Recent mobile telecommunications mergers

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*Disclaimer: the views expressed are those of the presenter and cannot be regarded as stating an official position of the European Commission
Past mobile telecom cases of the Commission

<table>
<thead>
<tr>
<th>Case</th>
<th>Description, Outcome</th>
</tr>
</thead>
<tbody>
<tr>
<td>T-Mobile/tele.ring (2006)</td>
<td>• 5 to 4 in Austria</td>
</tr>
<tr>
<td></td>
<td>• Phase II, cleared with remedies</td>
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<tr>
<td>T-Mobile/Orange NL (2007)</td>
<td>• 4 to 3 in the Netherlands</td>
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<td>• Phase I, cleared unconditionally</td>
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<td>T-Mobile/Orange UK (2010)</td>
<td>• 5 to 4 in the UK</td>
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<td>• Phase I, cleared with remedies</td>
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<tr>
<td>H3G Austria/Orange AT (2012)</td>
<td>• 4 to 3 in Austria</td>
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<td>• Phase II, cleared with remedies</td>
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<tr>
<td>H3G/telefónica IE (2014)</td>
<td>• 4 to 3 in Ireland</td>
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<tr>
<td></td>
<td>• Phase II, cleared with remedies</td>
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<tr>
<td>Telefónica DE/E-Plus (2014)</td>
<td>• 4 to 3 in Germany</td>
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<td>• Phase II, cleared with remedies</td>
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</tbody>
</table>
The H3G/Telefónica Ireland merger
Characteristics of (retail) Irish mobile telecommunications market

Retail market shares (subscribers)

- Three Ireland [~10]%
- O2 (including Tesco) [~30]%
- Vodafone [~40]%
- Eircom [~20]%

Further characteristics

- Existing Network Sharing agreements of O2/Eircom as well as Three/Vodafone
- Especially residential customers (atomistic with virtually no bargaining power)
- Entry of MNOs very unlikely (high investment costs and relatively low profitability)
- MVNO entry (absent commitments) unlikely to create significant competitive pressure
Key Notifying Party's claims

- Three and O2 target different customer groups (different brand perceptions)

- Merger will lead to large cost savings and higher cashflows

- Both Three Ireland and O2 will be constrained in their ability to compete effectively if the merger does not happen
## Main Theory of Harm

### Main observations
- Focus on non-coordinated effects
- Loss of an important competitive force:
  - Three is currently an important competitive force
  - Degradation of competition in the absence of the merger unlikely
  - Competitors likely to follow price increases after the merger
- Weakening of Eircom due to degradation of network sharing

### Used evidence
- Diversion ratios and market shares (also at the segment level)
- Internal documents
- Accounting data (profitability)
- Market investigation
- Quantitative analysis
  - "UPP" analysis (based on diversion ratios and margins)
  - Demand estimation based on detailed tariff data proved eventually unreliable
Quantitative analysis

- Calibration-based approach used segment level data (i.e. post-paid, pre-paid, business)
  - Diversion ratios computed from mobile number portability data
  - 2 margin measures used: (i) contribution margins; (ii) estimated incremental margins
  - Price measure: ARPUs
  - Reaction of non-merging parties incorporated into analysis

- Results (conservative scenario)
  - 5-8% price effects for merging parties (post-paid)
  - 4-6% price effects across all post-paid segment
Quantitative analysis (contd.)

• Parties argued that analysis inappropriate by ignoring:
  • Quality competition through investments;
  • Customer inertia;
  • Product repositioning.

• EC considered that
  • Model of quality competition presented by Parties not sufficiently robust, and in any event consistent with adverse unilateral effects
  • Incentives for product repositioning by non-merging parties are weak
Efficiencies: mobile network synergies?

Although network savings are generally plausible...

- Combined spectrum allows to use equipment more efficiently

... there are some important issues

- A large part of network savings can be achieved by network sharing
- Final effect of reduction in network costs on customers unclear (better network quality and/or more aggressive competition?)
Efficiencies

Key claims

1. **Scale economies**
   - Reduction in costs will lead to a higher cash flow which triggers additional investments
   - Similar savings could not be achieved by network sharing

2. **LTE deployment efficiencies**
   - Improved coverage and speed because without the merger
     - Three lacks 800 MHz spectrum
     - O2 plans slower LTE rollout

3. **Continued service in NBS\(^1\) area**
   - Without the merger, Three would dismantle unprofitable sites and stop satellite solutions as well as repeaters

EC assessment

- Presented evidence (e.g. price concentration study; cashflow constraints in internal capital markets) insufficient to show customer benefit from fixed cost savings
- Network sharing would lead to similar cost savings
- O2 would roll out LTE to a similar extent
- Significant improvement of download speeds unlikely
- Small part of submitted efficiencies accepted
- In the long run, LTE coverage of competitors in entire NBS area

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1: National Broadband Scheme
Final Commitments

• One MVNO upfront; one as a condition
• Capacity-based MVNO model: MVNOs commit to purchase a share of the merged entity's capacity (committed capacity share increases over time)
• Option to acquire up to 30% of the merged entity's network capacity (more than the overlap due to the merger)
• Minimum term of five years, with the possibility to extend the agreement up to 10 years
• Spectrum offered during 10 years to capacity MVNOs (additional remedy involving Eircom also included)
Telefónica DE/E-Plus (Germany)
## Characteristics of German mobile telecommunications market

### Retail market shares (subscribers)

<table>
<thead>
<tr>
<th>Merging Parties</th>
<th>[10-15]%</th>
<th>[0-5]%</th>
<th>[15-20]%</th>
<th>[20-25]%</th>
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</thead>
<tbody>
<tr>
<td>T-Mobile (DTAG)</td>
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<tr>
<td>Vodafone</td>
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<tr>
<td>E-Plus</td>
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<tr>
<td>O2 Deutschland</td>
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<tr>
<td>Freenet</td>
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<td>Drillisch</td>
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<tr>
<td>Other SPs/MVNOs</td>
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</table>

### Further market characteristics

- Both O2 and E-Plus strong in prepaid segment
- Freenet hosted by all MNOs, in particular by T-Mobile and VF
- Especially residential customers atomistic with virtually no bargaining power
- Industry generally profitable
- Entry of MNOs post-merger might be possible but barriers to entry remain high
- MVNO entry (absent commitments) unlikely to create significant competitive pressure

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Key claims of Notifying Party

- Merged entity intends to offer improved quality network and become stronger in the segment of high value customers ("Merger to compete")
- In low value segment, competitive pressure maintained due to non-MNOs
- E-Plus declining force in the future
- Large claimed synergies with NPV of roughly EUR 5 bln, mostly stemming from network consolidation
### Main Theory of Harm

**Main observations**

- Focus on non-coordinated effects
- Both E-Plus and O2 are currently important competitive forces (especially E-Plus growing, and profitable)
- E-Plus and O2 are close competitors with a focus on prepaid customers
- Competitors would likely follow price increases

**Used evidence**

- Diversion ratios and market shares (also at the segment level)
- Market investigation
- Internal documents
- Accounting data (profitability)
- Quantitative analysis
  - UPP analysis (based on diversion ratios and margins)
  - Demand estimation & Merger simulation (successfully implemented in this case)
Efficiency analysis: Some differences between German and Irish case

<table>
<thead>
<tr>
<th>Network sharing</th>
<th>Three Ireland/O2 Ireland</th>
<th>Telefónica DE/E-Plus</th>
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</thead>
<tbody>
<tr>
<td>• Two preexisting network sharing (NS) agreements</td>
<td>• NS may be reduced as a consequence of the Transaction</td>
<td>• No existing NS, but MNOs have been in NS negotiations</td>
</tr>
<tr>
<td>• NS may be reduced as a consequence of the Transaction</td>
<td>• Claimed positive impact because of more investments due to relaxed liquidity constraints</td>
<td>• Transaction may prevent NS that otherwise would likely occur</td>
</tr>
<tr>
<td>Impact of (fixed) cost savings</td>
<td>Claimed positive impact because of more investments due to relaxed liquidity constraints</td>
<td>Claimed positive impact because of MNO's pricing approach that includes also non-incremental cost savings</td>
</tr>
<tr>
<td>Presented evidence</td>
<td>Submitted evidence contains mostly general arguments as to why Transaction is pro-competitive (studies on price effects, financial constraints and quality enhancing effects)</td>
<td>Submitted evidence quantifies specific benefits of German Transaction (on demand and supply side)</td>
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</tbody>
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## Final Commitments

<table>
<thead>
<tr>
<th>MVNO Remedy</th>
<th>MNO Remedy</th>
<th>Non-MNO Remedy</th>
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<tbody>
<tr>
<td>• Commitment to sell share of total capacity of the merged company's network (up to 30%) to capacity MVNO(s)</td>
<td>• Offer designed to facilitate MNO entry</td>
<td>• Extend existing wholesale agreements with wholesale partners</td>
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<td>• Capacity MVNO(s) need to commit to buying capacity upfront</td>
<td>• Spectrum lease of 2x10 MHz in the 2.1 GHz band and of 2x10 MHz in the 2.6 GHz band</td>
<td>• Offer 4G services to the wholesale market</td>
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<tr>
<td>• Capacity MVNO(s) obtain access to all current and future technologies</td>
<td>• National roaming</td>
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<td>• Divestiture of sites</td>
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<td></td>
<td>• Passive radio network sharing</td>
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<td>• Sale of shops offer</td>
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</tbody>
</table>
Conclusions on Irish and German cases

• Theories of harm based on standard unilateral effects in concentrated markets with high barriers to entry
• Reaction of non-merging parties does not mitigate competition concerns
• Quantitative assessment aimed at providing order of magnitude of likely price effects
• Efficiency claims failed at least one of the three criteria in the Horizontal Merger Guidelines (most notably merger specificity)
• Remedies seek to replicate ability/incentives to compete of MNOs