

Statement of Preliminary Issues

Expedia / Wotif

8 August 2014

Introduction

1. On 21 July 2014, the Commerce Commission received an application from Expedia, Inc. (Expedia) seeking clearance to acquire up to 100% of the issued shares of Wotif.com Holdings Limited (Wotif).
2. The public version of the application is available on our website at: <http://www.comcom.govt.nz/business-competition/mergers-and-acquisitions/clearances/clearances-register/detail/829>.
3. This Statement of Preliminary Issues outlines the key competition issues we currently consider will be important in deciding whether or not to grant clearance. The issues highlighted in this statement are based on the information available at the time of publication, and may change as our assessment of the application for clearance progresses. Therefore, the issues highlighted in this statement are not binding on us.
4. We invite interested parties to make comment on the likely competitive effects of the proposed acquisition and request that parties who wish to make a submission do so by **Wednesday 20 August 2014**.

The transaction and the parties

5. Expedia is a global travel agency that provides online and telephone booking services for accommodation, flights, vacation packages, car hire and other retail travel products. Expedia's websites include Expedia.co.nz, Hotels.com and Trivago.co.nz.
6. Wotif is an Australian-based travel agency that provides online booking services for accommodation, flights, travel packages and other travel products. Wotif's websites include Wotif.com and Lastminute.com.au.
7. Expedia and Wotif overlap in the supply of online travel booking services. Expedia and Wotif act as intermediaries between consumers and the suppliers of travel products (eg, accommodation providers, airlines, rental car companies).
8. With the transaction Expedia would operate Wotif.com and Wotif's other websites in addition to its existing travel websites.

Our framework

9. As required by the Commerce Act 1986, we assess whether an acquisition is likely to result in a substantial lessening of competition. How we assess this is set out in our Mergers and Acquisitions Guidelines.¹

¹ Commerce Commission, *Mergers and Acquisitions Guidelines*, July 2013.

10. We ask whether an acquisition is likely to substantially lessen competition in a market by comparing the likely state of competition if the acquisition proceeds (the scenario with the acquisition, often referred to as the factual), with the likely state of competition if the acquisition does not proceed (the scenario without the acquisition, often referred to as the counterfactual).²
11. A tool used to assess competitive effects is market definition. Market definition provides a framework to help identify and assess the close competitive constraints a merged firm would likely face.³ A market is defined in the Commerce Act as a market in New Zealand for goods or services as well as other goods or services that are substitutable for them as a matter of “fact and commercial common sense”.⁴
12. We define markets in the way that we consider best isolates the key competitive constraints on the parties to an acquisition. In many cases this may not require us to precisely define the boundaries of a market.
13. We analyse the extent of competition in each relevant market both with and without the acquisition to determine whether the acquisition would be likely to substantially lessen competition.
14. We assess the following three factors when considering whether this is likely to be the case.
 - 14.1 Existing competition – the degree to which existing competitors compete.
 - 14.2 Potential competition – the extent to which existing competitors would expand their sales or new competitors would enter and compete effectively if prices were increased.
 - 14.3 The countervailing market power of buyers – the potential for a business to be sufficiently constrained by a purchaser’s ability to exert substantial influence on negotiations.
15. A comparison of the extent of competition both with and without the acquisition enables us to assess the degree by which the proposed acquisition might lessen competition. If the lessening is likely to be substantial, we may not give clearance to the proposed acquisition.

Preliminary issues

16. The Commission will assess the horizontal effects that might arise as a result of this acquisition. In particular, we will consider:

² *Commerce Commission v Woolworths Limited* (2008) 12 TCLR 194 (CA) at [63].

³ *Commerce Commission v New Zealand Bus Limited* (2006) 11 TCLR 679 (HC), at [123]. *Brambles New Zealand Ltd v Commerce Commission* (2003) TCLR 868 (HC) at [137].

⁴ Similarly, the courts have said that “[t]he boundaries of the market are defined by substitution between one product and another and between one source of supply and another, in response to changing prices”. See *Commerce Commission v New Zealand Bus Limited* (HC), above n 3 at [123] citing *Re Queensland Co-operative Milling Association Ltd* (1976) ATPR 40-012 at 17,247.

- 16.1 the two-sided nature of the market: that is, that travel intermediaries like Expedia and Wotif provide services to both suppliers of travel products as well as consumers, and how the prices set for these respective sides of the market interact;
- 16.2 in regard to services to suppliers of travel products, we will consider:
 - 16.2.1 whether there is a broad travel booking market or narrower markets for the supply of booking services for each of accommodation, flights, etc.;
 - 16.2.2 the extent to which the merged entity would be constrained by other travel intermediaries, both online travel agents such as Booking.com and 'bricks and mortar' travel agents;
 - 16.2.3 how closely online travel intermediaries like Expedia and Wotif compete with end service providers such as hotels; and
 - 16.2.4 the role of other search channels (eg, metasearch sites) in facilitating direct bookings and constraining the prices charged by online travel intermediaries; and
- 16.3 in regard to services to consumers, we will separately consider the above issues from the perspective of competitive options available to consumers.
- 17. We discuss these issues further below, considering both sides of the market together.

The two-sided nature of the market

- 18. Expedia and Wotif overlap in the supply of online travel booking services. Expedia and Wotif act as intermediaries, facilitating interactions between consumers and the suppliers of travel products. Expedia and Wotif supply services to both consumers and the suppliers of travel products, providing:
 - 18.1 New Zealand consumers with the ability to search, compare and book travel products globally; and
 - 18.2 suppliers of travel products (eg, New Zealand accommodation providers) with global advertising, listing and travel booking services.
- 19. In this market, there may be network effects because consumers value having access to a range of travel product suppliers through one website and, similarly, suppliers of travel products value having access to a broad range of consumers.
- 20. In assessing the competitive effects of the proposed acquisition (and defining the relevant markets within which to conduct that assessment), we will consider the two-sided (or multi-platform) nature of the market. A particular consideration is whether the need to attract either consumers or travel suppliers to a website will have a limiting effect on a potential exercise of market power. We will also consider whether there are network effects that make entry and expansion more difficult

(because it may be difficult to attract suppliers of travel products to a new website that has no existing consumer traffic and vice versa).

Is there a broad travel booking market or narrower markets for each travel product?

21. While Wotif supplies online travel booking services for a range of travel products, it is predominantly active in the supply of online accommodation booking services (which represents approximately 87% of its revenue). Expedia submits that accommodation is the individual travel product for which there is the greatest overlap between the parties' activities.
22. However, Expedia further submits that although individual travel products are not substitutable from a demand perspective (eg, flights are not substitutable for accommodation), there is a very high degree of supply-side substitutability and most travel agents and intermediaries offer booking services for a range of travel products.
23. We will consider whether there are separate markets for the supply of booking services for individual travel products (particularly, accommodation), or alternatively, a broad market for the supply of booking services for all travel products.

Constraint from other travel intermediaries

24. Expedia submits that, post-acquisition, it will continue to be constrained by a number of existing international and domestic online travel agents, along with low barriers to entry and expansion. It submits that existing competitors include the Priceline Group (which owns Booking.com and Agoda), Webjet and Orbitz Worldwide (which owns Hotel.com), who have all significantly expanded their activities in New Zealand over the past few years.
25. Expedia and Wotif are both focussed on the supply of online travel booking services. However, Expedia submits that post-acquisition, it will continue to be constrained by a wide range of 'bricks and mortar' travel agents (eg, Flight Centre, House of Travel) which continue to account for a large share of travel bookings in New Zealand. Expedia submits that many of these 'bricks and mortar' travel agents operate a mixed model and are expanding their online presence which increasingly blurs the line between online and 'bricks and mortar' distribution channels.
26. We will consider the extent to which the merged entity would be constrained by other travel intermediaries. As part of this we will consider how competition occurs between Expedia, Wotif and other intermediaries supplying online travel booking services (both for the business of the suppliers of travel products and for consumers' travel bookings). We will also consider how closely online travel intermediaries compete with 'bricks and mortar' travel agents. We will consider the constraint from potential (as well as existing) travel intermediaries by examining entry and expansion conditions. In each case, we will consider whether the level of competition, constraint or entry conditions varies for individual travel products or based on the size and scale of suppliers of travel products.

Closeness of competition with end service providers

27. Expedia submits that, post-acquisition, it will continue to be constrained by direct booking channels (where consumers book directly with accommodation providers, airlines and other suppliers of travel products). It submits that virtually all domestic and international airlines, and a large number of accommodation providers, have strong and effective direct online sales offerings. Expedia further submits that large-scale investment is not required for accommodation owners to have effective direct online booking capability, due to the presence of travel software solutions providers, channel managers, meta-search sites and other online platforms.
28. We will also consider how closely online travel intermediaries like Expedia and Wotif compete with end service providers (eg, accommodation providers, airlines, rental car companies). In terms of services to suppliers of travel products, we will specifically consider whether suppliers of travel products could, in response to an increase in prices post-acquisition, choose to rely simply on their own direct booking channels. In terms of services to consumers, we will specifically consider whether, in face of the introduction or increase in booking fees, or decrease in service quality, consumers would switch to booking directly with suppliers of travel products. In each case, we will consider whether the closeness of competition varies for individual travel products or based on the size and scale of suppliers of travel products.

The role of other search channels

29. Expedia submits that meta-search sites (eg, TripAdvisor, HotelsCombined, Kayak and trivago) are similar to online travel agents like Expedia and Wotif. It further submits that, by offering side-by-side price comparisons from online travel agents and direct booking channels, meta-search sites increase price transparency and lower searching costs for consumers by giving them the ability to browse many providers at once. Expedia also submits that meta-search sites give suppliers of travel products an additional avenue by which to directly target consumers and bring them to their own websites, by-passing online and 'bricks and mortar' travel agents.
30. In assessing the competitive effects of the proposed acquisition, we will consider the role of these other search channels. We will consider whether the role of such search channels varies for individual travel products or based on the size and scale of suppliers of travel products.

Next steps

31. We are currently aiming to make our decision by **Friday 10 October 2014**. However, this date may change as the investigation progresses.
32. To keep up to date with any changes to our deadline and to find relevant documents, visit our clearance register on our website at <http://www.comcom.govt.nz/clearances-register/>
33. As part of our investigation, we will identify the parties we believe will provide the best information to help us assess the preliminary issues identified above.

34. We also invite submissions from any other parties who consider they have information relevant to our consideration of this matter. If you wish to make a submission, please send it to us at registrar@comcom.govt.nz with the reference Expedia / Wotif in the subject line of your email, or The Registrar, PO Box 2351, Wellington 6140 by close of business **Wednesday 20 August 2014**. Please clearly identify any confidential information contained in the submission and provide contact details.