

**In the Matter of the Proposed
Acquisition by Chelsea Logistics
Holdings Corporation of Shares in
KGLI-NM Holdings, Inc.**

**(PCC Case No. M-2018-002)
(MAO Case No. M-39-2017)**

**Chelsea Logistics Holdings
Corporation, KGLI-NM Holdings, Inc.**

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**FULL CASE REPORT ON COMMISSION
DECISION NO. 022-M-039/2018**

I. STATEMENT OF THE CASE

1. This case involves the proposed acquisition by Chelsea Logistics Holding Corporation (“Chelsea”) of shares in KGLI-NM Holdings, Inc. (“KGLI-NM”) (the “Transaction”).¹

The Acquiring Parties

2. Chelsea, a wholly-owned subsidiary of Udenna Corporation (“Udenna”), is a corporation organized and registered with the Philippine Securities and Exchange Commission (“SEC”) on 26 August 2016. Chelsea, through its wholly-owned subsidiaries, is engaged in the shipping transport business (tankering, passage, freight, tugboat services, and logistics service business), whose shares are listed and traded in the Philippine Stock Exchange.
3. Udenna, Chelsea’s ultimate parent entity, is a domestic holding company with registered principal office located in Davao City, Philippines. Its subsidiaries are engaged in the distribution and retail of petroleum products, commercial shipping, ship management, logistics, financial services, environmental services, and property development.
4. Among Chelsea’s subsidiaries are: (1) Chelsea Shipping Corporation, which is engaged in the business of petroleum hauling; (2) Starlite Ferries Inc. (“Starlite”), which is engaged in domestic shipping; (3) Worklink Services, Inc., which provides domestic logistics solutions for various local industries; and (4) Trans-Asia Shipping Lines, Inc. (“Trans-Asia”),² which is engaged in the business of transporting passengers and cargo, through its Roll-on-Roll-off Passenger Ships (“RoPax”) and cargo-only vessels.

¹ Chelsea, KGLI-NM, and their respective Ultimate Parent Entities shall be referred to as “Respondents”.

² The acquisition of which is subject to a Decision dated 28 June 2018 by the Philippine Competition Commission in PCC Case No. M-2018-003.

5. Through its subsidiaries, Chelsea has a total fleet of 52 vessels consisting of tankers, tugboats, passenger and passenger/cargo vessels, containerized cargo vessels, and general cargo vessels.

The Acquired Parties

6. KGLI-NM Holdings, Inc. (“KGLI-NM”) is a domestic holding corporation, borne out of the strategic partnership between Negros Holdings and Management Corp. (“Negros Holdings”) and KGL Investments BV (“KGLI-BV”), a private liability company organized under the laws of the Netherlands. KGLI-NM was created solely to own shares in Negros Navigation Company, Inc. (“Negros Navigation”), a holding corporation, which in turn holds shares in companies engaged in passenger and cargo shipping and support services.
 - 6.1. KGLI-BV was previously owned by The Port Fund L.P. (“Port Fund”), a private equity fund established in the Cayman Islands. On 28 July 2016, Port Fund executed a Share Purchase Agreement with Udenna for the latter’s purchase of 100% of KGLI-BV’s outstanding capital stock from the former. Said Share Purchase Agreement was declared void by the Commission in its Decision dated 15 February 2018, which found Udenna and KGLI-BV to have violated the compulsory notification requirement under Section 17 of the Philippine Competition Act (“PCA”).
 - 6.2. After a ratification of said Share Purchase Agreement and filing of a notification before the MAO, the Commission cleared the acquisition of KGLI-BV on 4 May 2018.
7. Negros Holdings is the ultimate parent entity of KGLI-NM. Negros Holdings holds interests in companies engaged in passenger transportation and cargo freight services, logistics services, and supply chain management.
8. One of Negros Navigation’s subsidiaries is 2GO Group, Inc. (“2GO Group”), where it holds approximately 88.31% of the latter’s outstanding capital stock. 2GO Group provides shipping, logistics, and distribution services throughout the Philippines.
9. 2GO Group has a fleet of 26 vessels consisting of RoPax vessels (8), fast craft vessels (10), and cargo-only vessels (8).

The Transaction

10. As stated in the notification documents submitted by the Respondents to the MAO, the transaction involves the acquisition by Chelsea of shares in KGLI-NM to consolidate its shareholdings over KGLI-NM (“Transaction”).

Relevant Proceedings

11. On 3 October 2017, the Commission, through the Mergers and Acquisitions Office (“MAO”), received the Respondents’ Notification Forms, pursuant to Section 12(b) and 16 of the PCA, and Section 1, Rule 4 of the Rules and Regulations to Implement the Provisions of the PCA (“IRR”).

12. At the end of Phase I Review, or on 10 November 2017, MAO identified competition concerns arising from the Transaction. On the same date, the Notice to Proceed to Phase II Review and Request for Additional Documents and Information were sent to the Respondents.
13. During Phase II Review, Chelsea manifested its desire to negotiate voluntary commitments addressing the competition concerns identified during Phase I Review.
 - 13.1. On 11 December 2017, Chelsea submitted a draft Voluntary Commitment to address competition concerns identified by MAO during the Phase I Review. Chelsea also requested the suspension of the Phase II Review period in order for the Commission to evaluate its proposed Commitments.
 - 13.2. The Commission evaluated the Commitments and explored alternative remedies. However, despite several extensions of the Commitment review period, no agreement was reached to address the competition concerns identified by MAO.
 - 13.3. On 3 May 2018, considering that MAO did not receive any further proposal nor any further request for extension and waiver of the Phase II Review Period, the Commitment review period expired. Thus, on 4 May 2018, the Phase II Review of the Transaction resumed.
14. Subsequently, MAO issued its Statement of Concerns dated 29 May 2018 (“SOC”) and transmitted the same to the Commission on even date. In the SOC, the MAO was of the position that the Transaction will result in a substantial lessening of competition because:
 - “231. The Transaction shall eliminate existing competition in the markets for passenger and cargo shipping; x x x
 232. The market for domestic shipping, particularly for the identified legs where the [Respondents] overlap, is conducive for anti-competitive coordinated conduct; x x x
 233. As for the vertical relation between the Respondents, the Transaction will lead to a partial input foreclosure such that the [Respondents] will find it profitable to increase prices or reduce quality of cargo shipping services to other logistics companies.
 234. Barriers to entry are high such that entry into the relevant market will not be timely, likely, and significant such that a new entrant will not serve as a competitive constraint to the [Respondents].”³
15. On the same date, the Commission issued a Notice taking cognizance of the SOC issued by MAO. The Commission gave the Respondents ten (10) days

³ Statement of Concerns (“SOC”), par. 230-234.

from receipt of the said Notice to file their respective verified comments to the SOC.

16. On 8 and 18 June 2018, the Commission received requests for extension of time to file comments from the Respondents. The Commission granted an additional 10, and later on, an additional 5 days, or until 23 June 2018, for the Respondents to file their comments.
17. On 25 June 2018, Respondents filed their Comments of even date on the SOC.
18. The case was considered submitted for decision by the Commission on 25 June 2018.
19. In the evaluation of the case, the Commission also considered the developments in a related case involving a related party (Trans-Asia) in another proceeding.
 - 19.1. This case involved the acquisition of Udenna, through Chelsea, of the entire shareholdings of Trans-Asia for the sum of PhP205,366,987. In the final report issued by MAO, it was alleged that Udenna, Chelsea, and Trans-Asia violated the Compulsory Notification Requirements under Section 17 of the PCA and Rule 4, Section 2 of the IRR.
 - 19.2. The MAO recommended that the subject transactions be declared void, and a fine of 3% of the value of transaction be imposed on Udenna, Chelsea, and Trans-Asia.
 - 19.3. After receipt of the Comments from the respondents in the non-notification case, it was considered submitted for decision on 26 June 2018.

II. ISSUES

20. The main issue for resolution in the case is whether the Transaction is likely to substantially lessen competition in the relevant markets identified. In resolving this issue, the Commission considers the following sub-issues:
 - 20.1. Whether there is a merged entity for the purposes of the PCA;
 - 20.2. Whether Udenna will have effective control over 2GO after the alleged internal restructuring in April 2018;
 - 20.3. Whether the relevant markets are properly determined;
 - 20.4. Whether the Transaction enhances the likelihood of coordination or strengthens existing coordination of competitors in the relevant markets;
 - 20.5. Whether input foreclosure of downstream market competitors is likely post-Transaction;
 - 20.6. Whether entry of new competitors or expansion of existing market participants will be timely, likely, and sufficient post-Transaction;

- 20.7. Whether regulation sufficiently addresses any potential competitive concerns arising from the Transaction; and
- 20.8. Whether there are efficiency gains that have been substantiated by the Respondents.

III. DISCUSSION

Whether there is a merged entity for purposes of the PCA

21. On 20 April 2018, during the pendency of the review of the Transaction, Respondents informed MAO that the recent corporate restructuring of Negros Navigation and the 2GO Group resulted in the conversion of Negros Navigation preferred shares to common stock which would dilute Udenna's stake in Negros Navigation from 59.59% to 39.85%.
22. The restructuring involved the conversion by SM Investments Corporation ("SMIC") and China-ASEAN Marine BV's preferred shares in Negros Navigation to common shares.⁴ Additionally, Negros Navigation and 2GO Group were merged into a single entity, where each stockholder of Negros Navigation received common shares of stock in 2GO Group using the exchange ratio of 0.26 common shares in 2GO Group for every one Negros Navigation common share.⁵ These restructurings resulted in other shareholders of Negros Navigation taking an increased stake in 2GO Group and a dilution of Udenna's shareholdings in the same.
23. Respondents submit that due to this internal restructuring:
- 23.1. Udenna's shareholdings in 2GO Group would be diluted;
- 23.2. Udenna would not have effective control over 2GO Group; and
- 23.3. The Transaction would no longer result in a "merged entity."⁶
24. Respondents' claim has no merit. As clarified in Section 1.3 of the PCC Rules on Merger Procedure, the term "merger" refers to both mergers and acquisitions.
25. As stated in Section 4(a) of the PCA:

Acquisition refers to the purchase of securities or assets, through contract or other means, for the purpose of obtaining control by:

⁴ The conversion rates were disclosed as follows:

- a. 1 Common Negros Navigation Share for every 1 Preferred A Negros Navigation Share; or
- b. 3.25 Common Negros Navigation Share for every 1 Preferred B Negros Navigation Share.

⁵ See Annexes "H" and "I" of Chelsea's Comment dated 25 June 2018.

⁶ Chelsea's Comment dated 25 June 2018 ("Chelsea Comment"), p. 14-24; see also KGLI-NM's Comment dated 25 June 2018 ("KGLI-NM Comment"), p. 10-16.

- (1) One (1) entity of the whole or part of another;
- (2) Two (2) or more entities over another; or
- (3) One (1) or more entities over one (1) or more entities;

26. On the other hand, as stated in Section 4(j) of the PCA:

Merger refers to the joining of two (2) or more entities into an existing entity or to form a new entity;

27. The Transaction qualifies as a merger within the purview of the PCA and its IRR because:

- (1) It is a purchase of securities by one entity of the whole or part of another. It is beyond dispute that the Transaction involves Chelsea's purchase of shares in KGLI-NM; and
- (2) The Transaction was for the purpose of obtaining control as it will result in Udenna consolidating its full ownership over KGLI-NM. Control is presumed to exist when a parent owns directly or indirectly more than one half (1/2) of the voting power of an entity.⁷ The Transaction falls squarely within the definition of a merger as contemplated in the IRR as it is for the purpose of increasing Udenna's ownership of outstanding voting shares in KGLI-NM from 39.71% to 100%.

28. Thus, regardless of the subsequent internal restructuring of Negros Navigation and 2GO Group alleged by the Respondents, the fact remains that the Transaction, which is the acquisition by Chelsea of the shares in KGLI-NM, qualifies as a merger under the PCA and its IRR.

Whether Udenna will have effective control over 2GO after the alleged internal restructuring in April 2018

29. Respondents claim that Udenna will not have effective control over 2GO Group post-Transaction as a result of the internal restructuring and this lack of control will remove any overlaps identified in the relevant markets. This would negate the finding of a substantial lessening of competition in the relevant markets identified in the SOC.

30. Under the PCA "control" is defined as the "ability to substantially influence or direct the actions or decisions of an entity, whether by contract, agency, or otherwise."⁸

31. While there is no presumption of existence of control when an entity owns less than half of the voting shares of another entity, control may still be shown by various circumstances.⁹ These circumstances include:

⁷ Section 25, PCA.
⁸ Section 4(f), PCA.
⁹ Section 25, PCA.

- 1) the power over more than one half (1/2) of the voting rights by virtue of an agreement with investors;
 - 2) the power to direct or govern the financial and operating policies of the entity under a statute or agreement;
 - 3) the power to appoint or remove the majority of the members of the board of directors or equivalent governing body;
 - 4) the power to cast the majority votes at meetings of the board of directors or an equivalent governing body;
 - 5) the existence of ownership over or the right to use all or a significant part of the assets of the entity; and
 - 6) the existence of rights or contracts which confer decisive influence on the decisions of the entity.
32. Respondents allege that due to Udenna not owning a majority of the shares in 2GO Group brought about by the restructuring, the Transaction will not result in a substantial lessening of competition in the relevant markets identified.¹⁰
33. However, upon careful consideration, the Commission finds that several indicators of control point to the conclusion that Udenna will have effective control over 2GO Group post-Transaction.
34. A reading of the Shareholders Agreement dated 8 May 2017 (“SHA”) between Udenna and SMIC shows that Udenna elects the majority of all regular directors of Negros Navigation and 2GO Group.¹¹
35. Respondents do not dispute the existence of the SHA but argue that the same notwithstanding, “[Udenna] does not control the Boards of [Negros Navigation] and 2GO [Group].”¹² As explained by the Respondents in their Comment, of the nine directors of the 2GO Group, at least two directors are required by law to be independent, leaving at most seven regular directors left for election by Udenna. As such, Udenna can only elect a maximum of four directors, and never the majority of five.¹³
36. While it may be true that Udenna can only elect a maximum of four directors, the Commission finds that the power to elect 2GO Group’s independent directors rests with persons who are also directors of Chelsea and would therefore act in Chelsea’s best interest. Majority of the members of 2GO Group’s Nomination Committee are also affiliated with Chelsea. Dennis Uy (“Mr. Uy”), who is the Chairman of the Nomination Committee of the 2GO Group is Chairman of the Board of Directors of Chelsea. To add, Elmer Serrano (“Mr.

¹⁰ Chelsea Comment, p. 2.

¹¹ Chelsea Comment, Annex “M”

¹² Chelsea Comment, par. 130.

¹³ Chelsea Comment, p. 16.

Serrano”), a director of KGLI-NM and Negros Navigation, is a member of the Nomination Committee of 2GO Group.

37. The role of the Nomination Committee is explicitly stated as being “chiefly responsible for establishing the criteria used in the selection of directors and key officers and the recommendation of the former for membership of the Board...”.¹⁴ As such, the Commission finds that due to control of the Nomination Committee, Udenna will have the ability to appoint a majority of the board of directors of 2GO Group post-Transaction.
38. Furthermore, as reported by MAO, Mr. Uy and Mr. Serrano also serve as Executive Directors of the 2GO Group.¹⁵ According to the Corporate Governance Manual of 2GO Group, executive directors are those who have the responsibility of the day-to-day operations of the organization.
39. Respondents deny MAO’s conclusion that Mr. Uy and Mr. Serrano are Executive Directors and argue that the same are merely members of the Executive Committee.¹⁶
40. Even if Respondents allege that Mr. Uy and Mr. Serrano are not Executive Directors, but merely members of the Executive Committee, this does not alter the fact that Executive Committee members have the power to direct the operating policies of 2GO Group. A board committee, such as the Executive Committee, as described by the Respondents, may act by majority vote of all its members, on such specific matters within the competence of the board. They perform delegated functions on behalf of the Board of Directors of 2GO Group or when the full board cannot convene. Thus, there is basis to find that Mr. Uy and Mr. Serrano, being two out of the three members of the Executive Committee, can direct the operating policies of 2GO Group.
41. The MAO also reports that Mr. Uy and Mr. Serrano are members of the committee in charge of compensation and remuneration.¹⁷
42. The Respondents argue that the Compensation Committee, contrary to what the MAO is suggesting, was constituted to provide a check on management and to guard against the executives determining their own compensation. They allege that specific mandates and duties of the Compensation Committee are well-established in corporate practice, in Philippine corporate governance regulations, and are outlined in 2GO Group’s Corporate Governance Manual; none of which will point to control of any company and its operations.¹⁸
43. The Commission notes that membership in any one committee would not, in itself, show control over the operations of 2GO Group. However, the fact that the power to appoint or recommend members in the various committees involved in the day to day operations of 2GO Group is vested in key members

¹⁴ 2GO Group, Inc. Corporate Governance, <https://2go.com.ph/IR/governance.asp> accessed on 26 June 2018.

¹⁵ SOC, par. 32.6.

¹⁶ Chelsea Comment, par. 111 to 113.

¹⁷ Results of the Organizational Meeting dated 05 April 2018, <https://www.2go.com.ph/IR/governance.asp>

¹⁸ Chelsea Comment, par. 114.

of Udenna points to a conclusion that Udenna will have decisive influence over 2GO Group post-Transaction.

44. Furthermore, the Commission notes the submissions of Udenna reveal their objective to enter into the Transaction with the intention of gaining control over 2GO Group. Udenna has also consistently held itself out to the public as having control of 2GO Group through Chelsea.

44.1. In 2GO Group's Definitive Information Statement and Notice of Annual Stockholders Meeting dated 27 February 2018 ("Definitive Information Statement") which was posted in 2GO Group's official website on 14 March 2018, Udenna declared its indirect ownership of 2GO Group.¹⁹

44.2. The Definitive Information Statement already took into account the corporate restructuring of Negros Navigation and 2GO Group as well as the share swap of Negros Navigation and 2GO Group shares.²⁰ Interestingly, however, the very same Definitive Information Statement under the heading "**Changes in Control**" also notes the pendency of the PCC's review of the Transaction subject of the case at bar and reports that upon its completion, "**Udenna Group will indirectly own 52.62% voting and 35.19% economic interests in 2GO [Group], while SMIC will indirectly have a 14.01% voting and 30.46% economic interest in 2GO.**"²¹ This confirms the intent of Udenna for entering into the Transaction.

45. Finally, Chelsea, KGLI-NM, Negros Navigation, and 2GO Group have interlocking directors and officers.²²
46. Based on the foregoing, the Commission finds that Udenna will have the power, post-Transaction, to direct the operating policies of 2GO Group. Thus the Commission finds that Udenna will acquire control over 2GO Group post-Transaction.

Whether the relevant markets are properly determined

47. MAO has defined the relevant product markets as i.) the provision of passenger shipping services; and ii.) the provision of cargo shipping services.
48. For the provision of passenger shipping services MAO has determined the segment between the port of origin and the port of destination – referred to as "legs" - as the relevant geographic market. For the provision of cargo shipping services, MAO has likewise identified legs as the relevant geographic market.

¹⁹ https://2go.com.ph/IR/Documents/2go%20group,%20inc.%20-%20dis%202018._DDEE3.pdf (Accessed on 26 June 2018).

²⁰ *Id.*, at pp. 15 and 70.

²¹ *Id.*, at p. 3.

²² 2018 GIS of 2GO Group; 2018 GIS of Negros Navigation; 2016 Amended GIS of KGLI-NM submitted to SEC May 5, 2017; PSE Results of Organization Meeting of BOD of Chelsea dated 20 March 2018; and SEC FORM 17-C of Chelsea submitted to PSE dated 20 March 2018.

49. From the submissions of MAO: i) both Trans-Asia and 2GO Group provide passenger shipping services and cargo shipping services within the same geographic markets; and ii) consumers consider the services of Trans-Asia and 2GO Group to be substitutable.
50. The Respondents allege that MAO has wrongly identified the relevant markets. Particularly, Respondents raise that for both the markets of passenger shipping services and cargo shipping services, long-haul shipping services offered by 2GO Group and short-haul shipping services provided by Trans-Asia are not substitutable. If long-haul and short-haul shipping services do not belong in the same relevant market, Respondents claim that the market shares provided by MAO would be unreliable, hence, negating any finding of a substantial lessening of competition.
51. For cargo shipping services, Respondents also dispute the substitutability of containerized and breakbulk cargo shipping services. Respondents allege that containerized cargo shipping and breakbulk cargo shipping belong in separate markets. Similar to their argument stated above, Respondents claim that market shares would be unreliable if the relevant market is improperly defined.

Market Definition

52. A relevant market refers to the market in which a particular good or service is sold and which is a combination of the relevant product market and the relevant geographic market, defined as follows:
 - 52.1. A relevant product market comprises all those goods and/or services which are regarded as interchangeable or substitutable by the consumer or the customer, by reason of the goods and/or services' characteristics, their prices and their intended use;²³ and
 - 52.2. The relevant geographic market comprises the area in which the entity concerned is involved in the supply and demand of goods and services, in which the conditions of competition are sufficiently homogenous and which can be distinguished from neighboring areas because the conditions of competition are different in those areas.²⁴
53. The Commission's determination of the relevant market depends on the substitutability of services from the perspective of consumers.
54. The Commission evaluated the substitutability of the services provided by Chelsea, through its subsidiaries, and 2GO Group and found that both Respondents engage in the provision of passenger shipping services through their respective Roll-on/Passenger ("RoPax") vessels and in the provision of cargo shipping services through their respective RoPax and cargo-only vessels.

²³ Merger Review Guidelines, Section 5.5.

²⁴ *Id.*, Section 5.6.

Passenger Shipping

55. The Respondents operate between the same ports. Based on publicly available information²⁵ both Chelsea and 2GO Group provide passenger shipping services in the following legs: (i) Cebu to Cagayan de Oro (CEB-CAG); (ii) Cagayan de Oro to Cebu (CAG-CEB); (iii) Cebu to Ozamis (CEB-OZA); (iv) Ozamis to Cebu (OZA-CEB); (v) Cebu to Iligan (CEB-ILI); and (vi) Iligan to Cebu (ILI-CEB).
56. The Respondents allege that MAO's adoption of a leg as the geographic market ignores the "most basic" difference between the markets catered by Trans-Asia and 2GO Group which is that Trans-Asia's journeys are short-haul while 2GO Group's journeys are long-haul.²⁶ For instance, 2GO Group vessels plying the CEB-CAG leg are "not dedicated and are only doing so as part and parcel of the MNL-CEB-CAG-MNL long-haul route."²⁷ On the other hand, Trans-Asia's CEB-CAG trips are dedicated to such leg as alleged by Respondents.
57. While the Commission acknowledges that 2GO Group's trips are long-haul and Trans-Asia's trips are short-haul and mainly concentrated in Visayas and Mindanao, **the fact remains that both Respondents are able to carry passengers between the same ports, thus providing options for passengers to choose from.** 2GO Group is not precluded from accepting passengers from every port that its vessels visit.
58. From a demand-side perspective, the services of Trans-Asia and 2GO Group are substitutable based on the findings of the consumer survey commissioned by MAO.²⁸ Passengers would shift from Trans-Asia to 2GO Group in the event that Trans-Asia is not available to travel and vice versa.
59. Passengers of domestic shipping plan their itinerary by choosing a pair of specific ports closest to their origin and destination. Shipping lines are then selected based on various considerations such as cost, duration of travel, and quality of service.
60. Based on the foregoing, the Commission finds that consumers consider the passenger shipping services offered in each particular leg, whether serviced by a short-haul vessel or part of a long-haul journey, as substitutable, hence part of the same relevant market.

Cargo Shipping

61. The Respondents operate between the same ports. Based on publicly available information²⁹ both Chelsea and 2GO Group provide cargo shipping services in the following legs: (i) Cebu to Cagayan de Oro (CEB-CAG); (ii) Cagayan de Oro to Cebu (CAG-CEB); (iii) Cebu to Ozamis (CEB-OZA); (iv) Ozamis to Cebu

²⁵ Available on the website and cited by the Respondents.

²⁶ Comment of Chelsea par. 168.

²⁷ *Id.* at par. 172.

²⁸ The survey was conducted from 21 January to 05 February 2018.

²⁹ Available on the website and cited by the Respondents.

(OZA-CEB); (v) Cebu to Iligan (CEB-ILI); (vi) Iligan to Cebu (ILI-CEB); and (vii) Cebu to Zamboanga (CEB-ZAM).

62. In defining the product market, MAO did not distinguish between containerized³⁰ and breakbulk³¹ cargo shipping services, considering them as being in one relevant product market.
63. Respondents dispute the substitutability of containerized and breakbulk cargo shipping services, stating that they belong in separate product markets.³² Respondents allege that breakbulk cargo comes in various sizes, require special stowage, and the use of pallet boards. On the other hand, containerized cargo has a definite volume and do not require constant maintenance.³³
64. If the Commission were to adopt Respondents' product market definition, where breakbulk shipping and containerized shipping are considered as separate product markets, Respondents would have higher market shares for the legs involved. By adopting a broader definition of the relevant market for cargo shipping, the analysis allowed for the inclusion of more market players that diluted the market shares of the participants
65. The Commission finds that the market for cargo shipping in this case has been appropriately defined because i) the vessels of the Respondents can accommodate containerized and breakbulk cargo; and ii) cargo forwarders offer services that consolidate general goods into intermodal containers.
66. From a supply-side perspective, RoPax and cargo-only vessels can accommodate both intermodal containers and breakbulk cargo and easily shift from one mode of cargo transport to another. Shipping lines can transport both kinds of cargo without significant costs, or even allocate sections of the vessel for either type on the same trip.
67. The existence of different pricing structures for containerized and breakbulk cargo shipping only alludes to the fact each kind of shipment requires different modes of handling and hauling equipment which are readily available to Parties. Price differences alone do not preclude substitutability. The fact remains that the vessels of Trans-Asia and 2GO Group can accommodate both containerized cargo and breakbulk cargo.
68. As for the demand-side substitutability, the Commission finds that the existence of cargo forwarders and consolidators have significantly blurred the difference between breakbulk and containerized cargo. Customers have relied on cargo forwarders to consolidate goods that, on their own, would not fill an entire intermodal container. Even if a vessel can only accommodate intermodal

³⁰ Containerized shipping is a mode of transporting cargo that can be unitized and packed into standard 10, 20, or 40-foot intermodal containers.

³¹ General or breakbulk shipping is used for transporting packed or palletized cargo of different forms and/or sizes, including irregular-shaped cargo that cannot be shipped using containers.

³² Comment of Chelsea par. 196.

³³ *Id.* at pars. 196-197.

containers, cargo forwarders are able to provide logistics solutions to accommodate the transport of breakbulk cargo.

69. Further, the Commission takes note of MAO's report wherein a representative of Trans-Asia confirmed that previous breakbulk cargo customers shifted to containerized cargo when Trans-Asia introduced 10-foot container vans in 2010 and 20-foot container vans in 2015.³⁴ Such event supports the MAO's contention that breakbulk cargo and containerized cargo are interchangeable.
70. Considering the foregoing, and for purposes of this review, the Commission finds breakbulk and containerized cargo shipping to be substitutable and therefore part of the same relevant market.

Whether there will be a substantial lessening of competition in the relevant markets

71. With the disposition of the issue of market definition, the Commission will now determine whether Transaction will result in a substantial lessening of competition in the identified relevant markets.

Unilateral Horizontal Effects in Passenger Shipping

Market Shares and Concentration

72. The Commission's analysis of horizontal unilateral effects of a merger or acquisition includes assessing the competitive constraint provided by each firm according to its market share, such that if a firm involved in the Transaction has a large market share, the Transaction is more likely to create or enhance a dominant position.
73. MAO reported that the Transaction will result in a post-Transaction combined market share of 2GO Group and Trans-Asia in the six (6) passenger legs, computed based on current capacity in number of passengers, as follows:³⁵
 - a. Cebu-Cagayan: 92%
 - b. Cagayan-Cebu: 92%
 - c. Cebu-Ozamis: 50%
 - d. Ozamis-Cebu: 50%
 - e. Cebu-Iligan: 60%
 - f. Iligan-Cebu: 60%

³⁴ SOC, pp. 29-30, par. 82.2.

³⁵ Market shares computed based on data submitted by the Respondents as Notification Form, Appendix F, Section 6.3.

74. As such, the MAO reported that the Transaction is expected to lead to a significant increase in market concentration in these relevant markets.
75. While the Respondents argue that capacity is not the single indicator of market share, it did not put forward any other proposed measure or evidence to show the Respondents' market shares.
76. The Commission finds that using capacity as a measure of market share in the passenger shipping market is reasonable as it reflects the best available indication of a firms' competitive significance in each leg. Further, it can be used to influence prices, allowing firms to set prices that deviate from levels dictated by market forces. In this regard, the use of 2GO Group's full capacity accurately reflects its market potential as it provides a measure of the amount of available supply which the firm may readily use to serve the relevant markets.
77. In any event, whether capacity or another metric for market share is used, the number of players in the market post-Transaction will still be reduced, and the merger of the two largest competitors in the relevant markets identified would increase the concentration therein.
78. In view of the foregoing, the Commission finds that a significant increase in market concentration will result post-Transaction. Post-Transaction there will be a: (i) a merger to monopoly in each of CEB-CAG and CAG-CEB, and (ii) a three-to-two merger in the remaining four (4) legs where the Respondents will have very high combined market shares at or exceeding 50%.

Closeness of Competition between the Respondents

79. MAO conducted a competitive effects analysis that involved a comprehensive assessment of market conditions. MAO did not rely on market shares alone, but likewise investigated the closeness of competition between the Respondents, conducted a leg-by-leg analysis of the likelihood of a price increase, and submitted empirical evidence of actual harm to competition.
80. In their Comments, the Respondents argue that market shares do not fully reflect the competitive significance of firms in the market or the impact of a transaction. They argue that focusing on market share might lead to failure to take proper account of the degree to which competitors can constrain the behavior of the alleged dominant entity.³⁶
81. The Commission notes that MAO only used market shares as an initial step to provide an indication of the Respondents' competitive significance in the market. MAO also conducted an analysis of the closeness of competition between the Respondents.
 - 81.1. While the Respondents deny that they are each other's competitors pointing to the different schedules of their vessels, the consumer survey and focus group discussions conducted by the MAO show that passengers view Trans-Asia and 2GO Group as close substitutes. A

³⁶ Chelsea Comment, p.35. See also, KGLI-NM Comment, p. 27.

very high percentage of 2GO Group and Trans-Asia passengers confirmed that they will shift to the other party instead of other competitors operating in the same legs.³⁷

- 81.2. The Commission takes note that MAO tested the closeness of competition between Trans-Asia and 2GO Group through a price regression analysis using data obtained from the Respondents, MARINA, and Cebu Ports Authority.
- 81.3. Results of MAO's regression analysis show that the presence of 2GO Group in a leg has a significant and negative relationship with the fares of Trans-Asia, *i.e.* 2GO Group's presence corresponds to lower Trans-Asia prices. MAO reported that over the period considered and across all routes, Trans-Asia prices are on average 22% lower when 2GO Group is present in a leg.
82. The Commission deems it appropriate at this point to draw attention to the reference made in the SOC where the Respondents, despite every opportunity, still failed to provide business plans, presentations to management committees, budget and financial projections to the MAO.³⁸ The Respondents' Comments likewise do not contain such submissions that could support its arguments. Thus, the Commission is unable to lend credence to the Respondents' bare denial that they are not close competitors, when there is no shred of evidence provided by Respondents to rebut MAO's findings.
83. The Commission finds that the empirical data and analysis conducted by MAO supports the passengers' view that 2GO Group and Trans-Asia as closer substitutes than any other competitors in the markets where they operate.
84. Mergers involving firms whose services are regarded as close substitutes are more likely to result in significant unilateral effects. When consumers view the services as close substitutes, it is more likely that the parties to a merger will have the ability and incentive to profitably raise prices.
85. Hence, the removal of the competitive constraint that the Respondents exercise against each other would lead to a substantial lessening of competition in the relevant markets.

Likelihood of an Increase in Prices Post-Transaction

86. Substantial lessening of competition will result from a transaction when the merged entity would find it profitable to increase its prices, acting independently of its competitors. The existence of high profit margins is an indication that a firm is able to price above competitive level and act independently of its competitors. A merger between competitors that already enjoy high margins will result in an increased ability to charge higher prices.

³⁷ Annex J of the SOC "FGD and Survey Results for details on the sampling methodology, sample size, and summary of passenger demographics"

³⁸ SOC, par. 116.

87. To prove that there is a likelihood of price increase post-Transaction, the MAO computed the profit margins of Trans-Asia and 2GO Group by leg and by vessel.³⁹ The MAO found that Trans-Asia enjoys high margins for most passenger legs.⁴⁰ Similarly, 2GO Group enjoys high margins for majority of its passenger legs.⁴¹
- 87.1. The results of the profit margin analysis conducted by MAO, taken together with the results of the consumer survey and FGDs which suggest that passengers are willing to absorb incremental increase in rates when they are repeat customers of a particular shipping line,⁴² demonstrate that Trans-Asia and 2GO Group have ability to increase prices.
88. From an examination of MAO's analysis as shown in the SOC, the Commission finds that pre-Transaction, Trans-Asia already has the ability to charge high prices in all overlapping legs except Iligan-Cebu, and post-Transaction, its ability to price above competitive levels will be further enhanced.⁴³
89. Likewise, the Commission agrees with MAO's findings that 2GO Group has pre-Transaction ability to price above the competitive level in Cebu-Cagayan and Cagayan-Cebu.⁴⁴ For overlapping legs reporting negative margins (Cebu-Ozamis, Ozamis-Cebu, Cebu-Iligan, Iligan-Cebu), the Transaction will likely create dominance for the Respondents that would enable them to increase prices unilaterally.
90. To further verify if the Transaction will lead to the Respondents finding it profitable to increase its prices, the MAO analyzed the profitability of a price increase post-Transaction.
- 90.1. The Commission finds that there is merit in conducting this test considering that a merger between two (2) competitors will alter their pricing incentives. The Respondents, after the Transaction, will find it profitable to increase prices as any demand lost from the services of one Respondent due to a price increase will be offset by the demand that will be recaptured by the other Respondent. Hence, if the sum of the revenues earned directly from the increase in price and the revenues recaptured through the Transaction is higher than the cost of foregone sales, the merged entity will find it profitable to increase its prices.
- 90.2. To assess the trade-off between costs and benefits of a price increase post-Transaction, MAO conducted econometric analysis to estimate

³⁹ SOC, par. 125.

⁴⁰ *Id.*

⁴¹ *Id.*

⁴² A series of Focus Group Discussions was conducted from October 23-24, 2017, November 6-7, 2017 and May 21-22, 2018 for passengers of overlapping legs. See Annex J of the SOC: "FGD and Survey Results".

⁴³ SOC, par. 125.

⁴⁴ SOC, par. 128.

own-price elasticities,⁴⁵ cross-price elasticities,⁴⁶ and diversion ratios.⁴⁷ The results of MAO's regression show that demand for passenger shipping services in Cebu-Cagayan and Cagayan-Cebu legs is generally elastic such that a percentage increase in the prices of shipping lines corresponds to a bigger percentage decrease in their individual volumes.⁴⁸ Cross-price elasticities show that if 2GO Group increases its prices, 77% of foregone sales due to reduction in demand will be diverted to Trans-Asia.⁴⁹ A 10% increase in the prices of 2GO Group will result in an increase of as much as 34% in the Respondents' post-Transaction combined revenues.⁵⁰

- 90.3. For passenger shipping in Cebu-Ozamis and Ozamis-Cebu legs, using the computed elasticities and diversion ratios, MAO reported that if 2GO Group increases its prices, 70% of foregone sales due to reduction in demand will be diverted to Trans-Asia. MAO compared the pre- and post-Transaction revenues given a 10% increase in 2GO Group fares and found that the Respondents have a strong incentive to increase fares in the Cebu-Ozamis and Ozamis-Cebu legs since their combined revenues will increase by as much as 33% post-Transaction.
- 90.4. In the Cebu-Iligan and Iligan-Cebu legs, MAO reported that post-Transaction revenues will increase up to 36% if 2GO Group fares increase by 10%. Consequently, the Respondents have a strong incentive to increase the prices of 2GO Group in Cebu-Iligan and Iligan-Cebu post-Transaction.
91. Respondents, in disputing MAO's conclusion that they have the incentive to increase prices, state "the basis of these figures is not reliable" as these rely on market shares which were estimated by the Respondents.⁵¹ However, the Commission notes that in calculating the incentive to raise prices, what was used were data independently gathered by the MAO through consumer surveys. It was such independently gathered data that was used to compute elasticities and diversion ratios without relying on market shares.
92. The comprehensive analysis conducted by MAO convinces the Commission that the Transaction gives strong incentive to the merged entity to increase prices in all six (6) legs for passenger shipping services.

⁴⁵ The percentage change in quantity sold by a firm given a percentage increase in the price of its own product or service. Own-price elasticities show the degree of responsiveness of the sales of a firm to a change in its own price, all other factors held constant.

⁴⁶ The percentage change in quantity sold by a firm given a percentage increase in the price of a competing firm. Cross-price elasticities show the relationship between two competing products or services, specifically the degree of responsiveness of the sales of a firm to a change in the price of a competitor, all other factors held constant.

⁴⁷ The proportion of foregone sales following a price increase that is diverted to or regained by a competitor in the market. Diversion ratios are computed using own and cross-price elasticities. Higher cross-price elasticities between two products correspond to a higher diversion ratio, while higher own-price elasticities correspond to a lower diversion ratio.

⁴⁸ SOC, par. 143.

⁴⁹ SOC, par. 144.

⁵⁰ SOC, par. 146.

⁵¹ Comment of KLG1-NM, par. 157

Actual Harm to Competition

93. The MAO presented empirical evidence of actual harm to competition as a result of one of the Respondents exiting the market.
 - 93.1. The MAO reported that 2GO Group temporarily ceased its service in the Cebu-Ozamis and Ozamis-Cebu legs in November 2014. To determine Trans-Asia's response, MAO constructed a regression model to test the impact of the 2GO Group's exit from the market. Results showed that on average, prices in these legs were 15% higher than the average price in legs where 2GO Group did not cease operations post-November 2014.
94. The resulting behavior of Trans-Asia due to an actual event that happened in the past, and undisputed by the Respondents, convinces the Commission that not only are Trans-Asia and 2GO Group close competitors, but also that post-Transaction, the Respondents can and will profitably increase prices in the relevant markets.
95. Therefore, considering that Respondents are each other's closest competitors, the significant market shares of the Respondents, evidence of pre-Transaction market power to price above the competitive level, and evidence of the Respondents' incentive to increase prices, the Commission finds that there will be a substantial lessening of competition post-Transaction as no other entity provides or will provide a sufficient competitive constraint on the Respondents. The Transaction would result in an increase in the Respondents' market power such that they can profitably raise prices above pre-Transaction levels in the market for passenger shipping services in the identified legs.

Unilateral Horizontal Effects in Cargo Shipping

Market Shares and Concentration

96. For the cargo shipping markets, MAO likewise examined the change in market shares and concentration in the overlapping legs.
97. The operations of 2GO Group and Trans-Asia overlap in ten (10) cargo legs. Among these, four⁵² are considered to be high volume legs, where it is often the case that several players compete but only one (1) to two (2) dominant players get the bulk of the market share. The rest of the routes where 2GO Group and Trans-Asia overlap are niche markets with lower trade volumes but were considered by the MAO in its analysis.
98. The MAO reports that upon considering market shares based on both capacity and actual volume shipped, the Transaction will result in significant increase in market concentration.⁵³ In the Cebu-Manila and Manila-Cebu legs, the MAO submitted that small increases in concentration may be expected due to

⁵² Particularly, CEB-CAG, CAG-CEB, CEB-MNL, and MNL-CEB.

⁵³ Changes in HHI based on actual volume shipped as high as 3,492 (on the CEB-CAG leg and vice versa) and 3,225 (on the CEB-OZA leg and vice versa).

sufficient competitive constraint exerted by large carriers like PSACC and Gothong, who are concentrated in Manila markets. For the rest of the legs from Cebu to parts of Mindanao and vice versa, the MAO submitted that the merged entity will have a high combined market share of 92% based on capacity and 62% based on actual volume shipped.⁵⁴

99. In the Comments submitted by the Respondents, they argue that capacity is not a reliable measure, arguing that capacity “is not the single indicator of market share”.⁵⁵ The Commission notes that MAO considered not only market shares based on capacity, but also market shares based on actual volume shipped.
100. Respondents argue that there is an oversupply in the cargo shipping market as a global trend, adding that, in fact, 2GO Group only accounts for 7% of container capacity. For this purpose, Respondents submitted a spreadsheet of capacities of 2GO Group and other shipping lines throughout the country.⁵⁶
101. However, the Commission observes that the spreadsheet submitted by Respondents to prove 2GO Group’s capacity includes vessels in other legs not identified by the MAO in its SOC. The submission of the Parties cannot be used as a reliable indicator of capacity for the purposes of this review. Since the assessment concerns the specific legs identified, then it is the market share in those legs which is relevant. The 7% market share provided by Respondents is based on national data which includes geographic areas outside the legs where Respondents overlap.
102. The Commission thus cannot rely on the spreadsheet submitted by the Respondents.

Likelihood of an Increase in Prices Post-Transaction

103. The MAO notes that the Respondents have pre-Transaction ability to price above competitive levels in several overlapping cargo legs, and expects that market power will remain in these legs post-Transaction. In the legs where the Respondents are currently reporting losses, the Transaction will enhance the ability of the Respondents to increase prices.⁵⁷
104. The MAO reported that Trans-Asia enjoys high margins for most of its cargo legs. Several of Trans-Asia’s most profitable legs, with margins as high as 44%, have been identified by the MAO as overlaps. Out of the ten (10) overlapping cargo legs, three (3) incurred losses in 2016, namely Zamboanga-Cebu, Iligan-Cebu, and Cebu-Manila.⁵⁸ However, all but one of the vessels that ply these legs earn positive profits.
105. The MAO also submits that the 2GO Group earns high margins in its cargo operations. While it incurs losses in two (2) legs, including Ozamis-

⁵⁴ SOC par. 173.2

⁵⁵ Chelsea Comment, p.32-33. *See also*, KGLI-NM Comment, p. 24-25.

⁵⁶ Chelsea Comment, Annex “R”.

⁵⁷ SOC, par. 182.

⁵⁸ *Id.*

Cebu, it is able to earn profits from the other legs within the same route.⁵⁹ MAO observed that for some overlapping legs where 2GO Group incurred losses from passenger operations (Cebu-Ozamis, Cebu-Iligan, and Iligan-Cebu), losses are offset by high margins from cargo operations in the same leg.⁶⁰

106. Out of the ten (10) overlapping legs, nine (9) are profitable for 2GO Group, with margins ranging from 16% to 56%.⁶¹ The 2GO Group also reported high margins for the overlapping legs where Trans-Asia operates at a loss (Zamboanga-Cebu, Iligan-Cebu, and Cebu-Manila).⁶²
107. Thus, in all cases either one of the Respondents has high margins for these legs. Hence, the Transaction will create an enhanced ability for the Respondents to increase prices.
108. To verify whether the merged entity will find it profitable to increase prices in the relevant markets, MAO used the Gross Upward Pricing Pressure test to quantify a firm's incentive to increase prices post-Transaction.⁶³
109. The results of MAO's analysis indicate that the Respondents would find it profitable post-Transaction to increase the prices of the 2GO Group for breakbulk in order to match current Trans-Asia rates.⁶⁴ According to MAO, the only legs where the Merged Entity does not appear to have an incentive to increase price is Cebu-Manila, Manila-Cebu, and Zamboanga-Cebu.
110. On the other hand, the assertions of the Respondents are unsubstantiated and insufficient to controvert the analysis and evidence presented by the MAO.
111. After a review of MAO's analysis, the Commission finds that the Transaction is likely to result in a unilateral increase in prices of several overlapping cargo markets. Given high combined market shares, evidence of pre-Transaction market power to price above the competitive level, and evidence of the Respondents' incentive to increase prices, the Transaction is likely to lead to a substantial lessening of competition in the following legs: (i) CEB-CAG, (ii) CAG-CEB, (iii) CEB-OZA, (iv) OZA-CEB, (v) CEB-ILI, (vi) ILI-CEB, and (vii) CEB-ZAM.

⁵⁹ 2016 MARINA Traffic Reports

⁶⁰ *Id.*

⁶¹ *Id.*

⁶² *Id.*

⁶³ The Gross Upward Pricing Pressure Index (GUPPI) was calculated to provide a simple benchmark to evaluate the magnitude of the Transaction's impact to the merging parties' incentive to increase prices. The test analyzes how much sales are recaptured by the Merged Entity, which is a function of the diversion ratio, and determine the profitability of these recaptured sales, which can be determined through the margins.

⁶⁴ SOC, par. 192.

Whether the Transaction enhances the likelihood of coordination or strengthens existing coordination of competitor in the relevant markets

112. A merger or acquisition may also lessen competition substantially by increasing the possibility that, post-Transaction, some or all the firms in the same relevant market may find it profitable to coordinate their behavior by raising prices or restricting output. Coordinated effects may arise where a merger reduces competitive constraints from actual or potential competition, thus increasing the possibility that competitors will collude or strengthening the tendency to do so. MAO believed that the market for domestic shipping, whether for passenger or cargo, particularly for the identified legs where the Respondents overlap, is conducive for anti-competitive coordinated conduct because the domestic shipping industry is oligopolistic in nature and highly concentrated, and information on prices, schedules and routes are easily accessible to competing firms. No other evidence was provided to the Commission to substantiate MAO's finding on such an effect of the Transaction.
113. The Commission finds the evidence submitted by MAO in the SOC insufficient to make a conclusion as to the likelihood of coordinated effects post-Transaction.

Whether input foreclosure of downstream market competitors is likely post-Transaction

114. A merger or acquisition may allow a merged entity to impair the competitive process in the downstream market, through input or customer foreclosure. Input foreclosure may arise when the Merged Entity's upstream entities restricts access or increases the prices of inputs or complementary services it supplies to downstream competitors. Customer foreclosure may arise when the merged entity's downstream entities sources inputs and complementary services only from its upstream counterparts foreclosing rival upstream entities.
115. The SOC reported that the Transaction may lead to partial foreclosure in the shipping services market since the Respondents will find it profitable to increase prices or reduce quality of cargo shipping services to the Respondents' competing logistics companies.⁶⁵
116. In their Comments, Respondents argue that the potential input foreclosure of cargo shipping services by 2GO Group or Trans-Asia to other companies a mere conjecture and is contrary to business sense or acumen.⁶⁶
117. The Commission finds insufficient evidence to conclude that partial input foreclosure is likely. There is little proof of incentive should the Respondents choose to foreclose its competitors in the downstream market for logistics services, whether totally or partially.

⁶⁵ SOC, par. 205.

⁶⁶ Chelsea Comment, p. 39.

Whether regulation sufficiently addresses any potential competitive concerns

118. Despite the foregoing findings, the Respondents in their Comments, allege that there are sufficient regulations, particularly those introduced by way of Republic Act No. 9295, otherwise known as the Domestic Shipping Development Act and Republic Act No. 10668, otherwise known as the Foreign Ships Co-Loading Act (“RA 10668”), in place to prevent arbitrary increase in pricing and compromise in quality of service in the shipping industry.
119. The Commission finds no basis to refrain from exercising its mandate under the PCA to review mergers or acquisitions and prohibit the same if it finds that the transaction will substantially prevent, restrict or lessen competition in the relevant market.⁶⁷ Section 32 of the PCA in fact acknowledges that there are markets which are regulated by sector regulators. However, the law granted jurisdiction over competition-related issues to the Commission, recognizing that economic and standard regulation are not meant to supplant antitrust enforcement.
120. Competition policy is designed to prevent the development or creation of market structures that threaten the effective functioning of competitive market forces. It is focused on ensuring that the competitive process is functioning such that desirable market outcomes are achieved, which is not the province or objective of economic regulation.
121. In addition, the domestic shipping industry has been deregulated as pointed by the Respondents. The Maritime Industry Authority (“MARINA”), as the sector regulator for the industry, monitors the activities of domestic ship operators but it neither approves rate adjustments initiated by shipping companies, nor does it make a determination on what rates are competitive. It also imposes mandatory minimum service and safety standards for all vessels operated by domestic ship operators.
122. Contrary to the Respondents’ assertion, MARINA’s prescription of minimum service standards for ship operators through Memorandum Circular No. 65 (1991) cannot be equated to competitive market outcomes. While the Respondents claim that the MARINA-prescribed minimum standards “very much dictates (sic) the quality of service in the domestic shipping industry”,⁶⁸ market competition can deliver services that go well beyond the bare minimum for the welfare of consumers.
123. It is important to note that the liberalization of the domestic shipping industry in Executive Order No. 185 (“EO 185”) is intimately tied to the entry or increase of the number of players in the industry. Thus, EO 185 cannot be raised as a defense in this case since a consolidation is inconsistent with EO 185’s vision of enhancing the level of competition through increasing the number of players.
124. It appears to the Commission that the Respondents are trying to present fundamentally contradictory and irreconcilable claims on how the government

⁶⁷ PCA, Section 12 and 20.

⁶⁸ Chelsea Comment, p.25.

views competition in the domestic shipping industry. The Respondents insist there is no need for the intervention of the Commission as the competition authority since the existing sector regulator, MARINA, is already cognizant of how important market competition is as evidenced by a slew of executive orders and memorandum circulars. However, the Respondents' mention of how MARINA considers the possibility that more competition may be ruinous runs contrary to the claim that competition is a generally engendered principle in the domestic shipping market in particular. The Commission strongly rejects any insinuation that competition in the domestic shipping industry may be ruinous. An assertion that the concept of ruinous competition may be applicable to the industry at this point in time is simply unfounded.

125. Another contention of the Respondents is that the enactment of RA 10668, in addition to current MARINA regulations, already afforded sufficient conditions to allow entry of new competitors resulting in oversupply of cargo shipping services. The Commission finds however, that said law does not result in a sufficient increase in competition pressure on domestic cargo firms in the relevant geographic markets as RA 10668 is limited to goods that are for import or export.
126. Considering the foregoing, the Commission finds that the Respondents' attempt to evade the application of the PCA is futile and unsound. Any anti-competitive effect in the relevant markets resulting from the Transaction is undeniably within the Commission's authority to prohibit or remedy in a manner it deems appropriate.

Whether entry of new competitors or expansion of existing market participants will be timely, likely, and sufficient post-Transaction

127. A merger or acquisition is not likely to enhance market power if entry into the market is easy such that the merged entity and its remaining rivals in the market, either unilaterally or collectively, could not profitably raise prices or otherwise reduce competition. Entry is easy if it is timely, likely and sufficient in magnitude, character, and scope to deter or counteract the competitive effects of a transaction.
128. The SOC highlighted the barriers to entry in the domestic shipping market. MAO reported that entering into the market is capital-intensive and requires significant start-up costs. Further, a license has to be secured to operate a shipping company, subject to a summary hearing where incumbents on applied routes may oppose the application on grounds that markets may be too small to accommodate another player. MAO considered that this may delay the entry of a new competitor, add to its start-up costs, and even prevent entry.
129. MAO also identified policies that have an indirect effect of deterring investment into the industry, e.g. nationality requirements and the grant of pioneer status.
130. MAO notes that former officers of 2GO Group are barred from entering the market by a non-compete clause, for a period of five (5) years from April 2017. Consequently, while these individuals may have the expertise and the financial

backing to participate in the domestic shipping and compete with 2GO Group, they are unable to enter the market and compete due to said non-compete clause. The MAO submitted that in the course of its market investigation, it was unable to identify any potential entrant that is likely to compete with the Respondents post-Transaction. The Comment points to government policies and regulatory issuances that liberalized and encouraged entry of new players in the market. While these are acknowledged, other government regulations as pointed out by the MAO continue to impose formidable barriers to entry.

131. In this regard, the Commission also finds that competitive constraint from new entrants or from the expansion of existing market participants is unlikely. Timely entry of a sufficient competitor is not likely given the high entry barriers to the industry, and existing market conditions (*i.e.* high market concentration). The possibility of new entrants or current players expanding their operations is remote and, if at all possible, may not be immediate to constrain the Respondents from exercising market power.

Whether there are efficiency gains that have been substantiated by the Respondents

132. The Respondents argue in their Comment that consolidation or mergers in the shipping industry, such as the Transaction, can bring about efficiency gains, in the form of quality improvements and lower prices by way of increased investments.
133. It is however observed by the Commission that the Respondents have failed to substantiate any potential efficiency gains specific to the Transaction prior to the Comment and in the Comment itself. According to the Section 22 of the PCA, and Rule 4, Section 11 of the IRR, “a party seeking to rely on an efficiencies justification must demonstrate that if the proposed merger or acquisition were implemented, significant efficiency gains would be realized”.
134. These unsubstantiated and vague allusions on the potential benefits of the Transaction are dwarfed by the range of qualitative and quantitative evidence presented in the SOC on the potential adverse effects of the Transaction.

Summary of Competitive Effects

135. Based on the foregoing, the Commission finds that the Transaction will result in substantial lessening of competition in the following geographic markets for passenger shipping: (i) Cebu to Cagayan de Oro (CEB-CAG); (ii) Cagayan de Oro to Cebu (CAG-CEB); (iii) Cebu to Ozamis (CEB-OZA); (iv) Ozamis to Cebu (OZA-CEB); (v) Cebu to Iligan (CEB-ILI); and (vi) Iligan to Cebu (ILI-CEB). The Commission also finds that the Transaction will result in substantial lessening of competition in the following geographic markets for cargo shipping: (i) Cebu to Cagayan de Oro (CEB-CAG); (ii) Cagayan de Oro to Cebu (CAG-CEB); (iii) Cebu to Ozamis (CEB-OZA); (iv) Ozamis to Cebu (OZA-CEB); (v) Cebu to Iligan (CEB-ILI); (vi) Iligan to Cebu (ILI-CEB); and (vii) Cebu to Zamboanga (CEB-ZAM). The finding of substantial lessening of competition in these relevant markets is based on the following:

- 135.1. The transaction eliminates a competitor that was previously a source of competitive constraint.
- 135.2. In these markets, there is a strong likelihood of price increases of a magnitude that adversely affects customers.
- 135.3. Barriers to entry are high. Entry into the relevant market will not be timely, likely, and significant such that a new entrant will not serve as a competitive constraint to the Respondents.

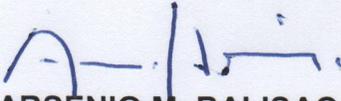
Commission Decision in PCC Case No. M-2018-003

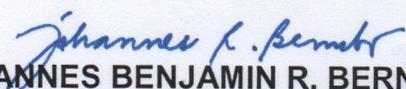
136. Notwithstanding a finding of substantial lessening of competition, the Commission notes that on 28 June 2018, the Commission in PCC Case No. M-2018-003 (“Non-notification Decision”), declared void the Deeds of Absolute Sale of Shares dated 12 December 2016 executed by Chelsea Shipping Group Corp. with each of Arthur Kenneth L. Sy, Judith Ann S. Sandoval, Abraham L. Sy, Julian L. Sy, Sr., and JG Symarine Management and Allied Ventures Corp. for the purchase of 100% of the shares in Trans-Asia Shipping Lines, Inc. (“Trans-Asia Agreements”).
137. Considering that the ownership by Udenna through Chelsea of Trans-Asia gives rise to the horizontal overlaps with 2Go Group which result in the finding of a substantial lessening of competition, the nullification of the Trans-Asia Agreements eliminates such horizontal overlaps. While MAO in its SOC treats the Trans-Asia Agreements as valid, the Commission considers said agreements void in accordance with the Non-notification Decision.
138. Nonetheless, the Commission emphasizes that the harms identified are still likely to occur, if not for the Non-notification Decision. The Commission undertook a full review of the relevant theories of harm during the 90-day period prescribed by law, which notably was suspended from 11 December 2017 to 3 May 2018 during which the Commission negotiated voluntary commitments proposed by the Respondents to address competition concerns.

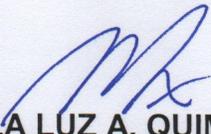
WHEREFORE, the Commission hereby resolves that it will take no further action with respect to the Transaction, *on the condition that the transaction subject of the Non-notification Decision is void*. Should Udenna or any of its subsidiaries or affiliates re-execute or in any way pursue the sale of shares of Trans-Asia, or acquire the business, or any portion thereof, of Trans-Asia through sale, assignment, corporate restructuring, or any other means, the Respondents shall notify such transaction to the Philippine Competition Commission, regardless of whether the same is notifiable under the mandatory notification regime of the PCA and its IRR. The Commission shall review such transaction pursuant to Section 16 of the PCA and Sections 3.3 and 13 of the PCC Rules on Merger Procedure.

SO ORDERED.

3 July 2018, Quezon City, Philippines.


ARSENIO M. BALISACAN
Chairman


JOHANNES BENJAMIN R. BERNABE
Commissioner


STELLA LUZ A. QIMBO
Commissioner


AMABELLE C. ASUNCION
Commissioner