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Overview – ICASA Discussion Document on priority markets in the electronic communications sector (March 2018)

Summary: The Discussion Document sets out the methodology used to identify three markets which ICASA believes it should prioritise for investigation for competitive failure. These markets are:

- *Wholesale fixed access, comprising fixed access services and the wholesale supply of asymmetric broadband origination;*
- *Upstream infrastructure markets for national transmission services and metropolitan connectivity; and,*
- *Wholesale mobile services incorporating mobile radio access network services and the wholesale supply of mobile network services.*

Comments – due by 2 April 2018 – are invited on the methodology and the markets identified. A set of questions posed in the Discussion Document is contained in Annexure A.

ICASA's approach to identifying markets

The following principles were followed:

- This is not an exercise of defining markets as required by section 67(4) of the ECA – it is a less rigorous identification and prioritisation exercise.
- Markets were identified through consideration of competition law, precedent and inputs from licensees.
- Identify broad rather than narrow markets so that the focus is on a set of related market segments.
- Use a layer model where (1) an upstream infrastructure layer inputs into (2) a wholesale network service layer, which inputs into (3) a retail services layer.
- Electronic communications facilities are not markets, so it is not correct to focus in this process on a facility or class of facilities.

ICASA's approach to prioritising markets

ICASA took the following steps to rank the identified markets according to priority:

- Competition-screening measures: an examination of (1) market shares and concentration – the number and size distribution of sellers – and (2) barriers to entry and expansion into a market (i.e. an assessment of the potential for competition to enter into a market).
    - Evidence shows that the higher the market share and the longer the period for which it is held the more likely there is to be a dominant player and possible abusive conduct.
    - The threat of entry by new competitors may by itself be enough of a constraint on the behaviour of incumbents in a market.
- Assessing importance of the market to consumers and government policy. The materiality of a market

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will also be a function of other factors such as the size of the market and its future importance. A market revealing ineffective competition will not be prioritised if the market does not have broader socio-economic impact.

- **It is more effective to intervene in wholesale markets** before considering intervening in retail markets. Intervening in wholesale markets allows a broader impact on downstream retail markets. This does not preclude intervening in retail markets if this is justified. It is not necessary to establish ineffective competition in a retail market before intervening in the upstream wholesale market.

What markets are there?

The table in Annexure A reflects the broad markets identified by ICASA and their inter-relationships.

Markets to be prioritised

ICASA's preliminary view is that three markets should be prioritised:

- Wholesale fixed access services;
- National transmission and metropolitan connectivity; and,
- Wholesale supply of mobile network services and RAN services.

Wholesale fixed access services (U4) and wholesale supply of asymmetric broadband origination (W6)

This refers to the provision of last mile connectivity in fixed networks. This includes:

- wholesale services that allow **access via the local loop** (the connection between a customer's premises and the nearest local exchange).
- wholesale services that allow **access via the terminating segments of leased lines**, used as inputs into downstream retail services such as leased line Internet access, MDNS as well as mobile services which require backhaul services from their RAN to their core network.
- downstream **wholesale supply of asymmetric broadband origination** via fixed access technologies allowing interconnection between the wholesale provider and its customer(s). This market includes any bitstream services used as an input for the provision of broadband internet access to the mass market.

ICASA notes that any regulatory action at the access level may take time to implement and yield results, and for this reason it is appropriate to simultaneously review the immediate downstream market for internet services given the priority placed on retail data services by government.

<u>Structural features of the market and likelihood of competition concerns</u>

- *Market concentration*: Telkom is the largest provider of wholesale fixed last mile access, covering access technologies used by the mass market and wholesale leased line access and both copper and fibre networks.
    - *Mass market*: predominant form of fixed broadband usage is DSL and this is likely to remain the

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case in the foreseeable future, despite its declining share of connections. FTTx is currently less than 5% of connections but growing. Fixed wireless was at less than 17% of connections in 2016. Telkom is the sole provider of last mile DSL connectivity offered through the IPC wholesale product (market W6)

  - *Leased line last mile access*: Telkom is also the largest provider of leased lines services in South Africa and the only operator with a ubiquitous access network.
  - Both markets are highly concentrated.

- *Barriers to entry and expansion*: high sunk costs and investment, considerable lead and deployment time, need for economies of scale, practical and regulatory barriers. Accepted that feasible in certain areas but not on a national scale. Accordingly, barriers for both markets regarded as high and non-transitory.
- *The likelihood of competition concerns*: the dominance of Telkom means that competition bottlenecks in last mile access are likely to exist. Issues raised include:
  - lack of close substitutes to the access infrastructure Telkom controls or the access services it provides;
  - inability of licensees other than Telkom to access passive fixed access infrastructure, such as ducts and poles;
  - risk of inefficient duplication of fixed access infrastructure through investments made by licensees other than Telkom, in a potential future wherein competitive access to passive infrastructure is possible; and,
  - lack of local loop unbundling and the lack of regulation of Telkom's wholesale fixed access services.

<u>Importance of these markets</u>

- Wholesale fixed access services form an important input into a range of downstream electronic communications. Access services are an important input and cost for operators.
- By prioritising this broad market for a market review there is the potential to have a positive and significant impact across a number of markets.
- The prioritisation of wholesale fixed access services would also contribute towards the broader government policy objectives of promoting broadband access in South Africa, for which wholesale fixed access services is a critical input.

National transmission (U2) and metropolitan connectivity (U3)

This refers to:

- wholesale provision of national leased line services providing high-bandwidth connectivity between distant locations within South Africa used by third parties to build their core networks; and,

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- the wholesale provision of connectivity between local sites within high-density urban and sub-urban areas and metropolitan points of presence, which are located within high-bandwidth ring-networks surrounding each metropolitan area in South Africa.

Structural features of the market and likelihood of competition concerns

- *Market concentration*: Telkom holds the largest market share by a considerable margin in national transmission and metropolitan services, and these are highly-concentrated markets.
- *Barriers to entry*: substantial capital investment and need for economies of scale, lead times for permissions. There has been entry by a number of players – generally easier at national long-distance level than at access level – but it is unlikely that any provider will be able to replicate Telkom's existing national and metropolitan networks. A significant number of routes are provided only by Telkom.

Importance of these markets

- These markets are fundamental to the ability of most providers to compete and the associated connectivity cost is a significant input cost across other markets.

Wholesale supply of mobile network services (U5) and RAN services (W3)

Structural features and likelihood of competition concerns

- *Market concentration*: Licensed MNOs are the only participants in both markets. Only Vodacom and MTN provide national roaming services (which requires national coverage). Vodacom and MTN control significant shares of the retail market for mobile services and have done so for some time. Concentration at retail level also indicates the likelihood of competition concerns in upstream wholesale markets.
- *Barriers to entry into or expansion within these markets* – such as access to spectrum and capital investment – are significant, naturally limiting the number of market participants and generating relatively high concentration levels. MNOs are all vertically-integrated into the retail market – which is also concentrated – and this limits the incentives of MNOs to introduce competitive wholesale markets. Competitive wholesale markets are necessary to create opportunities for non-MNOs to compete more effectively in the provision of certain mobile services at the retail level.
- *The likelihood of competition concerns at the wholesale level:*
    - Vodacom (approx. 12 000 sites) and MTN (approx. 11 000 sites) are the only two networks with national coverage, relied upon by Cell C (over 5 000 sites) and Telkom Mobile (2 663 sites) in order to provide competitive services nationally. There is limited competition between Vodacom and MTN for the provision of national roaming services. The dependence of Cell C and Telkom on Vodacom and MTN for national roaming services is likely to endure given the greater capacity of the incumbents to invest in future development.
    - MVNOs collectively control a smaller share of the retail market than Telkom Mobile. The competitive irrelevance of MVNOs in part reflects the absence of any competition at the wholesale level for the provision of wholesale inputs to MVNOs. Only Cell C provides wholesale

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services of this nature. Vodacom's and MTN's decisions not to contest for MVNO customers as evident from the lack of MVNOs on their networks suggests that there is limited incentive to do so.

- There is limited development of wholesale markets for mobile network services, particularly in respect of mobile data. Wholesale mobile network and mobile RAN services are key inputs into the provision of services in the retail market for mobile services. Therefore, the importance of ensuring competitive outcomes at the wholesale level lies in the potential this has for improving competition and reducing pricing levels at the retail level.

Importance of these markets

- Mobile is the primary and often sole mode of telecommunication available to most South African households, but there remains significant potential for growth in mobile broadband uptake. This demand gap suggests that many are not able to afford these services.

Government policy objectives

- Reducing the cost of mobile data is a key government objective.

Next steps

ICASA may elect to hold public hearings. The final output of this process is a findings document setting out a list of markets susceptible to s67(4) regulation and a list of priority markets to be subjected to s67(4) market reviews.

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Annexure A: Questions raised by ICASA in the Discussion Document

Question 1: In your opinion, is the above approach to prioritisation adopted by the Authority appropriate in identifying markets to be prioritised for future market reviews? Motivate your response by providing reasons and any supporting evidence or data, as far as possible.

Question 2: Do you agree with the Authority's responses to the above issues with regard to the guiding principles on the Inquiry and the Authority's incorporation of some of the elements of the EC test? If not, motivate your response by providing comprehensive reasoning thereof.

Question 3: Do you agree with the Authority's identification of the markets? Please provide separate reasoning for each market you propose to delete from or add to the list.

Question 4: Do you agree with the Authority's preliminary view to prioritise the Wholesale fixed access services markets (fixed access services and wholesale supply of asymmetric broadband origination) outlined above or should one or both be removed from the list? Please provide reasons for your response.

Question 5: Do you agree with the Authority's preliminary view to prioritise the National transmission and metropolitan connectivity markets outlined above or should one or both be removed from the list? Please provide reasons for your response.

Question 6: Do you agree with the Authority's preliminary view to prioritise the Wholesale supply of mobile network services and RAN services markets outlined above or should one or both be removed from the list? Please provide reasons for your response.

Question 7: Do you agree with the Authority's preliminary the view not to prioritise the above markets or should any of these markets be added to the priority list? Please provide separate reasoning for each market you propose to add to the list.

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Annexure B: Table of markets identified and their inter-relationships

Table 1: Summary of markets and vertical links between them

	Broad market	Downstream from	Upstream of
Retail			
R1	Retail supply of mobile services	W1, W2, W3	
R2	Retail supply of voice telephony at fixed locations	W4, W5	
R3	Retail supply of access to the internet from fixed connections	W6, W7	
R4	Retail supply of managed data network services	U1, U2, U3, U4	
Wholesale			
W1	Wholesale supply of mobile termination services	U1, U2, U3, U4, U5	R1
W2	Wholesale supply of international roaming services	U1, U2, U3, U4, U5	R1
W3	Wholesale supply of mobile network services	U1, U2, U3, U4, U5	R1
W4	Wholesale supply of fixed termination services	U1, U2, U3, U4	R2
W5	Wholesale supply of fixed call access, origination, and transit	U1, U2, U3, U4	R2
W6	Wholesale supply of asymmetric broadband origination	U1, U2, U3, U4	R3
W7	Wholesale supply of internet connectivity	U1, U2, U3, U4	R3
Upstream			
U1	International transmission services		All W, R4
U2	National transmission service		All W, R4
U3	Metropolitan connectivity		All W, R4
U4	Fixed access services		All W, R4
U5	Mobile radio access network services		W1-W3