Efficiency arguments put forward by the Parties

1.1 The Parties submitted initial observations in support of the need for some residual restrictions on the ability of OTAs to discount the price of Room-Only hotel accommodation to end-users. These potential efficiency arguments relate primarily to the benefits that arise from a hotel having the ability to independently set and control the headline rate for its hotel rooms (and therefore restrict OTAs’ ability to freely discount off headline rates).

1.2 The potential efficiency arguments on which the Parties submitted initial observations can be summarised as follows:

- Firstly, IHG submitted that the headline rate for the hotel room acts as an important indicator of quality for consumers. Unrestricted discounting by OTAs may undermine this and damage the hotel’s brand or reputation. As a result, hotels may be reluctant to use OTAs which in turn is likely to result in lower availability of rooms to consumers, lower inter-brand competition and higher prices and search costs.

- Secondly, the Parties submitted that in a market which is characterised by intense inter-brand competition, hotels have to balance an uncertain and variable demand against a fixed and perishable inventory of rooms. Because of this, yield (revenue) management pricing\(^1\) has become an essential tool within the industry. This enables hotels to adjust room rates frequently in the

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\(^1\) Yield management usually involves sophisticated price modelling to enable providers to discriminate between different customer groups based on their willingness to pay. It is now widely used in transport sectors such as airlines and has also been adopted by the hotel industry as a means of maximising revenue.
window between the time at which a room becomes available to book and the occupancy date, responding to updated information about the level of demand for their rooms. Yield management may include price discrimination between early bookers who may be more price-sensitive and late bookers who are less price-sensitive, typically as they have less flexibility around the date (for example, business travellers). This form of dynamic price discrimination can deliver significant benefits to consumers both by allowing more rooms to be sold and by ensuring that these rooms are allocated efficiently to those who value them the most and therefore are prepared to pay the most for them. Any form of discounting by OTAs has the potential to undermine the benefits of yield management to some extent, if it is difficult for hotels to predict and take into account when setting headline rates over time. Since OTAs do not take any of the inventory risk of unsold rooms, unrestricted discounting would further result in the hotels’ inability to ensure that the costs they incur for the provision of hotel rooms are properly taken into account by an OTA pricing decision. This could lead to a distortion in hotel room pricing and available inventory, ultimately resulting in the possibility that hotels would rely on selective distribution systems or even cease using OTAs as a distribution channel altogether.

- Thirdly, IHG considers that unrestricted discounting by OTAs would **cannibalise sales in the hotels’ direct online sales channels**. IHG argues that hotels’ direct online sales channels are currently very significant, particularly for large hotel chains. As hotels do not pay commission in their direct channel, unrestricted discounting by OTAs would have a significant impact on their profitability and may create a risk that certain hotels refuse to deal with OTAs, deal with fewer OTAs, or offer less inventory to the OTAs they use. This may significantly undermine the OTA model and erode the benefits that the model brings to consumers: consumers would be left with fewer hotels on OTAs, potentially increasing consumer search costs, reducing inter-brand competition between hotels and requiring hotels to engage in more of their own advertising/online customer acquisition, potentially resulting in duplication of cost. The Parties submitted that all of this is likely to increase price and
cost to consumers.

- Fourthly, Expedia and Booking.com submitted that by enabling OTAs to engage in unrestricted discounting, there is a risk that no-frills websites could free-ride on the investment made by other OTAs, for example in the functionality of its website, range of travel offers, customer support, enhanced content quality or in advertising. This may undermine the incentive for OTAs to invest in valuable services for consumers. The retention by hotels of control over headline rates may therefore have the potential to result in enhanced competition between OTAs on the quality of their platforms, which in turn improves consumer choice, and hence enhance inter-brand competition between hotels on any one platform.