Telia/Phonero

ACE

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Norwegian Competition Authority

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The acquisition

- Telia notified the acquisition of Phonero 11 November 2016
  - Overlap in the business segment of the market for mobile telecommunications services in Norway
- Statement of objections (SO) sent 27 February 2017
  - 3 → 2 merger in the business segment
    - Horizontal non-coordinated and coordinated effects
- Cleared 3 April 2017
  - Efficiency gains counteract the parties' incentives to raise prices due to loss of competition
  - Phonero integrated into Telia's network → elimination of double marginalisation (roaming costs)

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Market structure in Norway

- Two nationwide mobile networks
  - Telenor and Telia (complete MNOs)
- One regional mobile network
  - ICE (partial MNO) with coverage 40 %
- Number of MVNOs and SPs
  - Phonero significantly larger than the rest («maverick»)
- Regulatory aspects
  - Margin squeeze regulation of incumbent (Telenor)

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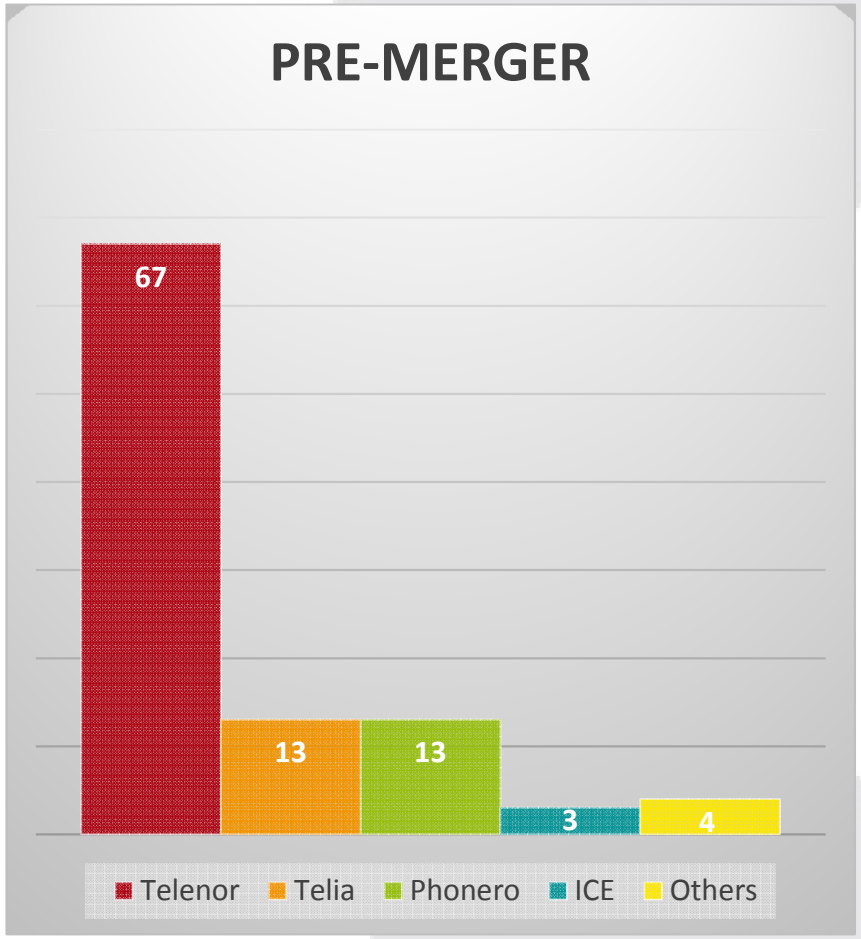
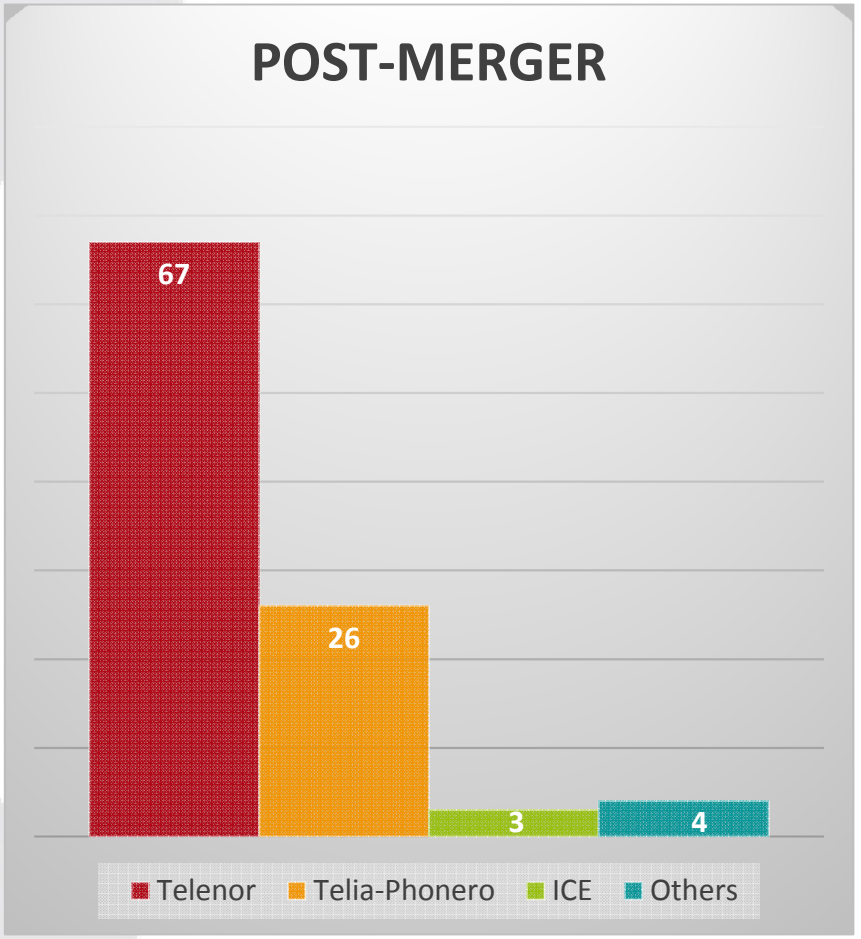
Market shares in business segment





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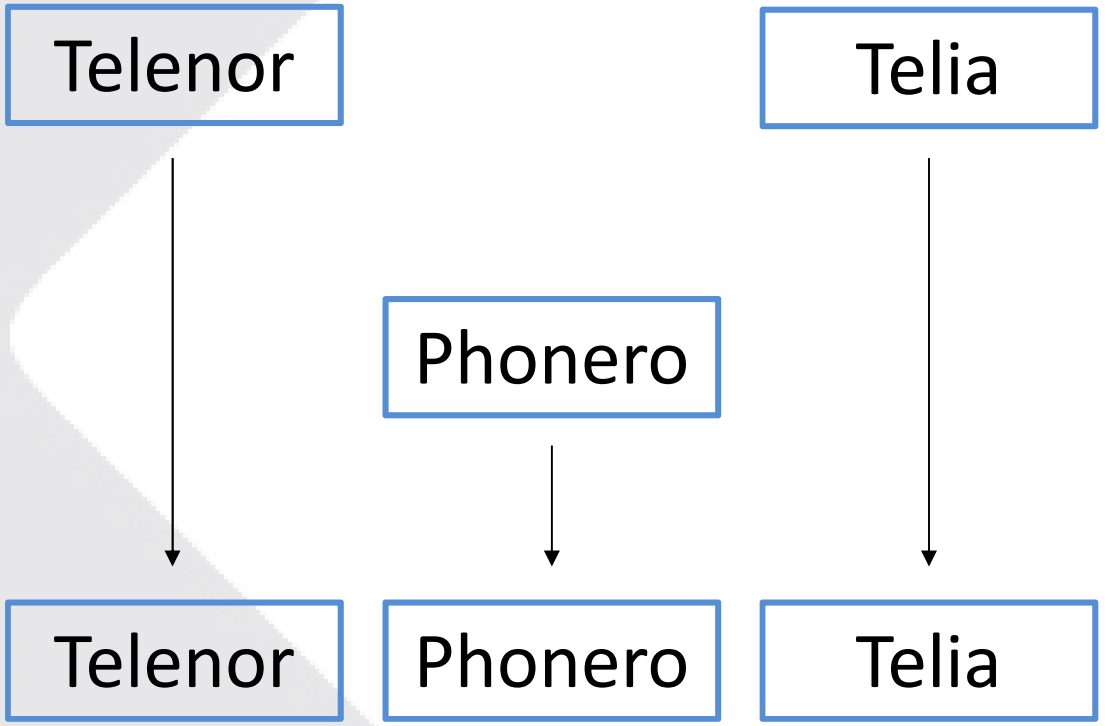
Vertical structure

MNO
Mobile Network Operators

MVNO (SPs)
Buy access to (resell services from) the MNOs network

Distribution to business customers



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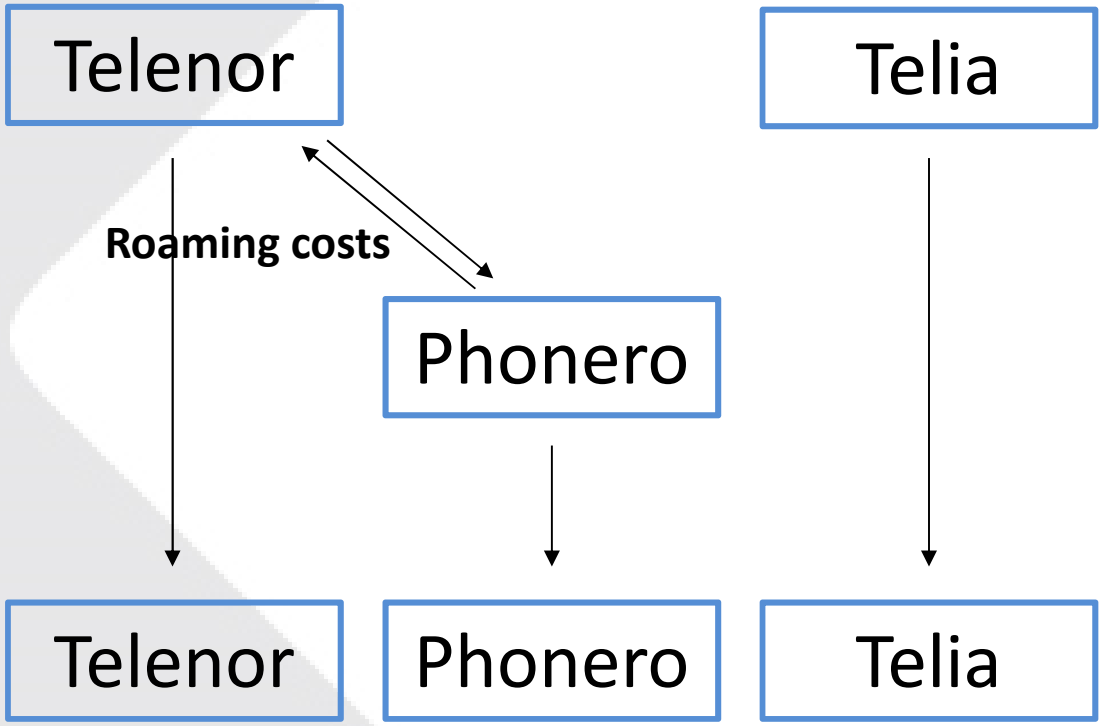
Vertical structure – pre-merger

MNO
Mobile Network Operators

MVNO (SPs)
Buy access to (resell services from) the MNOs network

Distribution to business customers



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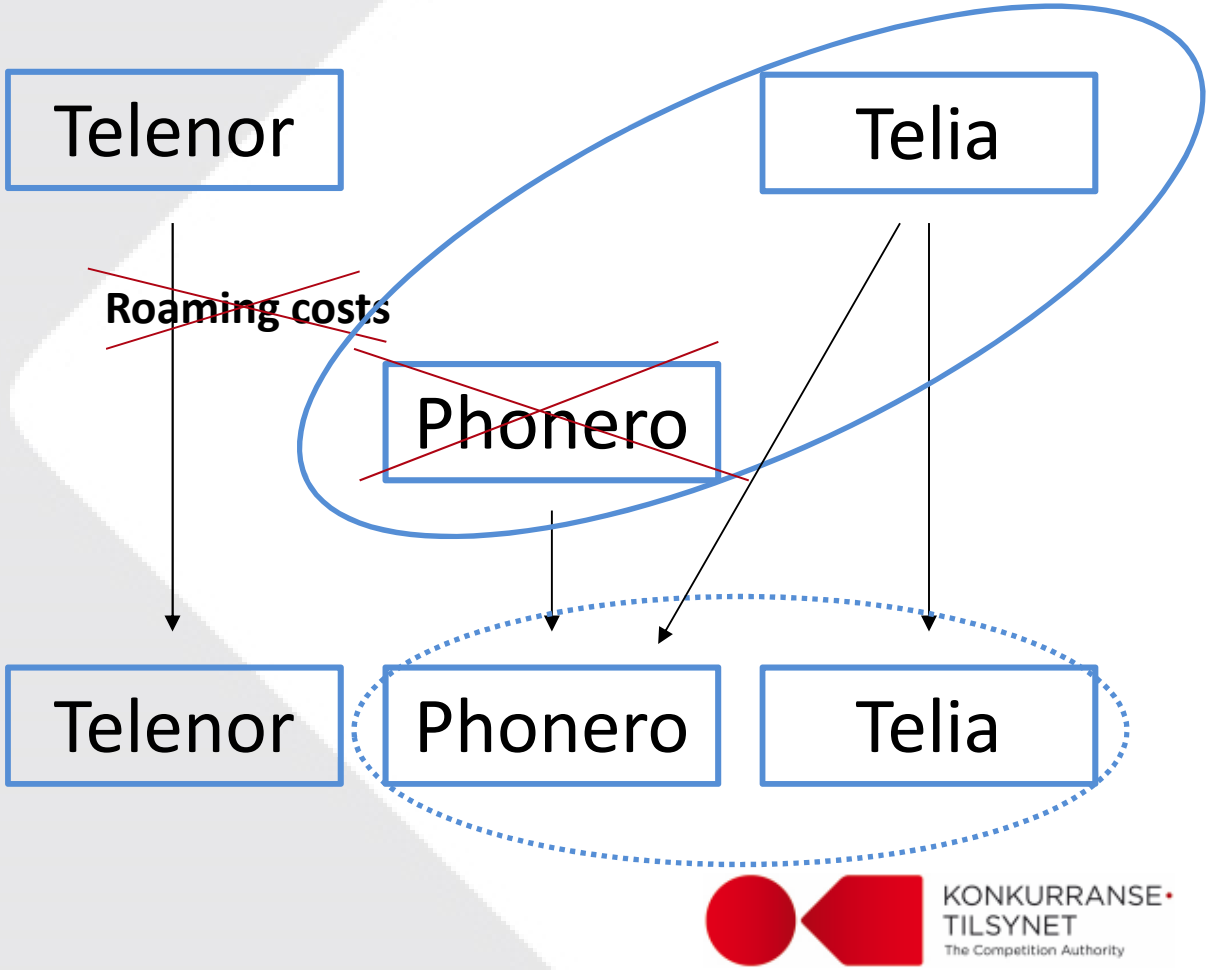
Vertical structure – post-merger

MNO
Mobile Network Operators

MVNO (SPs)
Buy access to (resell services from) the MNOs network

Distribution to business customers



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Response from Telenor

- In their pricing pressure analyses, the parties added Telenor's response to losing Phonero as a wholesale customer
  - They claimed this was a direct effect of the merger, which should be taken into account in the pricing pressure analyses
- The NCA took this argument into consideration when assessing the effect of the merger, but did not quantify the effect in the pricing pressure analyses for the following reasons
  - Telenor is subject to margin squeeze regulation, which limits their scope/incentive to reduce prices as a response to the loss of Phonero as a wholesale customer
  - Obtaining reliable measures of Telenor's price response would require detailed information about the margin squeeze regulation and estimation of the demand in the business segment (as in a full merger simulation)

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Pricing pressure analyses

- Pricing pressure analyses conducted based on
  - Mobile number portability data to estimate diversion ratios
  - Accounting data to estimate profit margins
    - ARPU
    - Contributing and incremental margins
- NCA's analyses implemented in three steps:
  - Step 1: Analysing the "pure" horizontal effects in downstream market
  - Step 2: Telia's wholesale activity included to account for effects in upstream market
  - Step 3: Roaming cost savings included to account for efficiency gains (M.7421 – *Orange/Jazztel)*

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Modified UPP for Phonero (MVNO)

- Standard positive price pressure due to reduced competition in downstream market
  - $UPP_{phonero} = (P_{telia} - C_{telia}) \frac{\partial D_{telia}}{\partial P_{phonero}}$
- Additional positive price pressure due to Telia's wholesale activity to other MVNOs/SPs
  - $UPP_p = \cdots + (W_{telia} - C_{telia}) \frac{\partial D_{mvno's\ served\ by\ telia}}{\partial P_{phonero}}$
- Negative price pressure due to efficiency gains (double marginalisation/roaming costs)
  - $UPP_p = \cdots + (W_{telenor} - C_{telia}) \frac{\partial D_{phonero}}{\partial P_{phonero}}$

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Predicted price increase

- Predicted price increase (PP)*
  - Modified to take account of Telia's upstream activity and efficiencies

$$\frac{\Delta p_1}{p_1^0} = \frac{2\frac{p_2^0 - c_2^0 - \Delta c_2}{p_1^0} D_{12} + 2\frac{\Delta c_1}{p_1^0} + \frac{p_1^0 - c_1^0 - \Delta c_1}{p_1^0} D_{12} D_{21} + \frac{\Delta c_2}{p_1^0} D_{12} + \frac{p_1^0 - c_1^0}{p_2^0 - c_2^0} \frac{Q_2^0}{p_1^0 Q_1^0} ((p_1^0 - c_1^0 - \Delta c_1) D_{21} + \Delta c_2) D_{21}}{4 - 2D_{12}D_{21} - \frac{p_1^0 - c_1^0}{p_2^0 - c_2^0} \frac{Q_2^0}{Q_1^0} (D_{21})^2 - \frac{p_2^0 - c_2^0}{p_1^0 - c_1^0} \frac{Q_1^0}{Q_2^0} (D_{12})^2}$$

* Asphjell et al. (2017) "*Unilateral effects of horizontal mergers with vertical relations between firms and other structural market changes*", Rev Ind Organ. Based on paper by Hausman et al. (2011) "*Unilateral effects of mergers with general linear demand".*

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Results, step 1 and 2

- Step 1: Analysing the "pure" horizontal effect:
  - Does not account for Telia's wholesale activity or claimed cost savings
  - Both UPP and PP indicate a substantial positive price pressure for both Telia and Phonero
- Step 2: Including Telia's wholesale activity:
  - A price increase on Phonero's products will increase Telia's wholesale income
  - Both UPP and PP indicate an increased positive price pressure for both Telia and Phonero

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Relevant efficiency gains

- Double marginalisation
- Relevant efficiency gains: the relevant cost saving is the difference between Phonero's roaming costs and Telia's marginal costs of having Phonero customers in their network
  - See M.7421 – Orange/Jazztel
- The Parties:
  - Telia's marginal costs of having Phonero customers in their network would be insignificant
  - Large cost saving

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Results, step 3

- Estimation of the cost saving
  - Deducted roaming costs that were not merger specific, e.g. international roaming costs
  - Telia's network costs used as a proxy for Telia's marginal costs for having Phonero customers in their network
  - $$\text{Margin} = \frac{Roaming\ costs\ Phonero}{Customers\ Phonero} - \frac{Network\ costs\ Telia}{Customers\ Telia}$$
- Results step 3:
  - Telia: Both UPP and PP indicate a positive price pressure
  - Phonero: Both UPP and PP indicate a negative price pressure
  - Weighted average: Both UPP and PP indicate a (weak) negative price pressure

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Thank you for your attention

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