

Session 8: Market definition and Significant Market Power (SMP) designation in a broadband world

**ITU Regional Seminar on Costs
and Tariffs and
Meeting of Study Group 3 Regional
Group for Africa (SG3RG-AFR)**

Cairo, Egypt, 4-7 February 2013

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The issue (1/3)

- Ex ante regulation has been common
- Based on the assumption that some infrastructure is a natural monopoly
- Traditionally it was easy to know who to regulate
- The best pro-competitive measure was typically an interconnection obligation at wholesale prices



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The issue (2/3)

- The success of deregulation has made the situation more complicated
- The links between services and network technologies are no longer clear
- Different types of networks can now compete with each other
- Bundled offers (triple play) are common
- Flat rate is common
- Need to invest in network infrastructure
- Infrastructure may become a commodity



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The issue (3/3)

- Defining markets, and who has market power, is harder
- Market power might be abused in areas that were not traditionally regulated
- Markets change rapidly, which may make regulations obsolete
- There may be a need to focus:
 - More on promoting investment in infrastructure
 - Less on promoting access to existing infrastructure



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Market definition in a broadband world (1/3)

- Regulatory intervention is justified only in case of market failure:
 - Barriers to entry
 - Exploitation of significant market power (SMP)
- Establishing SMP requires defining a “market”
- In regulation, this is done ex ante, in competition law cases ex post



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Market definition in a broadband world (2/3)

- Markets are defined in terms of products and services that are:
 - Demand side substitutable
 - Supply side substitutable
- A market is typically defined for a given geographical area



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Market definition in a broadband world (3/3)

- The hypothetical monopolist test:
 - Can a company increase prices and maintain volume?
 - If yes, that is the “market”
 - If no (because customers move to alternatives), then include the alternatives in the “market”
- In telecommunications, it is important to distinguish between retail and wholesale markets



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The role of services

- Broadband is multi-service
- But bandwidth might restrict service availability
 - This might result in several “markets”
 - Low vs high bandwidth
 - Symmetrical vs asymmetrical
- Thus market definition depends on services
 - Their substitutability might change rapidly



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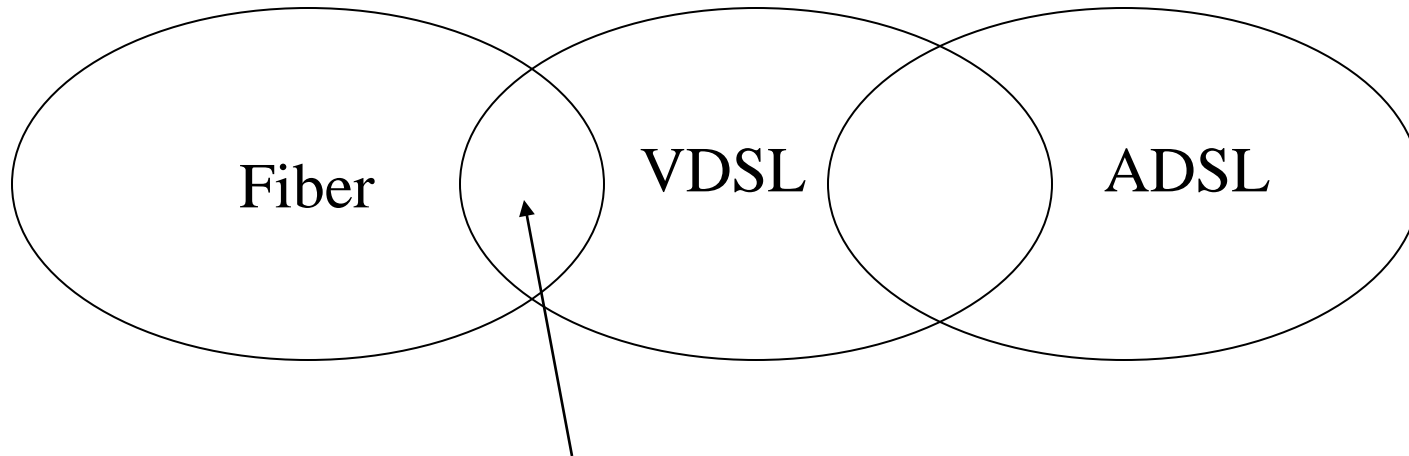
The role of customer flexibility

- Some customers have rigid requirements: they are “captive”
- Others are flexible: they are “marginal”
 - For example, some customers don’t need high upload speeds and so can use xDSL
- Market definition must focus on marginal customers
 - But watch out for price discrimination: charging different types of customers differently
 - Multiple complicated pricing plans



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Chain of substitution



Marginal Fiber customers

All three technologies are part of the same market
The chain depends on the services

Geography

- Different market if geographic restrictions
- Same market if geographic overlap and uniform pricing
- Different policies can be applied to different geographies:
 - For example, dense urban areas versus rural areas



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One-way substitution

- Customers may be willing to move from ADSL to fiber, but not the other way
 - If so, there are different markets
 - But there may not be SMP because of competition from the other market



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Vertical relations

- Availability of services may be restricted not by technology, but by commercial agreements:
 - Exclusive deals with copyright owners
 - Exclusive deals with specialized providers (e.g. for payment systems)
- Such situations can result in separate markets, since there is no substitutability



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Bundling

- Bundled offers (e.g. triple play) are common. Is the relevant market:
 - The bundled offer?
 - The individual services?
 - Both?
- Bundling may limit consumer substitutability
- As usual, one has to analyze the “marginal consumer”
 - In Hungary, a consumer survey was used



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Wholesale markets

- Regulatory intervention at retail level can be minimized by:
 - Wholesale access obligations
 - Including for key wholesale services
- Limit control over essential infrastructure
- But provide incentives for investment in additional infrastructure
- Layered approach (**unproven**)
 - Facilities
 - Services
 - Applications



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An example

- Are fixed and mobile broadband in the same market?
 - Leaders: fiber is widely available; separate markets moving towards one
 - Developed: ADSL/cable are widely available; separate markets
 - Developing: fixed is not widely available; same market



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Significant Market Power (SMP)

- Power to
 - Set high prices
 - Provide low quality
 - Not innovate
 - Lock out competition
- Some regulators look only at market share
- Others also consider
 - Control of essential facilities
 - Economies of scale
 - Barriers to entry



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Convergence

- Can be expected to reduce SMP
- But lack of investment in infrastructure can reduce competition
- Presence of competing infrastructures can stimulate competition
 - Cable
 - ADSL



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Vertical arrangement and bundling

- Over the top (OTT) services can
 - Reduce SMP
 - Increase SMP
- This depends on the vertical arrangements
 - Profits from exclusive deals may flow upstream, not remain with the network
 - So regulatory intervention at the network level may not be effective
- There may be similar issues if bundles cannot be replicated easily
 - For example bundling television content



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Traditional regulation

- Regulate retail prices
- Mandate access to infrastructure
- Regulate wholesale prices
- Enforce interoperability
- Impose transparency
- Impose non-discrimination
- Impose accounting separation

The objective is to
favor competition



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Implications of convergence

- Important to promote investment
 - How to do this is not obvious, since price controls may discourage investment
- Non-regulated services may play an important role
 - TV content
 - VoIP
- Vertical agreements and bundling may
 - Increase efficiency
 - Reduce competition



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Conclusions

- One size does not fit all
- Consider competition-law like regulation
 - This may require changes in the mandate of the regulatory agency
- Coordinate with the competition law authority



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For more information

- http://www.itu.int/ITU-D/treg/Events/Seminars/GSR/GSR12/documents/GSR12_BBReport_Koboldt_SMP_8.pdf



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