

10 November 2017

Russell McVeagh
PO Box 8
Auckland 1140

Attention: Troy Pilkington/Hannah Loke

Dear Troy and Hannah

Supplementary Letter of Issues - Trade Me Limited / Limelight Software Limited

1. We refer to the application (the Application) dated 11 July 2017 from Trade Me Limited (Trade Me) to acquire up to 100% of the shares in Limelight Software Limited, trading as Motorcentral (Motorcentral) (the merger).
2. This Supplementary Letter of Issues follows the Commission's Letter of Issues (LOI) dated 29 August 2017. This letter raises further issues not addressed in the LOI and also details our current thinking on the counterfactual and the relevant markets.
3. At this stage, we are not satisfied that the merger would not give rise to competition issues as a result of horizontal effects in the provision of dealer management system (DMS) products to independent dealers. We are also testing whether the merger raises competition concerns in the provision of online motor vehicle classified advertising to dealers as a result of horizontal effects.
4. The Commission has not yet made any decisions on the issues outlined below, or any other issues, including those raised in the LOI. Accordingly, our views may change, and new competition issues may arise, as the investigation continues. We will advise you if we identify any further issues during our analysis of the proposed merger that are not discussed in this letter.
5. We are available to meet with Trade Me to discuss this letter.

Timeline

6. We would like to receive submissions from Trade Me on the issues raised below. Please indicate by close of business on Tuesday 14 November 2017 the date on which you intend to provide your submission. We do not intend to publish your submission. However, please provide a public version in the event that we receive an Official Information Act request for disclosure of your submission.

The counterfactual

7. Trade Me submitted that
[

].¹

8. However, based on internal documents provided by Trade Me, we are considering whether, absent the merger, Trade Me would be likely to
[].

9. In summary, our preliminary view is that those documents indicate:

9.1 It is a strategic priority for Trade Me to
[

];²

9.2 Trade Me had previously sought to
[];³

9.3 Planning for
[

].⁴

[];⁵

9.4 Around March 2017, Trade Me started to consider
[].⁶
[

];

¹ Application at [8.1]–[8.3].

² See, for example: []; []; [].

³ See, for example: []; [].

⁴ []; []; [].

⁵ [].

⁶ [].

9.5 Discussions between Trade Me and Motorcentral progressed, and
[
];⁷

9.6 An email between Trade Me executives (including the Head of Trade Me
Motors) in preparation for
[
].⁸

10. Trade Me submitted that by March 2017 it had, for a number of reasons,
[
]. It reiterated that
[
].⁹

11. However, the internal documents provided by Trade Me
[
].

12. Finally, we consider that, absent the merger, Motorcentral would be likely to
continue be active in the supply of online motor vehicle classified advertising to
dealers through its Need-a-Car (NAC) platform. On its launch in September 2017
Stuff.co.nz reported that:¹⁰

⁷ [].

⁸ [].

⁹ [].

¹⁰ "Needacar website launches listing 23,000 vehicles for sale" (5 October 2017) Stuff
www.stuff.co.nz/business/industries/97568189/needacar-website-launches-listing-23000-vehicles-for-sale

Limelight director Mena Eskander said Needacar would continue with or without the [merger] ... Eskander said Limelight would begin promoting Needacar through television and magazine advertising in a few weeks.

Market definition

13. Based on the information currently before the Commission, including Trade Me's submission on the LOI and other market feedback, our preliminary view is that the markets relevant to this application are likely to be:

13.1 the national market for the supply of online motor vehicle classified advertising to dealers; and

13.2 the national market for the supply of DMS products to independent dealers.

Advertising market

14. Evidence we have received since the LOI continues to indicate that other forms of advertising are not good substitutes for online classified advertising. We also note that we have recently found that print advertising is not in the same market as digital advertising in *NZME/Fairfax*.¹¹

DMS market

15. Based on industry feedback, we consider that there are two categories of dealers:

15.1 Franchise dealers, which operate under franchise arrangements and sell mainly new cars; and

15.2 Independent dealers, which are not in franchise arrangements and typically sell used cars. These dealers are often referred to as "used car dealers".

16. Trade Me's internal documents indicate that
[

].¹²

17. Motorcentral's internal documents indicate that
[

].¹³

¹¹ *NZME/Fairfax* [2017] NZCC 8 at [240].

¹² [].

¹³ [].

18. Feedback from other DMS providers also indicated that there is a distinction between DMSs that are suitable for franchise dealers and those that are suitable for independent dealers. This feedback also suggested that suppliers of DMS products targeting franchise dealers would be unlikely to make changes to their products to target independent dealers, as they did not consider the independent dealer market to be attractive (citing independent dealers' high price sensitivity and credit risk).
19. Based on the above, our preliminary view is that the supply of DMS products to independent dealers may form a separate market to the supply of DMS products to franchise dealers.

Horizontal effects: DMS products

20. At this time, we are not satisfied that the merger would not have the effect or likely effect of substantially lessening competition in the national market for the supply of DMS products to independent dealers through horizontal effects.
21. The main concern that we are testing is that, []. The loss of competition between Motorcentral and Dealerbase could result in independent dealers facing less attractive terms of service, including some combination of higher prices, lower quality, or less innovation.

Loss of competition between Trade Me and Motorcentral

22. Trade Me's internal documents indicate that []. For example, one document noted that []. The same document called Motorcentral [].¹⁴
23. These concerns are also reflected in a Trade Me Board paper discussing the merger, which refers to []. That document notes that [].¹⁵
24. Accordingly, it appears that []. Head-to-head competition between DealerBase and Motorcentral could benefit dealers by resulting in more attractive terms of service, including some combination of lower prices, higher quality or more innovation.
25. The evidence before us currently suggests that there is little other existing competition in the independent dealer DMS market. Based on Motorcentral internal documents, we estimate the size of the independent dealer DMS market to be

¹⁴ [].

¹⁵ [].

approximately []dealers.¹⁶ In terms of market share, Motorcentral has approximately [] while the next largest competitors are [].¹⁷

26. Motorcentral told the Commission that [].¹⁸ This was consistent with other evidence we found:

26.1 A Trade Me internal document described other competitors as [].¹⁹

26.2 [] told the Commission that Top Gear and Grant Day [],²⁰ and

26.3 Top Gear told the Commission that [].²¹ This suggests that Top Gear is [].

27. On the other hand, Motorcentral’s FY17 and FY18 strategy documents note that [].²² Motorcentral explained this to us as follows:
[].²³

28. As such, absent the merger, competition between DealerBase and Motorcentral may be the key field of rivalry in the DMS market, the loss of which could harm dealers.

Potential competition

29. We are considering whether entry or expansion in the DMS market in response to the exercise of market power might constrain the merged entity.

30. The evidence we have found so far indicates that there are barriers to entry and expansion in the DMS market.

31. Trade Me’s internal documents suggest that []

¹⁶ [].

¹⁷ [].

¹⁸ [].

¹⁹ [].

²⁰ Commerce Commission interview with [] (6 October 2017).

²¹ Commerce Commission interview with Top Gear (14 September 2017).

²² [].

²³ [].

].

32. Feedback we received from dealers indicates that dealers are “sticky”, in that they face significant switching costs, including re-training staff and transferring data to the new DMS (which some indicated had to be done manually).

33. These challenges may be acute for potential new entrants. The independent dealer DMS market is relatively small and the sunk costs of development and marketing may be large relative to the size of the market. Faced with these costs, the size of the addressable market, and the stickiness of Motorcentral’s dealers, new entry may be unattractive. On the other hand,

[].²⁴

34. Evidence we found also suggests that entry into the independent dealer DMS market may not be attractive to those with an existing DMS product targeting franchise dealers. Feedback from these businesses indicated disinterest in the independent dealer DMS market, given the perceived price sensitivity and credit risk of independent dealers. This is consistent with

[].²⁵

35. We also consider that the merger itself may be likely to raise barriers to entry and expansion, as potential entrants may perceive entry to be unattractive where Motorcentral is vertically integrated with Trade Me. The merged entity may have the resources to engage in strategic entry deterrence (for example, by credibly signalling that entry would provoke an aggressive response) that Motorcentral, on its own, would not have.

36. Trade Me submitted that Motorcentral’s entry and expansion since 2011 indicates that there are no barriers to entry and expansion in this market.²⁶ However, this may be a reflection of market conditions at the time of Motorcentral’s entry. In particular, the DMS market may have been fragmented at the time with existing competitors falling behind with development of their DMS products, which may have made entry and expansion easier.

²⁴ [].

²⁵ [].

²⁶ Application at [9.17(b)].

37. Accordingly, given the evidence before us on barriers to entry and expansion, our preliminary view is that new entry and expansion in response to the exercise of market power may not constrain the merged entity.

Horizontal effects: online classified motor vehicle advertising

38. We are also considering whether the merger would have the effect or likely effect of substantially lessening competition in the national market for the supply of online motor vehicle classified advertising to dealers due to horizontal effects.

39. The main issue we are testing is that, in the counterfactual, Motorcentral will continue to be active in the market for the supply of online motor vehicle classified advertising to dealers through its NAC platform. The loss of competition between NAC and Trade Me could raise competition concerns in the market for the supply of online motor vehicle classified advertising to dealers.

40. NAC, launched in September 2017, is an online classified advertising platform for used motor vehicles that is operated by Motorcentral. It holds over 22,000 vehicle listings²⁷ and these listings are drawn from Motorcentral's DMS [].²⁸ NAC only holds listings from dealers – that is, it does not hold listings from private individuals.

41. Motorcentral described NAC to us as follows:²⁹

[

]

42. A Motorcentral internal document prepared before the merger was considered indicates that Motorcentral intends NAC to be a platform

[
].³⁰ That document also states that NAC was
[]

43. Accordingly, we consider that, in the counterfactual, it is likely that Motorcentral will continue to be active in the market for the supply of online motor vehicle classified advertising to dealers as an independent competitor to Trade Me, through its NAC platform.

²⁷ As at 2 November 2017.

²⁸ []

²⁹ []

³⁰ []

44. We are therefore considering the extent to which NAC and Trade Me would compete in the counterfactual, and whether the loss of that competition may be material.

Yours sincerely

A handwritten signature in blue ink, appearing to read 'Richard Davidson', with a stylized flourish extending to the right.

Richard Davidson

Investigations Team Leader, Competition