GSMA Europe Response to the European Commission Public Consultation on

the revision of the Recommendation on relevant markets

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About the GSMA

The GSMA represents the interests of mobile operators worldwide. Spanning more than 220 countries, the GSMA unites nearly 800 of the world's mobile operators with more than 230 companies in the broader mobile ecosystem, including handset makers, software companies, equipment providers and Internet companies, as well as organisations in industry sectors such as financial services, healthcare, media, transport and utilities. The GSMA also produces industry-leading events such as the Mobile World Congress and Mobile Asia Expo.

For more information, please visit the GSMA corporate website at www.gsma.com or Mobile World Live, the online portal for the mobile communications industry, at www.mobileworldlive.com

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In the European Union the GSMA represents over 100 operators providing more than 600 million subscriber connections across the region.

www.gsmworld.com/gsma_europe

Introduction

The GSMA welcomes the launch of the revision of the Recommendation on relevant markets and the opportunity to contribute to it. The appropriate definition of relevant markets susceptible to ex ante regulation is a key pillar of the electronic communications framework. It allows national regulatory authorities (NRAs) to focus on markets where competition might be not effective and helps give stakeholders legal certainty and stability for business planning.

The electronic communications sector is characterised by rapid and significant technological changes, together with increasing competition and the emergence of new type of competitors and new features, such as access and communication convergence. The scope of the markets within the sector changes over time as the characteristics of products and services evolve. Considering that the current Recommendation was adopted in 2007, it is appropriate to reassess its relevance at this point in time.

Over the past five years, mobile network operators have experienced rising traffic on their networks fuelled by new applications, increased usage of data services and the roll out of new device types. In response, the mobile industry is evolving, not just in terms of the technical and operational aspects of the network, but also in terms of commercial strategies and business models, to remain a key driver of the European economy. The emergence of new business models will help preserve consumer choice, providing opportunities for all the players in the value chain to add value and to contribute fairly to the investments required to sustain the Internet. These factors, combined with the fierce competition in play and the economic challenges faced by the industry, call for an objective assessment of the list of relevant markets, also considering the need for a fair level playing field between the different actors.

The definition of relevant markets for ex ante regulation is based on analysis of the state of competition at retail level. When competition is fierce, as is the case in mobile markets, there is no justification to add ex ante regulation to competition law, which is sufficient to tackle any issue that may occur. Therefore, no specific mobile market should be added to the current list of relevant markets.

The termination of voice calls on individual mobile networks has been heavily impacted by the 2009 Recommendation on mobile termination rates (MTRs). That Recommendation has led to the application of low MTRs on a symmetric basis. In parallel, the market has evolved with an increased use of alternative IP-based services to traditional voice calls. As a consequence, MTRs should be governed by a new approach, for example, reliant on symmetric regulation.

Finally, as the current consultation is rather open and does not include any specific proposals, we believe any subsequent decision by the Commission to modify the three criteria test, the scope of the current markets listed in the Recommendation, or to add new markets, should be subject to a second consultation process. This approach would enable the Commission to gather views of the relevant stakeholders on any proposed substantial changes.

Questions 1 to 3 – relevant trends in the electronic communications sector that have an impact on the definition of relevant markets and bottlenecks not addressed by the Recommendation on relevant markets

The following trends should be taken into account when assessing the evolution and functioning of individual markets.

- Current economic challenges

Europe continues to record slow economic growth, impacting all sectors, including the mobile sector.

In 2010, Europe's mobile operators' average revenue per user declined 9%. In 2011[1], despite growth in the number of subscriptions and usage, European mobile operators' total revenue declined by 0.8%. Revenues on mobile voice services fell 4.7%, while data revenues increased by 9.8%. Nevertheless, data revenues represented only 13.8% of total mobile operator revenues. Since economic conditions continue to deteriorate within several European countries, it is likely that revenues will continue on this trend.

EU operators are therefore facing a difficult situation which is different from other parts of the world; for instance in 2011 the US mobile market grew 4.5% per annum[2].

In addition, mobile operators are experiencing a huge rise in traffic volumes fuelled by an increase in traffic volume per user, as consumers watch more video over mobile networks. To handle such an increase, mobile operators are investing heavily – on average, European operators' capital expenditure represents approximately 10-13% of revenues in 2011-12. However, they also need to develop new business models to find a sustainable equilibrium within the value chain.

- Retail mobile market: fierce competition and lower prices

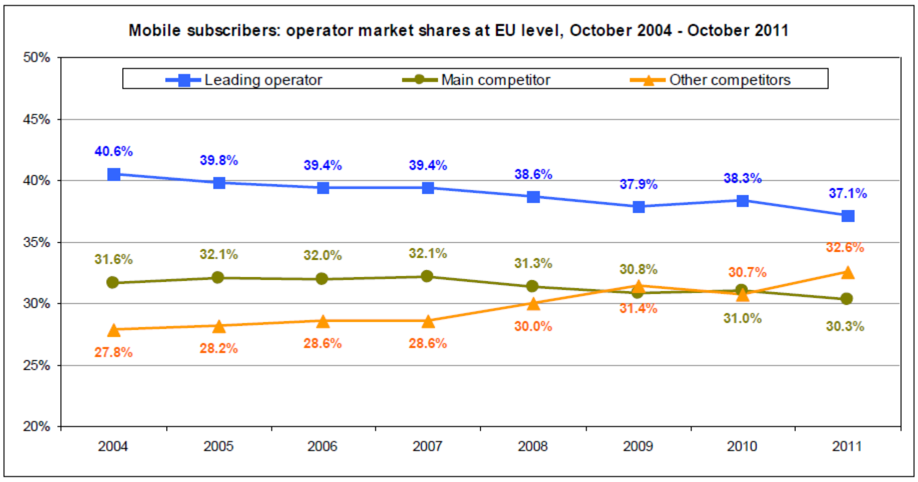
The mobile penetration rate in Europe increased significantly - by almost 40 percentage points - between 2004 and 2010. According to the European Commission scoreboard [3] for 2011, Europe has the highest mobile subscription penetration of any region in the world with 127% and that metric continues to grow: Penetration increased by 4.3 percentage points in 2011.

Intense competition between mobile operators has led to substantial falls in retail prices for voice and data, enhancing take up and usage. According to the Commission scoreboard, European consumers and businesses increasingly use mobile communication services and are getting greater and greater value. The cost of mobile communications fell between 31% and 42% between 2006 and 2010, according to analysis of representative usage baskets[4].

There is a high level of competition in EU mobile markets. Across the EU, the average market share by subscriptions of the leading mobile network in each country is 37% and that figure has fallen significantly over the past eight years (see chart below).

[1] p22 2011 Telecommunication Market and Regulatory Developments; http://ec.europa.eu/digital-agenda/sites/digital-agenda/files/Telecom_Horizontal_Chapter.pdf
[2] IDATE digital yearbook 2012, p16
[3] Digital Agenda Scoreboard 2011 - Fast and ultra fast Internet access
[4] p64 http://ec.europa.eu/digital-agenda/sites/digital-agenda/files/KKAH12001ENN-chap3-PDFWEB-3.pdf

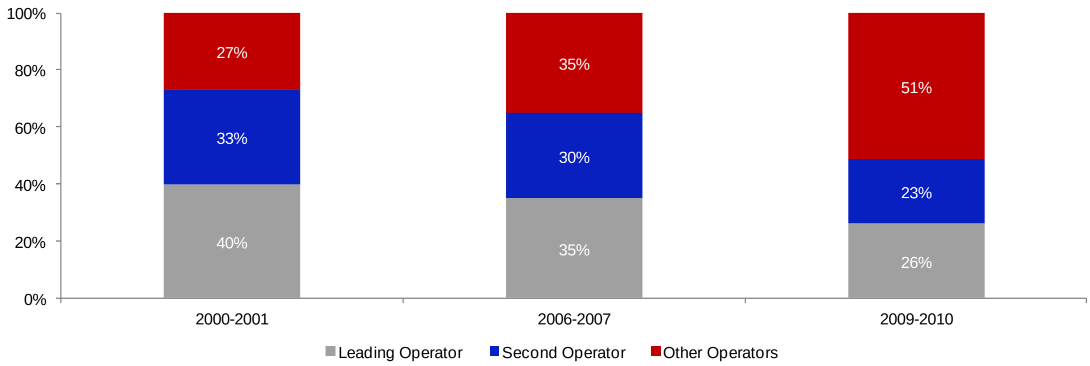
Figure 38: Operators' market shares at EU level, October 2004 – October 2011



Source: Commission services

By 2006-2007, smaller operators within Europe had generally become equally or more successful than the larger operators in attracting new consumers on a net basis, a trend that strengthened in 2009-2010 (see chart below).

Leading and Other Mobile Operators' Market Shares of Net Additions in the EEA



Source: Wireless Intelligence; A.T. Kearney analysis

Moreover, Europe has a large number of mobile virtual network operators (MVNOs) competing with network operators for customers. Some countries, such as Germany, the Netherlands, the UK or France, had between 40 and 150 active independent MVNOs in 2011. In the EU, MVNOs represent an average of 4.1% of the total subscriptions and in some countries, such as France, they have a market share of more than 10%.

The new roaming regulation adopted in June 2012 will also impact EU mobile markets. This regulation imposes substantial new decreases for voice, SMS and data wholesale and retail roaming prices, confirms the transparency measures adopted in 2009 and adds new wholesale obligations. These obligations (mandatory wholesale access and separate sale of roaming services) will enable new players to enter the roaming market and could also impact the functioning of some domestic mobile markets.

- <u>New spectrum allocations</u>

Several EU countries have recently issued new licenses for existing mobile bands, or for new spectrum resources - 800MHz, 2.6GHz - with possible refarming of the existing bands, such as in Germany, Spain, France or Belgium. These changes impact the competitive dynamics in mobile markets.

The spectrum auctions between 2008 and 2011 generated €11.2 billion in revenues for governments in just eight Member States. The majority of these auctions took place in 2011 (Germany, Italy, Spain, France, Sweden, Austria, Denmark and the Netherlands).

LTE networks, which offer a faster and more reliable mobile internet experience, are now being launched, enabling mobile operators to compete more directly with fixed broadband technologies. As of the 1st of January 2013, 45 mobile operators have commercially launched LTE services across 21 European Member States and Norway.[5]

- <u>Increased inter-platform competition and fixed-to-mobile complementarity</u>

Since 2007, EU retail markets have changed significantly as a result of an increase in inter-platform competition. Consumers increasingly regard wireline (cable and copper) and wireless networks as substitutes for each other.

From a technological point of view, the roll out of LTE is reducing the gap between the broadband speed of fixed and mobile networks. In addition, mobile retail prices have decreased more than fixed retail prices. There is increasing substitution between fixed and mobile in all EU countries, typically involving a move from fixed to mobile, but the situation differs significantly from one country to another.

However, fixed and mobile services still have very different characteristics, notably:

- the mobility feature of mobile services,
- the network capacity,
- the speed available,
- the existence of different usage patterns,
- differences in offers characteristics.

In addition, the attractiveness, from a consumer point of view, of bundled offers (including fixed, Internet and TV or fixed, Internet, TV and mobile services) suggest that mobile and fixed services can be regarded as complementing each other, rather than substitutes. Aside from the Austrian regulator, in its assessment of the residential segment, no other NRA has concluded that fixed and mobile services belong to the same retail market.

Whether or not one single retail market on voice and/or broadband encompassing both mobile and fixed services can be defined depends heavily on national circumstances, and would, in such cases, impact the fixed inputs rather than the mobile inputs. The European Commission reached the same conclusion in its comments on the Austrian notification declaring fixed and mobile as substitutes, and also by BEREC in its May 2012 report[6] on fixed-mobile substitution. Finally, it should be noted that substitution is less likely to occur at a wholesale level, even if the evolution at retail level could impact the SMP assessment or remedies at the wholesale level.

[5] GSMA
[6] BEREC report on the Impact of Fixed Mobile Substitution in Market definition, May 2012

- New type of competitors

The rapid growth of smartphone applications (apps) in the past four years has fundamentally changed the way in which people access and consume mobile services. This phenomenon is contributing to a shift in competitive dynamics; traditional voice and SMS are being replaced by "free" voice and messages over IP, through services such as Viber, Skype or WhatsApp. This has a direct impact on mobile operators' revenues and offerings, as highlighted by research firm Ovum in a recent study: "*consumers' increasing use of IP-based social messaging services on their smartphones cost telecom operators $8.7bn in lost SMS revenues in 2010, and $13.9bn in 2011. It expects the decline, representing nearly 6% of total messaging revenue in 2010 and 9% in 2011, to continue as the popularity of messaging apps continues to grow*"[7]

These trends are happening across the EU as customers' appetite for smartphones grows. Smartphones account for a growing percentage of mobile phone sales: In 2011, they accounted for 25% of handset sales worldwide, up from 20.5% in 2010 - an increase of 44% in unit sales year on year, according to IDATE. The research firm also predicts that by 2015, over 51% of mobile phones sold worldwide will be smartphones[8]. In Europe, the GSMA forecast in its 2011 European Mobile Industry Observatory that smartphones would represent 49% of mobile handsets sold within Western Europe and 16% within Central and Eastern Europe by 2014.

Another key competitive factor in the market is the way in which smartphone apps are distributed to consumers. Most apps are distributed through a handful of app stores run by leading device manufacturers or providers of smartphone operating systems. The increasing use of apps available via this small number of proprietary stores is giving the companies in control of app distribution strong market power vis à vis mobile operators.

On a related note, the EU smartphone operating system market is becoming increasingly consolidated with some device manufacturers having strong market power. Two companies dominate that sector - Google and Apple. These players, their market position and the fact that smartphones are becoming indispensable to end users are directly impacting the mobile industry.

To date, these important developments have fallen outside the scope of the Recommendation on relevant markets. However, they should be taken into account when assessing the level of competition and market power during the Article 7 process, in order to ensure a fair level playing field between actors.

[7] Ovum: The Casualties of Social Messaging, February 21, 2012: http://ovum.com/press_releases/ovum-estimates-that-operators-lost-13-9bn-in-2011-due-to-social-messaging/

[8] IDATE digital yearbook 2012, p90

Conclusion

Without any doubt there is fierce competition at play in EU mobile markets. The European Commission has confirmed that "*The mobile sector is a very competitive segment of the telecoms market*"[9]. This should definitively be taken into account when assessing the need to include any mobile markets in the new Recommendation on relevant markets.

At the same time, there are some bottlenecks and some positions of market power within the smartphone operating system and app distribution elements of the value chain which are currently not addressed by the Recommendation on relevant markets. The Commission and regulators should ensure that the ex ante approach followed within the electronic communications sector does not lead to asymmetric burdens on operators and thus to an uneven playing field between the different actors in the value chain.

Questions 4 to 6 – Three criteria test

The three criteria are there to ensure that ex ante regulation is imposed only in justified cases when a given market is subject to barriers to entry, does not tend towards effective competition and competition law is not sufficient to address the issues at stake. It is essential to use a forward looking assessment to ensure that any ex ante regulation focuses on bottlenecks and is withdrawn once the market moves towards competition.

Assessing the relevance of the three cumulative criteria test to the mobile sector raises the following comments:

- Barriers to entry;

  Spectrum has regularly been considered as a structural barrier to entry. However, several mobile network operators were able to enter the mobile markets in the 1990s in all Member States, followed in many countries by MVNOs and full MVNOs. In addition, new spectrum has been or will be soon allocated in all Member States giving the possibility for new players to enter the market (based on spectrum auction conditions). Finally, the secondary market for spectrum also offers another way for new companies to offer mobile services.

  Some commentators have also considered the need for investments as a possible barrier to entry. However, an investment requirement may be a characteristic of efficient technological markets and it should not be assessed negatively in the light of this first criteria.

- Towards effective competition;

  The trends outlined in the previous section of this response must definitively be taken into account when applying this criterion, as well as the requirement to assess markets on a fully forward looking approach.

- Competition law;

  Competition law is sufficient to tackle any issue in EU mobile markets.

[9] p64 http://ec.europa.eu/digital-agenda/sites/digital-agenda/files/KKAH12001ENN-chap3-PDFWEB-3.pdf

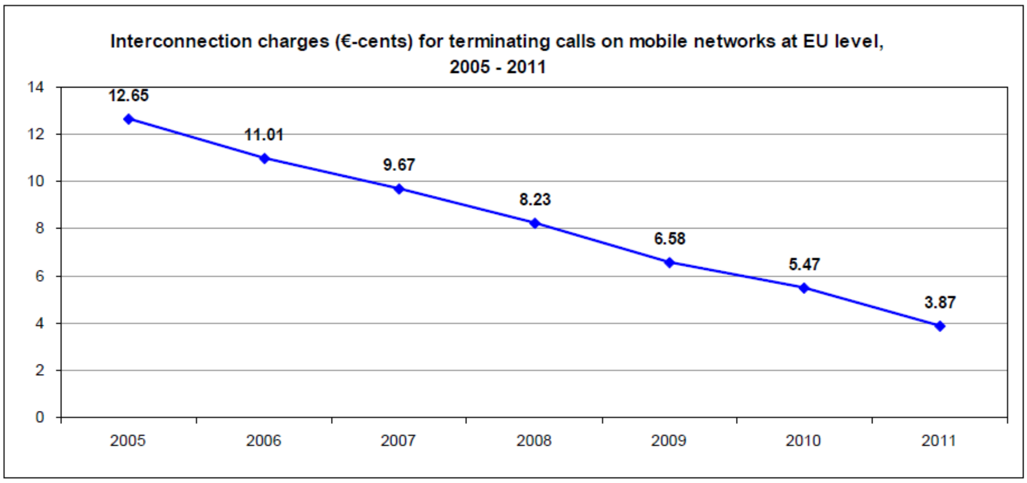
Questions 9 to 10 – Markets to be removed

In the MTR market, regulation, especially the European Commission Recommendation on MTRs adopted in 2009, which requires NRAs to apply a pure LRIC cost modelling on a symmetric basis, has had a severe impact on both this market and the broader mobile sector.

The 2009 Recommendation has drawn considerable criticism. For instance, Frontier Economics concluded in a study[10] published in 2012 that the significant decreases in MTRs have not necessarily managed to achieve the goals initially announced by the European Commission in its impact assessment, justifying the pure LRIC methodology. Frontier Economics concludes that there is no obvious link between MTR cuts and observed usage increase or retail price decreases. This lack of direct link between the methodology pushed forward and the anticipated outcome has also been raised by some NRAs as well as some jurisdictions, such as in the Netherlands.

As shown by the graphic below, MTR rates in the EU have substantially decreased over the past seven years.

Figure 45: Average mobile termination rates at EU level, 2005-2011



Source: Commission services

BEREC's snapshots of MTRs show that additional decreases occurred in 2012. By mid-2012 the simple average for the EU stood at €0.0357 per minute, whereas the EU weighted average is estimated to be €0.0276 per minute.

More and more NRAs in the EU imposed very low MTRs, converging towards pure LRIC costs, on a symmetric basis on all mobile operators. Before the new Recommendation on relevant markets will come into effect, the 2013 deadline imposed by the 2009 Recommendation on MTRs will have been reached, meaning further new decreases in MTRs on a symmetric basis. The context is therefore different from that when the previous Recommendations on relevant markets were adopted. MTRs are likely to continue evolving towards more and more pure LRIC levels on a symmetric basis. In those countries where the 2009 Recommendation outcomes are or will soon be achieved, further ex ante scrutiny

[10] May 2012 – A report prepared for Vodafone Group: The impact of recent cuts in mobile termination rates across Europe http://www.vodafone.com/content/dam/vodafone/about/public_policy/articles/mtr_impact_of_ec_recommendation.pdf

especially on costs modelling would not appear justified or proportionate, in terms of administrative or legal processes and corresponding costs.

In addition, and as further described in the first section to this answer, there are now voice-over-IP (such as Google Talk, Viber, etc) services that compete with voice call termination further impacting the functioning of that market. Those services are indeed growing and provide alternatives to traditional voice calls to reach the customers; they constitute a constraint also to be taken on board when running the three criteria test.

Based on those trends, there are serious grounds to question the relevance of the MTR market in the EU list for ex ante regulation in a forward looking assessment. In such case, the Commission could instead invite the NRAs to consider monitoring the MTR market to ensure that the market does not develop against the spirit of the framework, such as safeguarding symmetric levels between operators in case the market shows signs of market failure. This approach based, for example, on symmetric provisions could constitute a preliminary step before removing entirely the regulation of the MTR market. In this respect Article 5 of the Access Directive that relates to access to end users is a relevant basis for call termination, allowing NRAs to ensure, for instance, that MTRs remain symmetric. In addition, Article 20 of the Framework Directive allows operators to settle any dispute that may take place before the NRA and competition law will also remain as a relevant safeguard that could be applied, if needed.

Questions 11 to 12 – regulated markets at national level to be added in the revised Recommendation

- SMS wholesale termination market

In its questionnaire, the European Commission refers to the SMS termination market as a market not contained in the list of relevant markets, which is, nevertheless, regulated by some NRAs.

We consider that the SMS wholesale termination market cannot be identified as a relevant market at the EU level since the three criteria are not met.

The retail market has been evolving significantly, with flat rate tariffs becoming the standard offer for SMS. At the same time, there has been a significant expansion in the alternative means to send messages, such as IP-based messaging services accessible via smartphone apps (see previous section).

Such changes at a retail level have a major impact on the functioning of the wholesale market and reduce the potential to charge excessive wholesale rates. Therefore, the three criteria are not met and competition law will be sufficient to address any problem that may occur.

Moreover, to date, only France and Denmark have deemed it necessary, based on national circumstances, to regulate SMS termination rates by imposing wholesale caps. Poland has adopted a slightly different approach by defining the market as relevant, but letting the operators agree on the right level. Other NRAs haven't identified any competition problems that would justify an ex ante approach. The limited activity at a national level does not indicate a relevant threshold for intervention at an EU level.

The BEREC SMS benchmark shows that wholesale SMS termination rates decreased between 2011 and 2012 even in countries where they are not regulated. The EU average in July 2012 was €0.032 down from €0.0352 in January 2011. In France and Denmark, where wholesale SMS termination rates are regulated, the SMS termination rate is lower than the EU average, having decreased by 23% between January 2011 and January 2012. Similarly, the SMS termination rates in unregulated markets, such as Cyprus or Poland, which were at a comparable level to those in France and Denmark in 2011, have fallen by 44% on average between 2011 and 2012.

A recent public consultation by the Italian NRA, AGCOM, supports the points we have made in this section. This consultation, organised in October 2012, concluded that the SMS termination market is not relevant for ex ante regulation since the three criteria are not met. The main reason given is that mobile instant messaging services and email applications are substitutes to SMS, intensifying competition at a retail level directly and constraining wholesale SMS termination rates indirectly. AGCOM concluded that, if a mobile operator increased its wholesale SMS termination rates, all or part of this price increase would be passed on to the retail SMS prices. Consequently, end users would switch from SMS to instant messaging and email services. This would reduce demand for wholesale SMS termination services and, therefore, make the initial wholesale price increase unprofitable. AGCOM also highlighted that SMS termination rates have fallen on average 16% in 2011 in the Italian market and retail SMS prices also show a clear decreasing trend.

- <u>Mobile access and call origination</u>

This market was included in the initial 2007 Recommendation on relevant markets and was then deleted in the second version. Although a few EU countries have deemed it necessary to regulate the mobile access and call origination market due to national circumstances, almost all of them have recently concluded that it is now sufficiently competitive. During the summer of 2012, the Slovenian and Maltese NRAs announced their respective draft decisions to deregulate the market. The European Commission did not comment and the Spanish NRA is on its way to also deregulating this market.

There is quasi unanimous recognition across the EU of the competitive aspects of mobile access and call origination market

The competitive dynamics at play within this market are confirmed by the data presented elsewhere in this response, namely the high level of competition at a retail level, the arrival of new entrants with additional spectrum allocations, the increased number of MVNOs and Full MVNOs on a commercial basis and the growing market share of these players. It must also be noted that, despite existing commercial agreements, many NRAs have also imposed specific obligations on this market via conditions attached to new or additional spectrum auctions. These obligations include spectrum sharing and/or a requirement to negotiate agreements with MVNOs.

Those characteristics confirm the analysis made by the Commission in its explanatory memorandum to the 2007 Recommendation on relevant markets; the three criteria are not met in the mobile access and call origination market, which cannot be relevant for ex ante intervention.

Questions 13 – 14 – other markets to be added

We do not believe any additional market would meet the three criteria test justifying an ex ante intervention.

Questions 15 to 16 – transnational markets

We do not see the justification or need to create a transnational market.