

21 July 2010

# Statement of Issues — Jetset Travelworld's proposed acquisition of Stella Travel Services Holdings

- 1. Outlined below is the Statement of Issues released by the Australian Competition and Consumer Commission (ACCC) in relation to the proposed acquisition of Stella Travel Services Holdings Pty Ltd (Stella) by Jetset Travelworld Limited (Jetset) (proposed acquisition).
- 2. A Statement of Issues published by the ACCC is not a final decision about a proposed acquisition, but provides the ACCC's preliminary views, drawing attention to particular issues of varying degrees of competition concern, as well as identifying the lines of further inquiry that the ACCC wishes to undertake.
- 3. In line with the ACCC's *Merger Review Process Guidelines* (available on the ACCC's website at <a href="www.accc.gov.au">www.accc.gov.au</a>) the ACCC has established a secondary timeline for further consideration of the issues raised in this matter. The ACCC anticipates completing further market inquiries by 12 August 2010 and anticipates making a final decision on 2 September 2010. However, the anticipated timeline can change in line with the *Merger Review Process Guidelines*. To keep abreast of possible changes in relation to timing and to find relevant documents, market participants should visit the Mergers Register on the ACCC's website at <a href="www.accc.gov.au/mergersregister">www.accc.gov.au/mergersregister</a>.
- 4. A Statement of Issues provides an opportunity for all interested parties (including customers, competitors, shareholders and other stakeholders) to ascertain and consider the primary issues identified by the ACCC. It is also intended to provide the merger parties and other interested parties with the basis for making further submissions should they consider it necessary.

# **Background**

5. On 14 May 2010 the ACCC commenced a public review of the proposed acquisition after receiving a submission from Jetset and Stella seeking ACCC clearance.

# The parties

#### **Jetset Travelworld Limited**

- 6. Jetset is an ASX-listed company that operates one of Australia's largest integrated travel businesses. Its major shareholders include Qantas Airways Limited (**Qantas**) with 58% and Sintack Pty Ltd (**Sintack**) with 24.68%.
- 7. Jetset's extensive 'bricks and mortar' retail travel network consists of over 640 branded franchisee and non-branded affiliate member stores. As a franchisor, Jetset provides members with the permission to trade under its *Jetset* and *Travelworld* brands as well as access to preferred supplier relationships, network/advertising support and ticketing systems. In addition, Jetset provides access to its preferred supplier relationships to some buying groups, giving retail outlets who are members of these buying groups access to Jetset-negotiated buying terms for certain travel content.
- 8. In addition to its 'bricks and mortar' retail network, Jetset operates the <a href="www.jetset.com.au">www.jetset.com.au</a> and <a href="www.jetset.com.au">www.travelworld.com.au</a> websites and two separate retail websites, ReadyRooms.com and ReadyFlights.com, which allow customers to book and pay for a range of domestic and international accommodation and flights online.
- 9. At the wholesale level, Jetset compiles international and domestic travel packages and tours and distributes them to franchisees, non-branded affiliate stores and third party retailers under a number of brands including *Qantas Holidays* and *Viva! Holidays*. In addition, Jetset provides air ticket consolidation services to retailers through its wholly owned subsidiary, National Ticket Centre (NTC).
- 10. Jetset operates Qantas Business Travel, which provides corporate travel management services to large corporate and government clients. In addition, franchisees trading under Jetset's *Business Select* brand specialise in the provision of corporate travel services to small and medium sized businesses.

# Stella Travel Services Holdings Pty Ltd

- 11. Stella is a private integrated travel company predominantly operating in Australia and New Zealand. It is currently majority owned and controlled by funds advised by CVC Asia Pacific.
- 12. Stella operates an extensive 'bricks and mortar' retail network consisting of over 1,500 retail outlets in Australia, including approximately 700 franchisee stores operating under the *Harvey World Travel* and *Travelscene American Express* brands. In addition to its 'bricks and mortar' retail network, Stella operates websites for each of Harvey World Travel and Travelscene American Express, which allow direct online bookings for a limited range of products, and two separate retail websites Best Flights and Best Cruises. Stella also provides access to its preferred supplier relationships to some buying groups, giving retail outlets who are members of these buying groups access to Stella-negotiated buying terms for certain travel content.

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<sup>&</sup>lt;sup>1</sup> As at 13 August 2009, Jetset Travelworld *Annual Report* 2009, p. 93.

- 13. At the wholesale level, Stella compiles international travel packages and travel components and tours under a number of brands including *Travel2*, in-house wholesalers *Travescene Holidays* and *Harvey's Choice Holidays* (50% owned by Qantas), and other specialist brands such as *Travel Indochina*. Stella distributes these wholesale products to franchisees, non-branded affiliate stores and third party retailers.
- 14. Stella provides air ticket consolidation services through its wholly owned subsidiary, Air Tickets and corporate travel management services in Australia through Atlantic Pacific Travel and its *Travelscene Corporate* brand.

# Other industry participants

# **Flight Centre Limited**

- 15. Flight Centre Limited (**Flight Centre**) is one of Australia's largest integrated retail leisure and corporate travel businesses, with more than 2000 shops and businesses in 11 countries: Australia, New Zealand, the United States, Canada, the United Kingdom, South Africa, Hong Kong, India, China, Singapore and Dubai. Unlike Jetset and Stella, Flight Centre's 'bricks and mortar' retail network principally consists of stores that are owned by Flight Centre itself, rather than stores that are operated by franchisees and affiliates. As a consequence, Flight Centre typically only provides access to its preferred supplier relationships, wholesale travel packages and tours to its own retail outlets.
- 16. Flight Centre's corporate travel management operations consist of FCm Travel Solutions. The company's other leisure, corporate and wholesale brands include Escape Travel, Travel Associates, Student Flights, quickbeds.com, Stage & Screen Travel and Freight Services, Kistend and Campus Travel, CiEvents, Infinity Holidays and Overseas Working Holidays.

### **Consolidated Travel**

- 17. Consolidated Travel is the largest privately owned and operated ticket consolidator in Australia. It provides ticket and other travel-related services and facilities to over 4,000 retail travel agents.
- 18. The beneficial owner of Consolidated Travel, Mr Spiros Alysandratos, also currently holds the following interests:
  - a 24.68% shareholding in Jetset via Sintack; and
  - a 50% shareholding in the Orient Express Travel Group.

# **Orient Express Travel Group**

19. The Orient Express Travel Group is a vertically integrated travel company with operations in travel retail, wholesale and air ticket consolidation in Australia.

# **Industry background**

- 20. Travel products and services originate with content providers, such as airlines, hotels, car rental and tour companies, and are supplied to consumers both directly by content providers and via a number of intermediaries, such as retail travel agents, wholesalers and ticket consolidators.
- 21. Travel wholesalers package together the various components of a holiday in a particular destination, negotiating bulk rates from travel content suppliers and marketing the package to end customers via retailers. Holiday packages generally give the traveller independence once at the destination, whereas tours are escorted and provide less flexibility in terms of itineraries and activities.
- 22. Ticket consolidators act as an intermediary between airlines and travel agents. Airlines offer fares through ticket consolidators to avoid dealing with multiple retailers on an individual basis. Retailers use ticket consolidators to gain access to volume discounts and rebates that may not be available when dealing directly with airlines.
- 23. Traditional 'bricks and mortar' retail travel agents still account for the majority of total travel products and services sold in Australia, particularly for sales of prepacked holidays and tours, and international flight bookings. However, there has also been significant growth in sales of leisure travel products and services over the Internet, both via online retailers and directly via content supplier websites.

# **Market inquiries**

24. On 14 May 2010 the ACCC commenced market inquiries regarding the proposed acquisition. A range of interested parties provided responses, including retailers, buying groups, wholesalers, content providers (such as airlines and hotels), industry associations and regulatory bodies.

# Areas of overlap and market definition

25. The operations of Jetset and Stella overlap in relation to the retail distribution of travel products and services throughout Australia, both direct to end users via their online operations and some wholly owned 'bricks and mortar' retail stores, and via franchisees, non-branded affiliated stores and independent retail outlets that are members of various buying groups. On behalf of these franchisees, retail affiliates and retail outlets that are members of various buying groups, Jetset and Stella negotiate terms and conditions of supply with travel content suppliers (for example, airlines, coaches, hotels and tour operators). Jetset and Stella market their retail brands and the products of their preferred travel content suppliers to end customers. In addition, Jetset and Stella market their wholesale travel packages, tours and air ticket consolidation services to retailers.

#### **Market definition**

- 26. The ACCC's preliminary view is that the relevant markets for consideration of the proposed acquisition are markets for:
  - the retail supply of leisure travel products in Australia;
  - the retail supply of corporate travel management services in Australia;
  - the wholesale supply of travel packages and tours in Australia; and
  - the wholesale supply of air ticket consolidation services in Australia.
- 27. Given the varying degrees of vertical integration among the merger parties and other market participants, and the presence of participants that only operate at one functional level of the supply chain, the ACCC proposes to take a purposive approach and consider the proposed acquisition in the context of separate markets for each functional level. With respect to the retail market, the ACCC considers that it would include suppliers operating under a range of different retail business models including wholly-owned businesses, franchises, buying groups and independent agents.
- 28. Further, the ACCC has identified separate retail markets for leisure travel products and corporate travel management services respectively. The ACCC understands that the supply of corporate travel management services (particularly corporate travel management services for large clients) involves different customers and suppliers to leisure travel customers and suppliers, and demandand supply-side substitution between leisure and corporate travel management services are limited.
- 29. With respect to the national retail market for the supply of leisure travel products, taking a purposive approach based on the overlap between the operations of the merger parties, the ACCC considers that the retail market would likely include traditional 'bricks and mortar' retailers, online retailers and direct retail supply by travel content suppliers. However, the ACCC notes that the degree to which online retailers and direct retail supply by travel content suppliers are viable close substitutes for 'bricks and mortar' retailers is likely to vary considerably among different customers. Accordingly, the ACCC invites further information on the nature and extent of any limitations to substitution between these different distribution channels. For the purposes of this Statement of Issues, the ACCC has adopted a broad product dimension, with particular attention given to any competitive effects arising in the 'bricks and mortar' segment of the market.
- 30. In addition to the markets identified above, due to the significant shareholding Qantas would have in the merged firm, the ACCC's preliminary view is that various markets for the supply of domestic and international air travel services are also relevant markets for consideration of the proposed acquisition.

The ACCC invites industry participants to comment on the nature and extent of substitution between:

- 'bricks and mortar' retailers, online retailers and direct retail supply by travel content suppliers, including any differences according to the type of customer or the particular product or service being supplied;
- the supply of corporate travel management services and the supply of leisure travel products and services; and
- air ticket consolidation services, direct purchases from airlines or services provided by other intermediaries that aggregate retailer demand.

# Statement of issues

31. For the purposes of this Statement of Issues, the issues in this matter are divided into two categories, 'issues that may raise concerns requiring further analysis' and 'issues unlikely to pose concerns.' Three issues are categorised as issues that may raise concerns and three further issues are categorised as issues that are unlikely to pose concerns.

# Issues that may raise concerns requiring further analysis

Retail supply of leisure travel products and services

- 32. The retail networks of Jetset and Stella (including corporate-owned, franchise and affiliated retail stores) are two of the three largest retail store networks in Australia (the other being Flight Centre) and together account for a significant share of retail sales of leisure travel products and services.
- 33. While Jetset and Stella do not own and control each store within their respective networks, the merger parties have considerable influence over the range of product and pricing decisions of franchise and affiliated retail stores, given the role of the merger parties in negotiating terms and conditions of supply, and providing marketing and other support services to their respective networks.
- 34. Accordingly, the proposed acquisition would result in the merged firm acquiring a significant combined market share in the retail supply of leisure travel products and services (taking into account both corporate-owned stores and online outlets and non-owned outlets over which the merger parties have a significant influence).

# Rivalry between Jetset and Stella

35. In addition to their significant combined retail presence, the ACCC's market inquiries to date indicate that Jetset and Stella are each other's closest competitors due to the similarities in their business models. As the most significant franchise and retail buying group operators in Australia, Jetset and Stella currently compete to attract franchisees and other retailers to their networks by seeking to negotiate favourable preferred supplier agreements with travel content suppliers, such as airlines, hotel groups and travel package wholesalers. The removal of each other

as an alternative for retailers seeking affiliation to a network may increase the level of influence the merged firm has over the range and price of travel content offered by network members.

# Likely constraint from Flight Centre and online sales

- 36. Post-acquisition, Flight Centre, which is currently the largest leisure travel retailer in Australia, would remain a significant alternative to the merged firm. However, given that the proposed acquisition would give rise to a reduction in the number of major independent retail networks from three to two, the ACCC's preliminary view is that Flight Centre may not provide a sufficient competitive constraint on the merged firm. The ACCC is concerned that competition from Flight Centre may not effectively replace the vigorous competition between the Jetset and Stella retail networks and, post-acquisition, competition at the retail level may become muted, which may lead to higher commissions, higher prices, reduced choice and/or poorer levels of service for end customers.
- 37. The ACCC's inquiries to date reveal that there has been significant growth in sales of leisure travel products and services over the Internet, both via online retailers and directly via content supplier websites. While traditional 'bricks and mortar' stores still account for the majority of total travel products and services sold in Australia, particularly sales of pre-packed holidays and tours and international flights, the growth in online and direct channels may provide an effective competitive constraint on the merged firm. To the extent that online and direct sales are not a viable option for some customers, however, the merged firm and Flight Centre may, through tacit coordination, be able to achieve higher commissions from content providers or profitably reduce the choice of products available and level of service provided to consumers.

# Barriers to entry

- 38. Barriers to entry on a small scale do not appear to be high, with no significant regulatory barriers or sunk costs and lead times in setting up a single retail outlet. However, market inquiries indicate that there is unlikely to be sufficient new entry into the retail supply of leisure travel products and services to provide an effective competitive constraint on the merged firm and Flight Centre due to the sunk costs and lead times involved in achieving the economies of scale and brand recognition required to compete with large incumbent retail groups. In this context, the ACCC is considering the extent to which the exit of an incumbent buying group or block of franchisees from the merged firm's retail network, to form an independent rival network, may constrain the merged firm. The ACCC invites further submissions on this issue.
- 39. Barriers to entry at the retail level may also be exacerbated by the significant shareholding of Qantas in the merged firm. While the ACCC considers that the proposed acquisition is unlikely to raise competition concerns solely by virtue of the increased vertical integration of Qantas into retail distribution (discussed further below), the ACCC has some concerns that the alignment of Qantas and the merged firm is likely to increase barriers to entry in the retail market, given that access to Qantas domestic and international inventory at competitive terms is considered important to effective competition at the retail level in Australia. The

ACCC considers that while Qantas may not have the ability and incentive to substantially foreclose retail stores not affiliated with the merged firm, it may have some ability and incentive to restrict access to some or all of its products, to some extent.

# Preliminary conclusion

40. The ACCC's preliminary view is that the proposed acquisition may raise competition concerns in relation to the retail supply of leisure travel products and services in Australia. In particular, the ACCC has some concerns that the combination of two significant retail distribution networks could enable the merged firm to extract more favourable terms from preferred suppliers and retail members, while at the same time reducing competitive pressure to pass on any volume benefits to end consumers. Accordingly, the ACCC has some concerns that the proposed acquisition could result in a significant and sustained increase in the end prices leisure travellers pay for a range of content, or reduce the range of products and services offered to end customers. The ACCC is seeking further information on this issue.

The ACCC invites industry participants to comment and provide information in relation to:

- the extent to which potential growth in online retailing and direct sales by content providers would prevent the merged firm from extracting increased commissions, inducing member retailers to impose or increase booking fees, and/or reducing the choice and service available to consumers;
- the extent to which franchisees and affiliated agents of the Jetset and Stella networks are able to obtain access to travel products on competitive terms, independently of the merger parties;
- the ability and incentive of buying groups and franchisees to break away from the merged firm's retail network and establish a fully independent alternative to the merged firm;
- the extent to which alternative retail networks and buying groups are able to negotiate to obtain travel products on competitive terms for their members;
- the extent to which Flight Centre would be likely to compete vigorously with the merged firm in negotiating deals with travel content suppliers and supplying content to end customers; and
- the extent to which the merged firm could negotiate higher commissions from content providers as a result of the proposed acquisition and what effect that would have on end prices for travel consumers.

# Wholesale supply of travel packages and tours

41. Jetset and Stella account for a relatively small proportion of all travel packages sold by wholesalers to retailers in Australia. Both predominantly supply wholesale travel packages to their affiliated retail networks.

- 42. However, the ACCC's preliminary view is that the significant horizontal aggregation at the retail level brought about by the proposed acquisition may raise competition concerns at the wholesale level. In particular, if, as outlined above, the merged firm is likely to obtain market power in the retail market for the supply of leisure travel products, this may provide it with the ability and incentive to foreclose competitors in the market for the wholesale supply of travel packages and tours.
- 43. The merged firm's retail network would represent a very significant distribution channel for travel package and tour wholesalers. Furthermore, both the merged firm and Flight Centre would be expected to favour their own wholesale products over the products of their independent wholesale rivals. The proposed acquisition is more likely to raise competition concerns with respect to the wholesale supply of travel packages for independent travellers, where the merged firm would have the strong *Qantas Holidays* brand to promote at the expense of rival wholesale package suppliers. In the escorted traveller tour segment, the internal offering of the merged firm would be less extensive and, as a result, the merged firm may be more likely to supply the products of independent wholesale rivals.
- 44. The ACCC recognises that the merged firm's ability to prevent its franchisees and affiliates from supplying the products of the merged firm's wholesale rivals would be imperfect and incomplete. As a result, some wholesalers may be able to bypass the merged firm to some extent by marketing their products directly to members of the merged firm's retail network. However, the ACCC's market inquiries to date indicate that supplier agreements negotiated with franchisors and buying group head offices are the most important and efficient means of distribution for wholesalers. Furthermore, the removal of each other as an alternative for retailers seeking affiliation to a network may increase the level of influence the merged firm has over the wholesale travel content offered by network members. The ability for a wholesaler to market their products directly to individual retailers appears unlikely to effectively prevent the merged firm from successfully foreclosing rival wholesalers.
- 45. The ACCC's market inquiries to date indicate that the threat of vertical integration into retail distribution by wholesalers (for example, by direct online distribution) may be unlikely to effectively constrain the merged firm. The vast majority of travel packages and tours continue to be supplied via traditional 'bricks and mortar' stores in Australia, with limited uptake of online distribution models by customers.
- 46. With limited access to retail distribution, the ACCC also considers that new entry into the wholesale supply of travel packages and tours in Australia would be unlikely. Furthermore, barriers to entry at the wholesale level may be exacerbated by the significant shareholding of Qantas in the merged firm. The ACCC is concerned that the alignment of Qantas and the merged firm is likely to increase barriers to entry in the wholesale market, given that access to Qantas domestic and international inventory at competitive terms is considered important to effective competition at the wholesale level in Australia.

47. The ACCC is therefore concerned that the proposed acquisition may raise competition concerns in relation to the wholesale supply of travel packages and tours in Australia by foreclosing access to retail distribution by the merged firm's wholesale rivals. The ACCC is seeking further information on this issue.

The ACCC invites industry participants to comment and provide information in relation to:

- the extent to which travel package wholesalers and tour wholesalers supply directly to end customers or retailers, including franchisees and stores affiliated with Jetset or Stella, including examples and the capacity for expansion of any such direct supply;
- the extent to which potential loss of sales to other domestic airlines would prevent Qantas from foreclosing wholesalers competing with the merger parties; and
- the extent to which the merged firm would be able to influence the decisions of its franchisees about which wholesale inventory to stock.

#### Supply of air ticket consolidation services

- 48. Jetset, through its air ticket consolidation business NTC, and Stella, through its air ticket consolidation business Air Tickets, account for a significant proportion of the air ticket consolidation services provided in Australia. Furthermore, the beneficial owner of another major air ticket consolidator, Consolidated Travel, currently holds a material interest in Jetset and a 50% interest in the operator of the only other significant air ticket consolidation business, the Orient Express Travel Group. The ACCC's inquiries indicate that there would be limited options outside of the merged firm, Consolidated Travel and the Orient Express Travel Group for retailers that require the services of an air ticket consolidator.
- 49. Given the material interest that the beneficial owner of Consolidated Travel and 50% owner of the Orient Express Travel Group would hold in the merged firm, the ACCC considers it unlikely that there would be vigorous competition between the merged firm, Consolidated Travel and the Orient Express Travel Group. Rather, the ACCC considers that the other shareholders in the merged firm and Orient Express Travel Group would recognise the mutual benefits, in terms of higher profits, accruing from reduced competition. While limited transparency in the commissions negotiated by these air ticket consolidators and the proportions they pass on to retailers may facilitate deviations from any implicit consensus reached, the ACCC considers that the proposed acquisition puts competition at significant risk given that there are no other significant air ticket consolidators in the market.
- 50. The ACCC's market inquiries to date indicate that retailers may be able to bypass the air ticket consolidators by establishing direct accounts with airlines and entering into commission agreements with airlines separately. However, small retailers that choose to bypass air ticket consolidators in this way are unlikely to obtain the volume discounts and commissions they require to compete effectively

in the retail supply of travel products. Only by forming rival buying groups would individual retailers be able to effectively bypass the merged firm, Consolidated Travel and the Orient Express Travel Group. Given the scale of the merged firm's retail network, the ACCC is concerned that such bypass or sponsored entry may be unlikely.

51. The ACCC is therefore concerned that the proposed acquisition may raise competition concerns in relation to the supply of air ticket consolidation services in Australia, which may in turn further affect the ability of the merged firm's rivals in the downstream retail market to compete. The ACCC is seeking further information on this issue.

The ACCC invites industry participants to comment and provide information in relation to:

- the nature and extent of any impediments to an implicit consensus or muted competition arising between the merged firm, Consolidated Travel and the Orient Express Travel Group;
- the extent to which an incumbent buying group or block of franchisees in the merged firm's retail network would have the ability and incentive to form or sponsor an independent air ticket consolidator to effectively bypass the merged firm; and
- the magnitude of the difference between volume discounts and commissions available via air ticket consolidators and volume discounts and commissions available directly from airlines.

# Issues unlikely to pose concerns

52. The ACCC considers that the proposed acquisition is unlikely to pose competition concerns with respect to the following issues. However, the ACCC will accept further submissions from market participants on these issues and will further consider possible competition concerns if it considers that such an assessment is warranted.

National market for the supply of corporate travel management services

53. The ACCC considers that the proposed acquisition is unlikely to substantially lessen competition for the supply of corporate travel management services due to the relatively small presence of Stella in this market and the existence of several significant competitors that would likely provide an effective competitive constraint on the merged firm.

Increased vertical integration by Qantas into retail distribution

54. The ACCC considers that the proposed acquisition is unlikely to raise competition concerns at the retail level solely by virtue of the increased vertical integration by Qantas into retail distribution. While the size of the retail network in which Qantas would have a material interest would increase as a result of the proposed acquisition, Qantas's current majority shareholding in Jetset would be

reduced to a 29% interest in the merged firm. As a consequence, the ACCC considers that the proposed acquisition is not likely to change Qantas's incentives in a way that would alone amount to a substantial lessening of competition in downstream markets. However, as outlined above, Qantas's interest in the merged firm may to some extent exacerbate barriers to entry in downstream markets.

Markets for the supply of domestic and international air travel services

- 55. The ACCC considers that the proposed acquisition is unlikely to substantially lessen competition for the supply of domestic and international air travel services. While the size of the retail network in which Qantas would have a material interest would increase as a result of the proposed acquisition:
  - a significant proportion of domestic air travel services are booked directly with airlines, such that competition between Qantas and rival airlines in the supply of domestic air travel services is unlikely to be significantly affected; and
  - the merged firm would not be able to obtain all requisite international flight inventory from Qantas.

# **ACCC's future steps**

- 56. The ACCC will finalise its view on this matter after it considers market responses invited by this Statement of Issues.
- 57. The ACCC now seeks submissions from market participants on each of the issues identified in this Statement of Issues and on any other issue that may be relevant to the ACCC's assessment of this matter.
- 58. Submissions are to be received by the ACCC no later than **12 August 2010**. The ACCC will consider the submissions received from the market and the merger parties in light of the issues identified above and will, in conjunction with information and submissions already provided by the parties, come to a final view in light of the issues raised above.
- 59. The ACCC intends to publicly announce its final view by **2 September 2010**. However the anticipated timeline may change in line with the *Merger Review Process Guidelines*. A Public Competition Assessment for the purpose of explaining the ACCC's final view may be published following the ACCC's public announcement.