

CINEWORLD/CITY SCREEN PROVISIONAL FINDINGS

RESPONSE BY ODEON

1. INTRODUCTION

- 1.1 Odeon welcomes the opportunity to respond to the Competition Commission's ("CC") provisional findings report (the "**Report**") in relation to the completed acquisition by Cineworld Group ("**Cineworld**") of City Screen (the "**Transaction**").
- 1.2 Odeon agrees with the CC's provisional finding that the Transaction will result in a substantial lessening of competition ("**SLC**") in Aberdeen, Bury St Edmunds and Cambridge.
- 1.3 However, Odeon has concerns that the CC has failed properly to assess the effect of the Transaction on competition in the local markets in Brighton, Southampton and Greenwich. Having reviewed the facts, analysis and reasoning set out in the Report, combined with its extensive experience of operating cinemas in these areas, Odeon considers that the CC's decision making in each of these localities is deficient and inconsistent with its analysis of those areas where an SLC has been identified. Odeon considers that the evidence gathered in the inquiry to date points to an SLC in each of these areas.
- 1.4 Odeon is particularly concerned that the Report does not convey the CC's grounds for provisionally concluding that the Transaction will not lead to an SLC in Brighton, Greenwich and Southampton. Rather, it sets out a body of evidence which points towards an SLC finding, before proceeding to state that there is no SLC. As a result, the Report does not provide cinema operators (or indeed the OFT) with any guidance as to what parameters are relevant to concluding that an SLC arises in local cinema markets. Indeed, the seemingly inconsistent treatment of competition between localities in the Report (highlighted in Annex 1 to this response) introduces uncertainty into the methodology that competition authorities will use to assess the competitive effects of future transactions in the cinema industry.
- 1.5 Odeon has no agenda in relation to these areas (since it is already present in each area and thus does not believe it could acquire any disposals that would be recommended). However, in order to assist the CC to reach robust conclusions, Odeon sets out its views in relation to the competitive effects of the Transaction based on its knowledge of the three markets in section 2 below and contrasts the evidence with the CC's SLC findings in Aberdeen, Bury St Edmunds and Cambridge.
- 1.6 Finally, Odeon considers that the Report fails adequately to address the issue of access to the alternative content distributed by Picturehouse. Odeon's concerns in this area are set out in section 3 below.

2. THE CC'S ANALYSIS OF BRIGHTON, GREENWICH AND SOUTHAMPTON

Brighton

The CC's provisional findings are inconsistent with its analysis of other areas

- 2.1 The CC's provisional conclusion that no SLC will arise in Brighton are inconsistent with its analysis of those areas in which the CC has found an SLC. The evidence gathered by the CC appears sufficiently strong to reach an SLC finding in Brighton, particularly when compared to the evidence in relation to Cambridge. However, the CC concludes that no SLC is likely in Brighton, whereas an SLC may be expected in Cambridge. In particular, Odeon notes that:

- (a) the parties operate only two cinemas in Cambridge, but three in Brighton;
- (b) Odeon's 8 screen cinema is the only operator that constrains the parties in Brighton and Vue's 8 screen cinema the only operator that constrains the parties in Cambridge;
- (c) the proportion of revenue overlap of Picturehouse with Cineworld is of a similar or greater magnitude in Brighton than in Cambridge, standing at 50-60 per cent in Cambridge and as compared to 40-50 per cent in Brighton (Duke of York) and 60-70 per cent (Dukes @ Komedia). Moreover, the Brighton revenue overlap between the parties is of a similar magnitude to the overlap in Bury St Edmunds (50-60 per cent) and Aberdeen (62 per cent and 42 per cent);
- (d) the diversion ratio from Picturehouse to Cineworld is 30 per cent in both Cambridge and Brighton. Moreover, the diversion from Picturehouse to both Odeon Brighton and Cambridge Vue is 50-60 per cent. In relation to Cineworld, the diversion ratios to Picturehouse are also of similar magnitudes in both Cambridge and Brighton and identical (at 60-70 per cent) for diversion to Odeon Brighton and Cambridge Vue, the only remaining competitors in each locality; and
- (e) the GUPPI estimates in Brighton are of a similar magnitude to those in Cambridge. In particular, the GUPPI is 11 at Picturehouse Duke of York and 13-15 at Cambridge Picturehouse. Indeed, the CC states at paragraph 6.66 of the Report that the GUPPI calculations are of an order of magnitude which would suggest that the parties would have an incentive to increase prices at Picturehouse Duke of York.

2.2 It appears to Odeon inconsistent that the CC has provisionally concluded that no SLC may be expected in Brighton when the majority of the evidence is so similar to Cambridge, where it has reached a provisional SLC finding.

Cineworld and Picturehouse were close competitors in Brighton

- 2.3 Picturehouse and Cineworld were close competitors in Brighton prior to the Transaction. Odeon notes that Cineworld monitors Picturehouse Duke of York and that the opening of Duke's @ Komedia led to Picturehouse screening more films in Brighton in competition with Cineworld.
- 2.4 This is confirmed by the revenue overlap of 40-50 per cent between Picturehouse Duke of York and Cineworld and 60-70 per cent between Picturehouse Duke's @ Komedia and Cineworld. Moreover, Curzon's analysis showed that 65 per cent of the Duke of York's revenues came from films shown by Cineworld, whilst for Duke's @ Komedia the figure was 66 per cent.¹ As the CC also notes, Odeon monitors both Picturehouses in Brighton, indicating that they were a constraint on Odeon, and therefore Cineworld, pre-merger.² The Transaction will remove the strong competitive constraint that the parties exerted on each other, reducing choice for customers and allowing the parties to increase prices, and worsen their quality and range offering.
- 2.5 The CC's Report suggests that Odeon might be a closer competitor to Picturehouse than Cineworld. Based on its experience of operating in Brighton, Odeon does not consider this to be an accurate representation of the market in Brighton. In particular, Odeon considers that Cineworld is a closer competitor to Picturehouse than the diversion ratios based on the CC's survey suggest.

¹ Paragraph 73, Appendix G.

² Paragraph 75, Appendix G.

- 2.6 In relation to the online survey, Odeon notes that the response rate was only six per cent.³ Moreover, the telephone survey carried out in Bury St Edmunds and Brighton also had a response rate of just 6 per cent, varying by individual cinema between 4 and 11 per cent. The CC itself notes that this is low relative to most surveys it commissions and gives rise to potential non-response bias.⁴ The CC therefore cannot know whether the diversion to Odeon in Brighton is overstated and the diversion between the merging parties understated.
- 2.7 Odeon notes that both the online survey and the telephone survey offered a prompted list of the 12 nearest cinemas by drivetime to those stating that they would divert to another cinema. The joint OFT and CC guidance on good practice in the design and presentation of consumer survey evidence in merger inquiries states that good consumer survey design *"should not influence consumers to give particular answers"*.⁵ However, as the CC notes in its consideration of the customer survey at Appendix E to the Report, the list may have influenced the way people responded.⁶ Odeon does not agree that this effect is "almost certainly negligible outside London" – providing a prompted list of 12 alternative cinemas to respondents may make respondents feel obliged to pick an alternative that they would not consider in practice.
- 2.8 In any event, regardless of the precise magnitude of the diversion between the merging parties as compared to the diversion to Odeon, it is evident that Cineworld and Picturehouse were close competitors and that the Transaction will remove this competition, leaving just one effective competitor. Moreover, at the time of the CC's analysis, the Duke's @ Komedia had only been open for six months. As such, the cinema will not have reached its full potential and the diversion ratio analysis will have understated the cinema's competitive strength going forward relative to its current position.⁷

The Transaction creates a 3-2 in Brighton

- 2.9 The Transaction will result in a "three to two" within a 20 minute isochrone, removing the competitive constraint exerted by two Picturehouse cinemas.
- 2.10 Competition in Brighton is focused on the City Centre due to strong student demand and a significant proportion of customers coupling their visits to the cinema with other leisure options such as City Centre restaurants and bars. Odeon notes that the merging parties' own survey showed that 50-60 per cent of the audience at Duke of York's had travelled on foot.⁸ However, even within a 30 minute isochrone, there are no additional competitors capable of constraining the merged entity:
- (a) The Orion cinema is located in Burgess Hill rather than Brighton and will therefore not be an alternative option for the majority of customers which either want easy access from Central Brighton (e.g. students and those visiting the cinema after work) or wish to combine their cinema visit with other leisure options. In any event, the Orion is not capable of acting as an effective competitor to the parties. The cinema has only two screens with a total of 271 seats and is not monitored by Odeon; and

³ Paragraph 3, Appendix D.

⁴ Paragraph 6(d), Appendix D.

⁵ Paragraph 2.10, Good practice in the design and presentation of consumer survey evidence in merger inquiries, OFT and CC, March 2011.

⁶ Paragraph 6(d), Appendix D.

⁷ Odeon notes, for example, that Hackney Picturehouse's share of UK gross box office revenue grew by 15 per cent between 2012 and 2013. The Hackney Picturehouse opened in 2011 and Odeon would expect a similar year two increase in box office revenue at Duke's @ Komedia.

⁸ Paragraph 59, Appendix G.

- (b) The Curzon cinema is located in Crawley and has just one screen and 146 seats. The cinema is at the very edge of the 30 minute isochrone in Crawley and is not monitored by Odeon.

2.11 Excluding Orion and Curzon (in relation to which the CC presents no evidence of competitive strength), the parties' combined share of supply would be 58 per cent by screens and 55 per cent by seats and, together with Odeon, the parties would hold a share of 100 per cent.⁹ Even if The Orion and Curzon were considered competitors for the purpose of calculating market shares, the parties' combined share would be 50 per cent by screens and 44 per cent by seats, with the parties holding an 86 per cent and 87 per cent share with Odeon, respectively.

2.12 Whilst it appears to Odeon to be highly unusual to consider that a single competitor is sufficient to constrain three cinemas under the control of a merged entity in the same locality, the CC's conclusion in relation to Brighton is even more surprising given the position of Odeon's cinema, [3<]. Going forward, Odeon expects the [3<] facilities operated by Cineworld and Picturehouse to grow [3<].

Entry will not be timely or likely

2.13 The OFT and CC merger assessment guidelines state that in assessing whether entry or expansion might prevent an SLC, the authorities will consider whether such entry or expansion would be timely, likely and sufficient.¹⁰ Odeon does not consider that entry in Brighton on a scale sufficient to constrain the merged entity will be either timely or likely. In particular, Odeon notes that:

- (a) not only has the proposed new cinema not yet received planning permission, but the developer has not even applied for planning permission. Even if any such application were to be made, there is a strong possibility that the application may be refused given objections from the Theatre's Trust and the Regency Society. Odeon also notes that the site is a listed building, suggesting that planning permission is unlikely to be granted;
- (b) planning applications for cinemas are regularly rejected for a variety of reasons. For example, Odeon's plans for a new cinema at Pavilion Gardens in Bournemouth were forced to undergo substantial revisions in order to achieve planning consent, leading to significant further delay to the project. As the CC is aware, Odeon's plans for a cinema in Newmarket were also recently rejected;
- (c) even if permission were to be obtained, the process of obtaining permission and construction would take several years. For entry to be timely, the OFT and CC merger guidelines note that "*[t]he Authorities may consider entry or expansion within less than two years as timely, but this is assessed on a case-by-case basis, depending on the characteristics and dynamics of the market, as well as on the specific capabilities of potential entrants*".¹¹ In relation to Brighton, the timescale for any entry is clearly speculative, but could easily be six or seven years. Odeon's plans for a new cinema in Bournemouth have to date taken seven years;
- (d) Odeon has viewed the plans for the Hippodrome and found a number of concerns about the viability of a cinema on the site. In particular, Odeon's commercial property consultants had concerns about the listed building status, the difficulty in providing sufficient restaurant space and objections from local residents. They studied the site and found it to be derelict inside and to have listed status in many

⁹ Table 8, Appendix G.

¹⁰ Paragraph 5.83, Merger Assessment Guidelines, September 2010.

¹¹ Paragraph 5.8.11.

areas, concluding that it would be "ruinously expensive" to convert the site into a cinema;

- (e) the CC itself notes in the Report that "*we could not reach an expectation that the specific scheme being pursued would go ahead*".¹² Given that the Assistant Chief Executive of Brighton and Hove City Council stated that the proposals were "*the most viable*" option, it therefore follows that the CC cannot reach an expectation that a new entrant will open in Brighton. As a result, the merged entity which, as the CC notes, would have an incentive to increase prices in Brighton, will not be constrained by new entry and consumers will suffer several years of detriment in Brighton with only a vague possibility of a resolution by way of entry at a future date;
- (f) if the scheme ever were to go ahead, it is also possible that the eventual cinema operator might be an existing operator in Brighton, including either Odeon [Σ<] or Cineworld, thus generating no new competition;
- (g) moreover, if the scheme is not pursued, the CC notes that Brighton and Hove City Council's Assistant Chief Executive states that a possible alternative fate of the Hippodrome could be demolition. Odeon is not aware of any alternative sites that would be suitable for a new entrant to convert into a cinema in Brighton;

Conclusion

2.14 The evidence gathered during the CC's investigation to date demonstrates that:

- (a) Picturehouse and Cineworld were close competitors prior to the Transaction, as evidenced by high revenue overlap;
- (b) the Transaction will effectively result in a "three to two" in within a 20 or 30 minute isochrone;
- (c) the GUPPI results indicate that the parties will have an incentive to raise prices; and
- (d) the CC could not reach an expectation that the proposed scheme for new entry would go ahead, even though this was considered the most viable option.

2.15 Consistent with its assessment in other areas, the CC must therefore find an SLC in Brighton in its final report.

Southampton

The CC's provisional findings are inconsistent with its analysis of other areas

2.16 A number of the CC's provisional findings point towards an SLC in Southampton. In particular, Odeon notes that:

- (a) in Southampton, as in Aberdeen and Cambridge, there will be only one competitor within 20 minutes of the parties' cinemas, namely the Odeon Southampton;
- (b) the proportion of revenue overlap of Picturehouse with Cineworld is of a similar magnitude in Southampton to Bury St Edmunds and Cambridge. More specifically, in Southampton, the proportion of revenue overlap is 40-50 per cent, whereas in Bury St Edmunds and Cambridge it is 50-60 per cent;

¹² Paragraph 6.68.

- (c) the diversion ratio from Picturehouse to Cineworld is 20-30 per cent in Southampton, which is the same range as that in Cambridge; and
- (d) the Picturehouse in Southampton has a GUPPI measure of 11 (indicating an incentive to raise prices post-merger) whilst the Cambridge Picturehouse has a similar GUPPI measure of 13-15;

The Transaction will result in an SLC

- 2.17 Cineworld and Picturehouse are close competitors in Southampton, located just 0.1 miles apart at Ocean Village. Odeon is the only competing fascia remaining within a 20 minute drivetime isochrone. The Transaction therefore represents a "four to three".
- 2.18 Moreover, the GUPPI calculations suggest that Picturehouse Southampton would have an incentive to increase prices following the merger. Odeon therefore urges the CC to carefully consider the robustness and consistency of its provisional conclusions in relation to Southampton.
- 2.19 The CC appears to have placed significant weight on the presence of Vue Eastleigh in its assessment. Odeon considers the Vue Eastleigh to operate in a different catchment area to the cinemas in Southampton. The structure of local transport links leads to the Southampton cinemas drawing customers from Southampton City Centre and from the West of the City and Vue Eastleigh drawing customers from the East and North (largely due to its location close to the M3). Odeon therefore considers that Vue Eastleigh has a different target market to Southampton and has seen no evidence of the Vue cinema winning market share from cinemas in Southampton. Moreover, Odeon does not believe that Vue would seek to target City Centre customers in the event that the merged entity worsened its competitive offering in Southampton.
- 2.20 As set out in further detail at paragraph 2.7 above, Odeon also considers that the CC's survey may have overstated the diversion to Vue Eastleigh given the use of a prompted list that may encourage respondents to select a cinema outside the area that the respondent would be prepared to travel.

Entry will not be timely or likely

- 2.21 As in Brighton, Odeon does not consider that entry in Southampton on a scale sufficient to constrain the merged entity will be either timely or likely. In particular:
 - (a) the CC refers to the probability of entry in Southampton through the Hammerson development of a brown-field site adjacent to the West Quay Shopping Centre. The Report states that Hammerson told the CC the development would open by mid-2016 on the assumption that detailed planning permission was obtained within 12 months. Odeon believes that this opening date is unrealistic. The project has already suffered lengthy delays and is likely to suffer further delay. Moreover, in Odeon's experience, it would be unrealistic to obtain detailed planning permission within 12 months. Odeon would not be surprised if it took at least another four years for a new cinema to become operational. The development is therefore not timely for the purpose of entry assessment;
 - (b) the lease has not been signed and the identity of the eventual operator has not been determined. [§<];
 - (c) the CC should also be alert to the possibility that Cineworld may be selected as the operator of any cinema at the Hammerson site. Odeon understands that Cineworld has historically expressed an interest to Hammerson in operating the site. If Cineworld were to operate the site, Odeon could decide to close its existing cinema, thus reducing the number of fascia within 20 minutes from three to two. To prevent this occurring, Odeon would encourage the CC to seek a commitment from

Cineworld not to bid to operate the Hammerson development, or indeed any other new developments in the Southampton area.

Greenwich

- 2.22 As is the case for Brighton and Southampton, Odeon considers that much of the CC's evidence points towards an SLC in Greenwich, particularly when compared to the evidence in relation to the SLC areas. In particular:
- (a) the parties operate four cinemas in Greenwich, but only two in Bury St Edmunds and Cambridge;
 - (b) 50-60 per cent of Picturehouse Greenwich's revenues overlap with the Cineworld Greenwich-The O2 (the figure is also 50-60 per cent the other way around);
 - (c) The GUPPI at the Picturehouse Greenwich is 7-10 per cent, suggesting that the Picturehouse Greenwich would have an incentive to raise prices post-merger;
 - (d) for Picturehouse Greenwich, the merger would result in a four to three reduction in fascia based on a 20 minute isochrone by car. The Peckhamplex is not a close competitor to the parties due both to its location and more limited selection of mainstream blockbusters screened. Odeon does not monitor the Peckhamplex. In Greenwich, the merged entity's combined share on a 20 minute isochrone by car would be 55 per cent by screens (compared to 60 per cent in Cambridge) and 52 per cent by seats (compared to 55 per cent in Cambridge);
 - (e) Odeon considers that the distances covered by the drivetimes employed by the CC are very generous given the traffic congestion in the London area, particularly at peak times. Using journey times based on public transport options (the more realistic mode of transport for the majority of customers), Odeon Greenwich will be the only remaining competitor to Picturehouse Greenwich. The transaction therefore represents a "three to two", as in Cambridge and Aberdeen. Given the size of the parties' presence, their share would stand at 71 per cent by screens and 72 per cent by seats.
- 2.23 Odeon observes that in relation to the Cineworld/O2 transaction, Cineworld submitted to the OFT that the Picturehouse Greenwich was a main competitor to the O2 cinema.¹³ In addition, Picturehouse submitted that they competed with both the Cineworld O2 and Cineworld West India Quay cinemas.¹⁴
- 2.24 Moreover, despite the credible evidence that the Transaction will result in an SLC in Greenwich, it is unclear from the Report precisely what the reasons for finding that no SLC may be expected in this area. Given that the calculation of the GUPPI, which shows that Picturehouse would have the incentive to raise prices, already accommodates actual stated diversion to other competing cinemas in the area, it is not obvious what constraint will prevent this from arising in practice.
3. **THE TRANSACTION MAY RESTRICT FUTURE ACCESS TO ALTERNATIVE CONTENT**
- 3.1 Picturehouse has exclusive distribution rights in relation to a range of alternative content including the Bolshoi Ballet, David Bowie screenings and the next Royal Shakespeare Company season of shows. The Transaction grants Picturehouse the ability to guarantee sales of its alternative content to Cineworld on favourable terms and the ability and incentive to increase the price that it charges other operators in order to raise rivals'

¹³ Paragraph 53, Completed acquisition by Cineworld Group plc of the cinema business operating at the O2, London, OFT, 9 November 2010.

¹⁴ Paragraph 57.

costs. Any such action by Picturehouse would lead to rival operators being forced to charge customers higher prices. Odeon already has clear evidence of Picturehouse seeking to charge higher terms in the marketplace. Moreover, Picturehouse may refuse to supply rival operators altogether. For example, Odeon has recently been unable to gain access to either Bowie or King Richard II in Brighton.

- 3.2 Alternative content is a new aspect of cinema exhibition and is growing in importance. The CC should therefore carefully consider the impact of the Transaction on the supply of alternative content going forward, as access becomes critical for operators in order to compete and the market power of alternative distributors increases correspondingly.

ANNEX 1

COMPETITIVE CONDITIONS IN CAMBRIDGE COMPARED TO BRIGHTON, SOUTHAMPTON AND GREENWICH

	Cambridge	Brighton	Southampton	Greenwich
Number of Cineworlds	1	1	1	3
Number of Picturehouses	1	2	1	1
Number of competing fascia within 20 minutes	1 (Vue)	1 (Odeon)	1 (Odeon)	1 (Odeon) ¹
Market share (screens) of merged entity in 20 minutes	60%	58%	35%	71%
Market share (seats) of merged entity in 20 minutes	55%	55%	45%	72%
Revenue overlap of Picturehouse with Cineworld	50-60%	40-50% (DoY) 60-70% (Duke's @ Komedia)	40-50%	50-60% (Cineworld Greenwich)
GUPPI Picturehouse	13-15	11 (DoY) 5 (Duke's @ Komedia)	11	7-10 (Greenwich)
Diversion ratio from Picturehouse to Cineworld	20-30%	20-30%	20-30%	20-30%
Diversion ratio from Picturehouse to competitor	50-60% (Vue)	50-60% (Odeon)	40% (Odeon)	60-70% (Odeon)
Diversion ratio from Cineworld to Picturehouse	20-30%	10-20%	10-20%	
Diversion ratio from Cineworld to competitor	60-70% (Vue)	60-70% (Odeon)	60-70% (Odeon)	

Note 1: The Peckhamplex is outside the 20 minute isochrone by public transport, the most realistic mode of transport for the majority of customers in London. If the Peckhamplex were included, the parties' combined share would be 55 per cent by screens and 52 per cent by seats.