ICASA
COST TO COMMUNICATE PRESENTATION

11 FEBRUARY 2014

ICASA TEAM

- Ms Nomvuyiso Batyi- Councillor
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CONTENTS

- Policy background
- How termination affects retail prices
- ICASA’s 2010 and 2014 regulations
- Conclusion

ICASA MANDATE

- ICASA is established in terms of the ICASA Act of 2000

- ICASA is mandated to:
  – regulate electronic communications, broadcasting and postal sectors in the public interest
  – Ensure affordable services of high quality for all South Africans.

ICASA MANDATE Continued

- Assign spectrum to licensees
- Issue licenses for electronic communications network services, electronic communications services, broadcasting services and postal services
- Protect consumers from unfair business practices and poor quality of services
- Enforce compliance with rules and regulations

BACKGROUND

- Government Policy is to ensure fair retail prices through promotion of competition
  - Competition Act of 1998
  - Electronic Communications Act of 2005

- Implementation of policy:
  - Evaluate bottlenecks to competition
  - Such bottlenecks are prevalent in supply chains, e.g. telecommunications, etc.

PRINCIPLES CENTRAL TO ICASA'S REGULATION

- Regulate in the public interest

- Facilitate and foster competition in the electronic communications and broadcasting sectors

- Encourage innovation in all sectors it regulates

PROMOTION OF FAIR PRICES UNDER THE ECA

- Authority may regulate prices :
  - Where there is a lack of effective competition in a particular market

- What must the Authority do?
  - Evaluate the value chain over which retail services are provided
  - Regulate to reduce bottlenecks to fair competition

HISTORY FROM 1993 TO 2010

- Benign regulatory regime supported high penetration of mobile services
  - Population coverage > 95%
  - Geographic coverage > 78%

- Time for change:
  - Need for greater competition
  - Need for lower prices
  - Increased regulation of termination rates

FROM NONE TO 1ST INTERVENTION

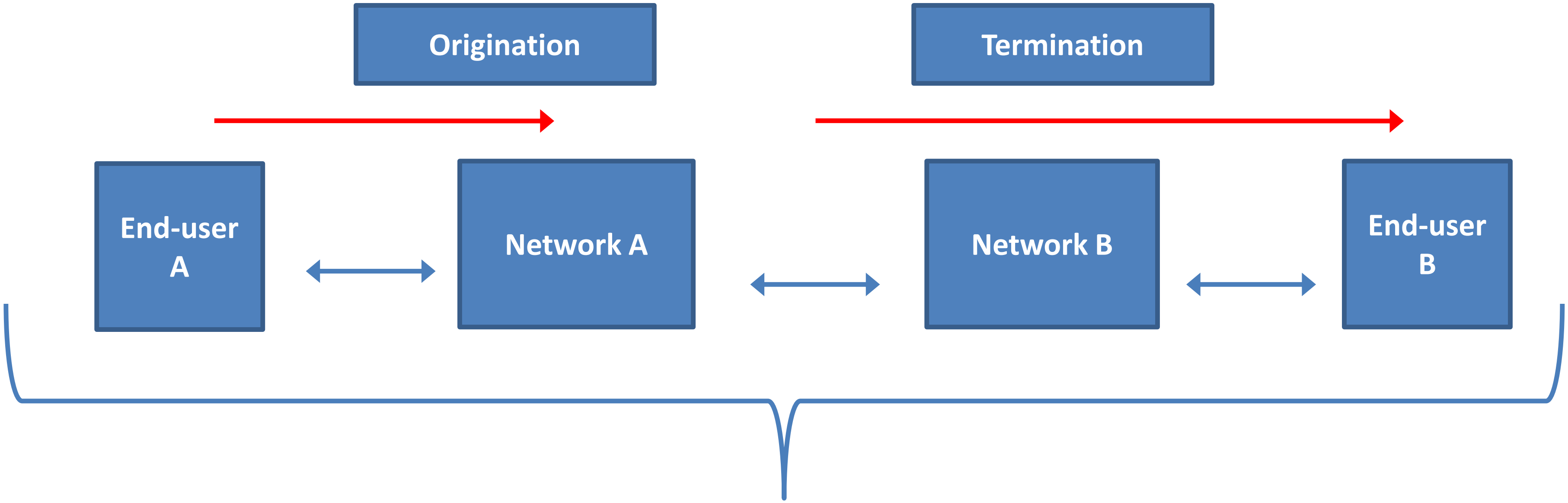
2007
- Findings document on Definition of Call Termination Market (GG 30449)

2008
- Stakeholder engagement on process for conducting market reviews

2009
- Requests for information for evaluation of effectiveness of competition (GG 32628)

2010
- Public consultation on draft regulations (GG 33121)
- Final regulations (GG 33698 29 October 2010)

On-net calls and termination

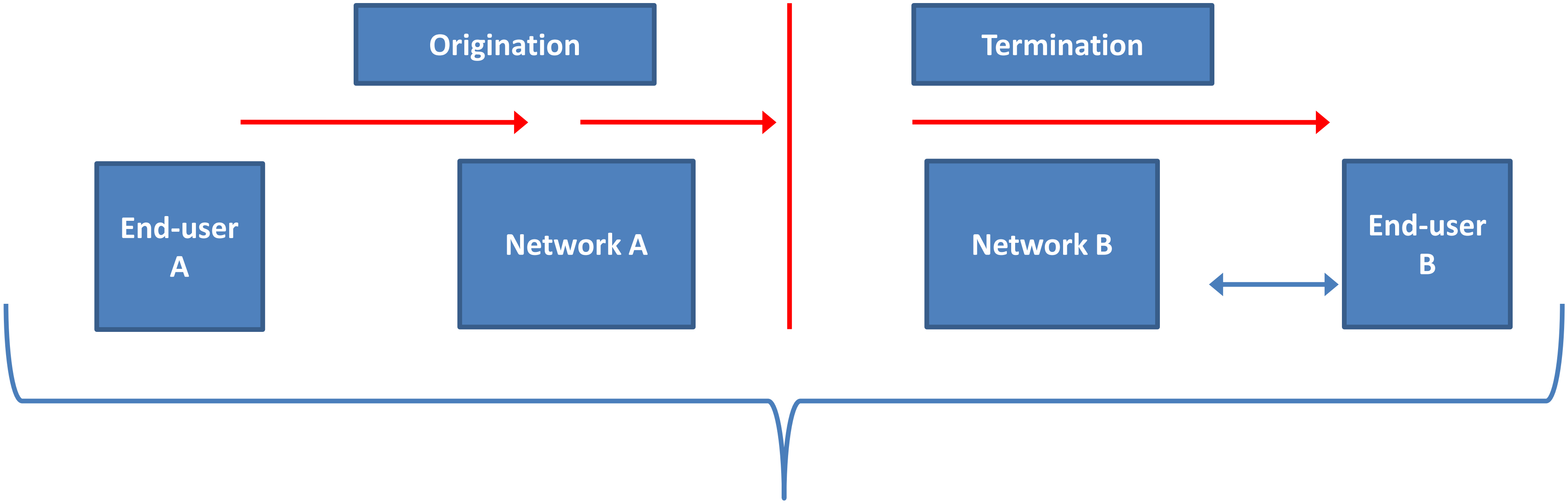


Step 1: End-user A starts a call to End-user B

Step 2: Network A routes the call through its own network to End-User B

Outcome: Network A completely controls retail price

Off–net calls and termination



Step 1: End-user A starts a call to End-user B

Step 2: Network A routes the call to Network B

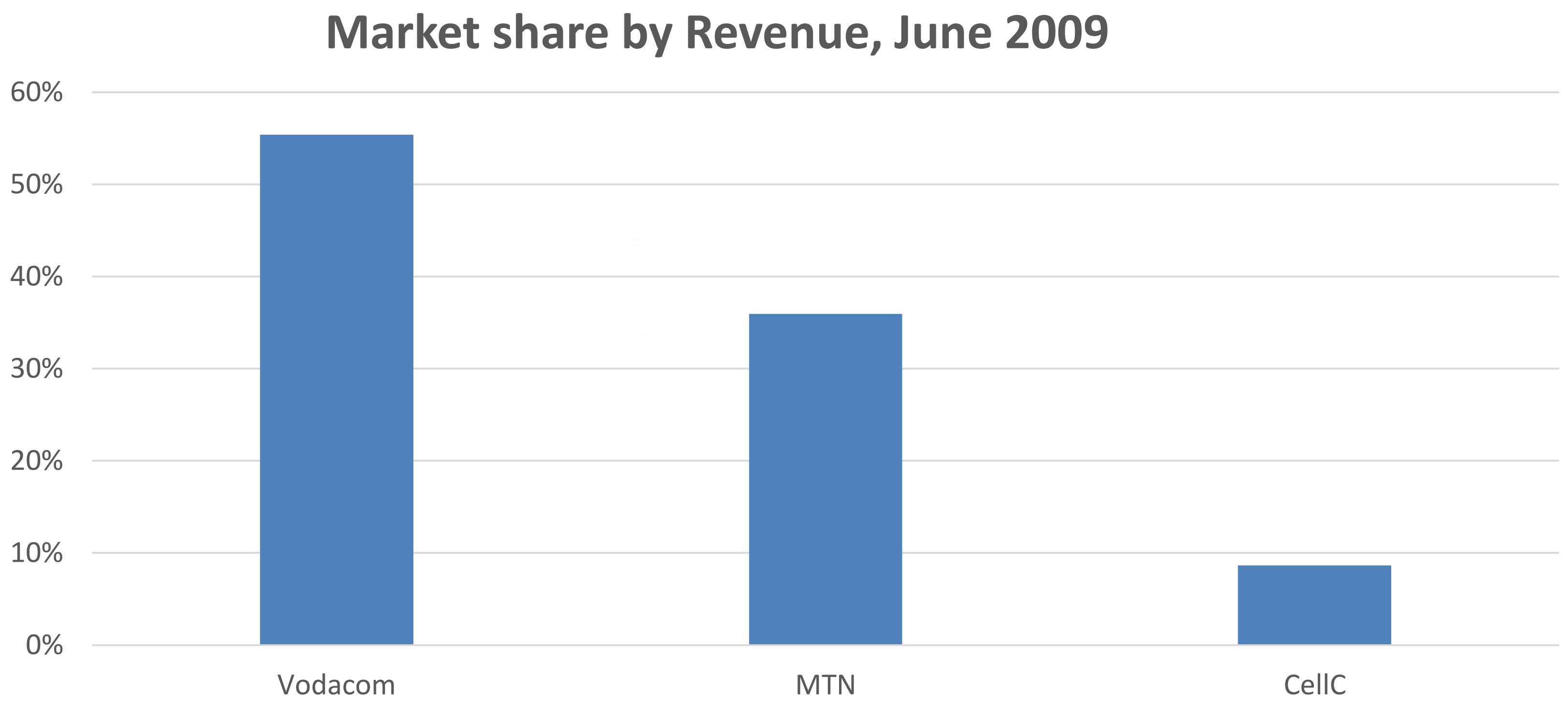
Step 3: Network B routes the call to End-user B

Outcome: Network B has an impact on the retail price

OFF–NET CALLS AND TERMINATION

Network B has an impact on the retail price …

- Network B charges Network A a Termination Rate
- This is a cost factor for Network A
- The higher the Termination Rate, the higher Network A's overall costs
- The retail price can never be lower than the Termination Rate – it acts as a "Price Floor"
- Lower costs make lower retail prices possible
- Lower Termination Rates allow challenger networks to drop prices to gain market share
- We have seen this recently, with 99c calling



This means:

- The market is ineffectively competitive
- Vodacom and MTN have countervailing bargaining power
- They can dictate the termination rate!

ICASA'S 2010 DETERMINATION

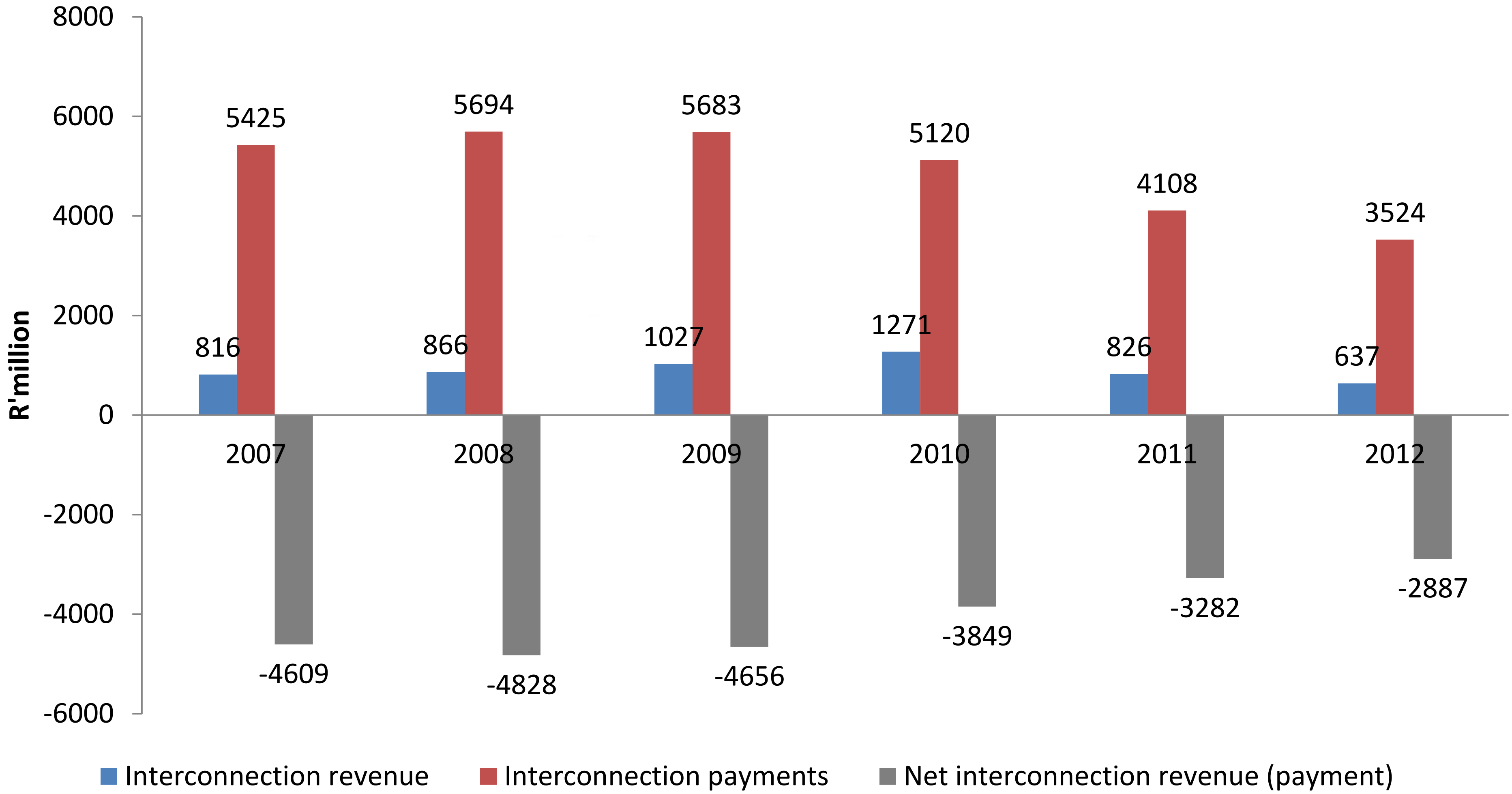
- Termination rates must be cost-based
- Vodacom & MTN must charge cost-based rates
- Asymmetry given to smaller players

	Rate	% reduction	Asymmetric Rate
Pre 2011	R 1.25		0%
Voluntary reduction	R 0.89	-29%	0%
March 2011	R 0.73	-18%	R 0.87
March 2012	R 0.56	-23%	R 0.64
March 2013	R 0.40	-29%	R 0.46

WHAT DID WE EXPECT?

- "The Authority expects the following to be visible outcomes of a reduction in wholesale voice call termination rates:
  - A reduction in the barriers to entry for competitors in competing for a broader spectrum of the retail market, i.e. smaller licensees are expected to move away from a pure niche retail market focus towards greater overall participation in the provision of services to all consumers;
  - A reduction in the price charged to an end-user for a voice call placed from a fixed location to a mobile location; and
  - An increase in dynamic pricing packages for voice calls between networks of licensees who offer termination to a mobile location."
- Reductions in the cost of doing business for operators

IMPACT OF RATE REDUCTION ON TELKOM



Telkom's net position has improved by 37 per cent based on the termination rate reduction

THE LINK BETWEEN WHOLESALE AND RETAIL RATES FOR OFF-NET CALLS

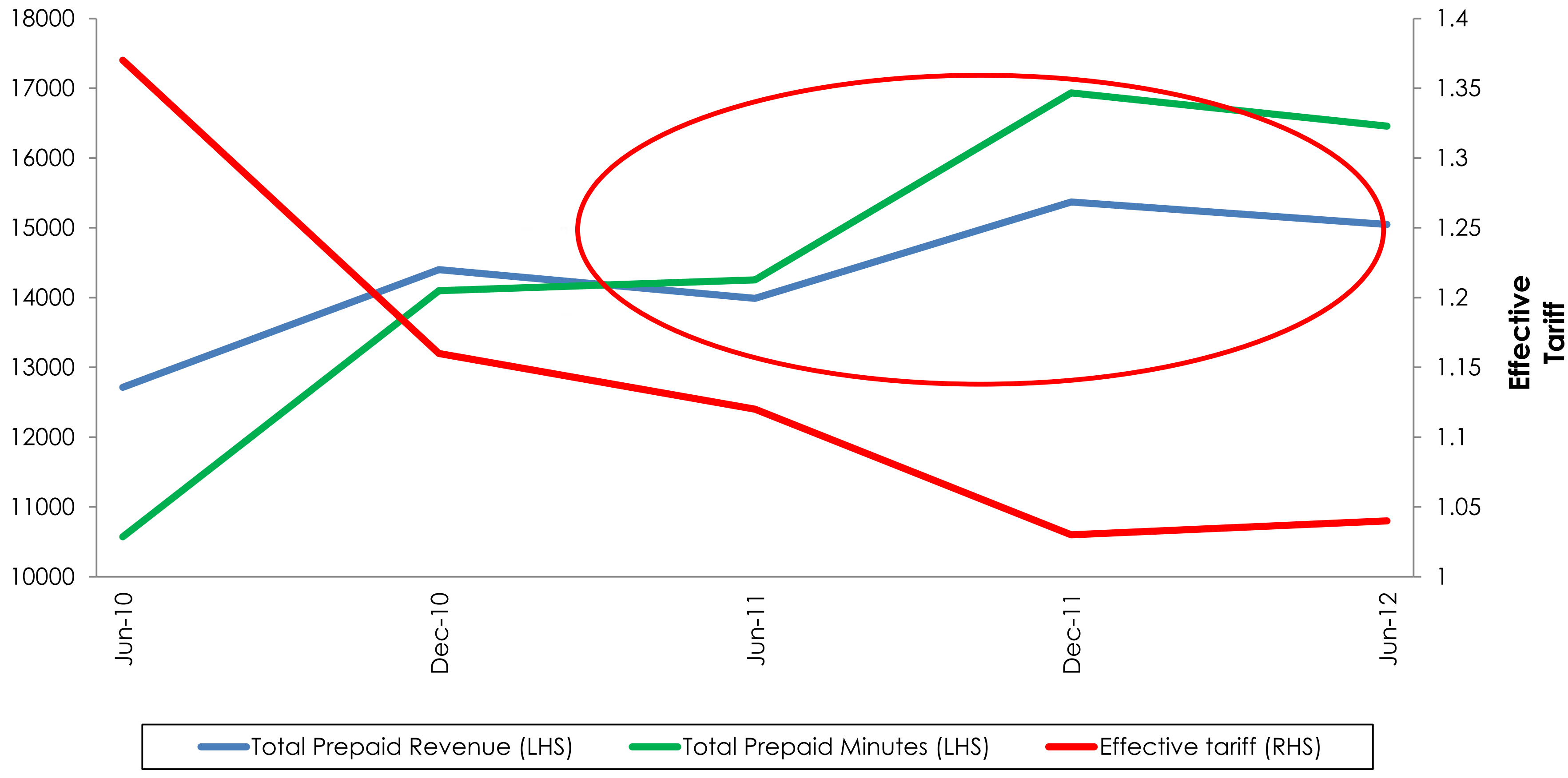
	Pre-2010	March 2011	March 2012	March 2013
Nominal Retail Rate per minute	R 2.50	R 2.50	R 2.50	R 2.50
Termination Rate	R 1.25	R 0.73	R 0.56	R 0.40
Margin	R 1.25	R 1.77	R 1.94	R 2.10
Less				
Origination (estimation)	R 0.60	R 0.60	R 0.60	R 0.60
Profit	R 0.65	R 1.17	R 1.34	R 1.50
% change in profit		80%	15%	12%

This benefit accrues to the smaller player as he pays lower termination rates

Only the smaller player has "regulated" pricing power

The increased profit margin makes room for price competition

Impact on Retail prices



Both consumers and mobile operators have benefited from the reduction in MTRs due to:

- **Operators: Increase in both termination minutes and revenue**
- **Consumers: Reduction in effective tariff per minute**

IMPACT ON RETAIL PRICES CONT'D

Telkom's reduction:

"Following notification from mobile cellular operators Vodacom and MTN in respect of a reduction of their Mobile Termination Rates (MTRs) as from 1 March 2010, Telkom has decided to give a 100% pass-through of this reduction to the Company's retail customers for fixed-to-mobile calls. This will see Telkom dropping its peak rate for fixed-to-mobile calls from 1 March 2010 by the full 36c resulting in Telkom customers now paying R1.475 per minute for conventional calls as opposed to R1.886 in 2009 (VAT inclusive rates). This will translate to a reduction of approximately 22% in fixed-to-mobile call charges for customers," said Nombulelo Moholi, MD for Telkom South Africa.

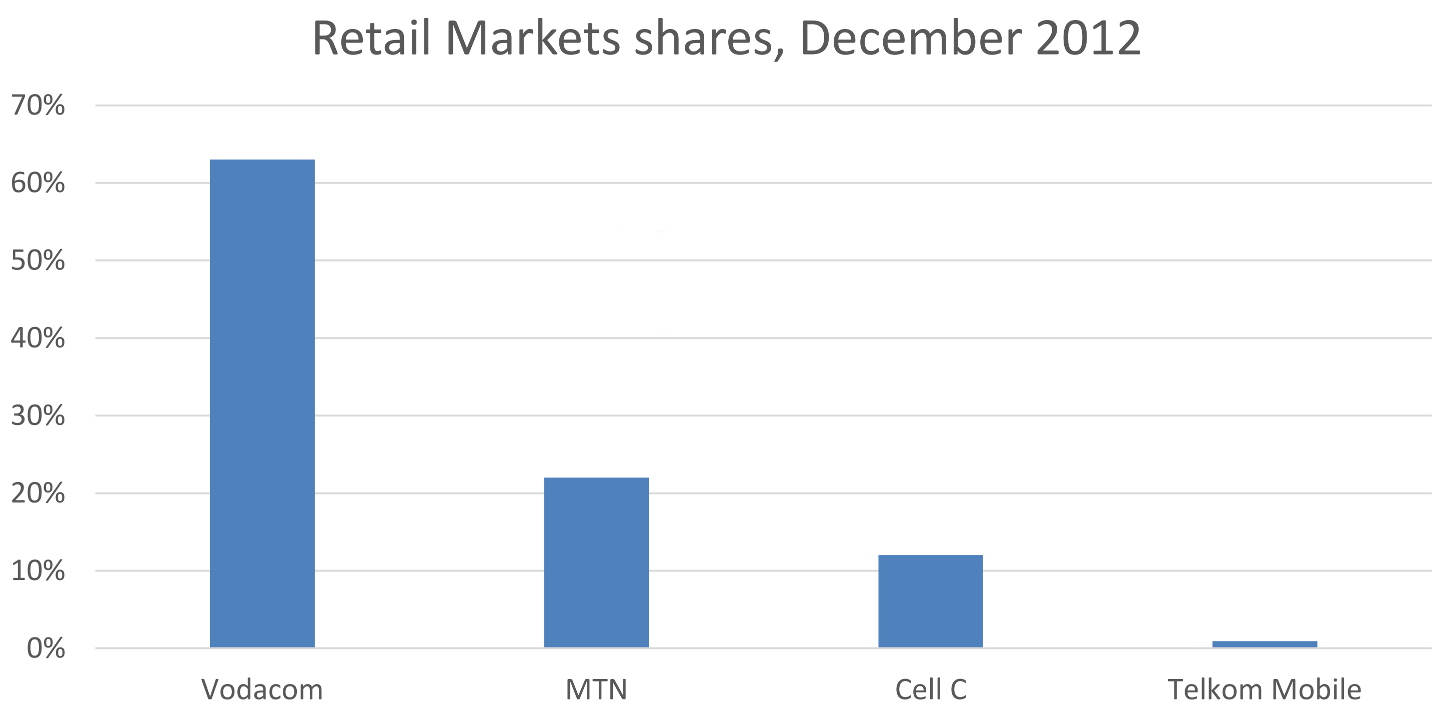
Press release on 16 February 2010

BUT

- Different operators behaved differently
- Fixed line operators reduced calls to mobile operators
  - Neotel dropped prices by 21%
  - Telkom dropped by 36c

- Mobile operators did not reduce calls to mobile operators
  - They never had a different call rate between mobile to mobile and mobile to fixed.
  - In essence a call to a fixed line represented profiteering and the failure to change this after 2010 when termination rate regulations were introduced is particularly stark

MARKET REVIEW AS OF 2012



Two major players still dominate the market

Termination Rates still represent a high cost of doing business

ICASA'S 2014 DETERMINATIONS

- Current rates do not adequately reflect costs
- Market remains ineffectively competitive
- Need to change termination rates, and
- Introduce greater asymmetry for a short period of time

THE NEW TERMINATION RATES

MTRs		FTRs	
Regulated Rate	**Asymmetric Rate**	**Regulated Rate**	**Asymmetric Rate**
		WON BON	WON BON
2014: R0.20	2014: R0.44	2014: R0.12 R0.16	2014: R0.13 R0.21
2015: R0.15	2015: R0.42	2015: R0.12	2015: R0.13
2016: R0.10	2016: R0.40	2016: R0.10	2016: R0.13
	2017: R0.20*		2017: R0.13*

*** Only for those with < 10% share of retail revenues in relevant market**

THE FOCUS OF 2014/15

- Excessive promotions make customer choice difficult
- Advertised tariffs never reflect the actual cost
- Vodacom's effective tariff is R 0.56 per minute! (December 2013 Quarterly Update)
- Vodacom effective tariff of 56c indicates that the majority of calls are originating and terminating at less than the regulated termination rate of 40 cents.
- This is an indicator of:
  - Possible Predatory pricing (Pricing below cost to gain market advantage)
  - The real cost of termination being far lower than what the rates are currently set at

PROMOTIONS

send a gift to anyone in South Africa! They'll receive 60 minutes talk time, 100MB data or 500 SMSs

1 hour on-net minutes, unlimited SMS to any network and 20MB data, from as little as R6.

Pay for the first 3 minutes of every call and get the rest of your call free, up to 1 hour

Get 60 minutes of FREE calls to Vodacom customers for 7 days from midnight to 5am

MTN ZONE
Mahala Nights (which now offers up to 100% discounts between 22:00 and 05:00) Mahala Day (offering up to 100% discounts between 06:00 and 18:00) on weekdays Mahala Weekend (offering continued discounted rates from Friday evenings right through to the end of the weekend).

EXAMPLES

- The average effective tariff per minute is R0.56
- However, promotions such as the “Vodacom Daily Free Calls” bring the call tariff down to as little as 6 cents.
- The “Everyday Extra” promotion brings the call tariff down to 23 cents.
- Both of these rates are significantly below the current termination rate
- Subscribers have no way of knowing beforehand how much they will be paying for a call.
- Some operators use “dynamic” tariffing which prices calls depending on location and time – they tell you a percentage reduction, not the actual Rand fee

THE 2014/15 PLAN

- ICASA intends to review the way tariffs and promotions are submitted to the Authority
  - On-net versus off-net pricing
  - Tariff transparency
  - Length of time of promotions

- The goal: Consumers will know what the cost of a call will be before they make it and this will allow them to make informed choices
- Removing the difference between on-net and off-net calls will improve competition
- Transparency will put downward pressure on prices, further reducing the Cost to Communicate

THANK YOU