

**COMPLETED ACQUISITION BY CINEWORLD GROUP PLC OF
CITY SCREEN LTD**

Statement of issues

29 May 2013

The reference and our issues statement

1. On 30 April 2013, the Office of Fair Trading (OFT) made a reference to the Competition Commission (CC) under section 22 of the Enterprise Act 2002 (the Act) concerning the completed acquisition by Cineworld Group plc (Cineworld) of City Screen Ltd, which trades mostly under the name Picturehouse (hereinafter referred to as Picturehouse) (collectively 'the parties').
2. The CC must decide:
 - (a) whether arrangements are in progress or in contemplation which, if carried into effect, will result in the creation of a relevant merger situation; and
 - (b) if so, whether the creation of that situation may be expected to result in a substantial lessening of competition (SLC) within any market or markets in the UK for goods or services.
3. In this statement we set out our view of the framework for our analysis and the main issues that we are likely to consider in reaching our decision (although this does not preclude the consideration of any other issues that may be identified during the course of our investigation). We are publishing this issues statement in order to assist parties submitting evidence to focus on the issues we currently envisage being relevant to our inquiry and to invite parties to notify us if there are any additional relevant issues which they believe we should consider.

Background

4. Both Cineworld and Picturehouse operate cinemas across the UK. Cineworld operates 79 cinemas with an average of ten screens each, while Picturehouse operates 21 cinemas with an average of three screens each. Their 2011 shares of UK box office revenues were 26 and 1.6 per cent respectively. Cineworld is listed on the London Stock Exchange, while Picturehouse was until the transaction funded principally through venture capital investment.
5. On 6 December 2012, Cineworld acquired the entire share capital of Picturehouse.

The markets in which the parties operate

6. The parties overlap in the operation of cinemas in the UK. We will examine the extent to which different types of cinemas compete with each other and we will consider the different factors which determine the closeness of this competition. We will also consider the scope of the relevant geographic markets.
7. We will assess the importance of constraints from products both inside and outside the relevant market in our analysis of the competitive effects of the transaction.

8. It appears to us that competition between cinemas is predominantly local in nature, and for this reason we intend to focus our analysis on local effects.

Assessment of the competitive effects of the merger

Counterfactual

9. We will consider the possible effects of the merger on competition compared with the competitive conditions in the counterfactual situation (ie the competitive situation without the merger). We will therefore assess what would have happened without the merger.

Theories of harm

10. We refer to the possible ways in which an SLC could arise as a result of the merger as theories of harm. We have set out below the theories of harm which we intend to investigate. However, we may revise our theories of harm as our inquiry progresses. Also, the identification of a theory of harm does not preclude an SLC being identified on another basis following further work by us or the receipt of additional evidence. We welcome the views of parties on all the theories of harm set out below.

Theory of harm 1: Unilateral horizontal effects at a local level

11. The concern under this theory of harm is that the removal of one competitor, in some or all of the areas where the parties both have cinemas, could allow the merging parties to increase their prices or reduce the quality of their services locally. Examples of quality reduction could include the quality and range of the films shown, the standards of the venues, associated product offerings (eg food and beverages) and opening times. It is also possible that the merger might incentivize the merged company to close one of its existing venues, with implications for customer choice and the variety of repertoire available.
12. The approach usually adopted by the CC in its assessment of retail mergers (with which cinema mergers share some characteristics) is first to identify the areas where the geographical proximity of the parties' sites might raise a preliminary concern about competition. Following this approach, we intend to use a suitable 'catchment area' analysis. In past cinema mergers, the CC has used boundaries delineated by drive-times around the parties' venues.
13. Within the catchment areas identified we will then identify those areas where it appears that the merger may reduce competition significantly. In its assessment of retail mergers, the CC has usually done this by looking at areas where a merger reduces the number of independent fascia below a certain level.
14. We note that, as a result of its catchment area and fascia analyses, the OFT identified ten areas which raised preliminary concerns, which were:
 - Aberdeen;
 - Brighton;
 - Bury St Edmunds;
 - Cambridge;

- Clapham;
 - Edinburgh;
 - Greenwich;
 - London—Stratford;
 - Southampton; and
 - Stratford upon Avon.
15. Once we have identified the geographical areas for further consideration, the analysis which will be particularly relevant to our assessment is likely to consider:
- consumption patterns—profiling of customers and films;
 - consumer switching;
 - film selection—the ease with which, and the extent to which, cinemas are able to switch between different types of film;
 - competitor offerings and the extent of differentiation;
 - price setting and competitor monitoring; and
 - the effects of historic structural changes to local markets—for example, openings and closures.
16. One piece of evidence which we intend to use is a consumer survey which we are in the process of commissioning.

Theory of harm 2: Unilateral effects at a local level due to the loss of a potential competitor

17. The second theory of harm is that the merger may lead to a loss of a potential competitor in an area. In particular, such an adverse effect may arise if, prior to the merger, the behaviour of either party was influenced by the threat of the other expanding and entering into direct competition with it. Under this theory of harm, by removing a potential competitor from some local markets, the merger may reduce the competitive pressure in those markets.
18. Our assessment of this theory of harm is likely to include us considering:
- internal documents relevant to the development of new sites and the permissions required, both before and after the merger; and
 - the previous experiences of parties in seeking to open or expand cinemas

Theory of harm 3: Unilateral effects at a local level in non-overlap areas

19. We understand that Picturehouse has agreements with many independent cinemas under which it supplies various services, including film selection and the provision of back office systems. As a result, the merger may affect the extent of competition

between some of these independent cinemas and Cineworld, due to the influence which Picturehouse is able to exert.

20. Currently, we do not have a clear view on the extent of the influence which Picturehouse is able to exert on those cinemas with which it has a service agreement or the length or terms of these contracts.

Possible theory of harm which we do not intend to investigate: coordinated effects

21. We do not intend to investigate the possibility of the merger increasing the likelihood of coordinated effects as it appears to us unlikely that the conditions for coordination will be significantly affected by the merger. However, should any party have reason for believing that we should investigate this possible harm it should tell us and provide its reasons.

Countervailing factors

22. We will consider whether there are countervailing factors which are likely to prevent or mitigate an SLC. In particular, we intend to consider the following:
 - (a) *Entry.* We will consider how easy it is to open a new cinema in the local areas of potential concern and whether entry would be timely, likely and sufficient to prevent any SLC. To do this we will:
 - (i) look at the history of actual expansion and exit by the parties and by their competitors and review any future plans; and
 - (ii) examine the factors which might inhibit entry or the expansion of existing competitors into the local areas of potential concern within, say, two years, including the availability of suitable premises and planning restrictions.
 - (b) *Efficiencies.* We will examine any arguments made in relation to efficiencies arising from the merger. In particular, we will examine whether any postulated efficiencies are rivalry-enhancing and can be expected to offset any loss of competition. We may also consider arguments relating to the extent to which the offerings of Cineworld and Picturehouse are complementary and, for this reason, how the merger might benefit consumers, for example in the potential for common membership schemes or bundled pricing.
23. We are not currently aware of any other countervailing factors.

Possible remedies and relevant customer benefits

24. Should we conclude that the merger may be expected to result in an SLC in one or more markets, we will consider whether, and if so what, remedies might be appropriate, and will issue a further statement.
25. In any consideration of possible remedies, we will take into account whether any relevant customer benefits might be expected to arise as a result of the merger and, if so, what these benefits are likely to be and which customers would benefit.

Responses to the issues statement

26. Any party wishing to respond to this issues statement should do so in writing, by no later than 5pm on 13 June 2013. Please email cineworldcityscreen@cc.gsi.gov.uk or write to:

Inquiry Manager
Cineworld/City Screen merger inquiry
Competition Commission
Victoria House
Southampton Row
LONDON
WC1B 4AD