for its CRM rivals, the CMA has considered whether the gains Facebook would generate from businesses that switch to Kustomer would exceed the losses Facebook would incur in connection with those businesses that keep using foreclosed CRM providers. Where businesses keep using a foreclosed CRM provider, Facebook would likely see reduced usage of its messaging channels and CTM ads, and potentially of its other services, resulting in reduced access to data from those business and likely reduced revenue. Limiting or degrading API access could also damage Facebook's reputation among its messaging partners, which could lead them to focus on other suppliers.
19. The CMA found that a number of CRM suppliers focus on serving the same types of business customers as Kustomer – small and medium-sized businesses. There are also larger CRM suppliers, such as Salesforce and Oracle, that serve a broad range of customers, from very large business through to small and medium sized businesses. The CMA found evidence that partnering with CRM suppliers is an important avenue for Facebook to grow its B2C messaging business. Kustomer is not designed to support the needs of large businesses. As such, Facebook is unlikely to limit or degrade access for those CRM suppliers that serve large businesses since doing so would limit Facebook's ability to supply its B2C messaging channels to those large businesses.

20. If Facebook were to restrict or degrade API access to its messaging channels for CRM suppliers that focus on serving small and medium-sized businesses, the CMA expects that some business customers would switch away from those CRM providers. Kustomer is a relatively small provider of CRM services, even to these small and medium-sized businesses, and while some businesses would likely switch to Kustomer, a larger proportion would be expected to switch to competing CRM suppliers, including suppliers such as Salesforce and Oracle that serve both large business and small and medium sized businesses. Given that Kustomer would be unlikely to capture a large proportion of switching businesses, the CMA considers that the gains to Facebook from a foreclosure strategy would be unlikely to exceed the losses. As such, the CMA does not consider that Facebook would have an incentive to pursue such a foreclosure strategy.
21. On that basis, the CMA found that there was no realistic prospect that the Merger would result in an SLC as a result of Facebook foreclosing customer service and support CRM suppliers that compete with Kustomer by restricting or degrading their access to Facebook's messaging channels.

Theory of Harm 3: whether Facebook could reduce the competitiveness of other suppliers of B2C messaging services by preventing them from integrating their services with Kustomer

22. As explained above, Facebook sees integration with CRM suppliers as an important avenue to grow its B2C messaging business. The CMA has considered whether Facebook could harm its B2C messaging rivals, and reduce competition in B2C messaging, by restricting the ability of other B2C messaging channels to integrate with Kustomer's CRM software.
23. The CMA received input from other B2C messaging providers and most of them indicated that they have avenues other than CRM integration to reach business customers.
24. The CMA also considered the significance of Kustomer as a CRM provider. Kustomer is a very small provider of CRM software today. While Kustomer is expected to grow, even if it grew substantially larger than Facebook has forecast in its internal documents, Kustomer would remain a small provider of CRM software. As such, even for B2C messaging rivals that seek to promote their services through CRM connections, many alternatives would remain following the Merger.

25. As such, the CMA found that there is no realistic prospect that the Merger would result in an SLC as a result of Facebook foreclosing its B2C messaging rivals by restricting their ability to integrate with Kustomer's CRM software.

Theory of Harm 4: whether Facebook could rely on cross subsidisation from its online display advertising business to offer Kustomer on a free or freemium basis making it difficult for other suppliers of customer service and support CRM software to compete

26. Advertising on Facebook properties is common among businesses serving consumers. Moreover, Facebook expects that businesses adopting Kustomer CRM software would increase their advertising spend on Facebook. This may give Facebook the ability and incentive to cross-subsidise Kustomer software with advertising revenues, for example by offering it for free. The concern under this theory of harm is that such a strategy may increase barriers to entry and expansion in customer service and support CRM software to such an extent that other providers, who would not be able to generate additional revenues from advertising spend to the same extent as Facebook can, are substantially harmed. This would reduce competition in the market in the medium term.
27. The Parties submitted that the strategy described above would represent price reductions associated with a marginal cost reduction for Facebook, not a cross-subsidy, and that it would be highly beneficial to businesses purchasing CRM software. The CMA agrees that the Merged Entity's incentive to offer Kustomer software on a free or freemium basis would result from merger efficiencies and that, at least in the short term, businesses would benefit from the lower price of Kustomer software. However, the CMA considers that, when one of the merging parties already has significant market power, the presence of large merger-specific efficiencies may result in a reduction of competition in the longer term that more than offsets the short-term customer benefits. The CMA therefore considered whether there is a realistic prospect of this happening in the context of the Merger.
28. The CMA considers that Facebook would have an incentive to cross-subsidise Kustomer, as losses on the provision of CRM software would be compensated by higher revenues from online display advertising and, in the longer term, further services to businesses. The CMA also notes that offering a CRM service on a free or freemium basis would be consistent with Facebook's overall business model, which is based on offering free services and generating revenues through advertising. Furthermore, Facebook's internal documents show [REDACTED].

29. In order for this strategy to result in a reduction of competition, rival CRM providers (either existing or future entrants) would need to be placed at such a disadvantage that their ability to compete would be substantially limited. The reduction in competition needs to be significant enough that the long-term impact on price, quality and innovation in customer service and support CRM software more than offsets the short-term customer benefits from the lower price of Kustomer software.
30. The CMA considers that those conditions are not met in the context of the Merger. The CRM market is characterised by the presence of large and established competitors, and Kustomer is currently a very small supplier. If Kustomer's software were offered at a lower price, that would tend to increase the competitive constraint on larger providers.
31. The CMA needs to consider the effect of a merger on competition in the market rather than on individual competitors. The CMA considers that, even if some competitors would struggle to respond to Facebook offering Kustomer on a free or freemium basis, sufficient competitive constraints would remain. For example, the CMA considers that the largest providers may be in a position to adopt a freemium model, or to develop a basic low-price CRM product targeted at small businesses, with the expectation that CRM revenues would increase as businesses' needs grew. Most importantly, it is not necessary for other CRM providers to replicate the Merged Entity's strategy in order to remain competitive. While price is certainly an important dimension of competition, there are several other dimensions along which CRM providers could compete against the Merged Entity.
32. As a result, the CMA found that the Merger would not give rise to a realistic prospect of an SLC as a result of a cross-subsidisation strategy leading to increased barriers to entry and expansion in customer service and support CRM software.
33. The Merger will therefore **not be referred** under section 33(1) of the Enterprise Act 2002 (the **Act**).