

Mobile mergers: complex connections?

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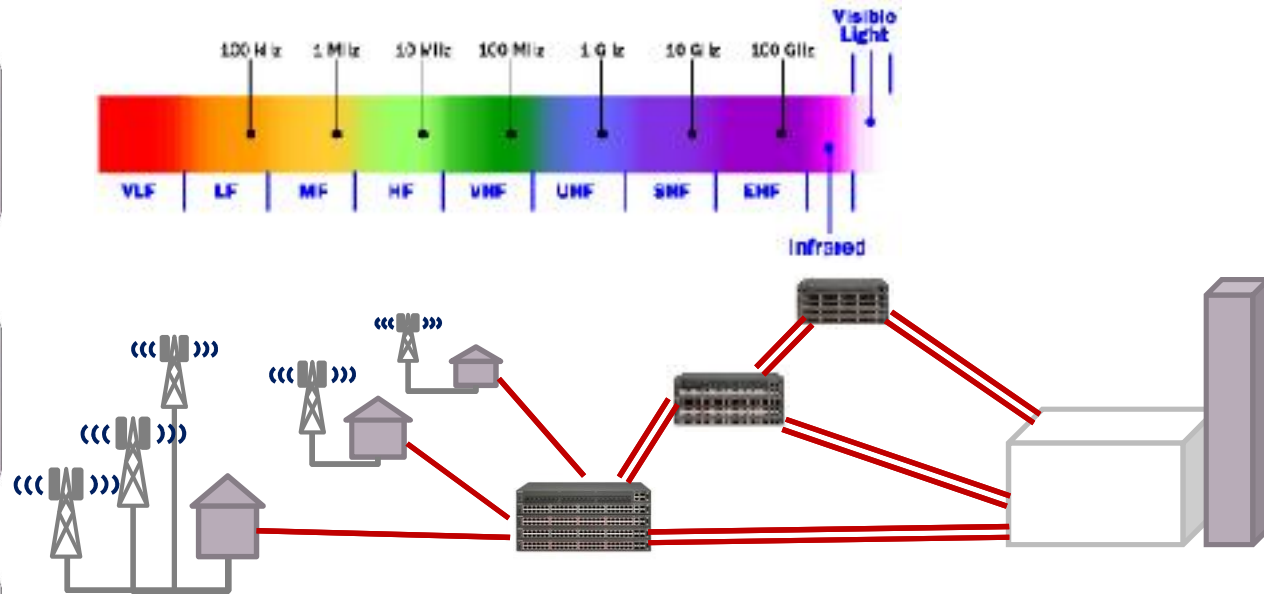
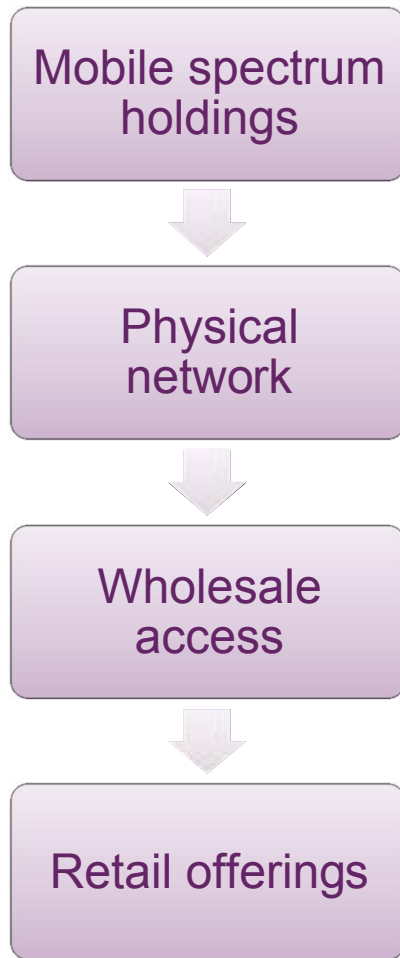
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Any views expressed in this presentation are my own, and not necessarily those of Ofcom, unless expressly stated. In particular, my comments about the issues that may be raised by mergers in the telecoms sector are intended to be general in nature, and not specifically related to the ongoing consideration of possible mergers in the sector. These mergers will be assessed by the relevant authorities on their specific facts, with input from Ofcom as appropriate.

Overview

- Introduction to mobile value chain
- Role of national wholesalers in retail competition
- Approach to analysis- every deal is different
- Some possible effects of mergers at different levels of value chain:
 - Direct effect on retail competition;
 - Impact on wholesale access for MVNOs;
 - Effect of spectrum consolidation on wholesale competition; and
 - Efficiencies and other considerations in network consolidation.

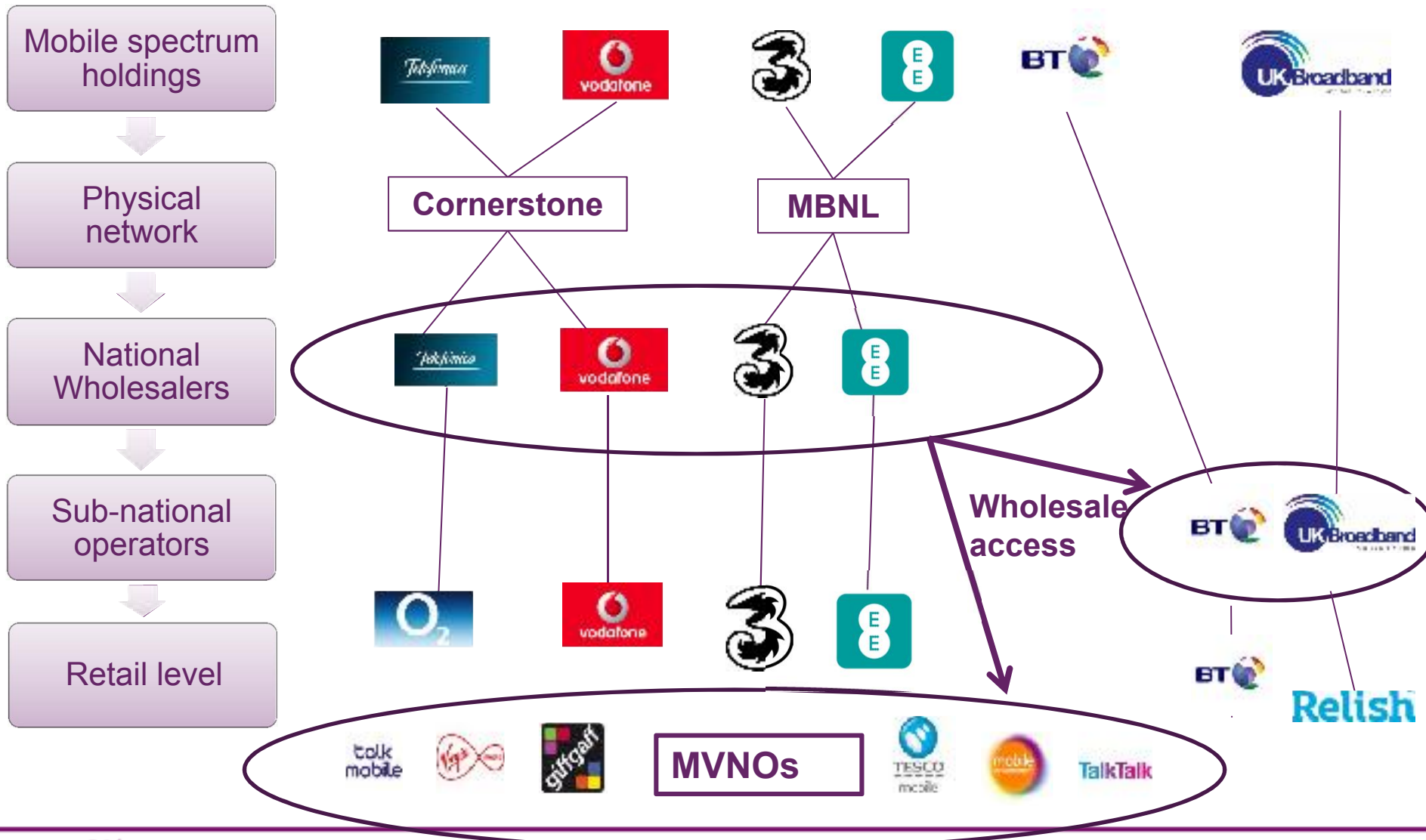
Mobile value chain - a simplified view



- National wholesalers provide network access to their own downstream arms as well as other retail operations



Mobile value chain - a UK illustration



What do we mean by a national wholesaler?

- A national wholesaler is an operator who controls wholesale access to a national network:
 - Must be capable of supplying access to their own downstream retail operations as well as other retail operators (sub-national operators, MVNOs)
 - Includes those who engage in network sharing but maintain independence as a wholesaler on a national basis
 - e.g. EE and Three have a network sharing agreement but compete against one another at the wholesale access level*
 - Must have minimum level of capability in key dimensions relative to rivals to provide an effective constraint (e.g. Coverage, average download speeds)

Competition between national wholesalers is important for retail outcomes

- Ofcom's experience to date has been that competition between national wholesalers has underpinned effective retail competition:
 - National wholesalers are typically vertically integrated and compete directly with one another at retail level;
 - Competition between national wholesalers allows MVNOs and sub-national operators to obtain wholesale access on terms that mean they can provide an effective constraint at the retail level.
- Mergers between mobile operators can affect competition between national wholesalers by:
 - Directly reducing the number of national wholesalers; and
 - Affecting the ability of rival wholesalers to exert an effective constraint post-merger
 - *Effect of spectrum consolidation*
 - *Impact on existing network sharing agreements*

However, every deal is different and requires a tailored approach

- Mobile operators have different business models and market positions
- They may be active at different levels of the supply chain and have existing relationships with other mobile operators or operators in related markets, adding complexity to transactions
- Not possible to provide an exhaustive list of possible theories of harm or comment on current mergers
- Instead provide an overview of some possible effects at different levels of mobile supply chain

Mobile mergers may have a direct impact on retail competition

- Mobile operators typically compete directly with one another at the retail level for subscribers
- The impact of this loss of competition can be assessed using standard horizontal merger tools:
 - Market share of merged entity
 - Closeness of competition
 - Removal of important competitive force etc.
- Some aspects of standard analysis may be complicated by features of the retail mobile market e.g.
 - How to treat different customer segments? e.g. business users, heavy data users
 - Application of pricing pressure tests- Which price? Which margin?

Reduction in competition between national wholesalers may affect wholesale access terms for MVNOs

- MVNOs rely on national wholesalers for network access
- A reduction in the number of national wholesalers could affect the terms on which MVNOs can obtain access, reducing the effectiveness of their constraint at the retail level
- Some relevant questions in thinking about this effect:
 - Do MVNOs target niche customer groups?
 - What options remain for MVNOs post merger?
 - Do these networks offer comparable quality in terms of coverage, capacity etc?
 - Are there any barriers to switching?
 - How might a reduction in choice of network affect bargaining power of MVNOs?
- Trend towards bundled offerings (e.g. mobile, landline, broadband and TV) may introduce additional lines of inquiry as markets evolve

Consolidation of spectrum holdings may also affect competition between national wholesalers

- Mobile spectrum is an essential input to the provision of mobile services and is also a scarce resource
- Consolidation of spectrum holdings could give the merged entity an unmatched advantage over other national wholesalers, causing a further weakening of competition between wholesalers
 - There are alternative means of adding to coverage and capacity (e.g. building sites) but these are expensive and may have limits
 - Very large share of overall spectrum may weaken ability of rivals to compete with merged entity in terms of coverage and/or capacity
 - *e.g. rationale for overall spectrum caps in UK 4G auction*
 - A large share of certain types of spectrum may also allow merged entity to offer services that rivals cannot match
 - *e.g. Orange/T-Mobile concern about early route to 4G remedied by spectrum divestment*
- Symmetry in spectrum holdings not necessary – at what level do concerns arise?

Impact of spectrum consolidation requires individual approach and detailed assessment

- Overall spectrum cap in 4G auction was intended as safeguard against risk of award leading to competition concerns
 - Intention was to avoid the effects of consolidation through the auction
 - We recognised that future mergers would be subject to scrutiny by relevant authorities
- Different spectrum holdings have different properties, requiring individual approach
- The impact of any consolidation will also depend on market context at the time
- Some relevant questions include:
 - What is combined share of merged entity mobile spectrum holdings?
 - Does the merged entity have an advantage in a particular type of spectrum?
 - Could merged entity do something with spectrum that others couldn't match?
 - How would this affect competition? Could rivals respond in other ways?
 - How is usefulness of spectrum holdings likely to evolve in the near future? (e.g. due to anticipated changes in devices available)

Combining physical infrastructure has the potential to deliver significant efficiencies

- Combining physical infrastructure may deliver various efficiencies e.g.:
 - Reduces site duplication (e.g. cost savings from investing in one new base station rather than two)
 - Can increase coverage (e.g. some sites may be uneconomic for single operator to cover)
 - May help address congestion issues (e.g. may be difficult to obtain planning permission in more congested urban areas)
- These efficiencies may lead to material benefits:
 - Physical infrastructure is expensive so potential cost savings are large
 - Consumers value coverage and capacity, so may benefit from improved quality

.....but need to consider other ways of achieving these efficiencies as well as potentially harmful effects

- Combining physical infrastructure through merger has the potential to reduce competition at the wholesale and/or retail level
- Network sharing can offer an alternative means of achieving network synergies without these potentially harmful effects

e.g. MBNL and Cornerstone allow mobile network operators in the UK to share physical infrastructure whilst still competing as distinct national wholesalers

- Combining physical infrastructure may have implications for competition:
 - Impact on existing network sharing agreements – could weaken competition between national wholesalers

E.g. In Orange/T-Mobile there was a concern over the impact of the merger on an existing network sharing arrangement with Three

- Reduction in coverage-based competition