



UKHospitality is the voice of a sector that generates £130bn revenue each year. Representing more than 700-member companies, operating 65,000 venues in a sector that employs 3.2 million people, UKHospitality spearheads hospitality's representation on the strategic, structural and regulatory issues it faces, campaigning for policies to help the sector achieve further growth as a key driver of the UK economy. These businesses represent 10% of UK employment and generate £39bn of tax for the Exchequer. Hospitality has faced myriad cost pressures in recent years which have severely impacted the sector and its potential to grow, yet it continues to play a central role on Britain's high streets and in its communities.

Our members have experience with a number of digital operators including short term letting platforms and online food delivery platforms.

With regard to this call for evidence, we focus specifically on concerns with two types of operators in digital markets:

- **Online travel agents (OTAs)**, which are online platforms like Booking.com and Expedia that consumers use to search for and book hotel accommodations; and
- **Metasearch engines (MSEs)**, which are online platforms like TripAdvisor that provide comparisons of various OTA (and sometimes hotel) listings on a single web page.

OTAs and MSEs are **multi-sided platforms** that serve both hotels (who advertise their properties on the platforms) and consumers (who use the platforms to search for and/or book hotel accommodations). Each of them benefits from substantial **indirect network effects**, where growth in the number of users on one side of the platform (e.g. consumers) fuels growth in the number of users on the other side (hotels).

**(a) What market features are likely to be relevant to the assessment of mergers in digital markets?**

- *Assessing market structure: Pricing*

Merger investigations typically start with the definition of relevant "markets", for which the CMA's Merger Assessment Guidelines (MAG) provide only limited guidance insofar as online intermediaries are concerned, and it can too readily be assumed that all online intermediaries listing a particular type of good/service compete in the same space. However, leading operators may have such substantial strategic advantages (in the amounts of data/listings they carry, which often leads consumers to regard their search results as uniquely comprehensive and objective, and in their ever-expanding network effects) they are broadly insulated from effective competition with smaller platforms.

Under the MAG, market shares (and presumptions of market power) are assessed on the basis of sales in "markets" that are defined as that group of products/services over which a hypothetical monopolist could profitably impose a small but significant, non-transitory increase

in price (SSNIP). The SSNIP test essentially is meant to identify that group of products/services that customers are likely to regard as commercially acceptable substitutes for each other.<sup>1</sup>

Whilst the SSNIP test has been used constructively in non-digital markets for a number of years, it does not appear to be fit for purpose in the definition of digital markets, because [i] the prices charged by leading platforms essentially represent a “tax” on access to large numbers of Internet users, rather than a measure of commercial value to business users who are free to choose amongst commercial alternatives, and [ii] small platforms are often contractually or practically constrained from offering prices that are different from those charged by the market leaders (even though the scope of their services is significantly different).

In sum, application of the SSNIP test, in assessing competition amongst online intermediaries, almost certainly leads to erroneous assessments of market shares and structure, giving the impression that digital markets are much less concentrated and more competitive than, in fact, they are.<sup>2</sup> More workable tests of market definition are needed. To the extent these are quantitative in nature, they might well focus to a greater extent on absolute price levels, variable profit margins,<sup>3</sup> and the existence of platform terms of service that affect incumbents’ pricing incentives and ability, in order to ensure that merger reviews are not based on an assumption of effective competition where little or none actually exists.

- *Assessing market performance: Asymmetric constraints and “tipping”*

Regulatory assessments of mergers in digital markets often appear to rely on the existence of relatively low barriers to entry, and frequent platform launches, as evidence that any transaction-related loss of competition will be self-correcting. However, such assessments appear to disregard the critical importance of indirect network effects, which make the largest platforms ever more powerful and relegate smaller rivals to niche (if any) markets.

Whilst it may be apparent in digital markets that potential entry can be both timely (i.e. frequent) and likely, greater emphasis should be placed on the critical question whether new entry/expansion by small platforms can be *sufficient* to offset the strategic advantages and growing economic power of the largest platforms.<sup>4</sup> As noted in MAG paragraph 5.8.10, “*entry into some market niche may be possible, but the niche product may not necessarily compete strongly with other products in the overall market and so may not constrain incumbents effectively.*” Given the growing consolidation of the OTA sector, and the failure or exit of many smaller platforms, merger assessments should be better informed by consideration “*whether past entry or expansion modified the pattern of behaviour and competition in the market*”.<sup>5</sup>

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<sup>1</sup> Because online intermediaries typically offer their services to consumers free of charge, the only “prices” to which the SSNIP test might be applied are those levied against business users who list their goods/services on their platforms. However, for reasons discussed above, these prices do not provide a meaningful basis for market definition.

<sup>2</sup> The CMA in fact has recognised the difficulty of applying the SSNIP test to two-sided markets (MAG paragraph 5.2.20). The views expressed above highlight further the extent to which the SSNIP test is not well suited for purpose in defining digital markets.

<sup>3</sup> The CMA has recognized the importance of variable profit margins to proper market assessment in, e.g. MAG paragraph 5.2.15(b); see also *id.* paragraph 5.3.2.

<sup>4</sup> Cf. MAG paragraph 5.8.3 *et seq.*

<sup>5</sup> *Id.* paragraph 5.8.12.

Further, it must be acknowledged that even small acquisitions “*may increase barriers to entry and/or expansion by, for example, allowing the merged firm to benefit from positive network effects, strengthening its incumbency advantage in a network market*”.<sup>6</sup>

The CMA has recognised the existence of asymmetric constraints in the assessment of market characteristics,<sup>7</sup> and these play a critical role in digital markets like those in which OTAs operate – given the importance of network effects, and the massive data advantages that the leading platforms have in listing millions of properties, small platforms are unable to constrain the competitive and commercial strategies of the larger firms. Similarly, the CMA has recognised the danger that markets in which network effects are important may “tip” in favour of an unassailable leader<sup>8</sup> (or, as experience in the OTA sector demonstrates, two leading platforms). The CMA should accord full recognition of these dynamics in its merger assessments, so that the existence of a long tail of small rivals does not obscure genuine competition issues.

- *Assessing market development: Trends toward concentration*

One of the difficulties in effective merger-law enforcement in digital markets is that acquisition targets often are small entrants/rivals whose commercial and/or innovation potential cannot be forecast with a high degree of certainty. Further, it is often the case that each acquisition target is sufficiently small that the acquisition of it *alone* cannot be deemed to give rise to a substantial lessening of competition. However, sequential acquisitions of an appreciable number of such targets can begin to have effects similar to “death by a thousand cuts”, where no cut itself is sufficient to cause harm but all cuts together can be very damaging. In such cases, a history of small, consolidating acquisitions might well be regarded as compelling evidence that any further acquisitions would contribute to a substantial lessening of competition.

In the hospitality sector, many of the leading digital intermediaries have grown to a significant extent through the acquisition of smaller rivals and potential entrants.

Where a trend toward consolidation is observed, and given the risk that digital markets may tip toward only one or a few dominant platforms (at which point it is likely too late to undo the damage from a string of prior acquisitions), it is critical that regulatory assessments be informed not only by relatively short-term foreseeable effects (which are difficult to forecast in the fast-developing digital space) but, more importantly, by a fully informed understanding of the strategic objectives of large platforms. These may be evidenced in an acquirer’s internal documents, prior acquisitions, management/performance of previously acquired companies, and the like. Competition regulation could be greatly enhanced in digital markets by requiring that an acquirer that has a share of, say, 20% or more (i.e. a level at which network effects may become significant) be entitled to clearance only if it can provide a pro-competitive, economically beneficial business justification for the transaction under review.

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<sup>6</sup> *Id.* paragraph 5.8.13.

<sup>7</sup> MAG paragraph 5.2.20; see also *id.* paragraph 5.3.2.

<sup>8</sup> MAG paragraph 5.8.6.

- *Assessing barriers to entry: Advertising/search engine optimisation*

Digital markets typically commercialise information and transaction processing capability. Accordingly, where incumbents are engaged in activities that may actually undermine, rather than promote, the informational benefits of online trade, this is an indication that such markets are unlikely to function competitively (and that pre-merger reviews should be correspondingly strict).

**(d) How should we approach the assessment of non-price parameters of competition in digital markets?**

Competition amongst platforms, as noted above, has tended to evolve into outsize spending campaigns on search engine optimisation and other advertising – spending that does not provide genuine informational benefits to consumers, and that threatens further entrenchment of leading. As a preliminary step in effective merger enforcement, it might well be appropriate to measure shares in the markets in which online intermediaries operate on the basis of sponsored search results (rather than shares, e.g. of sales or traffic), which would capture the effect of such tactics and the market power exercised by the leading platforms.

**(e) When determining the counterfactual:**

**(i) Which types of evidence should we take into account and how should these be weighted?**

As noted above, given the dynamic nature of digital markets, with which regulators have relatively limited experience, and the fact that irremediable competitive harms may become evident only after the fact, it is critical that regulatory assessments take into account not only reasonably foreseeable effects (which are difficult to forecast in the fast-developing digital space) but, more importantly, a fully informed assessment of the strategic objectives and longer-term forecasts of large platforms. These may be evidenced in, for example:

- An acquirer's internal strategic plans, acquisition documents, and the like; and
- Review of the acquirer's past acquisitions, and its management/performance of previously acquired companies.

Acquiring companies, who have unique competitive insights into their businesses and are willing to invest substantial sums in acquiring other companies, can be presumed to have credible and compelling evidence about likely market developments. Further, given the inherently speculative nature of future development in fast-moving technology markets, competition regulation could be greatly enhanced in digital markets by requiring that an acquirer that has a share of, say, 20% or more in an affected market (i.e. a sufficient share to give rise to appreciable network effects) be entitled to clearance only if it can provide a pro-competitive, economically beneficial business justification for the transaction under review.

- (ii) **How should we assess: (A) The growth prospects of the target? (B) The availability of other routes for the target to grow (eg by attracting external financing)? (C) The possibility of the target being acquired by an alternative party?**

Please see the response to Question (e)(i) above.

- (f) **What evidential weight should be attached to: (i) Internal documents indicating that the purpose of the transaction is to eliminate a competitive threat? (ii) A high transaction value relative to the market value or turnover?**

Please see the response to Question (e) above. Given the limited investments in innovation being made by leading platforms in the hospitality sector (notwithstanding their extraordinary levels of SEO/promotional spending that simply heighten barriers to entry without delivering true informational benefits to consumers), it would be reasonable and appropriate to presume that a high transaction value reflects an acquirer's intention to co-opt potential rivals rather than to achieve genuine economic or innovative efficiencies.

- (g) **Are there particular features of digital mergers that would be relevant to our assessment of efficiencies and relevant customer benefits?**

Roughly 20 years ago, when the first OTAs and MSEs were launched, the emergence of such platforms provided clear "matchmaking" benefits to small/independent hoteliers and consumers, who were able to reach each other more effectively. (The benefits for larger hotel chains were less clear, as their brands were already well known, they had the scale to advertise effectively on their own, and consumers were likely to seek them out.) However, those benefits have largely been realised, and consolidation of the leading OTAs/MSEs threatens significant harm to other platforms, hotel operators and, ultimately, consumers.

- (h) **Are there any other aspects of the MAGs that should be supplemented or revised in relation to mergers in digital markets?**

Whilst we consider that the MAGs are generally fit for purpose, as noted above, some of their provisions should be given greater emphasis in order to ensure their proper application to digital markets. Areas in which we believe some greater modification might be warranted are discussed in response to Question (a).

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