

Competition as the necessary condition for good performance

a look at some successful emerging Asian markets

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Big picture*

- What if there is no or little competition?
 - Think about utilities and degree of competition
 - Monopoly?
 - State monopoly
 - Justified by political objectives than markets failures? [shortages, inequities, protect certain groups etc.]
 - Government failure [political interests, misallocation of resources, corruption etc. also, imperfect information]
 - Private monopoly
 - Natural monopoly
 - Duopoly, oligopoly?
- Now think about a utility with robust competition?



Big picture 2

- Can there be competition in every component of every industry/utility?
 - Vertically integrated monopolies
 - unbundling
 - Best practice: “Competition wherever possible, regulation where necessary”
- Competition in network markets
 - Competition in the market with a number of active players
 - Competition for the market through concessions won at competitive auctions etc.
 - Bottlenecks; access to backbone, undersea cable



Plan of presentation

- As a reflective practitioner some observations on competition being the **necessary**, but not **sufficient**, condition for **good performance**
 - Good performance is not only desired, but is prerequisite for equitable growth
 - Observations
 - India
 - Pakistan
 - Sri Lanka
 - Recap



Thesis

- Policy → Competition → ← Regulation →
Market innovation → Good performance



Good performance

Multi-dimensional. Must be win-win

Multiple stakeholders

multiple objectives

- Consumers
 - Easy **access** at affordable **prices** at acceptable **quality** of service and **choice**
- Operators
 - **Profitable** venture acceptable to shareholders
- Country
 - Contribute towards economic **development**; growth and equity

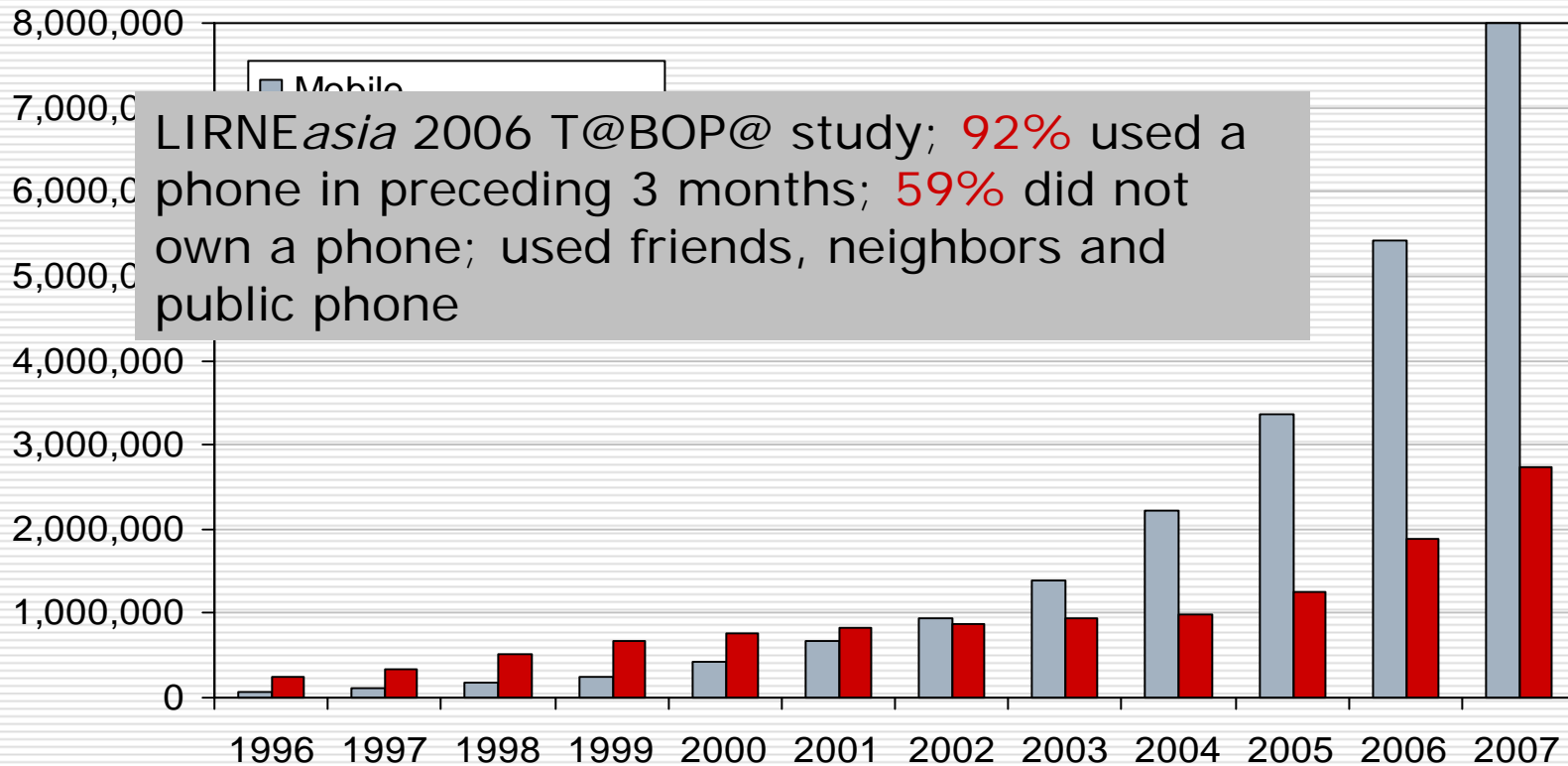


Sri Lanka

Good performance, or at least, on its way...

Consumers; easy access*

Sri Lanka population is 20m



Operators; profitable

Table 6: EBITDA margin

	2005	2006	2007
Dialog	52%	53%	46%
Mobitel	24%	39%	37%
Hutch	49%*	49%	49%
Tigo	50%*	50%*	50%

Note: * Estimated values

Source: company annual reports, press releases by companies

Source: LIRNEasia

- Dialog
 - Largest market capitalization on the CSE
 - Most profitable on the CSE



Country; important sector* *

Table 2.1

Sectoral Composition and Increase in Gross Domestic Product by Industrial Origin at Constant (2002) Prices

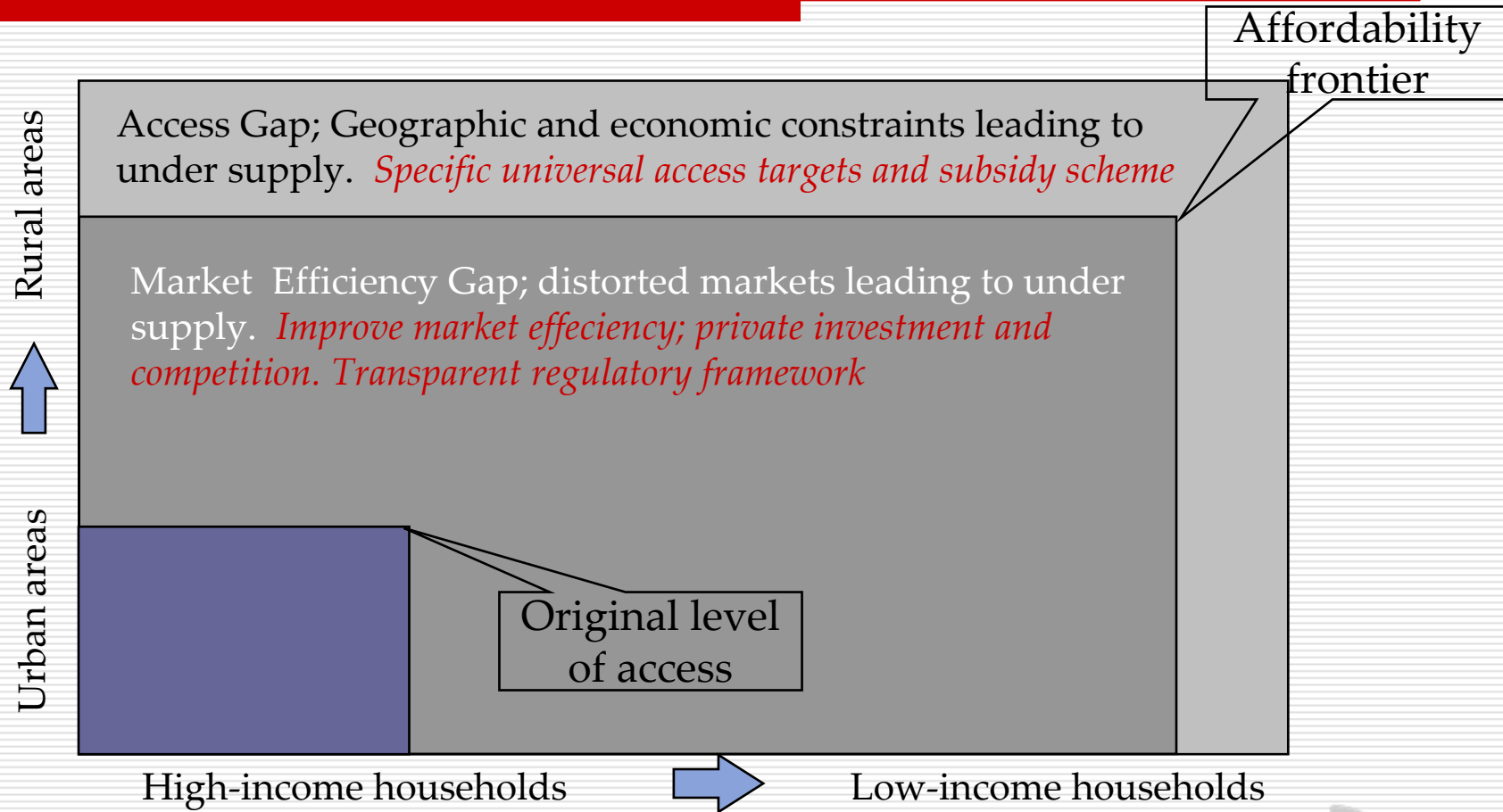
Sector	Rate of Change (%)		Contribution to Change in GDP (%)		Share of GDP (%)	
	2006	2007(a)	2006	2007(a)	2006	2007(a)
9. Transport and Communication	12.6	10.5	19.4	19.2	12.4	12.8
9.1 Transport	11.2	9.4	14.9	14.6	10.6	10.8
9.2 Cargo Handling, Ports and Civil Aviation	20.0	8.8	1.5	0.8	0.6	0.7
9.3 Post and Telecommunication	21.6	21.5	3.0	3.8	1.2	1.4
10. Banking, Insurance and Real Estate etc.	8.5	8.7	9.4	11.0	8.5	8.7
11. Ownership of Dwellings	1.1	1.1	0.5	0.6	3.4	3.2
12. Government Services	5.0	6.0	5.2	6.8	7.7	7.7
Sector	Rate of Change (%)		Contribution to Change in GDP (%)		Share of GDP (%)	
	2006	2007(a)	2006	2007(a)	2006	2007(a)
Agriculture	6.3	3.3	10.3	6.0	12.3	11.9
1. Agriculture, Livestock and Forestry	3.4	2.2	5.3	3.6	11.3	10.8
1.1 Tea	-2.0	-2.0	-0.4	-0.4	1.3	1.2
1.2 Rubber	4.6	7.7	0.1	0.3	0.2	0.2
1.3 Coconut	6.4	3.9	1.2	0.8	1.4	1.3
1.4 Minor Export Crops	2.2	5.1	0.1	0.4	0.5	0.5
1.5 Paddy	2.9	-6.4	0.7	-1.7	1.8	1.6
1.6 Livestock	8.1	7.9	0.9	1.0	0.9	0.9

How to drive towards good performance

Closing the **Market Efficiency Gap**

Market failures*

understanding reality. limits do exist

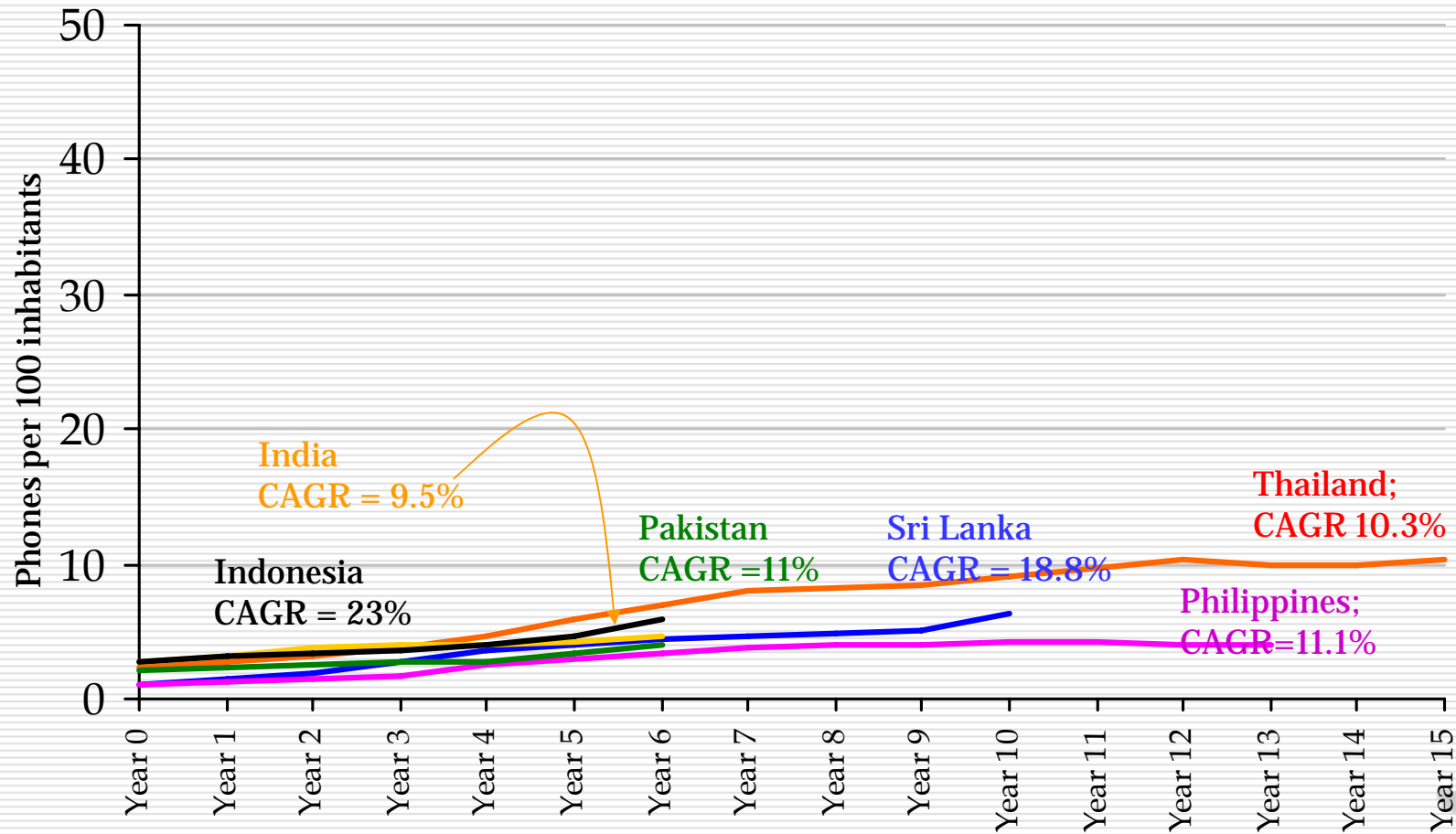


Closing the Market Efficiency Gap

Competition. Regulation. [Market innovation](#)

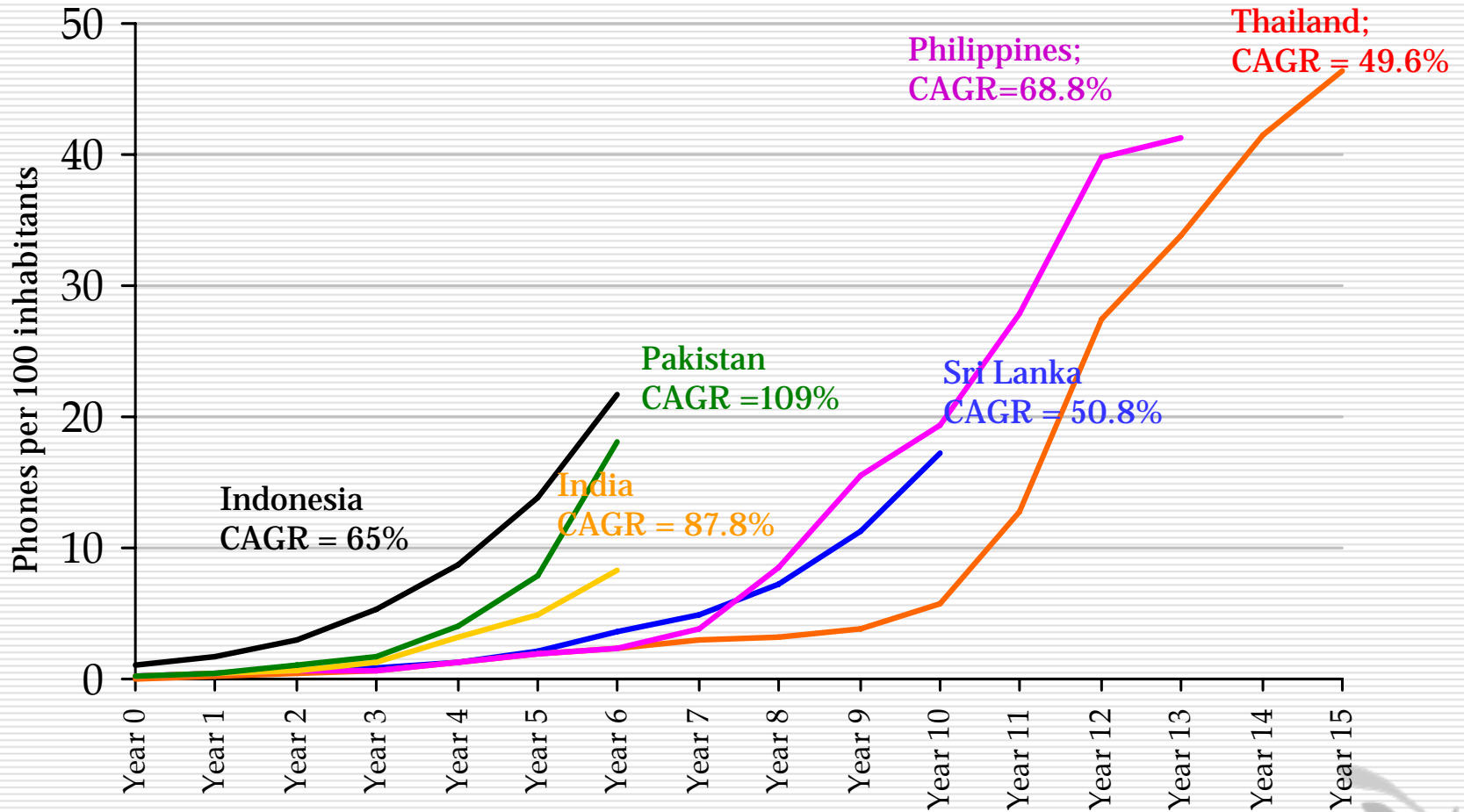
Fixed phones per 100 inhabitants

low competition



Mobile phones per 100 inhabitants

high competition



Theory vs. practice

unpacking the outcomes

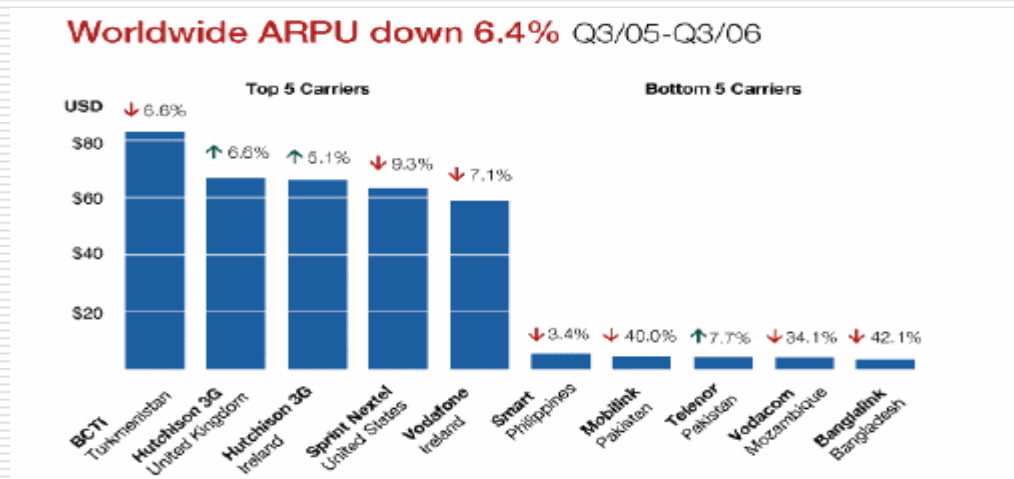
- **Competition** is key
 - High competition → high growth
 - The way in which effective competition came to being not as important as hypothesized
- Good **regulation** is important
 - But, better TRE is **not if and only if** condition
 - Work around solutions
- Text book sequencing of liberalization not as important
 - Establish regulator → open up sector → privatize incumbent
- In not so well governed countries; second, third best solution are still ok



Competition is a dynamic concept*

market innovation is crucial to survive in competition

- In this case, success lies in competing profitably in markets with majority 'poor consumers'



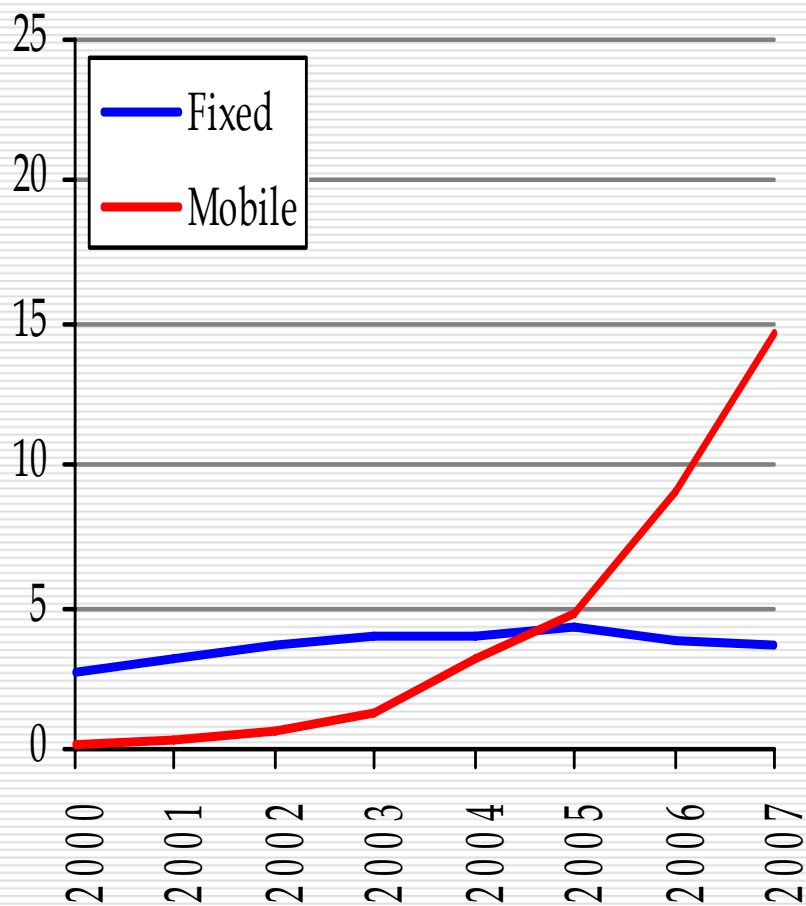
- Exploiting the long tail of the market [recent RS work]
 - Large number of small users; but large share
 - Also, small number of important large users



India

Strong commitment to competition in the mobile sector. **Innovation** by competitors.

Strong post-reform growth

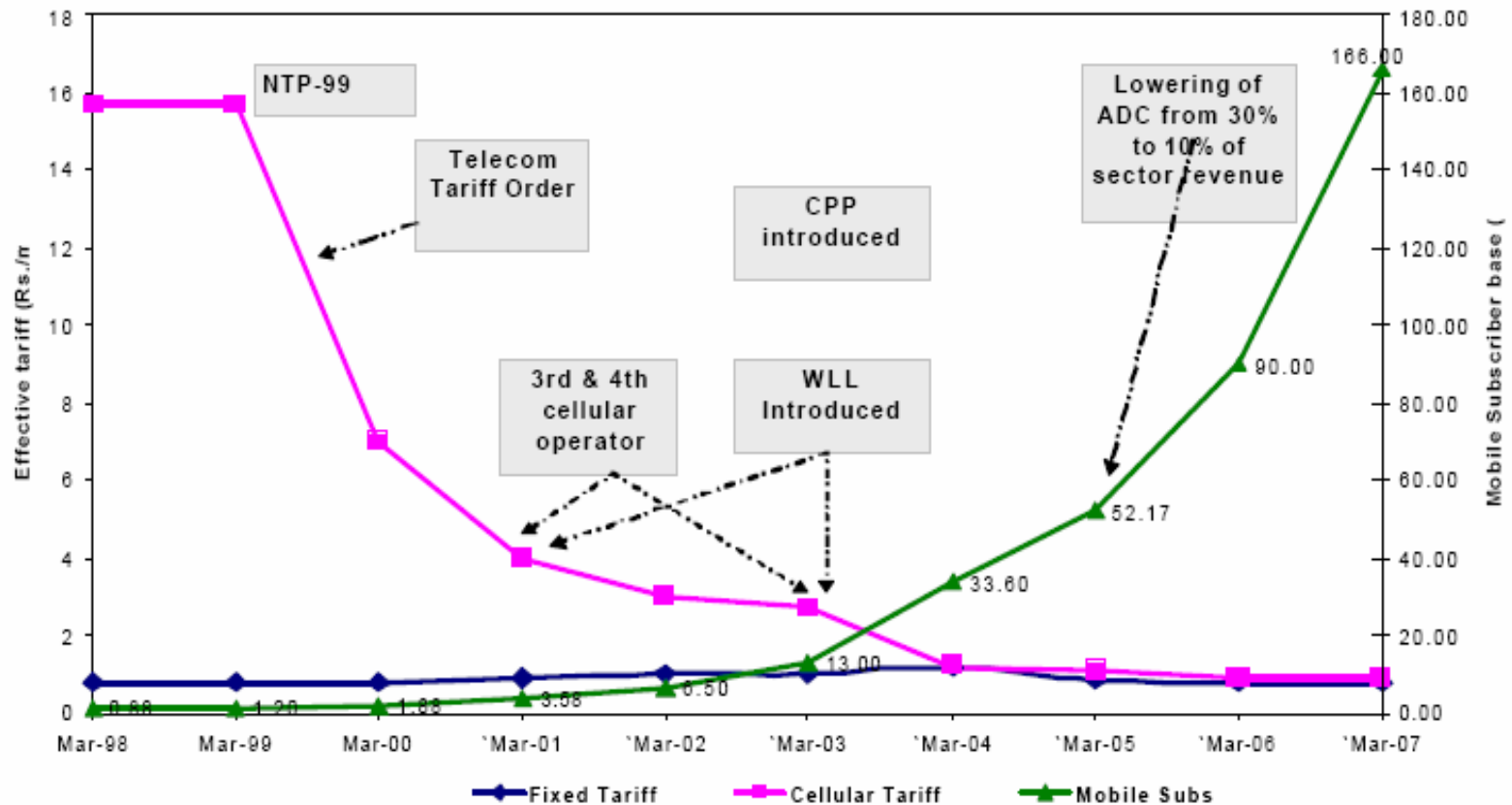


- False start 1995/96
- 1999 NTP
 - Strong Regulator
 - Renegotiate contracts
 - High fees → Rev share
- Fierce competition in mobile; market entry and price
 - Late 2002 forbearance of mobile tariffs → free fall
 - Not so in fixed. State dominance.
- Not 'textbook' sequencing of liberalization
 - No privatization except for partial in overseas carrier

Source: TRAI, COAI, AUSPI



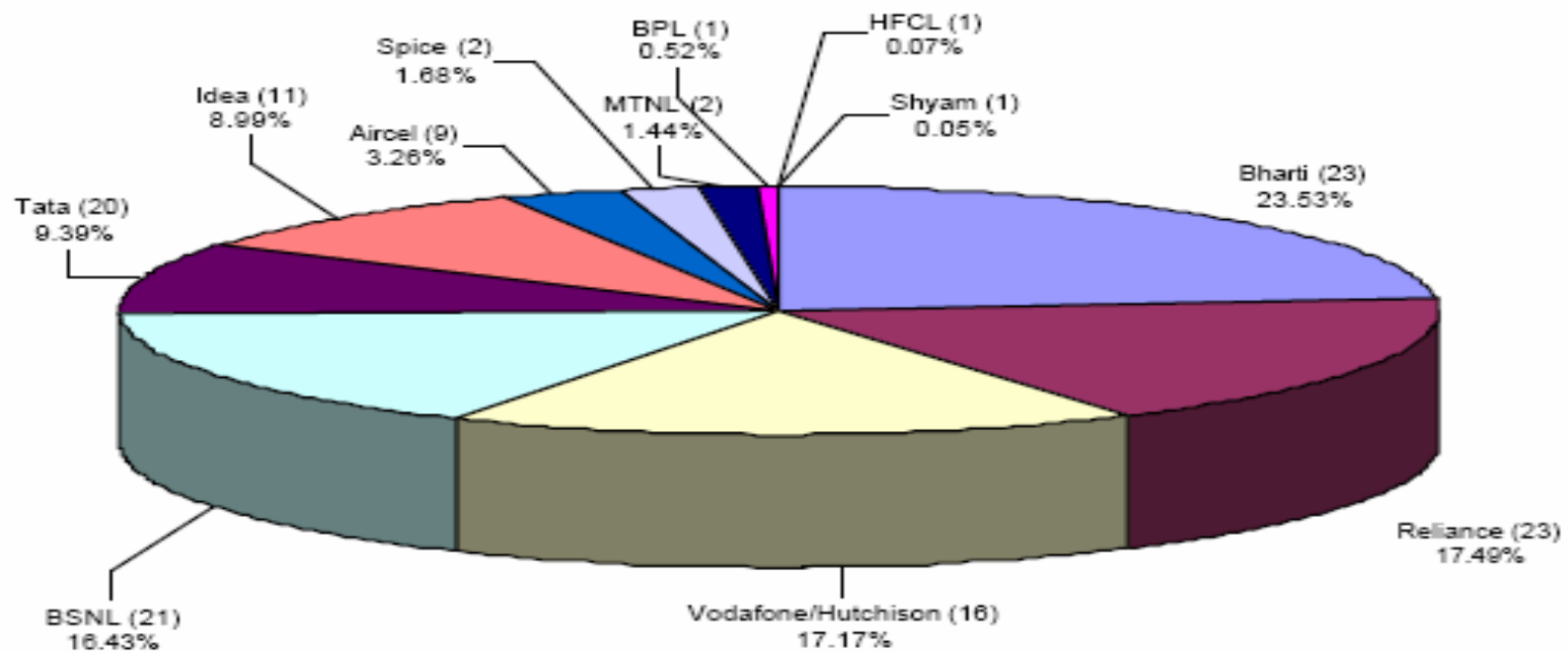
Key policy and regulatory initiatives



Fierce competition today

numerous players

Market share of the mobile operators as of March 31, 2007⁴²

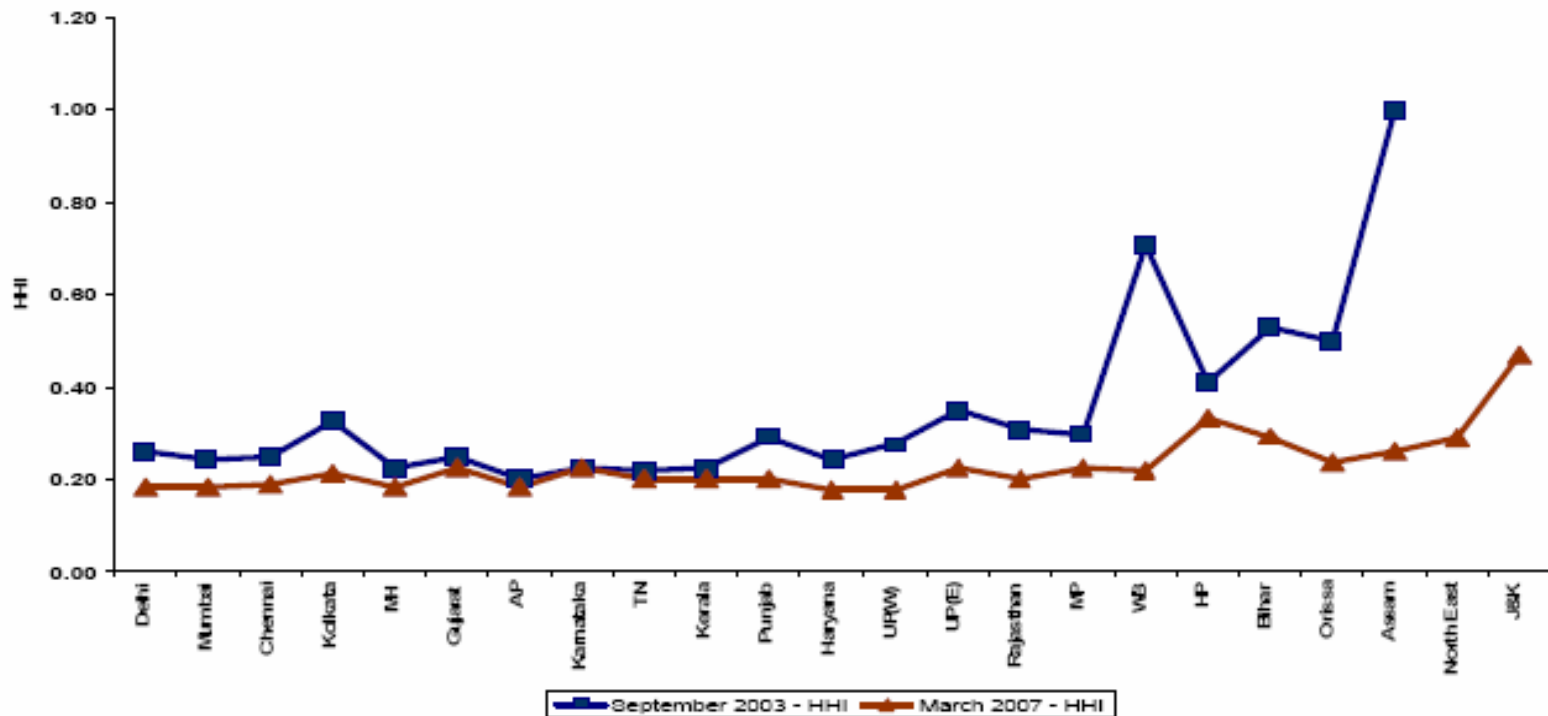


Moderately concentrated

Can improve, but how much?

Increasing competition 2003-2007

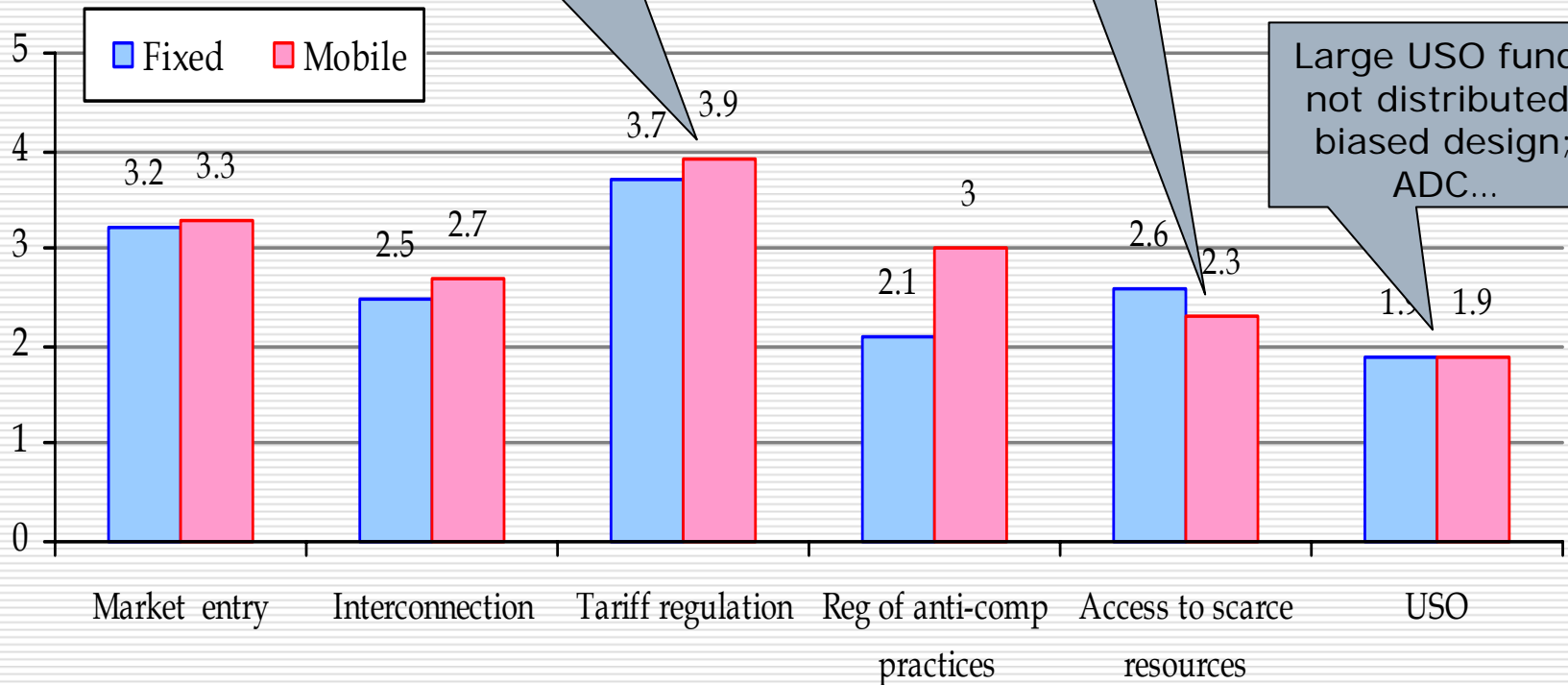
Comparison of Circle-wise HHI 2003-2007



Reasonably good T

Best region

tariff regulation



Market driven innovations*

Demand-side

- Remember, competition is a dynamic process
- “Once competition was established, which was a necessary condition for the growth of the sector, the market took over. New entrants eager to expand their market shares by increasing their pie and not just by eating each other’s market shares offered alternatives to standard services.”
 - Payal Malik, India Country Study for Nokia, LIRNEasia and CONNECTasia, 2008



Competitive business model

Malik study

- In the monopoly era [certain] consumers were deterred from obtaining a phone due to different factors
 - Affordability
 - High installation charges
 - High rentals
 - Uncertainty
 - Fear about building up large bills and of incurring debt



Competitive business model...2

Malik study

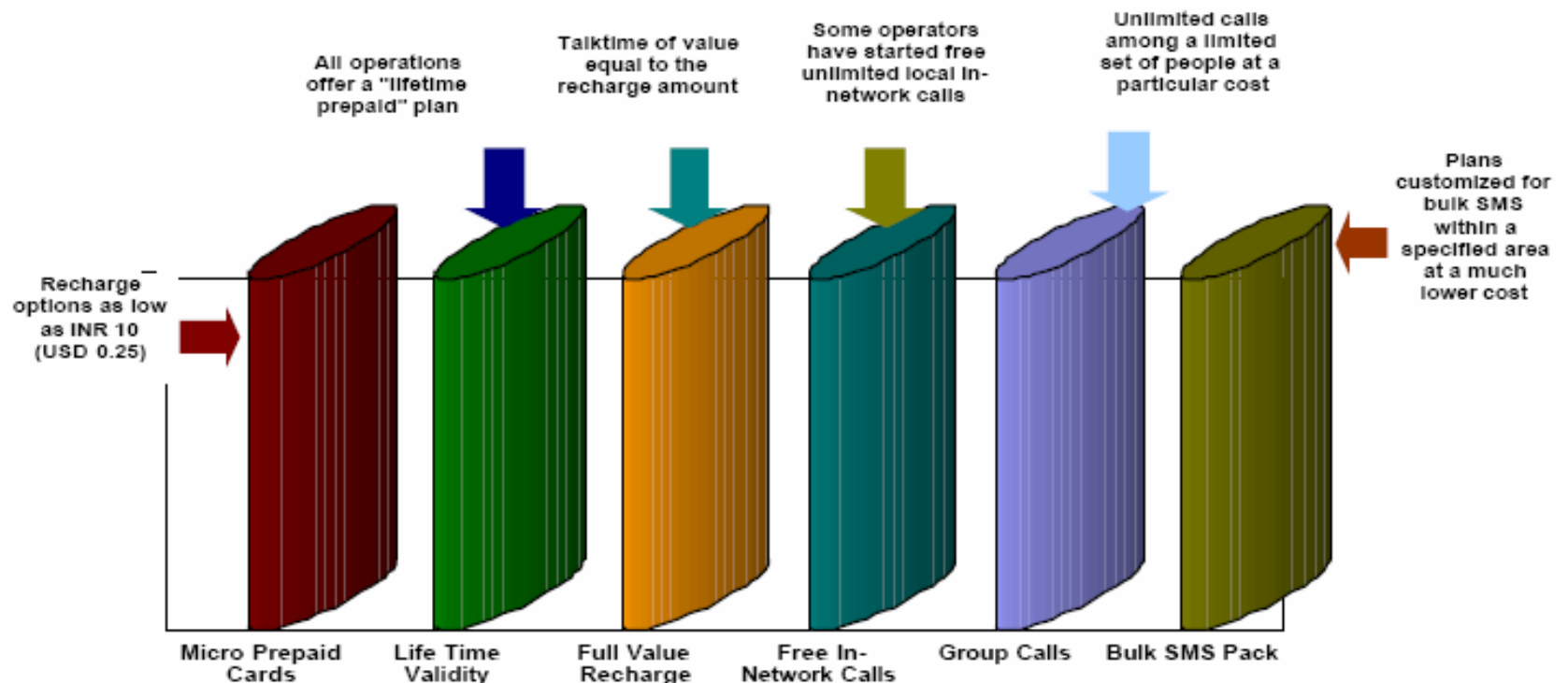
- “Consequently, after liberalization... service providers realize[d] that options need to be offered to consumers that are differentiated by service quality and price enabling [them] to select the option most suited to [their] needs.”
- Understanding demand
 - More on this later...
- As the Market Efficiency Gap becomes smaller, so will the spending capacity of each new subscriber → declining ARPU



Competitive business model...3

Malik study

Market Response to a consumer with low affordability



Competitive business model...4

Malik study

Keeping costs low

■ Innovations

- Shelter-less base stations
- Auto-provisioning of subscribers
- Over-the-air SIM card charging
- Incorporating adaptive multi-rate [AMR] codec etc.

■ Outsourcing [Example Bharti Airtel]

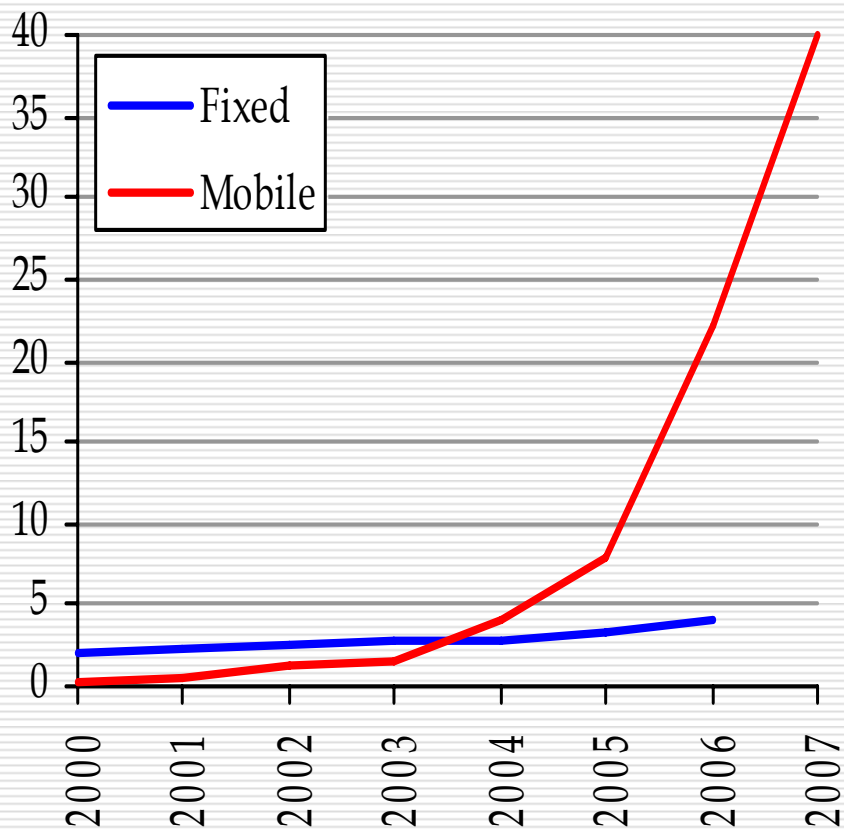
- Network outsourcing agreement with Ericsson linked revenue growth with network expansion
- IT outsourcing with IBM



Pakistan

Strong commitment to competition.
Aggressive FDI led growth

A text-book case of liberalization



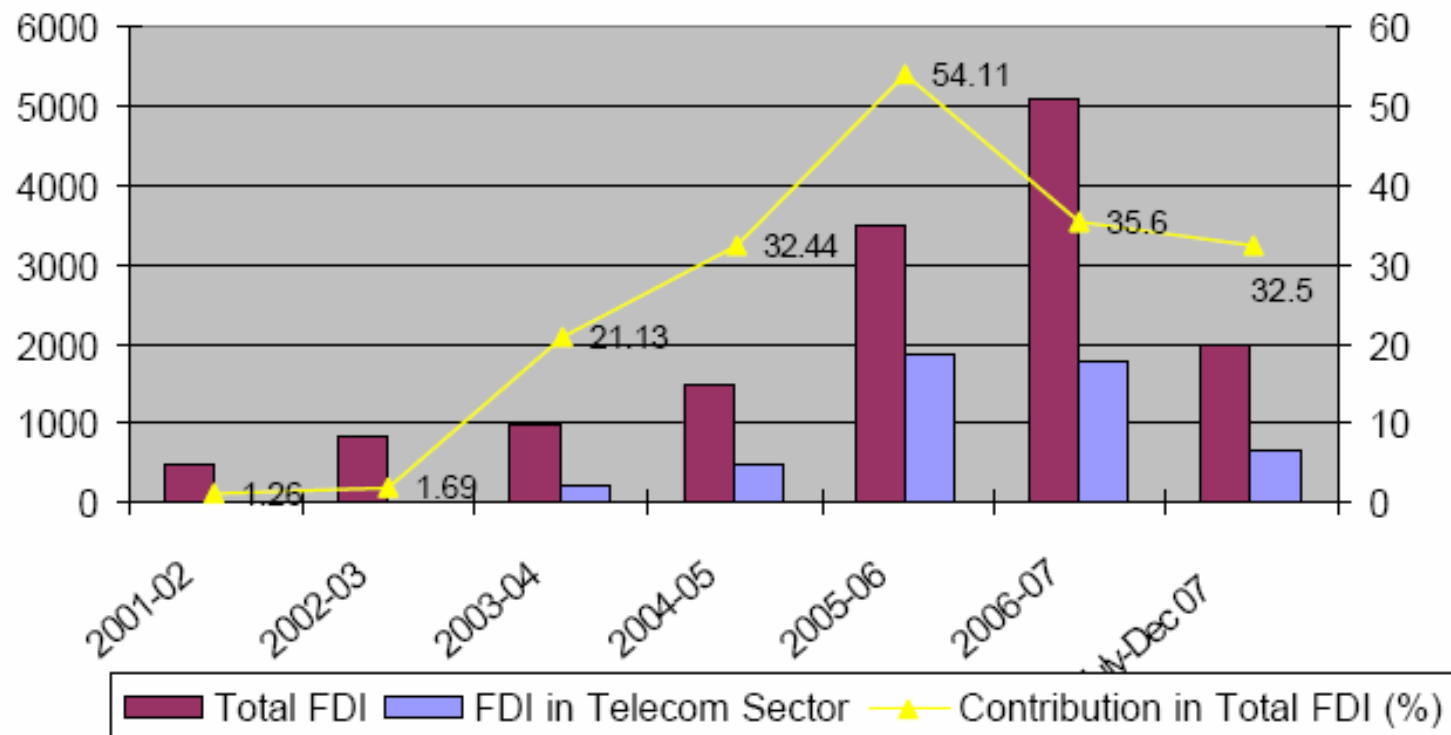
Source: PTA

- Liberalization more along the lines of text book; regulator established, competition increased, incumbent privatized
- Strong competition in mobile sector post 2003 reform
 - 2005 entry of 2 players
 - 6 players, 100% foreign ownership allowed
 - Massive FDI in to sector
- Fixed still 98% incumbent
 - Recently privatized, spike after WLL entry 17 licenses issued, 4 operational [now 9]
- Effective and transparent regulation; credibility
 - Mobile Number Portability, 2007

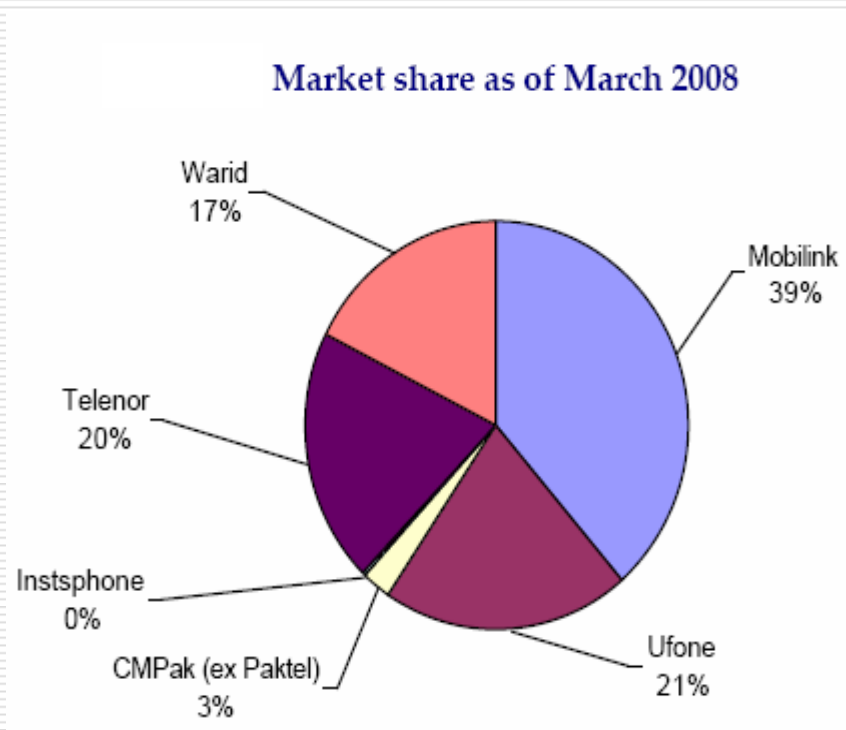


Massive FDI triggered by liberalization

Total FDI and its Share in the Telecom Sector



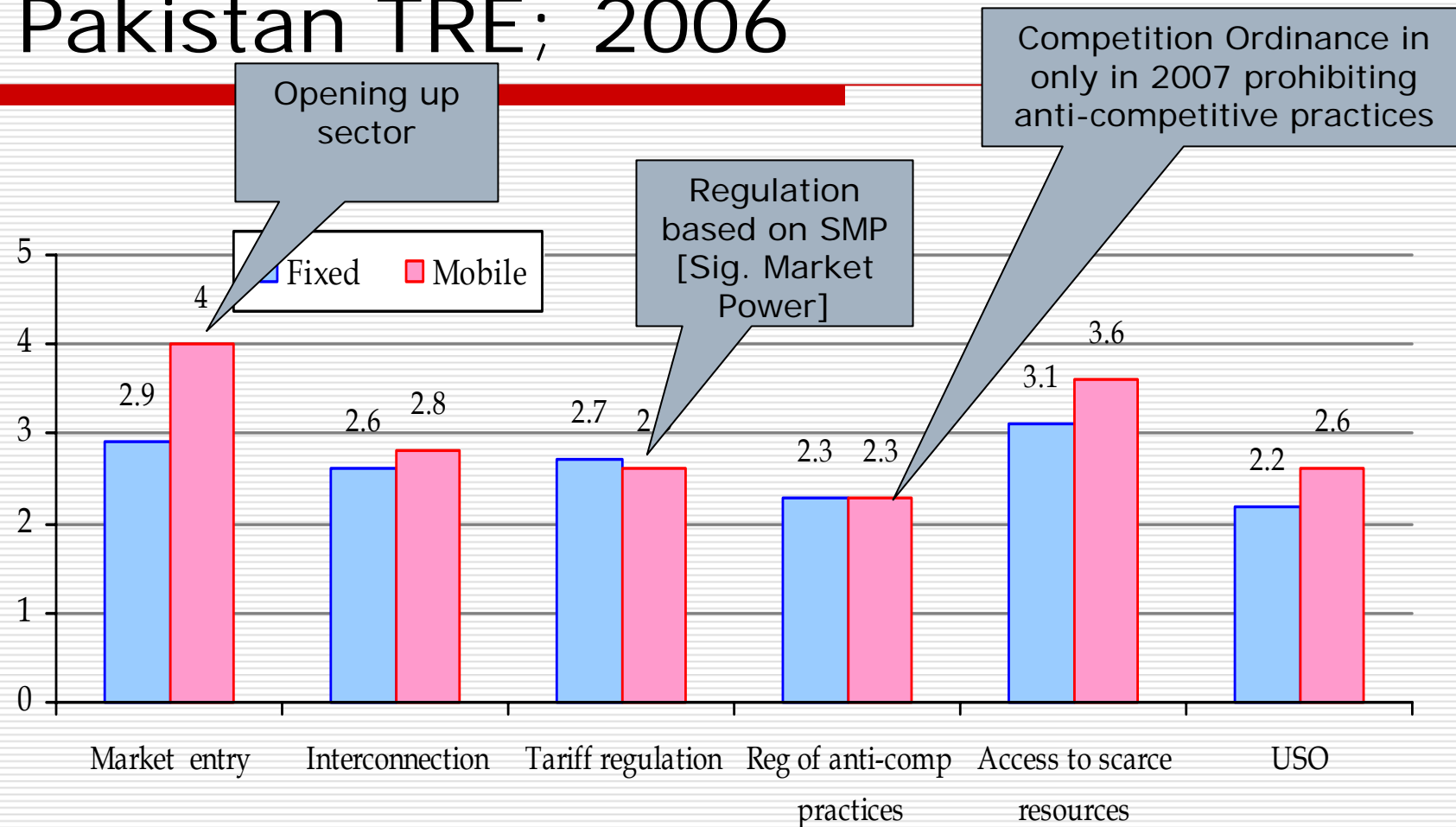
Increasing competition



- Continuing competition through mergers and acquisitions; 2007
 - China Mobile 100% of PakTel
 - Orascom in Mobilink
 - SingTel 30% of Warid
- HHI = 2,660; still high concentration, more room for competition [$1/\text{HHI} = 3.8$]
 - Aggressive strategy by CMPak launching ZONG in April 2008
 - Largest mobile operator in the world [380m]; 1st overseas investment
 - Bring in technical expertise and equipment
- ARPU
 - 2002: USD18. 2006: USD4



Pakistan TRE; 2006



But, India-Pakistan politics! * *

- Overheard recently
 - “A call from Lahore to New York [a distance of 15-hour flight] costs Rs.1 per minute, while a call between Lahore and Amritsar [a distance of 15-minute flight] costs a whopping Rs. 9 per minute in either direction!”
 - Nothing to do with competition!!

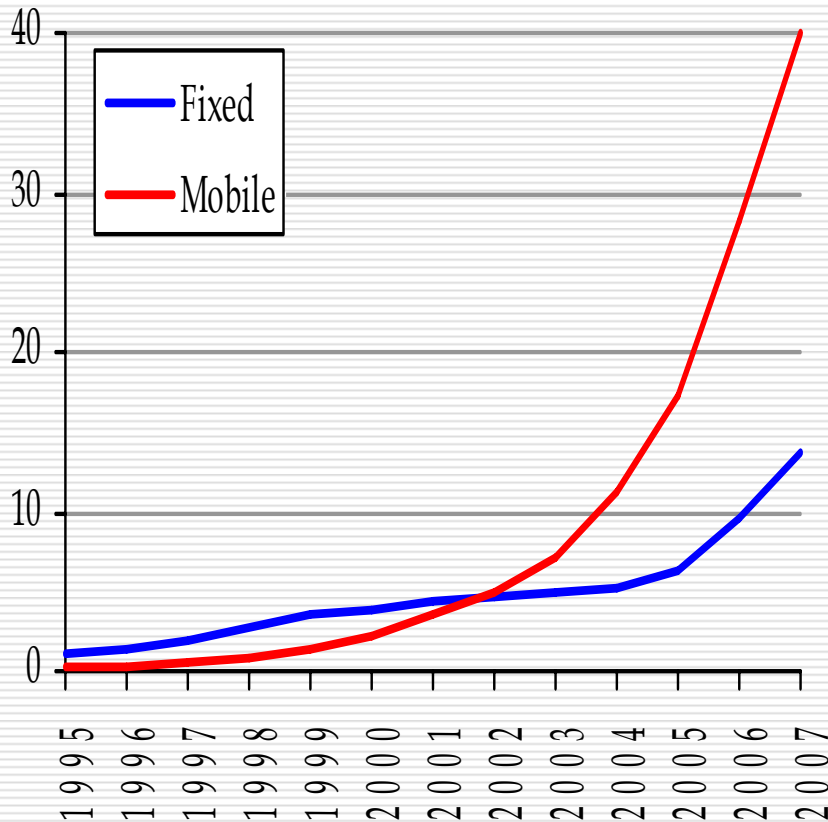


Sri Lanka

Strong commitment to competition.
Enough space for a **disruptive
competitor**

Surge in competition

internal dynamics



- Competition driven growth; Mobile and fixed WLL
 - Fixed: 2 WLL licenses 1996
 - Growth spurt
 - CDMA frequencies 2005
 - 4 mobile operators
 - 5th and 6th; but...
 - Let “sleepy” also ran → “disruptive competitor” 2006
- Liberalization not follow ideal sequencing
 - All mobile operators present when proper regulator set up
- Regulatory regime generally good, but unresolved issues



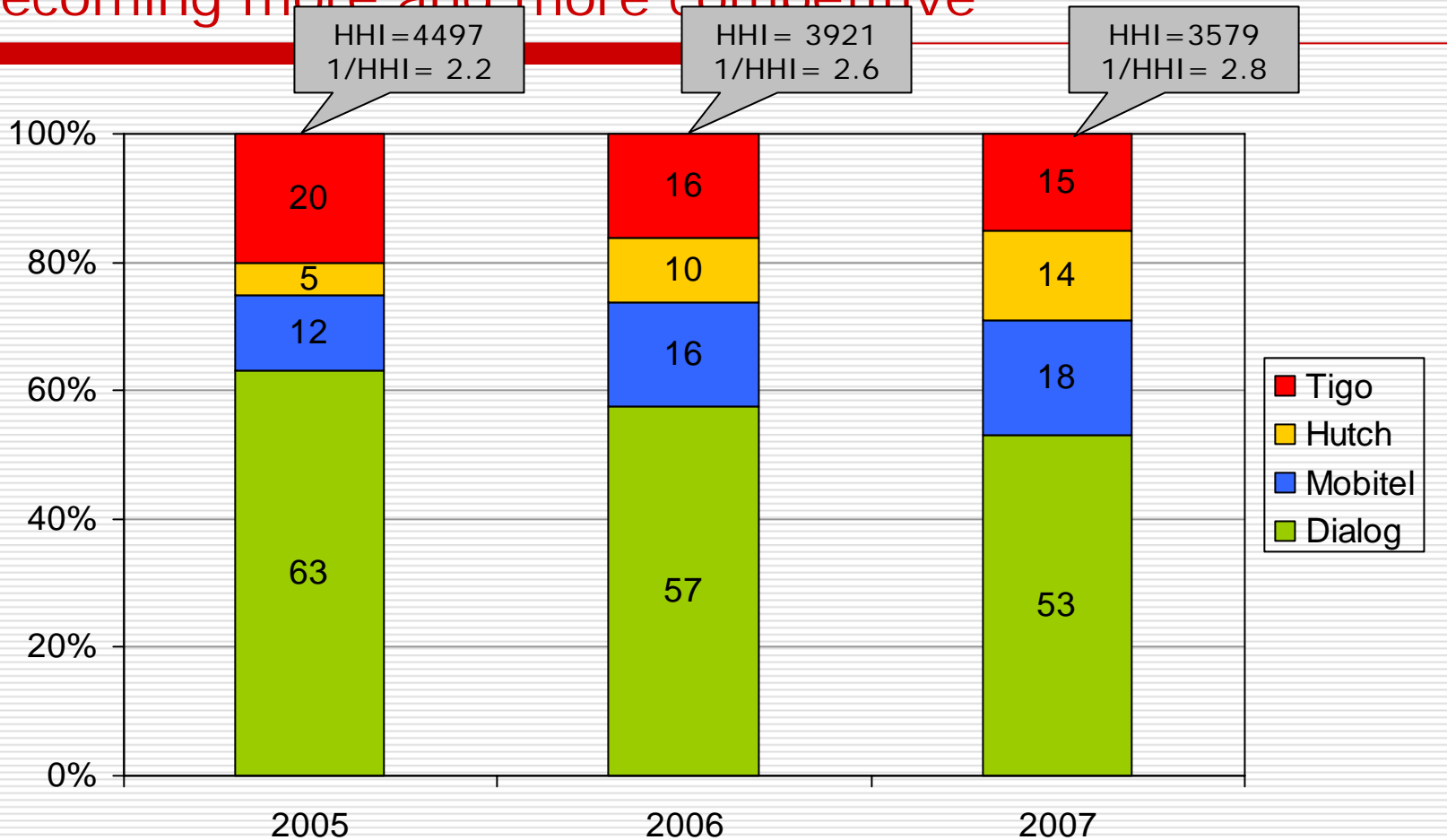
Pro-competition regulation

- Soft regulation; 'light touch' for the most part, but meaning business when necessary
 - Improvement in the fixed-mobile interconnection; USD 1 million fine 1999
 - Liberalization of the external gateway operations
 - 32 EGO licenses at a nominal USD 50K each
 - Dramatic drop in IDD rates at threat of competition
 - Unhindered space for price war



Market shares and HHI*

becoming more and more competitive

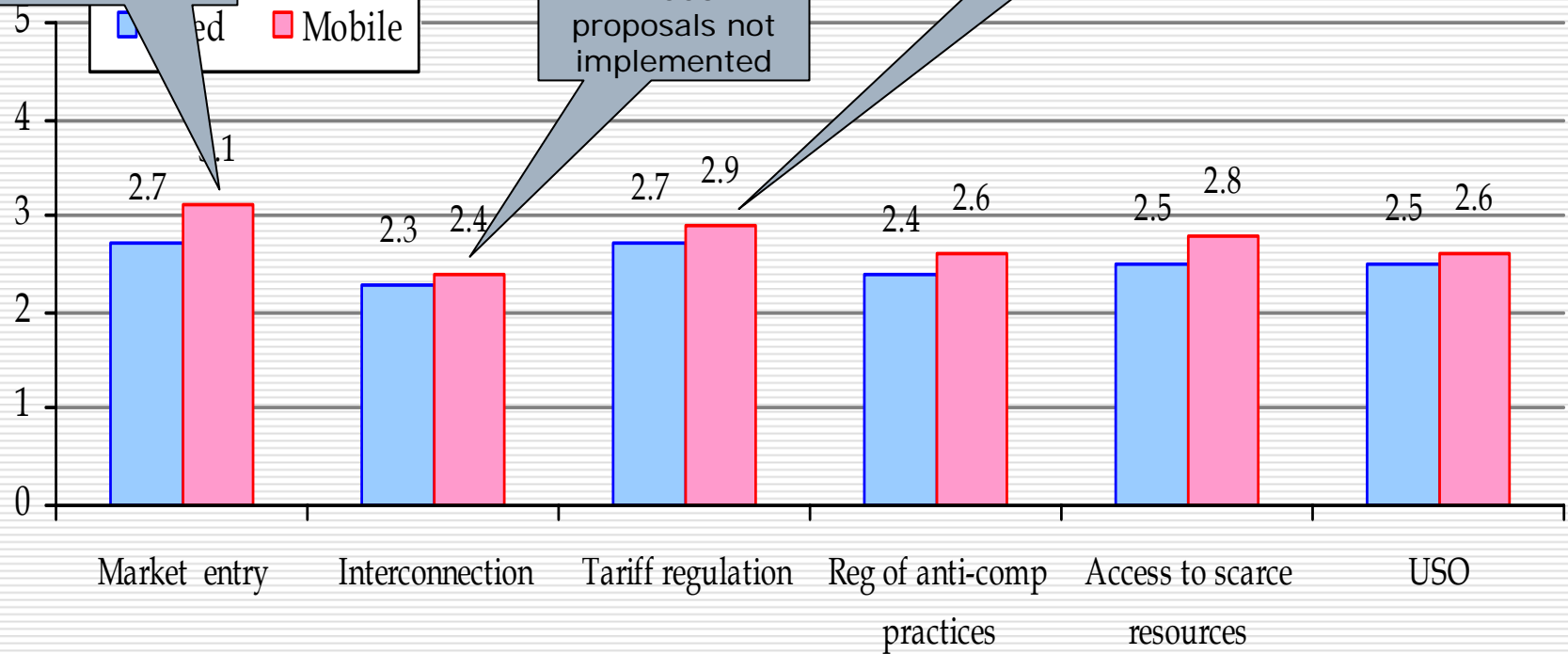


TRE 2006. Average*

CDMA frequencies for WLL operators; 5th mobile license [6th?]

Allowed space for dramatic tariff reduction leading to price war

2003 proposals not implemented



Price war → dramatic tariff cuts* *

- 2006 March
 - Loss making small operator [16%], under new management, dropped prices from LKR 11 to [unheard of] LKR 5
 - Did away with peak and off-peak pricing
- Within weeks
 - Leader hit back with deep cuts
 - Spurred others in to matching tariffs → price war
- Currently
 - Leader on-net LKR 4 [p, o/p] LKR 3 [night]; off 6,5,3
 - Two others [including disruptor] on net LKR 2; off 5,5,2
 - Other per-second billing [higher min wise 3; off 6]



Sustaining cut-throat competition

need to dramatically cut costs too

- Capex cuts
 - Moving from traditional European vendors to low-cost Chinese suppliers
 - Some create heavy supplier competition
 - Multi-rate solutions
 - Base-station software
 - Variable capacity procurement
 - Sharing passive infrastructure
 - Revenue share for Capex on VAS
- Opex cuts
 - Squeezing acquisition costs
 - SIM, promotion, dealer commission = USD 1
 - Local staff, low overheads etc.



What happens now?

- How much can tariffs come down before the fierce competition takes it's toll?
 - Is there space?
 - Country-specific



Increasing ARPU?

- Increasing portfolio of services [Mobile 2.0]
 - Increase MOU
 - Yesterday's Buzz City example
- Building subscriber loyalty
- How?
 - Focused segmentation → understanding customer
 - Increase portfolio → Numerous VAS, but customize to segments; economic, entertainment, sports...



Thesis, revisited

- Policy → Competition → ← Regulation →
Market innovation → Good performance
- Next round?



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