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Common sense or non-sense? The ‘migration vs. substitution’ paradigm in market definition

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It is almost impossible these days to attend a competition law conference without the topic of ‘Competition law in the digital era’ making up part of the agenda. In addition, enforcers are publishing policy documents on this topic at a rate that makes it a challenge to keep up for even the most diligent competition law professional – notable examples of interesting reads include the report on Competition Policy for the Digital Era published by the European Commission, the CMA’s report on Unlocking Digital Competition, and the ACCC’s Digital Platforms Inquiry.

For good reason, enforcers are keen on exploring how best to apply – and if necessary adapt – antitrust tools and methodologies to cope with the digital disruptors now turned incumbents. How do we measure market power and competitive constraint in the digital world so as to avoid over- as well as underenforcement? This is an important question worthy of attention and debate.

There is one tremendously important aspect to this debate, however, that is not enjoying the level of attention that it perhaps should and which is especially relevant in merger control and abuse of market power cases: Are antitrust enforcers sufficiently recognizing that the market power now being enjoyed by operators in the digital world has not appeared out of a vacuum but rather at the expense of operators in the ‘brick & mortar’ world? And, accordingly, are they fully recognizing the competitive constraint that the digital disruptor is imposing on the traditional, legacy players?

Decisions subscribing to the ‘migration vs. substitution’ distinction in market definition may suggest that this is not the case. Indeed, more focus would be welcomed on how best to measure competitive pressure exerted by (digital) disruptors upon traditional or legacy products – in particular a debate on whether the traditional market definition exercise is a suitable tool. For example, what is the best approach for measuring competitive pressure exerted by Netflix upon traditional pay-TV providers or by Google & Facebook upon print newspapers?

What exactly is the ‘migration vs. substitution’ argument?

The principle is quite clearly explained in the CMA’s decision from 2016 in *Ladbrokes*

/ Coral concerning online vs. betting-shop gambling:

> *"Migration of customers to the online channel does not necessarily mean that customers […] who choose to gamble in [a Licensed Betting Office] would divert to the online channel to a sufficient degree to render a price increase or deterioration of quality in the retail channel unprofitable. Rather, it is entirely possible that general changes in customer preferences or behaviours over time result in a degree of migration which does not indicate a sufficient degree of substitutability between the retail and online channel and cannot be equated with diversion (which is relevant for market definition purposes)."*

In other words, if consumers are switching from betting-shop gambling to online gambling at a moderate but steady pace, this one-way substitution is a lesser or inferior competitive constraint than sudden switching triggered by a SSNIP. It is migration, not substitution.

Similar phrasing is used by the Danish Competition Council (the **"DCC"**) in its 2017 decision in *Imerco/Inspiration* concerning the sale of housing articles in online vs. in 'brick & mortar' shops:

> *"An increase in internet sales does not necessarily mean that there is high demand-side substitution between 'brick & mortar' shops and online shops. An increase in internet sales can also be reflective of "migration", meaning that consumers are seeking to switch to online shops even though there have been no changes in the 'brick and mortar' shops' prices or offerings." (translation from Danish)*

Adopting the CMA and DCC's reasoning from these cases it would seem obvious to apply the 'migration vs. substitution' principle to the TV market trend of 'cord cutting', i.e. the pattern of viewers cancelling their traditional pay-tv subscriptions and signing up to non-linear OTT/VOD services like Netflix, HBO GO, Amazon Prime etc. The European Commission did not advocate this principle, however, in its decision from 2018 in *Liberty Global/Ziggo* as it seems to equate – rather than distinguish between – migration and substitution:

> *"At the same time, non-linear is increasingly constraining linear broadcasting, with viewers replacing linear broadcasting with a selection of their preferred non-linear content ("cord cutting")."* (underlining added)

Importantly though, the European Commission qualifies this statement by saying that linear and non-linear broadcasting are still *"seen more as complements than as substitutes"* and that:

> *"Although the two distributions mode [sic] tend to converge and overlap, PPV/TVOD and OTT/SVOD do not yet seem as viable alternatives to Pay TV in case of switching."* (underlining added)

In another example from 2018, the Dutch Trade and Industry Appeals Tribunal (the **"TIAT"**) took issue with the Dutch Authority for Consumers & Markets' (the **"ACM"**) use of the 'migration vs. substitution' argument in a case concerning the market power of postal incumbent *PostNL*. In the contested decision, the ACM held that digital communication could not fall within the same relevant market as physical, 24-hour, business bulk-mail – relying heavily on the 'migration vs. substitution' paradigm:

> *"ACM considers it plausible that switching to digital involves organic migration as a result of the trend towards digitisation that is independent of price rises for 24-hour bulk mail. ACM considers that a 10-percent price rise is too small to have any major influence on the choice between mail and the more extensive range of digital transmission options. […] It follows from the above that digital transmission is not a demand substitute for 24-hour bulk mail. This could be demonstrated additionally by a critical loss analysis. In view of the real risk of the cellophane fallacy, however, the critical loss analysis is not sufficiently robust to draw a reliable conclusion."* (underlining added)

The TIAT annulled the ACM's decision saying that without carrying out a critical loss analysis (SSNIP), the ACM was wrong to exclude digital communication from the relevant market based on product characteristics and the 'migration vs. substitution' assumption.

Inherent challenges with the 'migration vs. substitution' reasoning

There is something counter-intuitive in the 'migration vs. substitution' reasoning if it leads to the conclusion that the disruptor product falling outside the relevant market is less of a competitive constraint than the products falling within. When consumers 'migrate' to a disruptor product – for example from a physical newspaper to online news consumption – they are doing so because the disruptor product offers more value to them than the traditional product (whether it be because of price, quality, convenience or any other competitive parameter). Surely this is fierce competition at work (?).

The 'migration vs. substitution' argument seems therefore to wrongly detach changes in consumer preferences and behavior over time from the market entry & disruption that drives these changes. It is competition that has driven the consumers to change their behavior. If the market definition exercise does not capture this dynamic, perhaps it is not a suitable tool to measure the competitive pressure exerted by a disruptor product upon a traditional product.

Moreover, in merger control enforcement policy there is consensus among enforcers to increase focus on innovation-competition and disruption as an important source of

competitive constraint. This is reflected, for example, in the *Dow/DuPont* theory of harm and also significantly in this year's report on Competition Policy for the Digital Era saying that *"competitive threats will typically come from the fringe"*. In a speech from 2017, Directorate General Laitenberger also emphasized the need to focus more on the competitive parameters of quality, choice and innovation as opposed to (just) price and quantity.

With this in mind, there is arguably a disconnect between saying – on one hand – that we must recognize innovation-competition and disruption as a strong competitive constraint to serve as a basis for theories of harm; while saying – on the other hand – that legacy players losing customers to disruptors through 'migration' is not a result of fierce competition. Either innovation-competition & disruption is a recognised source of fierce competition or it isn't.

No, market definition is not everything, but…

Defenders of the 'migration vs. substitution' argument will correctly point out that market definition is not the be-all & end-all in terms of analyzing effects and that the enforcer will still analyse competitive pressure from outside the relevant market. In theory at least, market definition in merger control is simply a filter for determining whether a more detailed assessment of the merger is required.

However, in practice there may be a sense that once the conclusion is reached that a disruptor product falls outside the relevant market from the perspective of the traditional product, this tends to frame the rest of the competitive assessment. Excluding the disruptor product from the relevant market means that the legacy player seeking to demonstrate substantial constraint is significantly behind on points and faces an uphill battle to show sufficient competitive pressure from outside the market.

Recognizing competition whatever the label

When it comes to market definition as a suitable tool for measuring competitive constraint, the report on Competition Policy for the Digital Era emphasizes the following:

> *"Even more crucially, it should be remembered that the importance of market definition, and the methodologies developed for identifying it, were built for standard goods and services. In the digital world, it is less clear that we can identify well-defined markets."*

This statement should stand to reason not just for measuring competitive constraint *upon* the digital disruptors turned incumbents but also measuring it *from* the digital disruptors upon the traditional products.

Ideally, if there is a strong, observable decline in the demand for the traditional/legacy product at the same time as an observed increase in demand for the disruptor product, the enforcer ought to adopt a presumption that they belong to the same

market when analyzing the constraint upon the traditional product. Or at least that the disruptor product exerts a level of competitive pressure equivalent to the products falling within the legacy player's relevant market.

At the end of the day, if a business loses customers to an innovative disruptor, enforcers should recognise this as a result of fierce competition – irrespective of whether you choose to label it as substitution or migration.

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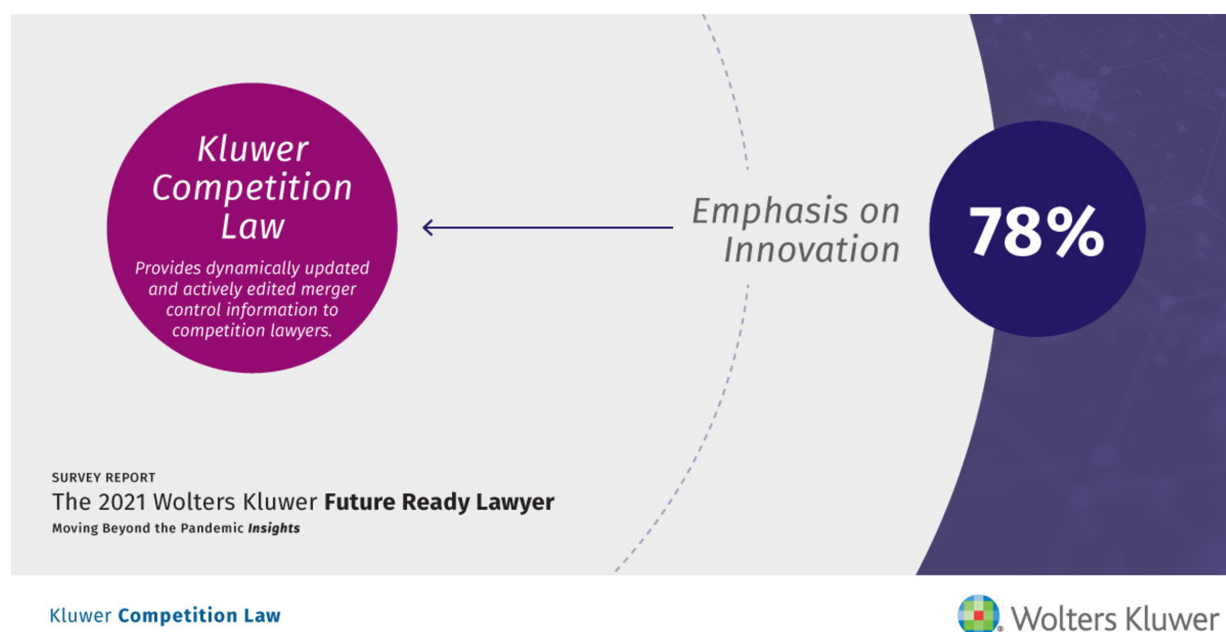

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