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RAGS IN TATTERS

Local papers are at the heart of the local community, holding local MPs, local authorities and rogue businesses to account: a vibrant local press is vital for our democracy. Yet the local press is in long-term decline. Why? Because of turbulent times, digital transformation, changing consumer preferences, policy blunders, the competition regime, and management waiting too long to respond to structural change. We ask: can anything be done to turn around the distressed business model and ensure that local papers remain in business? For the long term.

RAGS IN TATTERS[1]

"The transition to digital requires consolidation"

INTRODUCTION

The regional press is in long-term decline owing to a combination of changing consumer preferences, new technology, and failed management bets. Arguably there have been some policy blunders and the competition regime may be hampering the future fortunes of the sector. As is the case with so many sectors as they mature, there is a need, at least for some publishers, for consolidation to enable the realisation of cost efficiencies. The economics of the sector are such that for some publishers relatively small scale works – witness Tindle. For others, consolidation is the only way forward. Stay medium-sized, and the numbers don't stack up – the revenues won't cover the costs. We examine the various trends in the sector with a specific focus on the competition regime to assess the extent to which it may be an obstacle to the sector's future viability.

BACKDROP

Stephen Carter's interim Digital Britain Report presented local media groups' views that the transition to digital business models required consolidation but that the then current media merger regime did not take account of potential cross-media competition.[2] The first stage competition authority, the Office of Fair Trading ('OFT') immediately conducted a review, concluding that:

"…the current merger regime, which is broadly the same for newspapers as for other industries, is well placed to take into account developments such as competition from the internet because it is evidence-based and capable of reflecting market realities. The regime is also flexible in that it can take account of valid 'failing firm' arguments, as well as efficiencies and any other benefits to customers brought about through a merger. The OFT has therefore recommended that no legislative changes are needed to the media merger regime."[3]

"Is the competition regime a barrier to success or are management errors and policy blunders to blame?"

Nonetheless, in recognition of the benefit available from Ofcom's knowledge of the media sector, the OFT proposed to amend its merger guidance. Thus in future local media merger cases raising prima facie competition concerns, the OFT would ask Ofcom to provide a Local Media Assessment ('LMA') covering relevant factors arising from Ofcom's understanding of media markets.

"The OFT proposes that it will formally seek Ofcom's view in future newspaper merger cases, given its specific sector knowledge in the UK."[4]

As a result, in November 2010 the OFT and Ofcom agreed on a Memorandum of Understanding ('MoU') setting out the relationship between Ofcom and OFT in relation to LMAs. The MoU requires that the OFT takes account of Ofcom's assessment in its final decision on local media mergers, but that:

"The final conclusion on all aspects of the competitive analysis of the relevant local media merger case remains one for the OFT."[5]

[1] Thanks to Chris Goodall and Ken Harding for their insightful suggestions and comments on an earlier draft of this paper. This paper builds on Sprague, Alison and Olga Nuryaeva (2009), "From riches to rags - prospects for local newspapers." http://www.pwc.co.uk/eng/publications/on_media_5th_edition.html
[2] http://webarchive.nationalarchives.gov.uk/+/http://www.culture.gov.uk/images/publications/digital_britain_interimreportjan09.pdf
[3] http://www.oft.gov.uk/news-and-updates/press/2009/71-09
[4] http://www.oft.gov.uk/news-and-updates/press/2009/71-09
[5] Principles governing an LMA in the Memorandum of Understanding between the OFT and Ofcom on Local Media Assessments, November 2010.

Thus while the OFT reviews Ofcom's assessment relating to proposed mergers, it makes the final decision as whether to refer any relevant mergers to the Competition Commission ('CC') for second phase review.

In the remainder of this paper we assess whether the competition regime is working as Digital Britain's stakeholders intended. We consider three case studies: Kent Messenger, the Topper and Local World (the latter of course being somewhat speculative at this early stage). We consider also other key factors that may be adding to the regional press's woes - turbulent times, digital transformation, changing preferences, policy blunders and/or management mistakes. We also assess in brief whether lessons can be learnt from the US. A key question is: can anything be done to turn around the business model and ensure that regional papers – at the heart of the local community, holding local MPs, local authorities and rogue businesses to account – remain in business. For the long term.

CONSUMERS

"Around 31 million people read a local paper every day"

Consumers like their local paper – according to BMRB/TGI 2012, around 31 million people read one every week (equating to 61% of adults); the local press is the most widely read print medium in Britain. According to the Newspaper Society, the local press sister websites attract around 62 million unique visitors each month and advertising on local newspaper websites is 77% more likely to be believed and relied upon than advertising on other websites (the wanted ads III survey). Another survey, CrowdDNA/Loving Local, reports that more than 60% of people act on the ads in local newspapers. IPA Touchpoints reports an array of positive statistics from its survey:[6]

- Free newspapers are read by 84% of those surveyed;
- 72% state that they trust their local paper more than a national paper;
- 99% agree with the statement, 'I value the local newspapers because they cover local news'; and
- Advertising in local newspapers is trusted more than any other media channel.

Yet despite such promising reports, the local press is in long term decline.

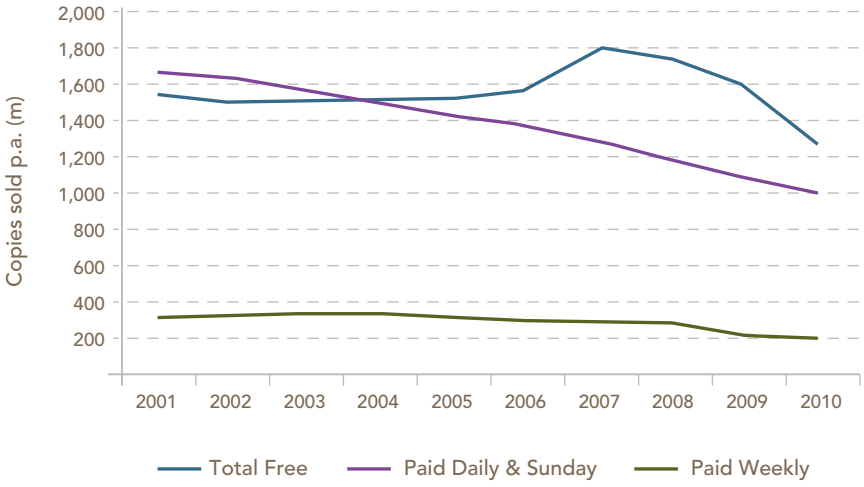
MARKET TRENDS

The Press Gazette states that between 2005 and 2011 around 70 new papers launched but around 242 local newspapers closed.[7] As a result identified "news gaps" include Port Talbot in South Wales, Rugeley in Lancashire, Cannock Chase in Staffordshire, Leominster in Herefordshire and Long Eaton in Derbyshire. Regional circulation trends since 2001 are shown in Figure 1.

[6] http://www.newspapersoc.org.uk/research-and-insight
[7] http://www.pressgazette.co.uk/story.asp?sectioncode=1&storycode=49215&c=1

"But the regional press is in long term decline"

Figure 1: Regional circulation trends[8]



Source: Ofcom (AA/ABC/Newspaper Society)

The most recent publicly available circulation data and number of titles for the regional press publishers are displayed in Table 1. This indicates that there are around 1,100 titles provided by 87 publishers, demonstrating wide range and variety, albeit with most publishers facing continued and not insignificant circulation decline.

Table 1: Circulation of regional newspapers in the UK January 2013 and January 2012

				January 2013		January 2012	
Rank	Group Name	Change in no. of Titles	Change in weekly circulation	No. of titles	Weekly circulation	No. of titles	Weekly circulation
1	Trinity Mirror Plc	-6%	-9%	132	9,197,259	140	10,087,945
2	Newsqueat Media Group	-1%	-8%	186	5,741,423	187	6,247,326
3	Local World (1)	-12%	-11%	115	5,068,765	130	5,664,006
4	Johnston Press Plc	-12%	-21%	215	4,947,195	243	6,248,426
5	Associated Newspapers Ltd	0%	2%	1	3,911,980	1	3,817,120
6	Evening Standard Ltd	0%	0%	1	3,502,530	1	3,503,640
7	Archant	-2%	-7%	65	1,607,081	66	1,725,083
8	D.C. Thomson & Co Ltd	0%	-8%	6	1,453,568	6	1,588,395
9	The Midland News Association Ltd	-6%	-13%	16	1,354,629	17	1,557,750
10	Tindle Newspapers Ltd	7%	0%	78	1,124,369	73	1,122,997
	Northcliffe Media Ltd					91	4,690,109
	Illife News & Media					39	973,897
	Total Top 20 Publishers	-4%	-7%	913	41,328,086	951	44,609,342
	Total Other Publishers	-6%	-13%	141	1,232,642	150	1,424,931
	Total All Publishers (88/87)	-4%	-8%	1054	42,560,728	1101	46,034,273

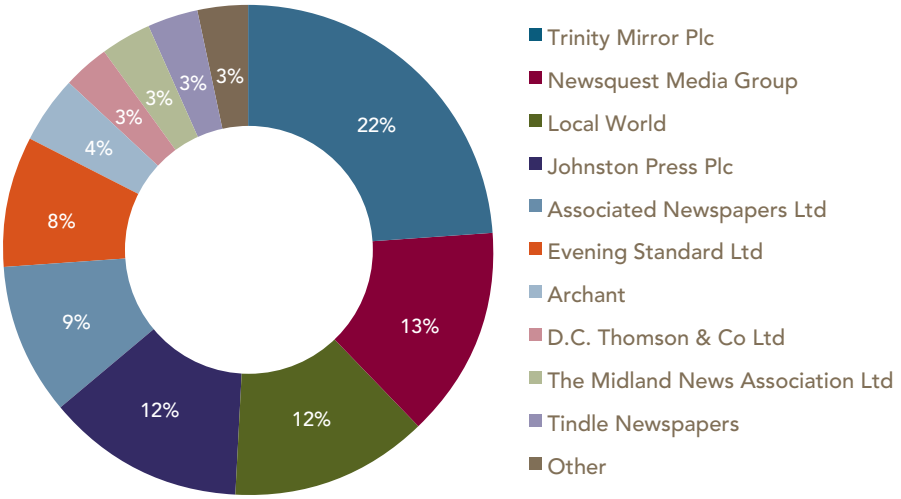
Source: Newspaper Society Intelligence unit 01 January 2013 and 01 January 2012 ABC/VFD/Independently audited figures. Note:(1) No. of titles/weekly circulation presented for Local World is the aggregate of Northcliffe Media and Iliffe News & Media.

[8] These are the latest data available in the public domain.

"The formation of Local World will be examined by the OFT"

The January 2013 circulation data are summarised in the following pie chart, as per Figure 2.

Figure 2: Share of average weekly circulation per title by regional newspaper group



Source: Newspaper Society Intelligence unit 01 January 2013 ABC/VFD/Independently audited figures

UK merger control provides alternative thresholds for mergers which qualify for investigation:

- Turnover test - the UK turnover associated with the enterprise which is being acquired exceeds £70m; or
- Share of supply test - as a result of the merger a share of 25% per cent or more in the supply or consumption of goods or services of a particular description in the UK (or in a substantial part of the UK) is created or enhanced.[9]

As shown above, the combined Northcliffe and Iliffe data demonstrates that Local World has an aggregate share of circulation of 12%. The share of supply test that the OFT applies is 25% (section 23 of the Act), as it determines whether there is a relevant merger situation in the UK.[10] However, the OFT will consider the share of supply test on a 'bottom-up' basis and examine each relevant ('JICREG') area, and then determine whether the areas in which the share of supply exceeds 25% constitute a substantial part of the UK.[11] Notwithstanding the micro analysis, the deal will in any case cross the revenue threshold and will therefore be investigated.

Re-organisation of all the data in Table 1 into a simple metric, average circulation per title, reveals a telling situation, as shown in Figure 3. The figures speak for themselves.

[9] http://www.oft.gov.uk/shared_oft/mergers/642749/OFT1254.pdf
[10] Local World, formed in 2012 by David Montgomery, former CEO of Mecom, combines the businesses of Northcliffe Media Ltd (formerly the regional press arm of DMGT) and Iliffe News & Media. Trinity Mirror has a 20% shareholding but none of its titles are included in the business.
[11] These are areas mapped out by the Joint Industry Committee for Regional Media Research or 'JICREG'.

"Average weekly circulation per title is around 40,000 copies with a very wide range"

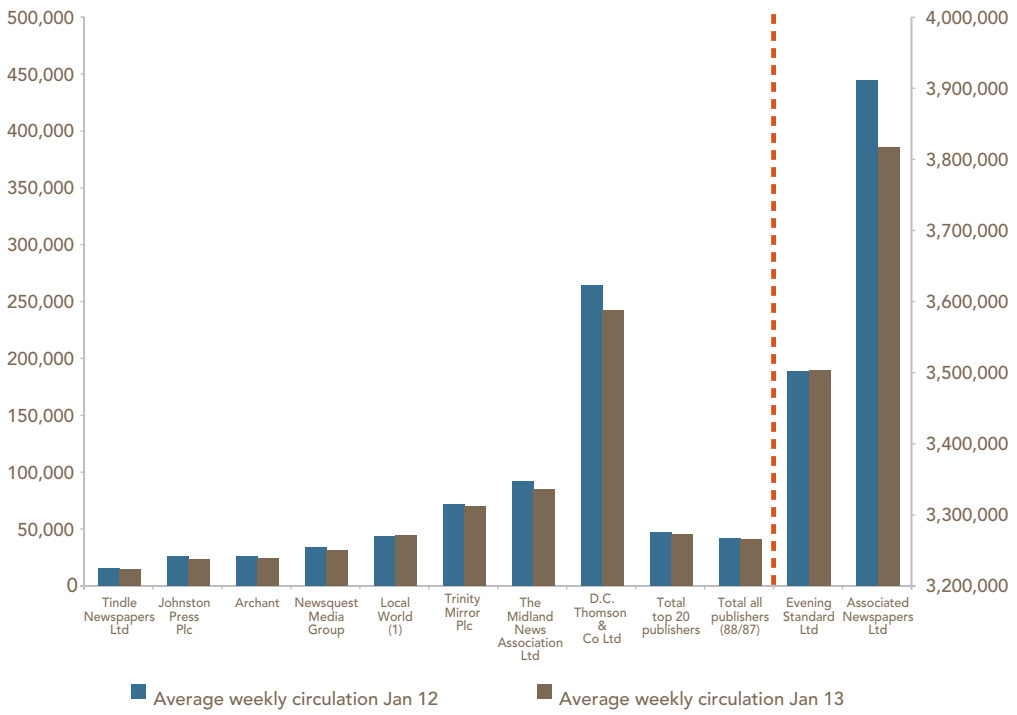
Average weekly circulation per title is around 40,000 copies with a very wide range. So while the Evening Standard in London records more than 3.5 million weekly copies and the Metro more than 3.8 million, the average weekly circulation per title is around 13,800 for Tindle and around 25,000 for Archant. It is obvious which groups are realising strong economies of scale (only a few) and those that are not (the rest). Economies of scale (and scope) are important in news provision, being evident in the editorial and publishing costs and also online where streamed lined websites that feed into one another are important. A good example of economies of scope is, say, Archant in East Anglia which has "News24" sites that involve advertisement listings etc. in a format consistent between sister papers and regions.

That said, for some, small may be beautiful – Sir Ray Tindle's operations are applauded by many commentators – with so-called hyper-local papers (Tindle has recently launched 7 more titles in London). Indeed, the new CEO at Johnston Press believes that a title with 30,000 circulation today declining at 5% per annum will yield 30 more years of profitability.[12]

Perhaps the regional press are a bit like 'indies' (i.e. independent TV producers) – small and large can be prosperous but rarely those in the middle, whereby the revenues generated are not sufficient to cover the companies' fixed costs. Small operations may face less loss to digital as the papers may serve to engage particularly well with small communities.

"Metro and the Standard are in a different league to the others"

Figure 3: Average weekly circulation per title by regional newspaper group



Note: (1) The weekly circulation for Local World for January 2012 is the aggregate of Northcliffe Media and Iliffe News & Media. Source: Newspaper Society Intelligence unit 01 January 2013 and 01 January 2012 ABC/VFD/Independently audited figures

[12] http://www.pressgazette.co.uk/ashley-highfield-decline-regional-newspapers-bottoming-out

"Radio's woes have been lightened through consolidation and a reduction in localness"

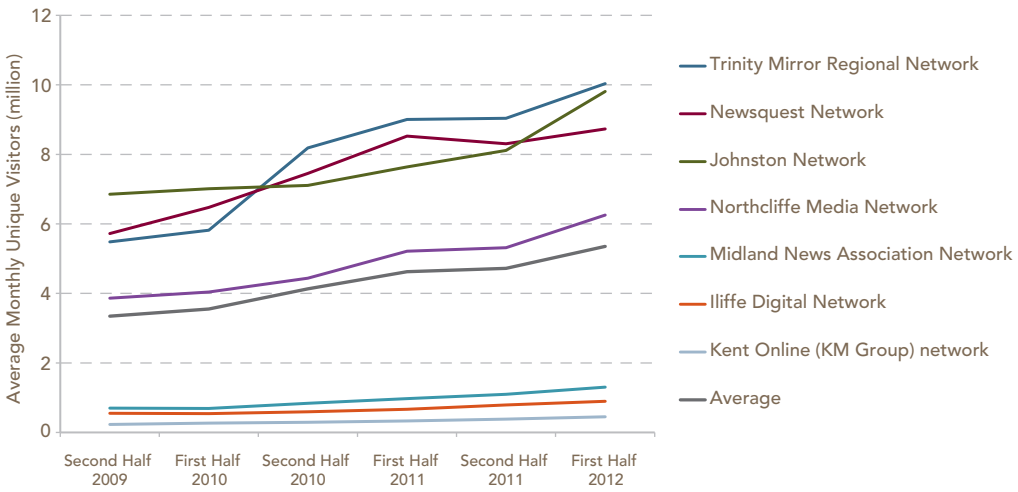
Another useful analogy here may be radio. The sector has undergone significant consolidation over time with Global – a combination of Capital, Chrysalis and GWR – emerging as the largest player. And consolidation continues with Global's recent acquisition of GMG radio (the Real and Smooth brands). Like in the local press, where the publisher groups tend to have large numbers of titles, station groups have large numbers of local radio licences. Global has around 30% of the total, amounting to around [150] licences including Classic FM, LBC, and various brands now rolled out across the country – Capital, Heart, Gold, and XFM. In tandem with Ofcom, the old-style Independent Local Radio ('ILR') model with localism at its heart has been transformed to a sector with a lighter touch 'localness' regime and large groups seeking permission to change the format of their licences and rolling out the national brands locally.

Radio revenues have increased for two consecutive years. While its fortunes have not always been positive and there have been some torrid times (and of course the BBC attracts a large share of listening), few would disagree that the early establishment of radio sales houses to provide advertisers with a national sell on top of each station's local advertising pot may have helped the sector considerably. Moreover, collaborative initiatives such as the Network Chart Show in 1984 became appealing for national advertisers and sponsors. Of course radio is free at the point of use and the gradual relaxation of localness is not what the local press should be about. Nevertheless, the main useful lesson is that consolidation must be an obvious way forward for survival in local press.

If we consider the online trends for the local press for a number of the groups, a much more positive trend emerges as shown in Figure 4.

"Online visitor trends are largely positive"

Figure 4: Regional newspaper group average monthly UV trends



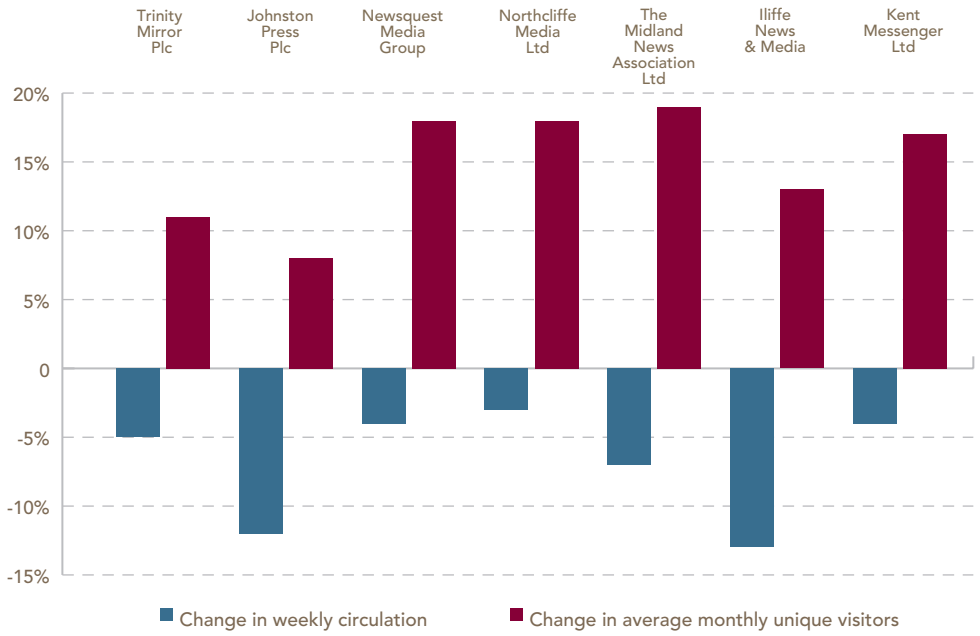
Source: Press Gazette, FTI analysis

Combining the online and circulation trends for a set of publishers, the following (neat and striking) chart emerges.[13]

[13] We acknowledge that the online metric is monthly and circulation is weekly.

"The upside of increased online visitors does not translate directly into increased revenues"

Figure 5: Regional newspaper group UV trends vs. circulation trends



Source: See Figure 2 and 3, FTI analysis

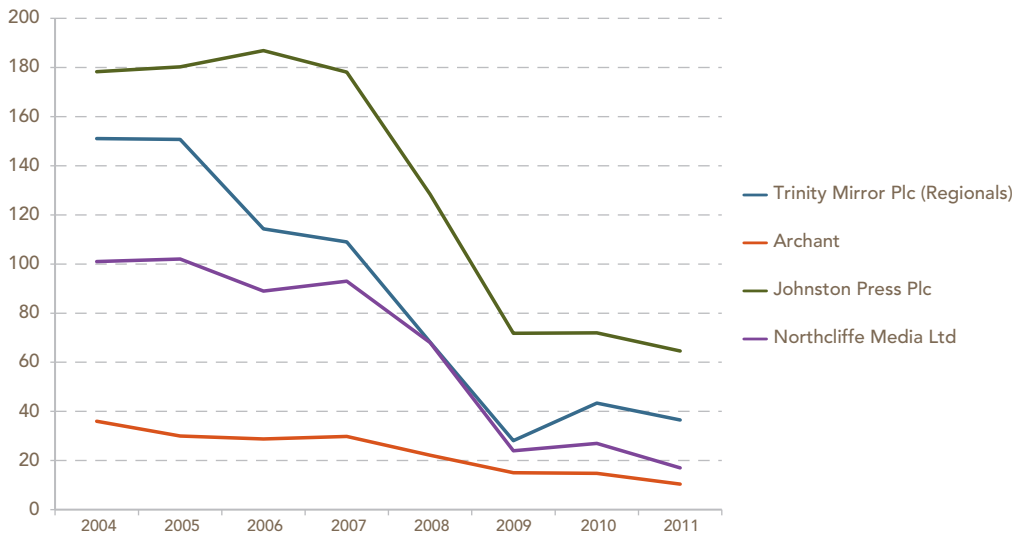
"Analogue dollars get converted into digital dimes"

For most groups online is on the up but printed circulation continues to fall. As everyone knows, the transition from offline to online tends not to be profitable, as coined by the former CEO of NBC Universal Jeff Zucker in 2008, who told the New York Times, that it is essentially trading 'analog dollars for digital dimes'.

Such metrics go straight to the bottom line, delivering a dismal downward trend in profitability, as indicated in Figure 6.

Figure 6: (Adjusted) Operating profit (before impairment, depreciation, amortisation and extraordinary items)

"This affects the bottom line, delivering a dismal downward trend in profitability"



Source: Published annual reports and accounts

"For some publishers, huge debts were racked up via reckless (?) expansion"

GREEKONOMICS?

While continued and significant technological (structural) change, combined with the dire (cyclical) trends in the economy have affected all media, newspapers have been particularly badly hit by the structural changes. The internet has fundamentally changed the technology for news production and consumption, broadening the market for news; newspapers face increased competition from alternative news sources – for both readers and advertising revenue. This represents a significant challenge for an industry already experiencing a long term decline in demand for its product.

Within the newspaper sector, the local/regional press has been hardest hit. Some commentators argue that the publishers themselves are in part to blame for extent of the damage the structural changes have had.

Chris Oakley, newspaper editor and owner of flagship regionals likens many of the regional press publishers to the Greek economy. Rather than invest for a fruitful future, Oakley argues that huge debts were racked up via reckless expenditure (on expansion). In attempts to preserve margins, cost cutting focused on letting journalists go. He says that the industry's catastrophic problems are self-inflicted and that they could largely have been avoided:[14]

"[they] failed to recognise the threat and opportunity of the internet and have come close to destroying an industry"[15]

According to the latest Annual Report & Accounts, Trinity Mirror's debt stood at more than £180 million and Johnston Press's at £351.7 million.

Of course not all publishers followed such a course. And, it is tricky to disentangle the data – how much of the demise is due to changing consumer preferences (long-term downward trend in circulation coupled with free online content and lower online ad revenues) and how much to management error? And, to what extent has public policy or the competition regime played a part?

"Quality journalism has been damaged"

QUALITY JOURNALISM UNDER PRESSURE

Notwithstanding the range and combination of possible causes of the downward trends, with such financial strain, as reported by the House of Lords, many local newspapers are unable to conduct the same amount of investigative or "accountability journalism" stories, such as those covering events at local council and town hall level. This was highlighted in evidence by Eric Gordon, Founder and Editor, Camden New Journal who stated, echoing Chris Oakley, that:

"What has happened with local newspapers is that they have been slimmed down by large groups in order to cut overheads ... in my opinion, in order to maintain a good net return the large groups—which were seeking 25%, even more, in the good, buoyant years of the 1990s, whereas we would get along with 10% or so - have cut overheads by slimming down the

[14] While there may be an element of truth in this, it is surely not that simple.
[15] Oakley, C (2012), "Five Minutes to Midnight: the death and possible re-birth of the regional newspaper industry", speech to Society of Editors Manchester Conference.

"One commentator states, "You know something has gone wrong with local media when your parents give up buying their weekly newspaper.""

editorial staff, which in turn means that local courts and councils are no longer covered as well as they should be. Sometimes they are not covered at all."[16]

As the Select Committee on Communications points out, a vibrant local press is vital for our democracy:

"Responsible, high quality, investigative journalism matters; it is a vital constituent of the UK's system of democratic governance and accountability. At its best, it informs and educates us, enhances our democracy, and is a force for good."[17]

But if the funds for investigative journalism are drying up then what next? Some commentators posit that the well-trodden path of journalist training at a local paper, rising to correspondent in the regions, eventually to leading reporter in the nationals is finished and that the only institution currently able to provide the ground work is the BBC. The situation at the local level is having repercussions for training and quality across the wider news sector.

"Yet quality, investigative journalism is vital for our democracy"

STRATEGIES GALORE

The regional press continues to respond to the challenges inherent in the modern media landscape. As stated by the Newspaper Society:

"Innovation, brand extension and portfolio publishing are the name of the game for Britain's local media.While successfully building the readership of their core titles, publishers are also developing a range targeted print, broadcast and digital channels to reach increasingly diverse audiences in their regional markets. As well as 1,200 [sadly now 1,100] regional and local, daily and weekly titles, the regional press now boasts 1,600 websites and hundreds of other print, digital and broadcast channels. In their individual markets, regional press brands reach more people than any other medium."[18]

Thus the press has responded, albeit, as many argue, somewhat late in the day, with investment in new platforms, special interest and ultra-local publications, converged multimedia newsrooms, video journalism, UGC, mobile sites, smartphone apps and other digital and print innovations. While reaching more of the population than previously, monetisation of increased reach remains tricky. We summarise below some of the headline strategy announcements made by Trinity, Johnston and the newly formed Local World.

"Various digital strategies are continually being tested"

Trinity Mirror's new CEO, Simon Fox (previously at HMV), has 'merged' the regional and national businesses into one. He has opened up the executive area on the 22nd floor of the Canary Wharf office and hopes that digital, and in particular a focused tablet strategy aimed towards monetisation, will turnaround the company's fortunes.

[16] http://www.publications.parliament.uk/pa/ld201012/ldselect/ldcomuni/256/256.pdf
[17] The future of investigative journalism, report, the Select Committee on Communications,16 February 2012. http://www.publications.parliament.uk/pa/ld201012/ldselect/ldcomuni/256/256.pdf
[18] http://www.newspapersoc.org.uk/circulation-and-distribution

Case study: Trinity Mirror

- One Trinity Mirror – a united business serving the nationals and regionals
- Shared content centre
- Clear digital proposition – technology investment, improved websites, mobile and tablet applications across platforms
- Focused tablet strategy – aim towards monetisation
- Cost effective central support with opened - up executive area in Canary Wharf

"What we want is to deliver great journalism every day and to see circulation and advertising increasing…a clear, forward-looking strategy across our entire publishing operations, both print and digital, which builds on and develops our editorial strength…an efficient operation where those closest to our readers and advertisers have the authority and autonomy to do what is best for each market." Simon Fox, CEO Trinity Mirror

Johnston Press has former BBC iPlayer and Microsoft's Ashley Highfield at its helm. Highfield believes that the papers can be templated, cover prices put up and, of course, digital has to be at the heart of the company. Johnston posits that mobile will be a key growth channel and is in the process of re-launching its titles – both paper and online - following re-design and re-vamping.

"Will CEOs, new digital strategies and a new company (Local World) pave the way for future success?"

Case study: Johnston Press

- Invest in content; platform 'neutrality' and increased UGC
- Re-launch titles: digital, combination of free to pay, daily to weekly and / or re-designs.
- Drive subscription levels.
- Mobile key growth channel
- Digital output and inputs (mobile / digital devices for all journalists)
- Partnerships with local communities; many more community contributors, deeper audience engagement , journalists on the ground in every town

"I think the future for our business is to drive subscription levels…what we're trying to do is move people to a subscription where they'll get the paper, the iPad app, the website, everything in one bundle for considerably less than the cover price of the paper." Ashley Highfield, CEO JohnstonPress.

It is early days yet but Steve Auckland, Local World's CEO has embarked on a business transformation of all of its centres, expected to take 18 months. It boasts being debt-free, will invest £10 million in digital and is focusing on 'localism' – content, sales and management. It aims to publish a high proportion of UGC.

"Digital is the order of the day"

Case study: Local World

- A "one-stop shop" serving content to local communities - local content, local sales, local management; high UGC
- Optimisation of local content and commerce across all platforms
- Business transformation at each centre over 18months - new innovative working practices
- Digitalled - £10m investment
- No property, printing presses and large scale distribution or any legacy issues such as highlevels of debt

"I'm looking forward to us building on our existing strengths, transforming our products and services, and ensuring we are the one-stop-shop for local content and commerce."
Steve Auckland, CEO Local World

The local press is certainly not resting on its laurels. The new impetus from the combination of new CEOs and re-engineered strategies may turn around its fortunes. But is this is enough and is it too late? May there be lessons from the US?

LESSONS FROM THE US?

The US is often held up as a beacon for the next big thing coming the UK's way. Unfortunately, the regional press on the other side of the pond is far from booming: it is, arguably, in an even worse state than its UK counterpart. According to the Economist, revenues in the sector by 2011 had fallen to around half of the level they were in 2000. A recent survey of six newspaper companies (accounting for 121 titles) found that the digital dollars transition remains challenging: for every $1 made in online advertising revenue, around $7 is lost in print ad revenue.

"Even in the US the digital transition remains challenging: for every $1 made online, $7 is lost in print"

The Pew Center, a respected US think tank on public issues and trends agrees that the printed press will continue to be a challenging market:

"To different degrees, executives predict newsrooms will continue to shrink, more papers will close and many surviving papers will deliver a print edition only a few days a week."[19]

In December 2012, however, The Economist reported that circulation had begun to stabilise, with some papers (albeit The New York Times and similar) managing to stave off the fall in ad revenues.[20] Moreover, success stories in respect of pay-walls were reported. Consumer willingness to pay is on the up, at least for content-rich papers, driven in part by tablet consumption. That said, the sector remains in a fragile state and for every success story there is probably a failure – News Corporation closed the Daily – a tablet only paper. Another publisher, Advance Newspapers, has moved 14 of its daily papers to three-day

[19] http://www.journalism.org/analysis_report/search_new_business_model
[20] http://www.economist.com/news/business/21567934-after-years-bad-headlines-industry-finally-has-some-good-news-news-adventures

publications; further evidence of the challenging nature of the sector in the US. While paywalls are becoming commonplace, revenues remain small; far too little compared to the level required to offset the decline in print revenues.

The US situation is unlikely to be a perfect indicator of the UK's prospects as there are at least three important differences between the two sectors. Firstly scale. In the UK there are 26 million TV households whereas in the US, TV households total 116m. Secondly subscriptions. A large majority of newspaper sales are by subscription whereas this is not commonplace in the UK. Thirdly revenue composition. In the US, advertising historically accounted for a relatively high proportion of newspaper revenues (more than 80%), whereas in the UK, it is around 50% (paid-for copies).[21]

We guess that the main lesson to be learned from the US is, like in many countries, the newspaper sector is in long-term decline and that managing the digital transition is fraught with difficulty. That said, there are several success stories of turnaround – broad organisational transformation, new ad sales management and content delivery systems combined with changes to the number and type of print days have had some promising results in staving off the inevitable. Anecdotal evidence however suggests that as in the UK, the quality of the journalism has also suffered.

POLICY BLUNDERS?

In 2008 the BBC Executive set out proposals for a new local video service. As per the regulatory regime, Ofcom conducted a market impact assessment ('MIA') of the BBC's proposed proposition and concluded that:

"the launch of the proposal would have a significant negative market impact on commercial providers."[22]

"IFNCs may have provided a stepping stone to a more sustainable local press"

This finding, as far as the local press (and radio) was concerned, was a good call and the proposal did not get the green light by the BBC Trust. Enter next Independently Funded News Consortia ('IFNCs'): brainchild of Ed Richards; announced at a session on the local and regional media at Westminster. The previous government waived them through at great speed, selecting the winners for the three pilot regions. Consortia comprised the regional press, TV, and experts in online and local community knowledge. And in some cases radio. Trinity Mirror, Johnston Press, D C Thomson and NWN Media were poised to receive a truckload of public money and the opportunity to parade their (IFNC) brand on the ITV regional news slots. The IFNCs of course were immediately cancelled, as promised, by Jeremy Hunt as the current government was formed. Instead, Hunt's second favourite hobby, local TV, was put on the table.[23] Local TV will of course be gunning for local advertising revenues and may further cannibalise regional press revenues.

IFNCs may have provided a stepping stone to a more sustainable local press. Local TV, assuming it gets off the ground, will be a staunch competitor for local advertising revenues.

[21] http://www.oecd.org/document/48/0,3746,en_2649_34223_45449136_1_1_1_1,00.html
[22] http://stakeholders.ofcom.org.uk/market-data-research/other/tv-research/bbc-mias/mia-local-video/
[23] Hunt's favourite hobby was high speed broadband.

"The OFT referred Kent Messenger's proposed acquisitions to the Competition Commission"

THE LOCAL MEDIA MERGER REGIME

While Ofcom's expert media advice feeds in to local media mergers, the OFT thus far remains unconvinced of the strength of cross-media competition. The Kent Messenger case provides a good illustration of the workings of the post-Digital Britain competition regime. In short, local/regional press markets were defined narrowly in product and geography; competition from other media (other print, online and radio) was not considered to be effective and the proposed merger was referred to the CC for a long, resource intensive and costly process.

Specific challenges are posed in assessing newspaper mergers. This is because they have the characteristics of a so-called 'two-sided' product: they are effectively in two different (albeit related) markets - for readers and for advertisers. The relationship between the two markets and hence separate groups of customers is termed 'intermediation' by practitioners and is typically illustrated by the following example. If the cover price of a paper is increased, it will most likely reduce circulation and hence the number of readers. This has a knock-on effect, reducing the demand from the advertisers (or the willingness to pay a certain rate). The tension between the levels of customers and charges in the two markets are termed 'indirect network effects'. Newspapers have to cover their costs and decide on the best mix of pricing to do so – the cover price (in many cases zero) to readers and the charges to advertisers.[24]

Notably, each of the two sides of the market may have very different characteristics and dynamics which in turn affects the merger assessment, adding a layer of complexity absent from 'one-sided' product markets. In its merger assessments, the OFT does take into account the two-sided nature of the local press.[25]

"The evidence on the competition for advertising from other media was not deemed compelling"

THE KENT MESSENGER CASE

Kent Messenger Group (KMG) proposed to buy seven Kent local weekly newspaper titles from Northcliffe Media (Kent Regional News & Media, 'KRNM'), to add to its then portfolio of seven paid for titles and seven free titles. With a long history of publishing in the county of Kent, KMG is a family-run business and the 16th largest news group in the UK. Compared to the larger regional press groups, it is a relatively small player.[26]

Northcliffe (albeit now subsumed into Local World) was the fourth largest regional publisher with a total of 115 titles across the UK, and had purchased KRNM from Trinity Mirror in 2007. These titles were run as a discrete group. Post the proposed merger, Northcliffe would have retained its remaining Kent titles within its portfolio.[27] According to KMG, there were three competitors in the Kent local newspaper sector: KMG, KRNM and Kent on Sunday published by Archant. Third parties appeared to provide the OFT with compelling submissions, expressing concerns about price rises following the deal.

[24] Other media face this challenge. A prime example is Channel 4's historic switch of Film Four (and other channels) from a subscription service (with relatively fewer viewers) to a free-to-air service on the terrestrial TV platform.

[25] There is a body of empirical literature on the effects of two-sided markets on merger situations. As reported by a Federal Trade Commission Roundtable publication (see: http://www.ftc.gov/bc/international/docs/roundtabletwosided.pdf), several papers report on newspaper mergers. Notably, two of the papers cited, one on Canada (Ambarish Chandra and Allan Collard-Wexler, "Mergers in Two-Sided Markets: An Application to the Canadian Newspaper Industry," Leonard N. Stern School of Business Working paper No. EC-07-03 (2008), available at http://ssrn.com/abstract=985581) and the other on the Netherlands (Patrick J.G. Van Cayseele and Stijn Vanormelingen, "Prices and Network Effects in Two-Sided Markets: The Belgian Newspaper Industry," (2009) available at http://ssrn.com/abstract=1404392) found that newspaper mergers had no or only a limited impact on prices for both advertisers and readers.

[26] Newspaper Society, FTI analysis.

[27] Proposed acquisition by Kent Messenger Group of seven newspaper titles from Northcliffe Media Local Media Assessment, Ofcom 2011.

Ofcom concluded in its LMA that:

"The evidence available to us suggests that the target business and the regional newspaper business of KMG will struggle to achieve profitability in their current form, which might lead them to respond by closing newspaper titles or reducing quality (or both).

In light of this, a merger may provide the opportunity to rationalise costs, maintain quality and investment, and provide a sounder commercial base from which to address long-term structural change, for example by expanding the availability of online and other digital local services. These potential benefits need to be weighed against any potential customer harm resulting from reduced competition identified in the OFT's overall assessment."[28]

The OFT, however, decided to refer the merger to the CC for a second phase review. It found that the parties (Northcliffe and KMG) were close competitors in the specific areas and that the joint share of supply in those areas amounted to 100% post-merger. It concluded that the deal would lead to a substantial lessening of competition as rivalry between the two firms would end post-merger. It was not convinced about widening the nature of the product market to include other media, stating that:

"The OFT does not consider the evidence – in relation to the constraints from print and non-print media – sufficiently compelling to justify widening the candidate market beyond the supply of advertising space in local weekly (paid-for and free) newspapers."[29]

As the OFT investigation is a first stage procedure, the OFT is more likley to fall back on accepted market definitions, making it difficult to challenge entrenched views. At the CC, there is much more open for debate but of course parties may abandon a deal rather than face a long and intensive CC inquiry.

Amelia Fletcher, OFT Chief Economist and Decision Maker in this case, said:

'Local newspapers face significant challenges, including falling readership and increased competition from other media, most notably, the internet. However, this merger would create a monopoly in local weekly newspapers in several local areas across East Kent. [Thanet, Canterbury, Swale, Dover, Ashford and Shepway] UK merger law requires the OFT to be cautious in its 'first phase' review of mergers. We require compelling evidence to dismiss concerns that the combination of such close competitors as these might result in substantially higher prices or less choice for advertisers and readers. The evidence in this case did not permit us to clear this transaction; therefore we think it is appropriate that the merger is referred to the Competition Commission for a more detailed 'second phase' review.'[30]

KMG subsequently withdrew its bid for the series of Northcliffe Media titles. Throughout the process KMG had maintained that it would not be able to afford a referral to the CC, and, in such an event, would have to withdraw its bid for the titles within Northcliffe's KRNM.[31]

[28] Proposed acquisition by Kent Messenger Group of seven newspaper titles from Northcliffe Media Local Media Assessment, Ofcom 2011.
[29] Anticipated acquisition by of seven local weekly newspaper titles by Kent Messenger Limited from Northcliffe Media Limited.
[30] http://www.oft.gov.uk/news-and-updates/press/2011/111-11
[31] http://www.kentonline.co.uk/kentonline/news/2011/october/18/km_group_pulls_out_of_bid.aspx

"The OFT is preventing the changes in the local newspaper industry which will allow it to survive, undermining local democracy in the process..."

Chairman of KMG, Geraldine Allinson said the company had invested "a huge amount of time" on the bid in recent months and that the costs and time necessary for a CC review (which she said would amount to £500,000) "would be completely unreasonable for a business of our size and for a deal of this scale".

In response to the OFT's decision, Baron Black of Brentwood, the Telegraph Media Group's executive director, said:

"The OFT is preventing the changes in the local newspaper industry which will allow it to survive, undermining local democracy in the process...

A few years ago... Trinity Mirror tried to sell eight free weekly newspapers in Northampton and Peterborough to Johnston Press. A ruling from the competition authorities meant the sale had to be abandoned. And... seven of those eight titles have now closed."[32]

Black called for urgent action:

"to show we understand the importance of our local press in the creative economy and in local democracy and set publishers free to renew their businesses for a new age."[33]

The OFT decision to refer the case to the CC was also harshly criticised in the House of Lords report on investigative journalism:

"Nonetheless, this case is an example of the damaging effect which the competition regime can have on the local newspaper industry, which is facing a significant economic threat."[34]

"The Topper got the 'all clear'"

THE TOPPER CASE

Roll forward to 2013 and industry commentators refer to a possible directional change by the OFT:

"There are signs that the OFT's tough stance may be thawing. Last year it cleared DMGT's acquisition of free Nottingham weekly The Topper. It gave unconditional clearance despite DMGT already owning the Nottingham Post, and noting that the deal would mean the publisher would have a 'high combined share of supply of local newspapers and local paper advertising space in Nottingham'."[35]

In the Topper case, the acquirer, Northcliffe, stated that it did not consider that an LMA from Ofcom was required. Ofcom considered that an LMA would not materially assist OFT's merger assessment and no LMA was requested. OFT defined the scope of the product market to comprise both daily and weekly papers. On the advertising side it stuck to the definition of advertising in printed newspapers alone (online/other media were, however, taken in to account as part of the competitive assessment), taking into account advertising by category (e.g. display vs. classified and industry segment). The geographic scope was deemed Nottingham:

[32] http://www.guardian.co.uk/media/greenslade/2011/nov/04/guy-black-local-newspapers
[33] http://www.guardian.co.uk/media/greenslade/2011/nov/04/guy-black-local-newspapers
[34] http://www.publications.parliament.uk/pa/ld201012/ldselect/ldcomuni/256/256.pdf, para 158, p43.
[35] http://www.guardian.co.uk/media/2013/jan/18/oft-considers-investigation-local-world?INTCMP=SRCH

"Yet the OFT said that the extent of the constraint posed by other media on the local papers was uncertain"

"the OFT believes that the candidate frame of reference is the supply of local newspapers in Nottingham taking into account different advertising categories where appropriate."[36]

Interestingly, post-merger the parties would have a combined share of circulation of 90% in 10 of the JICREG areas and more than 50% in the remaining 3 JIGREG areas. But the OFT concluded that the two papers in question, the Post and the Topper were not close competitors and that taken together, supply-side and demand-side constraints were jointly likely be sufficient to protect consumers. This is an important point - on their own, supply-side constraints (e.g. constraints posed by other media) were not considered sufficient. But once demand factors were included, 'taken in the round' all of the potential constraints were considered sufficient to protect consumers. Notably, the two-sided nature of the product market and the so-called indirect network effects were cited as important – that Northcliffe would not have the incentive to increase cover prices or ad prices. While the OFT found that the merger would lead to a lessening of competition, it did not believe that the lessening would be substantial. Hence the merger was cleared.

"Local World: done and dusted or doomed?"

LOCAL WORLD: DONE AND DUSTED OR DOOMED?

Lessons learnt from KMG and Topper competition cases may include:

- OFT can have jurisdiction over what appears to be a 'small' part of the UK – in Topper the number of households potential affected amounted to just over 1% of total UK households yet this was deemed sufficient scale to constitute a 'substantial part of the UK' – the share of supply test is not an economic market test;
- There is a relatively low threshold for referrals to the CC – the OFT adopts a cautious approach. Thus the issue becomes, how many deals sent to the CC get unconditional celarance?
- Evidence submisssions have to be detailed and compelling;
- Each case is assessed on its own merits - the outcome of each case is based on the OFT's review of the evidence and its subsequent judgement - whether it believes there to be a realistic prospect that the merger will result in a substantial lessening of competition;
- The OFT considers the advertising markets very narrowly and does not appear to have taken on board the major changes taking place in the consumption and provision of news and specifically the effects of online and social media;
- Ex-post market share per se is not the issue, rather whether ex-post there is a substantial lessening of competition. In determining that, the OFT takes into account both the closeness of competition between the parties and competitive constraints;
- Consequently it matters whether the merger is between rivals or non-rivals in any particular market;
- Don't assume that because your systems account for specific revenues in certain ways this will influence the way in which the OFT approaches the product and geographical scope of the market; and

[36] http://www.oft.gov.uk/shared_oft/mergers_ea02/2012/Northcliffe.pdf

– Parties should do their homework by assessing the most narrow markets imaginable before merging and be prepared to offer the OFT remedies (usually divestment), if appropriate.

What can we infer for Local World? The OFT has invited comments from interested stakeholders so it is investigating the deal. Owing to the level of the combined revenue of its partners, the deal will certainly pass the revenue threshold for a relevant merger (Local World says its total annual revenues are expected to exceed £270m). However, we understand that there are no geographical overlaps between the various titles so it is unlikely that concerns regarding local advertising markets would arise. Clearance seems the obvious outcome.

But this deal has a trickier side to it: the involvement of Trinity. Although this is highly speculative, we are reminded of the Sky 17.9% stake in ITV. This did not pass the competition test (it did pass the plurality test) – the CC determined that the level of Sky's stake would give Sky control over ITV's future strategy. Perhaps Trinity's 20% stake in Local World may be considered in a similar light? That is, prima facie evidence of a reduction in competition that may give rise to concerns. Moreover, Trinity is the leading UK regional publisher with around 22% of circulation. If so, then perhaps the OFT will consider each of the JICREG areas where both Local World and Trinity Mirror have a presence? We will have to wait around 40 days for the OFT's decision:

– Whether the merger is not a relevant merger situation;

– Whether the merger is not being referred to the CC;

– Whether undertakings in lieu of a reference have been accepted by the OFT; or

– Whether the merger is being referred to the CC.

The first is ruled out for sure.

"Subsidies are ruled out"

WHAT NEXT FOR THE LOCAL PRESS?

There is a clear tension between the democratic need for investigative local journalism, current business models and the competition regime. And it is not clear that the admirable new digital strategies of the regional press publishers will solve the sector's problems. Trends from the US show some green shoots but basically this may be stalling the inevitable – long-term decline. Perhaps Facebook, Twitter or the next 'big thing' will become the vital vehicle for democracy at the local level.

Public subsidies for journalism are available in Finland, the Netherlands and France. Louise Mensch, former Tory MP, led a private members' debate in Westminster Hall in April 2012, calling for subsidies for the local press in the UK. This did not gain traction with fellow MPs and was swept aside in the Select Committee discussions:

"… given the strong independent character of the printed press in the UK and our political traditions, we do not believe that it would be appropriate for the UK Government to fund investigative journalism directly in the form of state subsidies other than with the continued support for zero-VAT rating for newspapers and of the BBC licence fee in broadcasting."[37]

[37] http://www.publications.parliament.uk/pa/ld201012/ldselect/ldcomuni/256/256.pdf, para 216, p56.

The Select Committee did, however, propose that an investigative journalism fund could be set up, with monies coming from fines for breaches of the Editors' Code of Practice under a new system of press regulation. Such a system would require fair distribution by an accountable and independent regulatory body. While potentially useful support, this model is unlikely to solve the inherent problems faced by the regional press.

"The OFT's stance on market definition is a stumbling block"

The internet has fundamentally changed news consumption and provision. Newspapers now have to integrate their offering with online and social media. Readers have more choice than ever before and newspapers face competition from literally thousands of news sources. Such sources are often newspapers' rich content, edited news - yet available for free. While the OFT recognises the importance of the two-sided nature of newspapers, in merger cases the OFT's approach is generally to focus on the advertisers' side of the market. In cases it has expressed concerns about a single paper serving a single JICREG area. The importance of holding MPs, rogue businesses (et al) to account is not part of the OFT's remit. The OFT also appears to remain unconvinced about the competition from other media (radio, online and social media) in exerting pressure on local press advertising rates. Competition concerns are raised and the deals tend to get referred to the CC for a lengthy and resource intensive second phase investigation.

In any one local area, surely one paper is better than none? One option (and rarely implemented by the competition authorities) would be for the competition authority to impose price regulation on press advertising rates at the local level to alleviate its monopoly concerns.[38] More seriously, there must be superior options.

In our view, bigger is better or, as Ray Tindle has found, small (or hyper-local) is beautiful. The middle-ground should be avoided.[39] For many publishers therefore, further consolidation is a must for longer-term viability, to enable cost rationalisation, test digital strategies and, most importantly, to invest in content – good old quality journalism.

"The cost of going to the CC is a major barrier"

What are the stumbling blocks? The OFT's stance on market definition, its competitive assessment and its cautious approach to clearance. Two rival papers in an area coming together is unlikely to get the green light. At the local level it appears that advertisers see newspapers as their main (and only) effective channel. But this may change. Ten years ago advertising agencies and corporates alike were struggling with online advertising – whether to spend and if so how much, where to spend and what is the ROI? Now online and even social media are standard. If prices in the local press increased overnight, surely local advertisers would turn to other media? Over time, we would expect the constraints exerted by online et al to increase. But we don't have too much time.

And, of course, the cost of going to the CC is a major barrier. A number of groups should come together, gather compelling evidence and bite the bullet, ultimately at the CC.

[38] The often quoted example of a competition authority imposing a remedy of regulated prices on a non-regulated sector dates back to the 1980s. The then MMC stipulated that 'price increases are limited to a weighted index of production costs minus 2%' following a merger in the white salt market. The remedy was imposed in 1988, following the report by the Monopolies and Mergers Commission (1986) White Salt, Cmnd 9778, HMSO.

[39] By this we mean that small, hyper-local papers with a loyal following appear to be able to buck the structural decline thus far. Larger publishers are better able to build on economies of scale and scope that medium-sized publishers find challenging to realise.

> “Local papers have at least 30 years’ life left in them”

Hopefully the deal will get the green light (perhaps with a few disposals in certain areas). Indeed, publishers could seek a set of principles from the CC, analogous to those for supermarkets - at least the way forward may be paved a little clearer. The recent CC decision on Global Radio’s acquisition of GMG radio is a good example of how the CC views the local media landscape. The CC required divestments of overlapping stations on the grounds that local advertisers are unable to find alternative media. At root, there is a still a problem here – local radio and local newspapers perform valuable economic roles and aren’t perfect competitors for one another. So, the CC is implicitly saying, we cannot allow 2 to 1 mergers either in the case of radio or (one suspects) newspapers. But this is what needs to be tested. After then it is probably ‘fingers crossed’…

If Ashley Highfield is right, within a regional press group, local papers that have a circulation of 30,000 or so still have another 30 years’ life left in them. Papers with half that circulation another 15? For something so popular, surely the local press can last a lot longer than that? Perhaps not printed but certainly in tablet-form (or the next new device).

APPENDIX

OFT MERGER PROCEDURE

The below is a summary of the orginal source.

Following aprospective or completed merger the OFT initiates the following process:

Invitation to comment ('ITC')
The OFT considers whether the agreement has resulted in the creation of a relevant merger situation under the merger provisions of the Enterprise Act 2002 ('the Act') and ,if so, whether the creation of that situation has resulted, or may be expected to result, in a substantial lessening of competition within any market or markets in the United Kingdom for goods or services.

Interested third parties are invited to comment on relevant issues such as buyer power, the substitutability between different products or services and whether the party merged company might behave anti-competitively. When there are adverse views, the parties proposing the merger are normally told of the nature of the concerns expressed and they are given the opportunity to respond to them.

Decisions
Following its assessment of the information on the prospective or agreed merger, the OFT issues a press release and a supporting document in respect of its decision. This usually occurs within 40 working days of the closing date for the ITC. Notifying parties are informed of the decision one hour before the public announcement. Decisions fall in to one of four categories:

- That a merger is not a relevant merger situation;
- That the merger is not being referred to the Competition Commission (CC);
- That under takings in lieu of a reference have been accepted by the OFT; or
- That the merger is being referred to the CC.

Undertakings in lieu
Where the OFT has decided that a merger should be referred to the CC, specifying the adverse effects of the merger, it may accept undertakings, intended to remedy those adverse effects, as an alternative to reference. The OFT generally consults on the terms of the appropriate undertakings and the Enterprise Act Register of undertakings and orders contains final versions of the undertakings in lieu accepted by the OFT. In public interest cases the Secretary of State will make the decision on the case and will consider whether undertakings in lieu of a reference are justified.

Public interest cases
The Act also allows for the Secretary of State to assume responsibility for determining whether or not to refer a merger when defined public interest considerations are potentially relevant by issuing a public interest intervention notice (PIIN). Public interest considerations are limited to:

- National security (including public security)
- Plurality and other considerations relating to newspapers and other media, and
- The stability of the UK financial system.

Source: http://www.oft.gov.uk

OFCOM LMAs

The below is a summary of the orginal source.

LMAs are a new element in the OFTs existing merger procedure. They are a more formalised way for Ofcom to assist the OFT in its assessment of mergers involving local media.

In media mergers involving newspaper publishing and / or commercial radio or television broadcasting, where the case raises prima facie competition concerns, the OFT will ask Ofcom to provide it with a local media assessment in order further to inform the OFT's decisions on the reference test and on the application of any available exceptions to the duty to refer.

Drawing on Ofcom's understanding of media markets, the assessment would be likely to include Ofcom's views on:

- The relevant counterfactual to the merger (including the risk of the asset orbusiness in question failing);
- The scope of relevant product and geographic markets;
- The competitive effects of the merger, andexceptions to the duty to refer, and in particular Ofcom's views on whether the markets are of insufficient importance (de minimis) to warrant reference and whether there are 'relevant customer benefits' – such as higher quality (which, in the context of newspapers, could for example reflect the range and quality of newsreporting) or greater choice of products – which might be weighed against an identified substantial lessening of competition.

Although the decision on all of these matters remains one for the OFT, the OFT will take Ofcom's views into account in reaching its conclusions in the same way as it would consider views from other third parties received during the course of its investigation. The OFT will therefore consider Ofcom's local media assessment within the context and time frame of its normal review processes.

Source: Mergers Jurisdictional and procedural guidance at: http://www.oft.gov.uk/shared_oft/mergers_ea02/oft527.pdf

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