PHILIPPINE COMPETITION COMMISSION
Ensuring businesses compete and consumers benefit

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

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

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

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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").

2. On 29 May 2018 the Mergers and Acquisitions Office ("MAO") issued a Statement of Concerns ("SOC") pertaining to the Transaction. Thereafter, each of Chelsea and KGLI-NM filed their respective Comments on 25 June 2018.

3. Considering the submissions by MAO in the SOC and the respective Comments of Chelsea and KGLI-NM, the Commission makes the following findings.

The Acquiring Parties

4. Chelsea, a wholly-owned subsidiary of Udenna Corporation ("Udenna" and collectively with Chelsea and KGLI-NM, the "Parties"), is a corporation organized and registered with the Philippine Securities and Exchange Commission 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.

5. 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.

6. Among Chelsea's subsidiaries are: (1) Chelsea Shipping Corporation, which is engaged in the business of petroleum hauling; (2) Starlite Ferries ("Starlite") Inc. which is engaged in domestic shipping; (3) Worklink Services, Inc., which provides domestic logistics solution for various local industries; and (4) Trans-Asia Shipping Lines, Inc. ("Trans-Asia"),[1] which is engaged in the business of

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[1] The acquisition of which is subject to a Decision dated 28 June 2018 by the Philippine Competition Commission in Commission Decision No. 021-M-02/2018.

transporting passengers and cargo, through its seven Roll-on-Roll-off Passenger Ships ("RoPax") and three cargo-only vessels.

The Acquired Parties

7. 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, a private liability company organized under the laws of 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.

8. 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.

9. One of Negros Navigation's subsidiaries is 2GO Group, Inc. ("2GO Group"), where it holds 88.31% ownership. 2GO Group provides shipping, logistics and distribution services throughout the Philippines.

The Transaction

10. The Transaction involves the acquisition by Chelsea of shares in KGLI-NM to consolidate its shareholdings over KGLI-NM and gain majority ownership, or 52.98%, over 2GO Group.

Acquisition of Control of 2GO Group

11. Parties submit that due to an internal restructuring carried out in April 2018 which allegedly reduced Udenna's effective shareholdings in 2GO Group, Udenna will have no control over 2GO Group post-Transaction.

12. The Commission finds that several indicators of control point to the conclusion that Udenna will have effective control over 2GO Group post-Transaction due to the following circumstances:

  12.1. Udenna elects the majority of all regular directors of Negros Navigation and 2GO Group, as stated clearly in a Shareholders Agreement dated 8 May 2017 between Udenna and SM Investments Corporation.[2]

  12.2. A majority of the members of 2GO Group's Nomination Committee are also affiliated with Chelsea. Dennis 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 represents Chelsea on the Nomination Committee. 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…".[3] As such, the Commission finds that due to control of the Nomination

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2 Annex "M" of Chelsea's and KGLI-NM's respective Comments dated 25 June 2018.

3 See: https://2go.com.ph/IR/governance.asp (Accessed on 26 June 2018)

Committee, Udenna will have the ability to appoint a majority of the board of directors of 2GO Group post-Transaction.

12.3. Finally, Chelsea, KGLI-NM, Negros Navigation, and 2GO Group have overlapping directors and officers.[4]

13. Due to these circumstances, the Commission finds that Udenna will have the power, post-Transaction, to direct the operating policies of 2GO Group.

II. RELEVANT MARKETS AND COMPETITIVE ASSESSMENT

14. The Commission will assess the competitive effects of a merger or acquisition within relevant markets. 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:

14.1. 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; and

14.2. 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.

Substantial Lessening of Competition in Passenger Shipping Post-Transaction

Relevant Markets

15. The Commission adopts the findings of the MAO with respect to the relevant market for analysis. The relevant product market for analysis is the market for RoPax services.

16. The relevant geographic markets are the the following ports of origin and ports of destination (each of which is a "leg"): (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). Chelsea, through Trans-Asia and Starlite, and 2GO Group both provide domestic passenger shipping services. Chelsea operates RoPax passenger vessels while 2GO also operates RoPax passenger vessels across the same legs.

17. Parties have submitted that long-haul and short-haul passenger shipping services are not substitutable. However, the Commission finds that customers plan their trips depending on which ports are closest to their origin and destination, and do not take into consideration the entire route plied or the other ports served by a specific vessel. Regardless of whether routes are long-haul

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4 Statement of Concerns, p. 15.

or short-haul, customers are able to purchase tickets and check schedules on a per leg basis. Considering this, the Commission finds that passenger shipping services are substitutable and belong in the same relevant service market irrespective of whether they are long-haul or short-haul shipping services.

Substantial Lessening of Competition

18. The Commission finds that 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 Parties will have very high combined market shares exceeding 50%.

19. Considering that Parties are each other's closest competitors, the significant market shares of the Parties, evidence of pre-Transaction market power to price above the competitive level, and evidence of the Parties' 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 Parties. The Transaction would result in an increase in the Parties' market power such that they can profitably raise prices above pre-Transaction levels in the market for passenger shipping services in the identified legs.

Substantial Lessening of Competition in Cargo Shipping Post-Transaction

Relevant Markets

20. The Commission adopts the findings of the MAO that containerized cargo shipping and breakbulk cargo shipping are types of services that belong to the same relevant product market. Containerized shipping is a mode of transporting cargo that can be unitized and packed into standard 10, 20, or 40-foot intermodal containers while 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. Majority of goods are generally shippable in both modes. Functionally, the two are the same from the perspective of shippers. Further, shipping lines can easily shift from one mode to the other.

21. As to which legs shall form part of the geographic market, the Commission notes that both Trans-Asia and 2GO Group have breakbulk and containerized operations 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); (vi) Iligan to Cebu (ILI-CEB); and (vii) Cebu to Zamboanga (CEB-ZAM). Thus, those legs shall be identified as the relevant markets for cargo shipping with respect to this Transaction.

22. Similar to passenger shipping services, Parties have submitted that long-haul and short-haul cargo shipping services are not substitutable. As with the discussion in passenger shipping services, the Commission likewise finds that cargo shipping services are substitutable irrespective of whether they are long-haul or short-haul shipping services.

Substantial Lessening of Competition

23. The Commission finds that the Transaction is likely to result in a unilateral increase in prices of several overlapping passenger and cargo markets. Given high combined market shares, evidence of pre-Transaction market power to price above the competitive level, and evidence of the Parties' 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.

Entry and Expansion

24. 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 Parties from exercising market power.

Coordinated Effects

25. 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.

Vertical Effects

26. The Commission likewise finds insufficient evidence to conclude that partial input foreclosure is likely. There is little proof of incentive should the Parties choose to foreclose its competitors in the downstream market for logistics services, whether totally or partially.

Summary of Competitive Assessment

27. 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:

27.1. The transaction eliminates a competitor that was previously a source of competitive constraint.

27.2. In these markets, there is a strong likelihood of price increases of a magnitude that adversely affects customers.

27.3. 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 Parties.

III. COMMISSION DECISION IN PCC CASE NO. M-2018-003

28. Notwithstanding a finding of a 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").

29. Considering that the ownership by Udenna through Chelsea of Trans-Asia gives rise to the horizontal overlaps with 2Go 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 valid, the Commission considers said agreements void in accordance with the Non-notification Decision.

30. 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 the law, which notably was suspended from 11 December 2017 to 3 May 2018 during which the Commission negotiated voluntary commitments proposed by the parties 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 Parties shall notify any 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.

28 June 2018, Quezon City, Philippines.

ARSENIO M. BALISACAN
Chairman

JOHANNES BENJAMIN R. BERNABE
Commissioner

STELLA LUZ A. QUIMBO
Commissioner

AMABELLE C. ASUNCION
Commissioner