

EN

*Case No IV/M.202 -
THORN EMI / VIRGIN
MUSIC*

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**REGULATION (EEC) No 4064/89
MERGER PROCEDURE**

Article 6(1)(b) NON-OPPOSITION
Date: 27.04.1992

*Also available in the CELEX database
Document No 392M0202*

MERGER PROCEDURE
ARTICLE 6(1)b DECISION

PUBLIC VERSION

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To the notifying party

Dear Sirs,

Subject: Case No. IV/M202 - Thorn EMI/Virgin Music
Notification of 20.3.1992 pursuant to Article 4 of
Council Regulation No. 4064/89

1. This case concerns the proposed acquisition by Thorn EMI plc (Thorn EMI) of the entire share capital of Virgin Music Group Ltd (Virgin).
2. After examination of the notification, the Commission has concluded that the notified operation falls within the scope of Council Regulation No. 4064/89 (the Regulation) and does not raise serious doubts as to its compatibility with the common market.

I. THE PARTIES

3. Thorn EMI is the ultimate holding company for a large group of companies, the principal businesses of which are music (28% of total turnover) and the rental of consumer durables (also 28%). Its other businesses are retailing, lighting and security and electronics.
4. Thorn EMI's music activities include both music recording and music publishing. It is also a retailer of records. In music recording Thorn EMI is one of the five vertically integrated "major" record companies worldwide, its activities including the manufacturing and distribution of records and the ownership of recording studios.
5. Virgin is a record company and music publisher. Its music recording activities do not extend to manufacturing and distribution. The retailing (including record retailing), communications and airline businesses carried on under the Virgin name are separate groups of companies and are not connected with the proposed acquisition.

II. CONCENTRATION

6. The proposed operation is a concentration within the meaning of Article 3(1) of the Merger Regulation in that Thorn EMI will acquire control of the whole of Virgin.

III. COMMUNITY DIMENSION

7. The operation has a Community dimension. The combined aggregate worldwide turnover of Thorn EMI and Virgin amounts to more than 5,000 million ECU (5,172 million ECU for Thorn EMI in 1990/91, 472 million ECU for Virgin in 1990/91). The aggregate Community-wide turnover of each is more than 250 million ECU (3,456 million ECU for Thorn EMI, 316 million ECU for Virgin in the same period¹⁾) The parties do not achieve more than two-thirds of their Community-wide turnover in one and the same Member State.

IV. COMPATIBILITY WITH THE COMMON MARKET

8. The main effects of the proposed transaction are horizontal in nature, involving the elimination of Virgin as a competitor in music recording and music publishing. In addition, certain vertical effects may result from the fact that Thorn EMI has manufacturing and distribution activities, while Virgin does not. Furthermore, it is necessary to consider the impact of the proposed transaction on the interplay between music recording and music publishing.

Music recording

Product market

9. The central activity of record companies is the selling of records²⁾. This incorporates the signing up, recording and promotion of artists. Recorded music may be broadly divided into two major categories - "pop" and classical. Within the EEC, pop music is by far the most significant in terms of sales volume and value, representing around 90% of the total value.
10. The parties also differentiate between international pop (that is, English songs performed by UK and US artists) and national pop (that is, songs performed by non-UK or non-US artists in whatever language) as different product groups within the pop music market.
11. The narrowest product market definition would distinguish between individual artists or even individual songs. However, retailers, who are the customers of the record

¹⁾ The latter figure excludes the turnover in Denmark.

²⁾ "Records" are taken to include LPs, cassettes and compact discs unless otherwise specified.

companies, while mainly driven by the demand of the ultimate consumer, do not take such a limited approach.

12. For the purposes of the present case it is not necessary to decide whether or not product groups within the pop market constitute separate markets since the effects of the proposed transaction within these individual groups are similar to that for pop music as a whole and, as seen below, even on the narrower product definition, the proposed acquisition will not lead to the creation or strengthening of a dominant position.

Geographic reference market

13. The parties consider the geographic market for both international pop and classical music to be the EEC as a whole on the basis that the principal competitors are present in each national territory and cross-border trade occurs on a substantial scale. As regards national pop, the parties consider the reference market to be national, since national artists and their music are not generally present outside their own country.
14. However, a number of features of the music recording market tend to be national as opposed to Community-wide. For example, the record companies have distinct repertoire policies for each Member State, based on distinct demand, and differing levels of demand by consumers for national and international pop, and also, to a lesser extent, classical music. Growth rates are also different in individual Member States. It should be noted, however, that there seems to be a pan-European repertoire policy mainly for major artists³⁾.
15. In addition, the structure of the retail business differs from Member State to Member State. At present, there appear to be only two retailers operating in more than one Member State. All retailers, including those which are active in more than one Member State, purchase their requirements from the local outlets of the record companies. Record distribution is also organised on a Member State basis, with the exception of the Benelux States.
16. Record companies also price their products differently in the individual Member States. The patterns of discounts, rebates and other returns, as well as other contract terms, vary as between different Member States.
17. For purposes of this decision, however, it is not necessary to determine whether the geographic reference market is delineated by the individual Member States or is the EEC (or EEC and EFTA) as a whole, since, as seen below, even on the narrowest geographic reference market, the proposed acquisition will not lead to the creation or strengthening of a dominant position.

³⁾ An artist is considered to be a "major artist" if he or she generates a significant turnover over several years, sells more than one million albums, and usually generates export sales.

Assessment

18. As a result of the proposed acquisition the combined market share of Thorn EMI and Virgin for all types of music will in nearly all cases be less than 25% irrespective of the geographic reference market analysed.
19. In Greece and Portugal, although the combined market share of the parties will be higher than 25% for pop music overall and national pop, it is not increased significantly by the acquisition of Virgin. In addition, the other major participants are present on these markets (only Warner is absent in national pop in Portugal). These countries represent less than 2% of the total EEC market for pop music.
20. It follows from the above that the combined market share of Thorn EMI and Virgin, together with the existence of other strong players, would not normally indicate a dominant position for the acquiring party.
21. The structural features of the market(s) for recorded music could indicate a situation of collective dominance. However, the Commission has concluded in the present case that the proposed acquisition would not create or strengthen a dominant position among the five major record companies as a result of which effective competition would be significantly impeded in the common market or a substantial part of it.
22. The music recording industry is highly concentrated. In the pop music market concentration has been particularly marked since the latter half of the 1980s. Since 1988 at least six independent labels have been acquired by the top five major companies. Virgin is in fact the last remaining significant independent record company.
23. The combined market share of the leading five companies - Thorn EMI, Sony, Polygram, Warner and Bertelsmann (BMG) - is currently estimated at 77% for the EEC as a whole and ranges from around 70% to 80% in individual Member States. Each of Thorn EMI's major competitors are significant participants in the market. They are all active in most types of music and in every Member State.
24. In international pop the level of concentration for the five companies is around 70% in the UK, and 85% in France and Germany. For national pop the figures are the same for the UK (where all music is considered to be international pop) and around 70% and 80% for France and Germany, respectively.
25. For classical music the figures for UK, France and Germany are around 90% in each country. However, by contrast to the situation for pop music where market shares between the top five companies are fairly comparable, in classical music one company - Polygram holds more than half of the market.
26. As a result of the disappearance of Virgin from the market, the level of concentration will increase. Thus, the top five companies will then control an estimated 83% of the

EEC market. In individual Member States the level of concentration will range from around 70% to 95%.

27. In international pop, the level of concentration amongst the top five companies in the UK will increase to around 75%, and 90% in France and Germany. For national pop the figures are the same for the UK, and for France and Germany around 80% and 85%, respectively.
28. For classical music, Virgin's own small market share means there is little difference in the overall level of concentration generally and in individual Member States 3% or less in all Member States. As a result, the existing gap between Polygram and its main competitors will remain virtually the same.
29. The market(s) for recorded music is characterised by certain special features, including the heterogeneous nature and short life cycle of its products, the constant change in consumer preferences, based to some extent on changes in fashion, and the significance of individual artists or hit records to a record company's profitability rather than the development of brand loyalty to individual record labels on the part of the ultimate consumer.
30. Despite such dynamic characteristics, however, an examination of historical market shares shows that the top five companies have generally retained their strong market positions and, as a group, their combined market share has increased, at least for the UK, France and Germany. This increase has taken place at the expense of the smaller record companies.
31. The major record companies each have a large and varied collection of titles in their back catalogues from which they draw a significant proportion of their annual turnover. The back catalogue comprises all past single and album titles. A continuing demand exists for a number of these titles which generates a steady source of income for record companies. This income is obtained without any of the costs associated with promotion and marketing of new titles.
32. The income derived from the back catalogue is a valuable source of finance for investment in artists and enables the major record companies to take higher risks in the investment of artists by comparison to their smaller competitors. When combined with revenue from current hits, only the major companies are able to compete for major artists, some of whom can command extremely high advances.
33. In addition, market share is an indicator of a record company's success, which in turn provides significant leverage in promoting new releases and new talent. A proven track record in this industry, more than most, opens the door to the market through air play, advertising and retail promotion.
34. With regard to barriers to entry, there have been numerous entrants to the recorded music business in the EEC over the last five years. However, none have become a significant

market force. For example, while there have been nine entrants on the UK market in the last five years, their combined market share amounts to only 4% on the market for albums.

35. Amongst such competitors, however, is MCA, the only major record company which is currently not present in the EEC to a significant degree. MCA began its operations in the EEC through licensing its works to other major record companies. It has since set up its own businesses in the UK, Ireland and, most recently, in Germany. It appears that the only other entrants of any significance over the last twenty years have been Walt Disney (through Hollywood Records) and Virgin itself.
36. As regards growth, the music recording industry has grown significantly in value (around 10% annually) and volume since the introduction of the compact disc in the mid 1980s and as a result of favourable economic conditions in the major markets. Although the industry expects growth to continue in value terms in unit sales (but at a slower rate) as compact discs become the principal carrier it is expected to stabilise in volume terms in unit sales.
37. A number of cooperative agreements exist in the industry involving the five major record companies. These agreements relate to record compilations, distribution, electronic ordering and rack jobbing.
38. The main parameters for competition in the market(s) for recorded music are the promotion of records and the provision of a wide variety of artists and types of music. Because of the special nature of the products in this market(s), the scope for price competition seems to be limited. Other parameters have therefore become important such as promotion through advertising, radio air play, exposure in the media, concert tours and other promotional items. In addition, record companies can compete for access to window space and point-of-sale advertising in retail outlets. The most significant parameter of competition in the market for recorded music is the need to meet the demand for constant changes in music tastes and fashion, through new releases and signing up new artists.
39. As part of its examination the Commission carried out a certain number of enquiries in order to evaluate the market behaviour of the main participants in the market. The Commission concentrated its enquiry on the three principal markets within the EEC (UK, France and Germany). The level of concentration in these markets is representative of the other Member States. These enquiries did not produce any findings that the market is performing in an anti-competitive manner. There is competition vis-à-vis retailers with regard to discounts⁴⁾. There also is

⁴⁾ The Office of Fair Trading has recently informed Thorn EMI and, presumably, the other major record companies operating in the United Kingdom that it has concluded from its own review into the prices of compact discs in this country that there is no evidence to suggest any collusion between

effective competition with regards to budgets for artists and the number of new releases issued by the major record companies.

40. There are no indications that the proposed acquisition will fundamentally change conditions of competition in the market(s) for recorded music. Overall concentration in the market will increase to some extent. It appears, however, that the increase caused by this particular transaction will not, on its own, imply a perceptible lessening of competition in the market.
41. It follows, therefore, that the proposed transaction will not create a dominant position in the common market or a substantial part thereof in the market for recorded music.

Record distribution

42. The distributor's function is to distribute physically the records from the record company to the retailers in return for a fee. The distributor has a very limited role, if any, in the marketing of records.
43. Historically record distribution takes place largely on a national basis although there are moves to arrange it on a cross-border basis (in the Benelux countries).
44. The market for the distribution of records is in the hands of the major record companies, both within individual Member States and in the EEC as a whole. Thus, as regards the EEC, as well as in individual Member States the top five major companies hold at least 80% of the market. Thorn EMI's own market share is less than 25% in all Member States except Greece and Portugal.
45. Because Virgin does not distribute records, Thorn EMI will not acquire distribution capacity as a result of the concentration. In addition, Thorn EMI already distributes Virgin's output in France, Greece, Italy and, through a joint venture, in Denmark.
46. The vertical effects of the proposed transaction will be insignificant in the three Member States where Thorn EMI already distributes Virgin's records, and in Denmark. With regard to other Member States, Virgin's output may be simply redistributed mainly amongst the top five record companies, with the exception of Portugal, where Thorn EMI's market share may increase from 38% to 44%. It should be noted, however, that distribution contracts are normally short term, with no guarantee of renewal.
47. On the basis of the above it can be concluded that the proposed acquisition will not in practice change the current conditions of competition.

the record companies.

Record manufacturing

48. The record manufacturer's function is to manufacture the various music carriers - LPs, music cassettes and compact discs, including the recording of music on these carriers. Each carrier is technically distinguishable and uses different manufacturing techniques. They are therefore different product markets.
49. Each carrier is easily and economically transported across considerable distances, and the market for each is characterised by extensive cross-border movements. The geographic reference market is the EEC or possibly wider.
50. Market concentration within the EEC for the manufacture of cassettes and compact discs is relatively high. The five major companies hold around 45% of the cassette market, and around 60% of the compact disc market. Thorn EMI itself holds below 25% in the EEC.
51. Because Virgin does not manufacture records, Thorn EMI will not acquire additional capacity as a result of the proposed transaction.
52. Even if Thorn EMI were to manufacture all of Virgin's current requirements for all three formats, the increase in Thorn EMI's market share could not substantially alter conditions of competition in the common market. This is so, even when analysed at the EEC level which is the narrowest geographic reference market.

Other related markets

53. While both Thorn EMI and Virgin own recording studios the impact of the proposed acquisition on this market is negligible since over 60% of recording studios are independently owned.
54. With regard to the market for music videos, Thorn EMI is present on this market through the production and sale of videos. Virgin's activity on this market, by contrast, is confined to creating videos in the course of its activity in the record business which are licensed to a third party, together with the distribution of some videos through its record distribution agreements. As a result, there is currently no horizontal relationship between the parties. Moreover, given Thorn EMI's small market share in music videos, and Virgin's limited activity in this market, even if Thorn EMI were to sell Virgin's videos itself in the future, this would not have any significant effect on the market.
55. With regard to the retailing of records, Thorn EMI is active on this market while Virgin is not. As a result, there are no horizontal effects as a result of the proposed acquisition. In addition, given Thorn EMI's small market share in record retailing, which is confined to the UK within the EEC, the vertical effects are minimal.

Music publishing

Product market

56. Music publishing involves the promotion of a composer's songs and the administration and collection of the composer's income, mostly in the form of royalties. Income is collected from the following sources: mechanical royalties from record companies arising on the sale of recordings; performance royalties from sources such as radio, television and theatre; synchronisation fees from advertisers, television and film companies; and income from sheet music sales. Royalty fees are generally set by industry regulation in individual Member States.
57. Music publishing may be divided into two main markets: pop music and classical music publishing, the latter being limited in scope because most classical music is now out of copyright. In view of the fact that the parties have little involvement in classical music publishing (classical music accounts for less than 1% of Thorn EMI's music publishing turnover, and even less in the case of Virgin), it is not necessary to consider this market further. Turnover figures from this market are in fact included in the parties' pop music figures. With regard to pop music, the parties again distinguish international and national pop as separate product groups, for the same reasons as given for recorded music.

Geographic market

58. National pop publishing, by its very nature, tends to be geographically defined by cultural and linguistic borders. For this reason, therefore, the geographic reference market is confined to individual Member States. By contrast, pop publishing in the UK and Ireland is virtually all international pop. This music may face some competition from pop publishing in other countries so that the market may be broader than the UK and Ireland itself. As in the case of recorded music, however, no precise definition is necessary on the facts of the case because, even on the narrowest reference market, the proposed transaction does not create or strengthen a dominant position.

Assessment

59. Thorn EMI and Warner-Chappell are current joint leaders in music publishing in the EEC (16% each). They have become leaders through acquisitions made in the last ten years, in particular through Warner's acquisition of Polygram's publishing operations and Thorn EMI's acquisition of CBS's publishing businesses. Polygram and Sony (CBS) have now reentered the market and, together with BMG and, currently, Virgin, are the middle players on this market. In addition, a substantial number of smaller players exist, which collectively account for more than half of the total market.
60. As a result of the proposed acquisition, Thorn EMI will increase its market share to 21% in the EEC as a whole. The main strength of Thorn EMI and Virgin lies in international

pop publishing. Here their combined market shares will range between 10% and 34% for most Member States. The combined market shares in Greece and Portugal are higher but these markets are at an early stage of development and are currently very small in terms of value.

Conclusion

61. Given the fact that firstly, Warner-Chappell has a fairly comparable market position in all Member States, and secondly, that other major record companies are also active in music publishing, together with the fact that the market for music publishing has shown strong growth rates which are forecast to continue, the proposed acquisition will not create or strengthen a dominant position in the common market or a substantial part thereof.

Interplay between music recording and music publishing

62. Some vertical effects result from the proposed transaction in that Thorn EMI is strengthening its position as a music publisher through the acquisition of Virgin's music recording business. These vertical effects will be limited because, as stated above, music publishers receive income from, amongst other sources, mechanical royalties from record companies arising on the sale of recordings.
63. As to whether the proposed transaction has any foreclosure effects for other music publishers, the following observation can be made: In practice record companies seem to have no special allegiance to their own publishing arms. For its part, Thorn EMI has paid out more than three-quarters of its royalty fees to competing publishing companies. Even if such allegiances were to exist, in practice this would leave more than 80% (70% if Warner were included) of the market available to music publishers. Collectively, the five major record companies account for less than half of the world's published works.
64. As a result there is no foreclosure of the music recording industry for music publishers as a result of the proposed transaction.
65. As to the potential foreclosure of the music publishing market for record companies, it should be recalled that industry regulation requires that licences for the majority of exploitation of musical works are granted automatically to all users. In addition, industry regulates the licence fees charged by a publisher to a user irrespective of whether the user is an "in house" or third party record company.
66. For this reason, therefore, there is no foreclosure of the music publishing industry for record companies as a result of the proposed transaction.

V. ANCILLARY RESTRAINTS

67. A [*] non-competition clause is agreed between Thorn EMI and Richard Branson (a vendor of Virgin) in relation to music recording and music publishing. This clause is directly related and necessary to the implementation of the concentration and, as such, may be regarded as an ancillary clause within the meaning of the Commission's notice regarding restrictions ancillary to concentrations.

Overall conclusion

68. It follows from the above findings that the proposed acquisition will not create or strengthen a dominant position as a result of which competition would be significantly impeded in the common market or a substantial part thereof.

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For the above reasons the Commission has decided not to oppose the notified concentration and to declare it compatible with the common market. This decision is adopted in application of Article 6(1)(b) of Council Regulation No. 4064/89.

For the Commission,

**TEXTE RECONSTITUÉ ÉLECTRONIQUEMENT / ELECTRONICALLY RE-CREATED
TEXT / ELEKTRONISCH NACHGEBILDETER TEXT**

* Business secret deleted. The duration of the prohibition on competition is less than five years.