

T2RL'S First View is our rapid analysis of breaking news. It helps provide perspective, putting the facts in the context of our wider and deeper knowledge of the market.

## Google Loves IT(A). It's Official!

**T2R Staff**

### The Facts

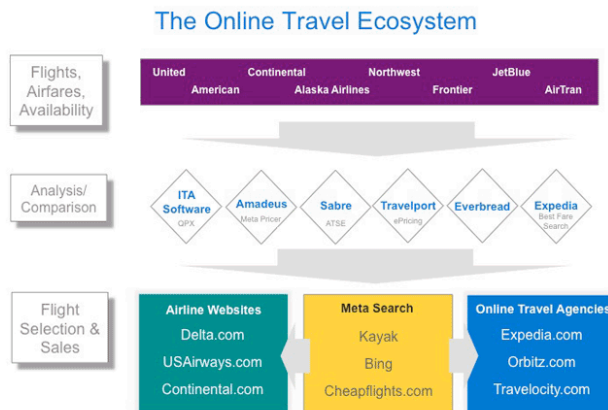
Google has announced an agreement to buy ITA Software for \$700M in cash. The two CEOs, Eric Schmidt and Jeremy Wertheimer hosted an analyst call on Thursday July 1st.

### The Analysis

The deal was expected (See FirstView Google Finally Makes a Move 7th May 2010). It is clear from the webcast and the information published that the focus of the merger is to improve end-user experience with respect to searching for travel products, concentrating, at least in the near term, on the sale of airline tickets.

The most interesting dimensions for T2RL are:

- 1) There was no mention of the airline IT business. ITA and Air Canada have spent many years specifying and building a new generation PSS that was not discussed at all. None of the financial analysts mentioned it on the call and neither did ITA's CEO. We believe that Google will seek to recoup some of its \$700M by selling this business on.
- 2) Google has placed Everbread on the landscape document alongside industry heavyweights like the GDSs and Expedia. Everbread's CEO Morten Lund was one of the founders of Skype but is equally famous for making and losing a fortune. Everbread has developed a high performance airline pricing system, but has still to fully solve the challenges relating to availability that ITA has largely overcome.



Source: <http://www.google.com/press/ita/>

- 3) Both CEOs referred to the US market in their analysis. The comment that 50% of airline seats are sold online certainly does not refer to the World market for flight segments according to our research. The US-centric approach is not surprising. We estimate that ITA generates a very small proportion of its revenue from services outside US Airlines and online travel agents.
- 4) Google's CEO seemed in awe of the team at ITA, talking about the "extraordinary things" ITA had done and the fact they were "pretty amazing". It was not lost on him that ITA's recruitment was from MIT. Google is very impressed with the people they have found and got to know throughout the interaction.
- 5) The regulatory review will take time and the CEOs expect close scrutiny before the agreement will be approved.

## The Speculation

As we have said before this deal could have far-reaching consequences. As such there is a great deal of speculation. The CEOs refused to be drawn into making statements about the future business, but there were some indications.

- By enhancing search processes there may be an opportunity to charge the sellers of air tickets for this improvement in efficiency.
- The idea that Google becomes a broker was not discounted, but it does seem unlikely. We believe this would be a significant regulatory issue and a barrier to completion even though the reality is that no one organisation really dominates the sale of air in the USA. There is both stiff competition and co-opetition between online agents and airline.com. The DoJ papers will be very interesting.
- Airline.com sites and online agents have always competed with each other but do have different customer propositions. Google and ITA have the potential to level this playing field. In the past GDS screens were regulated. Maybe the DoT and the DoJ will need to think about regulation once more as the potential for new abuses will not be in the consumer interest.
- Airlines will need to have the right products available on their sites and in the Google/ITA datasets, as will online agencies.
- Today online agents are powered via the GDSs. According to our research Sabre is currently generating more online bookings than any other GDS. Clients include the world's largest online agent, Expedia and Sabre's own Travelocity. We believe OTAs will now push their GDS partners for technology to play in the new world order of Google/ITA. We may see those like Expedia moving much closer to Amadeus. Board member and Amadeus former CEO José-Antonio Tazón knows better than most just how hard it is to develop the airline shopping solutions. After all even the "extraordinary" and

“pretty amazing” ITA has taken 14 years to achieve an estimated US market share for search of 50%.

- Airlines that have not signed full-content agreements and so are able to charge a premium for sales made in the GDSs may find their own web sites propelled to the ‘top’ of the new Google / ITA display.
- Low cost airlines like Ryanair will want to play with Google/ITA. So will Easyjet, Southwest and others. Interestingly Ryanair currently does not provide any information to ITA by filing schedules with OAG, fares and pricing with ATPCo or its own availability through industry-standard AVS messages. However it is currently believed to be in the process to renew or change its reservation system, possibly to include this functionality.
- Google/ITA will definitely impact airline business models in terms of the customer proposition in bundling and unbundling. Airlines want to communicate low lead-in fares, and push up revenues through add-ons and charges. Google/ITA will want to make sure users will find precisely what they want. Ancillaries like bags, sports equipment, seat selection, boarding priority, in-flight catering and even credit card or payment surcharges and taxes should become transparent. Search is all about finding what the customer wants and comparative shopping is definitely becoming harder. There is a great opportunity for improvement in the user experience. However airline yields are often built on a lack of transparency, so there is a potential downside for the airlines. This will need careful thought and commercial strategy.
- Whatever else happens this is likely to be good for consumers. It will be harder for airlines and online agents and probably a boost in value for the GDSs, specifically those like Amadeus, Sabre and Travelport that supply airline IT systems. The airlines will need smart tools to play in this space more than ever.