



Jersey Competition Regulatory Authority ('JCRA')

Decision M 093/06

**Proposed Acquisition of British Regional Air
Lines Group Limited by Flybe Group Limited**

The Notified Acquisition

1. On 4 December 2006, the JCRA received an Application for approval under Articles 20 and 21 of the Competition (Jersey) Law 2005 (the ‘Law’) with respect to a proposed acquisition by Flybe Group Limited (‘Flybe’) of the entire issued share capital of British Regional Air Lines Group Limited, and its subsidiaries (collectively, ‘BA Connect’), from British Airways Plc (‘BA’). Additional information was provided subsequently to complete this Application.
2. The JCRA published a notice of its receipt of the Application in the Jersey Gazette on 13 December 2006, and on its website (www.jcra.je), inviting the submission of comments on the proposed acquisition by 29 December 2006. Additionally, the JCRA contacted several of the parties’ competitors and customers concerning the proposed acquisition.

The Parties

3. The acquiring party, Flybe, is incorporated in England and Wales and headquartered in Exeter. Rosedale (J.W.) Investments Limited, incorporated in Jersey, is the holding company of the group to which Flybe belongs.
4. The acquired party, BA Connect, is a regional airline based in Manchester and currently owned by BA. It was formerly known as British Airways CitiExpress, but was renamed BA Connect in February 2006.
5. Based on information provided to the JCRA, the following table summarizes the respective current operations of Flybe and BA Connect:

Airline	Routes Served	Annual Passengers	Aircraft Fleet
Flybe	140	5.5 million	41
BA Connect	47	3.6 million	50

The Requirement for JCRA Approval

6. The parties notified the proposed acquisition to the JCRA under Article 1(4) of the Competition (Mergers and Acquisitions) (Jersey) Order 2005, due to Flybe having an existing share of supply of 40% or more for Jersey originating passengers on several routes from Jersey to the United Kingdom. On that basis, the JCRA's approval is required under Article 20(1) of the Law before the proposed acquisition is executed.

Assessment

7. Under Article 22(4) of the Law, the JCRA may refuse to approve a proposed acquisition if it is satisfied that it would substantially lessen competition in Jersey or in any part of Jersey. The analysis the JCRA follows to determine if a proposed acquisition would have this effect is detailed in the JCRA's Guideline on Mergers and Acquisitions.
8. Prior to engaging in this analysis, it is useful in this instance to specify the scope of the proposed acquisition. Flybe's proposed acquisition of BA Connect does not involve routes otherwise operated by BA Connect's current parent company, BA. Thus, the flights operated by BA between Jersey and London's Gatwick Airport are not part of the proposed acquisition and are not subject to this analysis. BA Connect's assets at London City Airport also are expressly excluded from the proposed acquisition, and will be retained by BA. As consideration for the acquisition of BA Connect, the parties currently intend that Flybe will issue BA shares equal to 15% of Flybe's ordinary share capital. However, BA's potential acquisition of this minority shareholding would not place it in a position of control in relation to Flybe, as the concept of control is defined in Article 2(2) of the Law. Thus, BA's potential acquisition of a minority shareholding in Flybe falls outside of the Law's definition of a 'merger' or 'acquisition', and is not part of this analysis.

9. Furthermore, the proposed acquisition notified to the JCRA under the Law has also been notified to the UK's Office of Fair Trading ('OFT') under applicable UK competition rules. The JCRA understands that the OFT is conducting its own analysis of the proposed acquisition's potential effects in the UK. The JCRA's Decision deals solely with the proposed acquisition with respect to Jersey, and does not concern the OFT's investigation with respect to the United Kingdom.
10. The JCRA's analysis of the proposed acquisition of BA Connect by Flybe raised three areas that required enquiry: (i) scheduled passenger air transport services, (ii) charter passenger air transport services, and (iii) certain ancillary agreements between Flybe and BA directly related to the proposed acquisition of BA Connect.
11. As explained below, the JCRA concludes that a substantial lessening of competition in Jersey or any part thereof will not result in any of these three areas of enquiry.
- (i) Scheduled Passenger Air Transport Services
12. Because customers requiring air transport services generally are inflexible about their points of origin and destination, the European Commission most often has defined relevant product and geographic markets in terms of a 'point of origin/point of destination' ('O&D') approach.¹ This, in turn, most often has been viewed on a city-pair basis, based on the O&D of a particular flight.
13. Here, because BA Connect's sole service offered to or from Jersey is a daily non-stop service to Manchester, the JCRA has analyzed the proposed acquisition on the basis that the Jersey – Manchester city pair (bi-directional) is a properly defined relevant market.

¹ See, e.g., *Case No COMP/M.3280 – Air France/KLM* at ¶¶ 9-16 (11 Feb. 2004). Article 60 of the Law requires that, so far as possible, matters arising under competition law in Jersey are treated in a manner that is consistent with the treatment of corresponding questions arising under competition law in the European Union.

14. This conclusion appears consistent with both European precedent and Jersey's particular economic realities. Specifically, a customer in Jersey wishing to travel to Manchester has no reasonable point of departure other than Jersey Airport.² For the UK destination, it may be the case that for some passengers other airports could be seen as substitutes to Manchester Airport, and thus potentially should be included in the relevant market. This may not be the case, however, for all customers wishing to travel to Manchester. By limiting the relevant market to the Jersey – Manchester city pair, the JCRA's analysis takes into account the interests of customers whose demand for Manchester Airport may be the most inelastic. Furthermore, if the proposed acquisition raises no risks of a substantial lessening of competition on a narrowly defined Jersey – Manchester basis, it is even less likely to raise concerns if the market is expanded to include additional destination airports served by other airlines.³
15. Flybe also transports passengers by air in between Jersey and Manchester. Unlike BA Connect, which serves this O&D with a daily non-stop service, a passenger currently wanting to fly between Jersey and Manchester on Flybe requires a stop and change of aircraft in Southampton. Flybe's current one-stop frequency between Jersey and Manchester is two flights per day on weekdays and one flight per day on Sundays. Flybe appears to have no immediate plans to otherwise commence non-stop on this city pair.
16. In analyzing competition on an O&D market, the European Commission 'will not only consider direct flights between the two airports concerned, but also other transport alternatives to the extent they are substitutable to these direct flights.'⁴ One possible alternative to a direct, non-stop flight can be indirect flights between the airports concerned. Whether an indirect flight is substitutable for a non-stop

² The parties accept that in this instance, travel by sea is not a substitute for air travel.

³ See *JCRA Decision M007/06 Proposed Acquisition by Halifax Corporate Trustees Limited of Mourant ECS Trustees (Jersey) Limited* ¶ 17 (7 July 2006) (if there is no substantial lessening of competition in a narrowly defined relevant market, 'then the proposed acquisition would almost by definition not have the required anti-competitive effect in more broadly defined markets').

⁴ See, e.g., *Case No COMP/M.3280 – Air France/KLM* at ¶ 9 (11 Feb. 2004).

flight depends on a multiplicity of factors, ‘such as the overall travel time, frequency of service and the price of the different alternatives.’⁵

17. Under certain circumstances, the Commission has included indirect flights with non-stop flights in the same relevant market. The Commission has stated, however, that the inclusion of indirect flights as a substitute for non-stop flights is exceptional for short-haul city pairs.⁶ The JCRA’s analysis indicates that for the Jersey – Manchester city pair, Flybe’s indirect service does not appear to be a reasonable substitute to BA Connect’s non-stop service. This is because the substantially increased travel time required for the indirect service compared to the non-stop (roughly three and half hours compared to an hour and a half), and the JCRA’s market research which indicates that the non-stop service tends to be less expensive than the indirect service on this route.⁷ The JCRA’s market inquiries support the notion that consumers would not likely view the current indirect service between Jersey and Manchester as a substitute for the current non-stop service.
18. These factors strongly support the view that Flybe’s indirect service between Jersey and Manchester is not a substitute for BA Connect’s non-stop service, and thus the two services should not be considered in the same relevant product market. On that basis, the proposed acquisition would not have a substantial lessening of competition with respect to the provision of scheduled passenger air transport services.
19. Even if, however, Flybe’s indirect service could be viewed by some customers as a substitute for BA Connect’s direct service, the proposed acquisition of BA Connect by Flybe would still not result in a substantial lessening of competition in scheduled passenger air transport services in between Jersey and Manchester. In addition to BA Connect, bmibaby also currently offers daily non-stop service on this city pair. Data provided to the JCRA shows that compared to BA Connect

⁵ *Ibid.*

⁶ *Ibid.* ¶ 20.

⁷ Based on price comparisons using the Internet websites of various carriers for sample itineraries in 2007.

and bmibaby, during 2005 and 2006 Flybe's indirect service accounted for only a very small proportion of the business on the Jersey – Manchester city pair, namely 1% or less of total passengers flown and revenues earned. Thus, the proposed acquisition would not appear to change appreciably the competitive conditions that currently exist on the Jersey – Manchester city pair for scheduled passenger air transport services, and hence would not lead to a substantial lessening of competition in Jersey or any part thereof.

(ii) Charter Passenger Air Transport Services

20. In addition to scheduled air transport services, both BA Connect and Flybe offer charter air transport services in between Jersey and Manchester. Charter air transport services are a means by which airlines enable flight capacity to be made available to travel agents or tour operators that combine the airline seats with accommodation and other ancillary services, and sell the resulting package to the public at an inclusive price. Both BA Connect and Flybe offer flight capacity to travel agents located in either Jersey or the United Kingdom, who then offer the resulting packages for travel to Jersey during the summer season.
21. Data provided by the parties show that during the previous two summers (2006 and 2005), Flybe and BA Connect flew the vast majority of charter passengers (over 98% combined) between Manchester and Jersey. Given the very large proportion of charter passengers carried by Flybe and BA Connect on this city pair, the JCRA analyzed whether the combination of Flybe and BA Connect could lead to a substantial lessening of competition with respect to charter passenger air transport services.
22. In prior merger decisions, the European Commission has identified a relevant market for the provision of charter passenger air transport services as distinct from scheduled air transport services.⁸ Compared to scheduled air transport services, the Commission has defined the relevant geographic market for charter

⁸ See *Case No COMP/M.2008 – AOM/Air Liberte/Air Littoral* ¶ 16 (27 July 2000); *Case No IV/M.1341 – Westdeutsche Landesbank/Carlson/Thomas Cook* at ¶¶ 13-14 (8 March 1999).

air transport on a wider basis, as being national in scope.⁹ A basis of this distinction appears to be that travel agents generally market charter packages on a national basis, notwithstanding the specific departure airport.¹⁰

23. Given the short-haul nature of travel between the United Kingdom and Jersey, it is uncertain how applicable these European precedents are to the current matter, and specifically, whether it is proper to define the relevant geographic market here to include all UK departure airports. It would appear unrealistic, for example, for travel agents to offer their customers located in the greater Manchester area charter packages to Jersey with flights departing from airports located in Northern Ireland or Scotland.
24. The parties agree that precedents which define the relevant geographic market to be national in scope for charter services may not be applicable here. With respect to Manchester, however, the parties contend that there is a great degree of substitutability between it and other airports in the Midlands or Northern England (for example, East Midlands, Doncaster, and Liverpool) for charter services to Jersey. Moreover, the parties also contend that factors such as the declining charter passenger numbers in the face of the greater availability of low cost airlines and the ability to arrange one's own holiday plans over the Internet, results in the traditional distinction between charter and scheduled passenger air transport services potentially being no longer applicable.
25. For the purpose of this Decision, the JCRA need not determine the substitutability between Manchester and other airports for the provision of charter passenger air transport services to Jersey, or whether the distinction between charter and scheduled air transport still is appropriate. This is because even focussing solely on the Jersey – Manchester city pair, there is strong evidence of the availability of supply side substitution in charter services from other airlines.

⁹ See *Westdeutsche Landesbank/Carlson/Thomas Cook* at ¶ 14.

¹⁰ *Ibid.*; *AOM/Air Liberte/Air Littoral* ¶ 16.

26. Supply side substitution exists when ‘suppliers can shift production easily and in the short-run, using largely unchanged production facilities and with little or no additional investment, when given the incentive to do[.]’¹¹ For supply side substitution to be relevant, potential suppliers must be capable of entering a given market in the short run, generally defined to be within one year.¹²
27. The JCRA’s investigation showed strong evidence of supply side substitution with respect to the provision of charter passenger air transport services. Specifically concerning the Jersey – Manchester city pair, while BA Connect and Flybe have provided a large majority of charter capacity during the previous two summers, we were informed that at least two other airlines have offered to customers the use of their existing assets for charter services on this city pair during the upcoming summer. In addition, examining charter passenger numbers departing from different UK airports over the past three summers reveals a fair amount of entry and exit among different airlines at different airports for the provision of charter passenger capacity to Jersey. This supports the notion that the barriers to entry and exit into the provision of charter passenger air transport services are low.
28. Therefore, the JCRA concludes that while the outer boundaries of the product and geographic market may be left open concerning the provision of charter passenger air transport services, restricting the geographic market solely to the Manchester - Jersey city pair is not appropriate. Thus, reliance on historical data for charter passengers flown between Manchester and Jersey is not appropriate to determine the competitive effects of the proposed acquisition. Based on the apparent availability of supply side substitution, the JCRA concludes that the proposed acquisition is not likely to result in a substantial lessening of competition with respect to charter passenger air transport services.

¹¹ *JCRA Guideline on Market Definition* at 8.

¹² *See ibid.*

(iii) Ancillary Restraints Between Flybe and BA Directly related to the proposed Acquisition of BA Connect

29. The previous two sections have dealt with potential horizontal concentrations resulting from the combination of BA Connect and Flybe. In addition, pursuant to prior JCRA decisions and consistent with EU precedent, so-called ‘ancillary restraints’ between the parent entities involved in the proposed acquisition also are subject to analysis in merger review.¹³
30. An ancillary restraint is an agreement that does not form part of the asset or share transfer but is considered to be ‘directly related and necessary to the implementation of the concentration.’¹⁴ [CONFIDENTIAL REDACTED]
31. [CONFIDENTIAL REDACTED]
32. [CONFIDENTIAL REDACTED]

Conclusion

33. Accordingly, based on the considerations discussed above, the JCRA has concluded that the proposed acquisition is not likely to lessen competition substantially in Jersey or in any part thereof, and hereby approves the acquisition.

29 January 2007

By Order of the JCRA Board

¹³ See JCRA Decision M072/06 *Neville Keith Moore, Glenda Faith Moore-Wilson & Island Estates LLP/A de Gruchy & Co Limited* ¶¶ 15-17 (8 Nov. 2006); *Commission Notice on restrictions directly related and necessary to concentrations*, O.J. C 56/03 (5 March 2005).

¹⁴ See O.J. C 56/03 ¶¶ 1, 10.