ICASA PUBLIC HEARINGS

Competition Commission Submissions

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competition commission south africa

DELEGATION

1. Mr James Hodge – Chief Economist
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OUTLINE

1. INTRODUCTION
2. EFFECTIVENESS OF COMPETITION
3. SPECTRUM
4. FACILITIES ACCESS
5. ROAMING
6. MVNO/APN
7. CONCLUSION

INTRODUCTION

The Data Services Market Inquiry (DSMI) report sets out the Commission's findings & recommendations on data markets

- Retail prices are high due to ineffective competition and not just spectrum constraints, and simply releasing spectrum will not reduce prices to competitive levels
- The implemented package of retail remedies addressed short-term price levels and structure, but the recommended package of wholesale remedies is required to address underlying competition issues and persistent dominance
- This is particularly so in the context of the move to 5G, as the lesson from prior technology upgrades is that they present an opportunity to transition and entrench existing dominance
- Market developments have not altered these recommendations as these developments were anticipated & spectrum related recommendations considered complementary

EFFECTIVENESS OF COMPETITION

Retail prices are high due to ineffective competition and not just spectrum constraints, and simply releasing spectrum will not reduce prices to competitive levels

- Vodacom ROCE [55% - 60%] in 2019; average price-cost mark-up (incl. capital costs) of [20-25%] since 2014; EBIT for SA 65% higher than RoA. MTN also highly profitable
- Vodacom & MTN pricing not constrained by competitors, shown through actual lack of response but also average price per GB
- Telkom/Cell C do not see themselves as effective constraints
- Vodacom & MTN dropped prices by 35% without new spectrum
- Temporary spectrum did not result in further price reductions & previously had more capacity access through RAIN anyway
- Persistence of a highly skewed market structure with Vodacom & MTN holding 80% of mobile revenue (incl. data)
- Price comparisons addressed in submission but results highly sensitive to selection of countries, choice of operator/bundle to compare and trends over time not considered

EFFECTIVENESS OF COMPETITION

Imbalance in structure reinforces dominance without adequate wholesale regulation

- Large subscriber base & profitability gives advantage in rolling out new technologies & services relative to challengers
  - Large capital expenditure required to provide wide coverage with sufficient capacity to maintain network quality (through builds or Rain/Liquid type roaming agreements) can be funded from retained earnings, also lower network costs
  - Smaller less profitable networks simply cannot keep pace with the network expenditure & do through debt (Telkom) or outsource (Cell C)
- Network coverage & quality advantage weakens price-based competition
  - Less need to respond to price reductions by challengers & challenger price drops less profitable as a result. This undermines the ability to fund infrastructure investment, essential to maintain quality as grow
- Wholesale roaming/site access could overcome disadvantage as converts capacity to variable costs but no incentive to provide competitive access without regulation
  - Uncompetitive roaming and site access instead raises costs of challengers & channels more profit to incumbents, reinforcing advantage

EFFECTIVENESS OF COMPETITION

The market has not changed and the move to 5G risks a further cycle of technological leadership entrenching dominance

- Focus on Telkom/RAIN growth but off a low base & small
  - Focused on urban high data users so not impacting on majority pre-paid
  - Ignores that Cell C shed 28% of subscribers and has shrunk due to financial difficulties. Move to convert capex to variable cost
- Spectrum is needed, but must operationalize through investment and this uniquely lies with the two dominant networks
  - Will provide pervasive 5G well ahead of rivals, entrenching position
  - Competitive roaming & site access essential to prevent such outcome
- Current roaming agreements inadequate
  - Quality & fee improvements but not wholesale, will not keep track with price drops & do not include 5G
  - Improved deals with RAIN/LIQUID due to spectrum constraints which will be released with assignment, others not as lucky
- Practically, site access is not addressed by regulations
  - Granted where mutually beneficial but otherwise inferior and different (‘different circumstances’), and not reflective of share of common cost but rather cost of alternative (i.e. build yourself)

SPECTRUM

The release of the ITA and WOAN RFP has pre-empted any finding & recommendation on spectrum, but do not solve the problems

- Spectrum assignment one of the wholesale tools to address competition and costs, not a ‘market’ per se
- WOAN does not make interventions redundant
  - WOAN will face the same challenges as other challengers in establishing a competitive wholesale presence with few additional advantages
  - Will take time to establish and outcome is uncertain
- ITA conditions also do not make interventions redundant
  - Spectrum cap still enables the dominant two to secure more than 50% of the spectrum on offer (excluding the WOAN)
  - Reference Offer for site sharing does not occur at a regulated price
  - Three MVNO of their selection will not impose a broad retail market constraint but more likely to be niche
- ITA may make regulations more important
  - Dependency of Tier 2 to achieve an 80% coverage to meet the licence conditions will require dependency on site access and/or roaming agreements from the dominant two which have coverage already
- Currently no scope for community licensing

SITE ACCESS

Vast imbalance in facilities reduce incentives to share on reasonable terms & puts small operators in a weak bargaining position

- Evidence of constructive refusals / frustrated attempts to access
- Evidence that small operators face higher prices for access than larger operators & not reasonable when consider sharing the costs
- Narrow focus on sites & municipalities not appropriate
  - Miss backbone infrastructure, urban micro sites & forward looking to 5G
  - Bargaining power from collective facilities & negotiated at operator level
  - Likely to be mired in legal disputes
- Agreement that changes to facilities leasing regulation are needed
  - Should include stricter rules, cost-based price regulation for essential facilities, FRAND reference price for other & be at an operator level
  - Should also cover the potential option of deep passive sharing
- Facilities access will not undermine incentives to invest
  - many facilities were acquired historically and a fair return from users contributes to recoupment on that facility & funds for investment
- Rapid deployment around municipal wayleaves is a complement and not a substitute for facilities leasing & regulations

ROAMING

The national coverage of Vodacom / MTN & scale of sites is why they are essential roaming partners & what gives them bargaining power

- Competitive roaming is essential to be able to profitably service market whilst infrastructure is rolled out
  - Roaming charges higher than own & provider's effective retail prices & will get worse given small reductions in current contracts
- Narrow focus on municipal areas inappropriate
  - Roaming required where lack infrastructure & not where others dominant
  - On a forward-looking basis (to 5G), roaming may be required in urban areas to access capacity/technology until infrastructure catches up
  - Roaming negotiated at operator level where can select areas
- Mandated access is insufficient as access already exists. It is the terms of that access that is the problem incl. pricing
- Regulated roaming will not undermine the incentive to invest
  - Own sites are preferred & will strongly be so if better site access. Existing roaming has not deterred rollout
  - Recommendation for Retail-minus approach which won't encourage cherry picking & maintains incentive to rollout

MVNO/APN

DSMI found that MVNO activity in SA is inadequate but could deliver considerable benefit to consumers through retail innovation / differentiation, but is not a substitute for infrastructure competition

- Lack of competitive MVNOs in South Africa not a problem of spectrum but incentives & extends to APN seekers
  - Vodacom yesterday pointed to the lack of "surplus" capacity to host MVNOs – no incentive for hosting MVNOs where it is substitutive
  - Similarly no incentive to support APN customers competing for business
- WOAN is the medium-term solution to this issue but not a timely nor certain outcome
  - Roaming & site access cannot provide short-term resolution as this too will take time to change the market
  - ITA in current form unlikely to deliver on substitutive MVNOs
- Competition concerns & benefits to consumers means short-run interventions must be considered
  - Given WOAN will rely on MVNOs, Commission recommends MVNO access with a soft retail minus pricing condition

CONCLUSION

- There is overwhelming evidence that the SA market suffers from ineffective competition due to the skewed market structure which perpetuates dominance unlike other more evenly traded markets
- The ITA for spectrum & the WOAN won't fix this problem
- Robust wholesale regulation is essential to break the vicious cycle related to infrastructure quality & funding differences
  - Cannot afford to 'wait & see' as the next 5 years transition to 5G will shape the market for the next 15 years
- Solutions need to be at a national operator level, not municipal
  - Bargaining power is derived from the collective coverage & number of facilities not localised dominance
  - Roaming and facilities access are negotiated at an operator level
- Regulation must include pricing oversight even if there may be different benchmarks (e.g. retail minus, cost-based)
- Regulation requires full accounting separation in order to monitor wholesale pricing against costs

THANK YOU!

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