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Vertical mergers in the technology, media and telecom sector – Note by Latvia

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More documents related to this discussion can be found at

http://www.oecd.org/daf/competition/vertical-mergers-in-the-technology-media-and-telecom-sector.htm

Please contact Mr. Antonio Capobianco if you have any questions about this document
[E-mail: Antonio.Capobianco@oecd.org]

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Latvia

1. General information

1. Telecom and technology sectors are evidently fast developing with obvious disruptive changes in the context of the different aspects of those markets. Identification of pure vertical integration of merged entities is becoming a harder task. Usually, mergers in media, telecom and technology sectors create a mix of potential synergies (vertical or conglomerate). They all play an important role in competition analysis, and it makes it necessary to asses such synergies from a number of perspectives. From one side, there may be efficiency gains presented by the parties. From the other side, synergies may involve risks of possible negative effects on competition (foreclosure, discrimination, etc.).

2. Non-horizontal mergers mostly are more prone to generate efficiencies for competition and customers. By entering new markets and pooling resources, it is possible to acquire new know-how from the market and combine important assets (telecom infrastructure, services, technologies, resources and clients). In most cases, it may lead to development and introduction of new innovative services, economy and improvement of the competitiveness of the merger parties. It may also incentivize other competitors or potential competitors to seek efficiencies.

3. From 2015 until present times, the Competition Council of Latvia (the CC) has reviewed 10 mergers, seven of them in media and telecom sectors, two in online retail, and one in the FinTech sector. Most of them involved both horizontal or potential horizontal overlap and different models of integration (synergy) of services (vertical or conglomerate). In one merger case that involved integration of mobile telecom service and TV content service providers the CC) applied behavioral remedies. CC intervention in vertical and conglomerate merger deals are significantly less frequent that horizontal mergers. In 2017 CC reviewed merger case that involved integration of mobile telecom service and TV content service providers in the result applying behavioral remedies. Before that CC applied remedies in 2011 in merger between pharmacy wholesaler and retail pharmacy chain.

4. There is no reliance on previously accepted market definitions when it comes to technology markets. Although, most of newly developed and innovative services are not substantially new and disruptive but they usually offer more demand side benefits for customers. An issue about potential competition of such similar services arise in most of the cases where telecom and technology sectors are involved. For example, questions may arise concerning product market definition due to arising potential overlap between mobile and fixed internet services. Mobile internet is becoming more competitive on price and quality parameters. Also, synergy of mobile operator and media holding may create an issues and effect competition due to increasing importance of TV and video content for telecom companies. Especially if the mobile operator acquires two biggest national wide TV channels.

5. The economic data requested and analyzed vary cases by case. Data could be more or less specific (detailed) due to the fact how narrow markets are defined but overall there is no substantial difference in data types. The basic data are that shows number of clients and the turnover in relevant market (or potential market). In some case, it may be important to split data representing corporate and individual clients especially in telecom and

technology markets where average consumer needs are different from requirements demanded from corporate clients. The main analytical information may consist of internal information of merging parties provided in merger notification or submitted later, opinions and information from competitors and clients gathered from the replies to the requests of information, and surveys. In the markets where technologies develop so fast it becomes increasingly important to reveal the strategies of the buyer that are planned to be implemented after the merger. That means, internal information (strategies, plans, internal analysis and studies) is obviously needed for putting together the puzzle of the possible future services, market and competition models.

6. That makes it much easier for the competition authority to discover potential competition issues in the future. Although, merging parties mostly reveal very general further scenarios and mainly aims to substantiate efficiency claims. That obliges the authority to shape and analyze its own hypothetical and reliable scenarios depending on the relevant markets defined, nature of merger (horizontal, vertical, conglomerate, or mix), market position in each market what could help later while analyzing the possible theories of harm. The other important part of information for analytics and data is gathered from surveys of competitors, clients, suppliers and their replies to authority's requests. Also, where new product or geographical market definition is valid, the merger review may involve customer surveys conducted by the authority or provided by merging parties.

2. Effects analyzed and remedies applied in telecom and media in 2017 decision

2.1. Information about the case

7. In 2017, the CC reviewed[1] merger between mobile operator UAB Bite Lietuva (Bite LT) and media holding MTG Broadcasting AB Group (MTG) that had portfolio of different TV channels. Both merging parties are active in the Latvia's geographical market, as well as in other Baltic countries. Merger included selling of assets in all three Baltic states. The mobile operator is active on mobile services (voice, internet, etc.) markets.

8. Technology development trends in these markets, business model and further development required to add different (TV, video, etc.) content-related services to its mobile business. Media holding portfolio included 6 national TV channels of which 2 were the biggest in the state. MTG was active on the TV channel production, wholesale level and TV advertising market. These national TV channels were regarded as the must-have in previous merger in 2012. Also, in this merger clients of MTG (TV retail operators and advertising agencies) recognized these 2 national TV channels as must-have for packaging their offers. The media holding was active on retail level offering TV channel packages to customers via satellite platform. Also, internet *video on demand* distribution platform was developed by the media holding and video subscription services via this platform were offered to customers.

9. There was no horizontal overlap, but this merger involved synergy that resulted from vertical integration and included future possibilities to combine and bundle different mobile, TV and other content-related services. On the retail level, it was evident that adding

[1] According to the merger notification UAB Bite Lietuva plans to acquire control over all companies of MTG Broadcasting AB Group in Latvia – SIA "TV3 LATVIA", AS "Latvijas Neatkarīgā Televīzija", VIASAT AS Latvia branch, SIA "Star FM" and SIA "Smart AD".

services of content distribution (TV and video) the mobile operator will be able to offer and develop new products in the future for the customers. Also, the vertical integration mostly motivate other rivals to seek efficiency from their business models and develop new services or bundle of services.

10. In Latvia, TV broadcasting market the main demand on retail level is for paid TV channel packages offered by TV operators. On digital terrestrial platform for free there are available only two biggest state-owned channels and one channel broadcasting regional TV programs. Most of the customers choose paid TV packages.[2] TV operators operates in different TV platforms (satellite, terrestrial, cable, IPTV). Offers consist of the basic TV channel package that include all general interest national TV channels and some specialized. Different advanced packages additionally include premium TV channels mostly with specific thematic content (sports, adventure, music, etc.). Most of the households in Latvia choose basic paid TV channel packages.

11. In previous cases and review of this merger from demand side, TV channels were distinguished by their theme (general interest and specialized) and language (Latvian and other languages) defining separate relevant product markets. The merger deal included general interest channels with national coverage of 35,6% watching share in 2016. Closest competitor that was the state-owned TV broadcasting company with 2 national channels had 20% watching share. Also, MTG portfolio included other TV channels also with specialized themes.

12. At the same time, the TV advertisement market that is the main source of income for national TV channel production was analysed. TV advertisements still form important part of the whole advertisement market (43% share in 2016)[3], and is also recognized as the most efficient form of advertisement to reach different specific audiences. TV advertising allows to monitor GRP (Gross Rating Point) data and measures the effectiveness. It also is important as marketing channel and tool for competition. Due to that, TV advertisement is not fully substitutable and was defined separately from other kinds of advertising (online, press, outdoor advertising, etc.).

13. While reviewing the merger, the CC identified two markets as affected by the transaction: wholesale market for the national general interest of the TV channels (in Latvian language) and TV advertisement market in these channels. Both markets may be regarded as two-sided because they form income for TV channel production.

2.2. Analysis during review

14. One of the risks analyzed in the merger case was possible restrictions of access to national general interest TV channel (in Latvian language) for competing TV operators in TV channel wholesale market or imposition of less favorable contract terms to them. These concerns were analyzed concerning possible restrictions on the TV wholesale level. Also, restriction of access to TV advertisement in these must-have channels for competing telecom and TV operators was regarded as possible competition risk in future.

15. In the downstream retail market, TV channels as input are important for the TV operator to compile competitive TV channel packages for selling these products to customers later. There is no need for particular TV or group of channels to be dominant.

[2] Only 4,2% households in 2015 watched free to air TV channels in digital terrestrial platform.

[3] TNS: https://goo.gl/4Bfosm

For customers it is important that offered basic package consists of all the must-have TV channels. Lack of essential TV channels in the package may result in loss of competitiveness and thus loss of customers in long term. It leads to a conclusion that there is a high risk that refuse of a deal or application of unfair contract terms with downstream competitors may result in diminishing of competition in the downstream market. The merger was likely to raise the costs of downstream competitors (other TV operators, OTT[4] providers) with the possibility to restrict access to an important input (must-have national TV channels).

16. It is essential for all the TV operators to be able to acquire rights of audio-visual content on a non-discriminatory basis, thus also giving consumers access to diverse content (both linear and on-demand). For development of new products (also using OTT), access of consumers to must-have content plays an important role.

17. Possibilities for merging parties to bundle or combine offers with mobile, TV and other content related services together with above mentioned restrictions raised concerns about possible exclusionary strategy in the future with the aim to utilize this competitive advantage in the upstream market.

18. Furthermore, TV advertisement as service is highly demanded from telecom and TV operators in order to carry out their marketing campaigns. TV advertisement in their budgets make 50% in average. Most of advertising budget is paid for ads in MTG TV channels whose market share in TV advertisement market was approximately 50-60% in 2016. At the same time, the closest competitor (state-owned national TV channels) faces certain administrative restrictions (barriers). The state-owned national TV channels have restrictions for the length of advertising (maximum 6 minutes in 1 hour) compared to commercial (maximum 12 minutes). Also, it is likely that state-owned TV channels will be banned to sell commercial TV advertising in future leading the TV advertisement market to become highly concentrated. Also, according to responses given by the industry, these MTG TV channels and their closest competitors (state-owned) have audiences with different age range (younger and older) that is important for advertisers to make a choice where to place the particular TV ads.

19. That means, restriction of TV advertisement placement on must-have channels may have a significant impact on the ability of other competitors to compete equally and effectively. In past, there were few cases when media holding restricted placement of advertisements for its competitors (TV operators). That creates also some risk that information concerning advertising campaigns of competitors might be used by merging entities.

20. Before the merger, the Bite LT was also a minority shareholder of the second biggest fixed telecom operator SIA "Baltcom" (Baltcom) and was represented by one board member that was also a board member of Bite LT companies belonging to group. The CC considered this as possible coordination risk. To minimise such risks, the mobile operator provided commitments to separate representation in the boards of both undertakings.

2.3. Remedies

21. Due to the nature of merger that certainly will generate substantial efficiencies (vertical and conglomerate), but as well as might affect competition negatively, the CC

[4] Over-The-Top.

raised objections. The merging parties proposed remedies that were acceptable from the perspective of the CC. Remedies included behavioral commitments binding to merging entity.

22. Remedies included following obligations:

- In order to prevent the restriction of access to the TV channels wholesale market for other TV operators, merging entity were obliged to distribute their own TV channels to all market participants on non-discriminatory conditions. The company also were obliged to inform on its website about the procedures and criteria (also for discounts) applied for granting of broadcasting rights in different platforms (terrestrial, cable, IPTV, OTT).
- The merged parties were restricted to tie the TV channels TV3 (and other channels - 3+, TV6) with the second national TV channel LNT when selling them to TV retail operators. This allowed the TV retail operators to acquire broadcasting rights of separate TV channels, not only the entire package of MTG TV channels. If these TV channels were offered in the bundle, the discount for all TV channel offer shall not exceed 20% of the price when TV channels are sold separately.
- In order to prevent competition restriction on the TV advertising market, for example, by denying competitors of merged entity to advertise in these TV channels, the merged entity shall ensure placement of TV advertising clips in these channels on non-discriminatory conditions. To comply with this obligation company amended the procedures and criteria and published on its website.
- To prevent the risk of using the commercial information of competitors, that used TV advertising services in TV channels of MTG media holding, merged entity were obliged to use the obtained information only for the intended purpose, i.e., for placement of advertisements. To fulfill this condition merging parties amended internal procedure.
- Taking into consideration, that Bite LT owns capital shares of Baltcom merged entity was obliged to separate management of the minority shares. To comply with this obligation Bite LT committed that representatives of Bite LT or representatives of other associated companies will not participate in management bodies and will not engage in adoption of strategical, tactical and operational decisions related to activity of Baltcom meaning that Bite LT must appoint independent representative in board of Baltcom.