



**ADDRESS TO ANALYSTS, MORGAN
STANLEY, 1 May 2006**

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Australian Competition and Consumer
Commission**

CONVERGENCE, MEDIA & THE ACCC

Good morning.

Thank you for inviting me to talk to you today about convergence, media and the ACCC.

On 14 March, the Minister for Communications released a discussion paper titled 'Meeting the digital challenge', which outlines the government's preferred options for media reform.

The Minister's package sets out options, including:

- the development of a digital action plan to expedite conversion to digital TV by 2010-2012;
- allocation in 2007 of spectrum for two channels for new digital services, including subscription TV services, narrowcasting or datacasting;
- new channels for the ABC and SBS; and
- some ability for commercial TV networks to experiment with different types of High Definition TV programming on their HDTV broadcast.

The package also includes reforms to the cross-media rules to allow cross-media transactions to proceed, subject to existing limits on the holding of radio and TV licences as well as a new 5/4 media diversity rule – to be administered by the Australian Communications and Media Authority (ACMA). Future media mergers and acquisitions would also remain subject to section 50 of the *Trade Practices Act 1974* (the Act) – administered by the ACCC.

It's the ACCC's role in assessing the competitive implications of potential media mergers that I want to discuss today.

Of course, it's important we keep in mind that the Minister's paper sets out the government's preferred media reform options for discussion and consultation only at this stage.

Indeed, the date for commencement of any changes to cross-media rules is still not settled – as the Minister's paper notes, while the Government considers that there are sound reasons for the changes to begin in 2007, they might be deferred until 2010-2012 to coincide with the digital TV switchover.

Obviously, any changes to cross-media rules are entirely a matter for Federal Parliament and I won't be commenting on the relative merits of one particular reform over another.

The Minister stated in her paper that, once the media reform framework is settled, the ACCC would be asked to articulate its proposed approach to media mergers, and in particular those factors that will affect its definition of media markets.

In anticipation of this request, the ACCC is currently considering how the Act would apply to cross-media mergers in the event that the proposed reforms are adopted.

Given the scope of the proposed changes, we recognise that it would be useful for industry to receive some guidance in advance from the ACCC.

Of course, we can't ignore the rapid pace of technological and commercial innovation in the media and communications sector and the ever evolving business environment.

Consequently, such guidance could not amount to hard and fast guidelines or fixed market definitions that would apply indefinitely and without regard to the particular circumstances of the proposed merger itself.

But what we can and will do once the media reform package is settled is provide guidance on our likely approach to assessing whether a cross-media merger raises competition concerns.

However, in the interim, I want to give you a flavour of the types of issues the ACCC is grappling with in its consideration of potential media mergers.

In particular, I want to discuss the impact of the new technologies and business models that are changing the media and communications landscape before our eyes.

I will then note a few of the issues on which the ACCC will increasingly focus its attention as we move forward into this new media world – that is, the related questions of who controls the media content and who controls the means of delivering it to consumers (the 'pipes').

Once we've covered this, I'll conclude with some comments about what it all might mean for the ACCC's assessment of media mergers in the future.

Digitisation and convergence

It goes without saying that speculation and pipe dreams cannot be the basis of decisions we make in administering the Act. However, in order to assess the competitive impacts that are likely to result from cross-media mergers in the foreseeable future, it is important for us to keep a close eye on the technological developments redefining the telecommunications and media sectors as we speak.

While it's likely we are only at the very beginning of this period of significant change, new technology is already revolutionising the way we produce, consume and regulate communications and media in Australia.

Not that long ago, the main forms of media content were restricted to separate and distinct delivery platforms – a handful of TV stations beamed moving pictures with audio into our homes; radio stations carried music and talk shows for our listening pleasure while we did the housework or drove the kids to school; and newspapers gave us our printed news and classified advertising to read over the breakfast table.

We have generally considered these three platforms as distinctly separate – complements rather than substitutes – and, consequently, defined them as different markets within the overall media sector.

More recently the internet began to intrude on these neat definitions, in particular, on the domain of newspapers, through the development of online news and advertising portals which replicated a newspaper's printed content.

But this is just the tip of the iceberg – new telecommunications technologies and the digitisation of content are changing the media landscape irrevocably.

Increasingly, different types of content are becoming interchangeable as a result of digitisation and the development of new platforms for delivery.

Formerly separate industries are converging, while whole new business models are being created.

For example, Fairfax Digital provides a richer form of content than traditional newsprint – with text, pictures, audio and visual reports of, for example, the recent Commonwealth Games in Melbourne.

This has not only changed the media experience for consumers, but has required Fairfax journalists and editors to fundamentally re-engineer their traditional work processes.

The work cycle was previously geared around day-end deadlines for overnight printing. But now, text and video footage on breaking news is posted throughout the day on Fairfax Digital's web-sites.

It's not only the established newspapers that are providing content to consumers over the internet.

According to research by the Carnegie Corporation of New York¹ general interest web sites such as Yahoo and MSN that provide news streams all day, every day are now the number one source of daily news for 18 to 34 year olds. Forty-four per cent of them access such sites at least once a day for

¹ *Abandoning the News* Carnegie Reporter Vol 3, no2, Spring 2005, Carnegie Corporation of New York.

news. Local TV comes in second at 37 per cent, followed by network or cable TV web sites at 19 per cent and then newspapers at just 19 per cent.

Sources of news are becoming even more diffused than that. During the recent Iraq war, readers could access 'news' from the front-line from a variety of bloggers, ranging from a 21 year old member of the US Army stationed in Baghdad to an anonymous young Iraqi citizen, nicknamed the Baghdad Blogger, whose frequent dispatches appeared as well received by consumers as those of the seasoned war reporters and foreign correspondents from the established media.

This revolution is also providing newspapers with competition for the advertising dollars from the newer, but increasingly powerful online search companies – the Googles, Yahoos and MSNs.

According to a recent survey of Australian internet usage, search engines account for almost 10 per cent of all web-site visits. In contrast, websites providing pure news from traditional and internet media firms account for just over 5 per cent.²

Advertising Age predicted that the advertising revenues of Google and Yahoo last year would match those of America's three largest television networks, ABC, CBS and NBC.

No wonder then that Bill Gates is forecasting that within five years the internet will attract \$30 billion in annual advertising revenue – equal to the entire advertising revenue of the world's newspapers.

The trend towards digitising content is also impinging on traditional radio and TV broadcasting.

Podcasting is revolutionising the way we consume radio programs. Listeners no longer have to put up with content in the order and format determined by radio programmers. Instead they can download digital recordings from radio broadcasters within Australia or overseas and listen to the content on their iPod or mobile phone at a time and place of their choosing.

There is no doubt there is a large and growing audience for this form of content – and it's not just young technophiles that are in on the act.

It would be fair to assume the audience of ABC Radio National is not drawn entirely from tech-savvy Generation Y. And yet, a record 175 000 MP3 files of ABC Radio National programs were downloaded from its podcasting service in the week to 26 February 2006, contributing to a record total of 350 000 downloads that week across the ABC.

² Internet survey for the week ending 18 March, Hitwise. See: <http://www.etravelblackboard.com/index.asp?id=49447>

Listeners can currently download podcasts from around 26 Radio National programs, with a further 12 programs to become available over the next few months.³ The podcasting phenomenon is so mainstream that the New Oxford American Dictionary declared the term 'podcast' the *2005 Word of the Year*.

And as to moving video, broadband services will allow the delivery of video directly into people's homes, onto their PCs and a range of other personal media devices.

This is a far cry from the traditional TV platform, with its limited number of analogue TV channels.

Already, cable is used to deliver subscription TV in much of metropolitan Australia, and indeed some interactive TV, while satellite TV currently reaches more than half a million viewers in Australia.

DSL technologies over Telstra's copper/fibre network now provide broadband services to millions of Australian households.

But while Telstra offers a 1.5 megabit per second service across DSL and higher speeds across cable, new entrants like iiNet are offering more than 12 megabits per second across DSL to some customers.

In response, Telstra has raised the possibility of introducing more fibre into its network, extending it from the current exchanges all the way up to street corner nodes, in order to further improve the speed and quality of broadband services for many users.

As broadband speeds increase, so too will the range of services that can be provided to consumers.

With them will come new business models for innovative content and service providers in the media sector.

For example, once broadband speeds reach around 6 megabits per second, IPTV can be provided allowing viewers to receive DVD-quality TV. This is already a reality for consumers in some parts of the world, such as Hong Kong.

Wireless spectrum can also be used for broadband services, using technologies such as WiMax.

Now there's a debate about whether wireless services can competitively constrain a fibre network in the cities – but there's no doubt that in some areas, wireless will be better placed than the fixed network to deliver many broadband services in the future.

³ 'New Podcast High for Radio National', Radio National Press Release, 5 March 2006.

And let's not suppose that traditional over-the-air delivery of TV is necessarily being left behind.

Digitisation of broadcasting technologies is proceeding apace. The Minister's digital package includes proposals to release two new digital channels, which could be used for new subscription TV services or perhaps for mobile TV.

The Commonwealth Games was an obvious source of content for Melbourne's first live demonstration showcase of mobile TV using Digital Video Broadcasting-Handheld (DVB-H) technology. A trial of the technology, which allows simultaneous transmission of television, radio, video, audio and internet content to handheld devices such as mobile phones and PDAs, was undertaken during the games. You could have used a 3G handset last month to view a range of finalists in the 2006 Sony Tropfest short-film festival, held on 26 February.

But these are all possibilities, limited services or trials – a window on a digital future that remains just out of reach. As yet, it's too early to tell who the future content providers on these high-speed broadband networks might be and what new entrepreneurial business models they are likely to adopt.

We just don't know yet what kind of substitutes will be provided – if any – for higher bandwidth services such as channels Seven, Nine, Ten, ABC and SBS.

What we can say though, is that it is far more likely over time that content will be delivered by multiple platforms to consumers.

It's a point Rupert Murdoch readily acknowledged in an address last month aptly titled 'The Dawn of a new Age of Discovery':

A new generation of media consumers has risen demanding content delivered when they want it, how they want it, and very much as they want it. This new media audience – and we are talking here of tens of millions of young people around the world – is already using technology, especially the web, to inform, entertain and above all to educate themselves...From the wheel to the web, from the printing press to fibre optic cable, it has always been technology that has driven history. Those in the driving seat have always been those who fully understood and used that technology.⁴

The new technology is likely to be generally good for competition. It allows new entrants into markets that have previously been closed due to the limitations of old technology. It means more choice for consumers.

⁴ Rupert Murdoch, 'The Dawn of A New Age of Discovery: Media 2006', Speech at the Annual Livery Lecture at the Worshipful Company of Stationers and Newspaper Makers, 13 March 2006.

It also means that media market boundaries may change over time. Some market borders may expand as firms formerly in different markets find themselves competing; some markets may become narrower.

It may be that one day, traditional retail services such as individual newspapers, television stations and radio stations are no longer so critical.

Rather, what may become more important is having content that people want to access; and having some way to deliver it to the customer across a communications network.

At one level it means a greater focus by the ACCC on content and markets for news and information than in the past. In the future, it is possible that concentration of the control of premium content could be leveraged across multiple distribution platforms, with a far more damaging effect on competition.

At another level, it also means we will continue our focus on ensuring that control of the communications 'pipes' being used to deliver future media services cannot be exploited to stymie competition in downstream media markets.

As technology advances and take-up of broadband continues, how people access the content they desire, and at what speed, will increasingly be determined by the control of the telecommunications networks – the pipes – connecting homes and businesses.

As we have already witnessed, telecommunication companies themselves will have the capacity to deliver broadcasting services to their customers, alongside traditional telephone and internet services.

The importance of content and 'pipes' for downstream media markets

Primarily I want to talk about mergers today, but as an aside, I should mention that other competition provisions of the Act are likely to be relevant to competition in the media sector. There are other parts of the Act that would prohibit attempts to use control of content or the communications 'pipes' to substantially lessen competition in downstream media markets.

Exclusive agreements for the supply of popular sporting content are already common in both the free to air and pay-TV sectors. Such agreements are not necessarily anti-competitive.

Having said this, section 47 of the Act prohibits a range of conduct collectively known as exclusive dealing. In particular, section 47 would prohibit, for example, a business acquiring sporting content on condition that the owner not supply it to other businesses, if the arrangement substantially lessens competition.

Where section 47 does not apply, section 45 prohibits companies from entering into any arrangements that result in a substantial lessening of

competition. So, a telecommunications or media company exclusively acquiring certain premium content might – at least potentially – breach the Act.

Similarly, in regard to the control of communications networks and its effect on downstream media markets, the ACCC has regulatory powers under Parts XIB and XIC of the Act to address telecommunications bottlenecks.

In applying those regulatory powers to the networks of the future, the ACCC's objectives under the Act are:

- to encourage efficient investment in (and use of) infrastructure – and that includes taking into account investment incentives and the degree of risk;
- to promote competition – for example, we would be concerned if control of the telecommunications pipes could be used to exert control over downstream media markets; and
- to see that Australians continue to have any-to-any connectivity in communication services between each other.

Regulation is and must remain targeted at the key bottlenecks. In the current environment, where quasi-infrastructure based DSL competition is starting to take shape but threats remain, it is timely to look forward and consider the interactions in a holistic way.

With this in mind, the ACCC is undertaking a broad-ranging review of the regulation of fixed network services, including consideration of the alternative technologies mentioned above – notably wireless, cable and fibre. The review will assess if and where it is possible to wind back existing regulation, and where bottlenecks remain.

ACCC and merger guidance

To return to the specific issue of mergers and acquisitions.

Of course the ACCC already looks at media mergers and acquisitions under section 50 of the Act.

For example, in September 2004 the ACCC decided that it would not oppose the acquisition of 92 regional radio stations by Macquarie Bank, after receiving an undertaking from the bank to divest seven radio stations in five regional markets.

Consultations with market participants at the time indicated that our traditional view of media advertising markets still held – that is, that television, print and radio were separate advertising markets.

In an industry characterised by constant changes in technology and consumer taste, and potentially significant regulatory changes, it is likely that views on market definition will evolve over time.

And section 50 of the Act specifically requires the ACCC to consider the dynamic characteristics of the market, including innovation.

That means that when we come to define markets we will not only consider what the situation looks like today but also what it is likely to look like in the foreseeable future. As a rule of thumb, we tend to look around two years into the future, but it can be longer if there is sufficient certainty about what is expected to occur.

So, in assessing market dynamics, we will obviously need to pay close attention to the realistic pace of technological change and to whether business models have been, or are likely to be, developed to exploit technological changes in a commercially viable way.

Clearly, views on market definition formed in 2004 might not necessarily hold by the time the ACCC comes to assess a cross-media merger.

It is worth remembering that the ACCC would not be required to assess a cross-media merger under the proposed reforms until 2007 at the earliest, at which time the ACCC would be looking at market dynamics up to at least 2009.

The process of convergence will likely change market boundaries over time. Some market borders may expand as firms that were previously in different markets find themselves competing; some markets may become narrower as old business models that used to provide substitutes decline in importance. Traditional 'silos' of print, radio, free-to-air TV and Pay TV may not remain in separate markets.

The analysis of likely competitive effects

While it is difficult and inappropriate for the ACCC to specify market definitions before it has a matter before it, perhaps I can say some specific things about how the ACCC would go about applying section 50 to liberalised media and communications markets.

Market definition, after all, is not the be all and end all of section 50. Market definition is merely a tool, albeit an important one, in the primary task of determining whether a proposed acquisition is likely to lead to a substantial lessening of competition in a relevant market. Further, market definition is a purposive tool: outcomes on market definition will vary according to the issue being addressed.

This analysis of likely competitive effects always begins with identifying the products of the acquiring and target firm. In dynamic markets this can be a difficult process. As discussed above, media companies that have produced a narrow range of traditional products in the past are likely to produce a greater range of products in the future.

For example, a traditional television services provider has bought television content, produced some content in-house, sold advertising time and broadcast an integrated television program largely to households free of charge. The content and advertising markets have been largely television specific so free-to-air television companies have, by-and-large, competed against and only against each other.

However, the traditional model has already changed and is continuing to change. Television companies on-sell content to pay-television, broadband service providers and mobile phone companies; and sometimes have to compete with this broader range of service providers for the acquisition of content. Similar trends can be observed in advertising markets: television advertising is not regarded as 'special' as it used to be.

The implications for traditional newspaper services are just as important. In the past, newspapers have sold advertising space, bought and developed content, and sold (or in some cases, given away) newspapers. Classified advertising, for some newspapers at least, have been the so-called 'rivers of gold'. This has been driven by a feature of traditional advertising services that economists call network externalities.

In simple terms, this means that classified newspaper advertising services have become more valuable for users of these services the more that people use them. For example, if you want to advertise your car for sale, you're more likely to advertise it where you know that there are lots of people looking for cars. And if you're looking to buy a car, you're more likely to look where lots of cars are advertised for sale.

This feature of classified advertising has, in the past, tended to concentrate newspaper classified advertising markets, and in turn, newspaper markets. The major regional newspapers have, in the past, enjoyed large market shares and significant market power.

But as outlined above, electronic and in particular online advertising services are gaining popularity at the expense of traditional classified advertising. Is it likely that online advertising will feature the same externality characteristics as traditional classified advertising?

Are there such synergies between continuing to provide newspaper advertising and online advertising such that it is inevitable that the provision of on-line services will be as concentrated as traditional newspaper markets?

Will the current geographic boundaries of traditional newspaper advertising competition still apply for on-line services?

While current market structures and trend for these new services can be observed, it is probably too early to provide definitive answers to these questions. But we know enough to predict that these questions will probably be important.

Does all this mean that all content and advertising is in the same product market? Probably not and certainly not necessarily so. At least one further question needs to be addressed: how effective is the competition between different forms of content and different advertising modes, and how effective is it likely to be in the future?

This question is easily expressed but extremely difficult to answer in dynamic markets. This is in large part because, contrary to the apparent certainty of market definition analysis, competition is neither a static nor a binary concept. There are degrees of competition which change over time and especially in dynamic markets.

Competition can be observed which is insufficient at any point in time to effectively discipline prices in a particular market. But that can change with new entry, expansion by existing market participants, changes in technology, changes in consumer tastes, innovation or any combination of these things. All of these considerations are likely to be relevant in consideration of a proposed acquisition in media and communication markets in the future. They will require careful comparison at the time of the proposed acquisition and two years or so beyond of the likely state of competition of a future with the acquisition and without it.

Meanwhile, it seems likely that in many media markets we should see an increase in competition due to convergence and the presence of new entrants in previously closed markets – just think of the examples from the Internet that we spoke about earlier.

In those markets, consumer choice will rise and lack of competition may not be an issue. That is part of the promise of the new digital age.

But at the same time, the ACCC does realise that we are still living in the early stages of that wave of technological change that is revolutionising our media and communications industry.

We all want to see new services, dynamic innovation and entrepreneurial energy and competition in the future of Australia's media and communications sector.

We can see already that the Internet is providing new business models and new outlets for some kinds of content and news and information.

But despite these changes and the real possibility of further technical developments, for many media services the future is not quite here yet. As I said earlier, in April 2006 it's just too early to say for sure what kind of substitutes will be provided – if any – for higher bandwidth services such as channels Seven, Nine, Ten, ABC and SBS. And while it is important for us to keep a close eye on technological developments, the law requires more than mere speculation.

So where new services develop or look likely to do so in the foreseeable future, we will take them into account in assessing media mergers and acquisitions under the provisions of the Act. But we won't base our decisions on mere speculation.

And at all times, the ACCC will be looking closely at any content, advertising or news and information markets where concentration appears to be occurring.

Not only in Australia as a whole, but also in regional markets, as the Act requires.

Conclusion

We are working hard to consider how the issues I have raised here may affect the ACCC's approach to media mergers under the Minister's proposed reform.

Of course, it is worth remembering that under the Government's proposed regulatory environment, the Act will not constitute the only potential hurdle to a cross-media merger – possible mergers will also need to satisfy the new 5/4 media diversity rule, to be administered by ACMA, and existing limits on the holding of radio and TV licences.

Once the reforms are settled and following the Minister's formal request, we will provide guidance on how the ACCC is likely to approach its consideration of a media merger or acquisition.

In developing our response, we will consider the range of factors I have mentioned today.

As I noted at the outset, this guidance cannot take the form of hard and fast rules or market boundaries fixed for all time – we will assess each merger on the basis of the specific facts and circumstances surrounding it at the time.

In the interim let me conclude by assuring you that the ACCC's approach will be consistent with the Act's general objectives.

Where a merger between firms would not substantially lessen competition in a relevant market then section 50 will be no barrier.

If we cannot satisfy ourselves of this, the law we have to follow is very clear – assets or shares cannot be acquired in a company if that is likely to have the effect of substantially lessening competition in a market.