# SA prepaid mobile prices plateau

*Mobile termination rate (MTR) reductions by the South African regulator in March 2013 impacted positively on prepaid mobile retail prices in the second quarter of last year. But by the last quarter of 2013, prepaid voice mobile prices had plateaued in South Africa with no further reductions in prices of the dominant operators: MTN and Vodacom. The absence of further responsiveness to pricing pressure from smaller operators, who reduced their prices dramatically during 2013, means South Africa's dominant operator prices remain expensive compared to other African countries.*

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**Absence of pricing pressure on dominant operators**

*Although the latest mobile entrant, Telkom Mobile, significantly reduced both on-net and off-net prices in the third quarter of 2013 - making available the cheapest tariff in the prepaid mobile voice market - this failed to bring down the prices of dominant operators MTN and Vodacom.*

**18 African countries score better than South Africa**

*South Africa's ranking based on the dominant operator in the country (a reflection of what most people in the country are paying) has only improved slightly compared to the third quarter 2013 but still stands at the 19th highest price in Africa on the RIA Africa Pre-paid Mobile Pricing Transparency Index.*

**Telkom Mobile brings SA ranking on the cheapest product down to 7th**

*Thanks to the introduction of 'Sim-SONKE' by Telkom Mobile, South Africa has improved its position measured by the cheapest product in the country, jumping from 20th in the second quarter of 2013 to 7th in the fourth quarter of 2013 on the 45-country index.*

**Dominant operators continue to thrive with reduced MTR**

*Although the rate at which the larger operators are able to attract new subscribers has slowed down, they remain positive. MTN managed to add 233 000 new subscribers in the third quarter of 2013, after experiencing a loss in the previous quarter when it was the only operator not to lower its prices immediately after the MTR reduction.*

**Competition has resulted in lower prices and higher traffic**

*Vodacom reported that lower prices - prepaid average price per minute has been reduced by 25% during 2013 - were offset by a growth of more than 23% in voice traffic.*

## Introduction

Research ICT Africa (RIA) monitors prepaid mobile prices across Africa quarterly. It does so by establishing the cost of a communication basket for all prepaid products and for all operators in a country. The basket is based on the OECD 40 call/60 SMS basket (OECD, 2010).

Previously, a single annual exchange rate was used for the entire data series from the forth quarter of 2010 to the third quarter of 2013. All local rates are now being converted based on average quarterly exchange rates. The purchasing power parity (PPP) conversion is done based on annual implied PPP conversion rates from the International Monetary Fund. The changes were required to reflect the volatility of African currencies - including the South African Rand.

In the fourth quarter of 2013, South Africa's 19th position by 'dominant operator' basket was a slight improvement on the 20th position it held in the third quarter of 2013 on the 45-country Africa Mobile Pre-paid Pricing Transparency Index. The Index measures both the cheapest offering in the country and the lowest price by dominant operator. This measure is a better reflection of the 'cost of communication' as it is the price paid for services by the largest number of users.

Late entrant, Telkom Mobile, dramatically reduced its prices in attempt to improve its market share and this resulted in a jump of 12 places up to 7th position from 20th in the Index of 'cheapest product in country'. However, in a market with two dominant players as strong and entrenched as MTN and Vodacom, a number of structural factors constrain the ability of small players to attract subscribers on the basis of pricing alone.

## Which prices have changed?

In third quarter of 2013, Telkom Mobile introduced the 'Sim-SONKE' tariff which substantially reduced both on-net and off-net tariffs. On-net prices went down from ZAR0.95 to ZAR0.29, while off-net tariffs were cut by 20 cents (ZAR). This even significantly undercut Cell C's lowest tariff of ZAR0.99 introduced in the second quarter 2012.

In March 2013, the mobile termination rate (MTR) reduction to ZAR0.40 per minute resulted in retail price reductions. Previous reductions in March 2011 and 2012 had little effect on retail prices, as they did not reduce the rate by a margin sufficient enough to allow smaller operators to undercut the prices of the entrenched dominant operators significantly. The final reduction of the three-year glide path in March 2013 appears to have enabled late entrants to drop their prices sufficiently to, this time, force a response from Vodacom. Vodacom brought its prices down to match Cell C's ZAR0.99. But having not lodged the tariff correctly with ICASA - and having staved off a churn from their network to Cell C - the price settled at ZAR1.20. In Q4 2013 Virgin Mobile, a virtual mobile network operator, followed

suit and introduced the '1, 2 Free' tariff, which has remained at ZAR0.99. MTN on the other hand sought to resist a price war by preserving their high prices and relying on their dynamically priced MTN Zone[1] to retain and attract price sensitive customers. As a result, they were punished in the second quarter of the year with their first loss of subscribers, which declined by 420 000 in interim results for the six months ending in June 2013, but managed to attract 230 000 in the third quarter.

By the fourth quarter however, mobile prices remained static, despite the massive price reduction by Telkom Mobile with 'SimSONKE' in the third quarter of 2013. The dominant operators did not adjust their tariffs. Telkom, on the other hand, claims to have had significant traction: signing up 6.9% of new mobile subscribers by September 2013 (compared with the previous year) and 1.598 million active subscribers in total.

With price more or less static since then, another termination rate reduction has been proposed for March 2014 at ZAR0.20.

## ICASA's new draft call termination regulations

In October 2013 ICASA proposed, in a draft call termination regulation, a glide path that starts with a reduction in MTR prices to ZAR0.20 in March 2014. In 2015, the rate will further decrease to ZAR0.15 and it will culminate in an MTR of ZAR0.10 by March 2016. The draft regulation also proposed asymmetrical termination rates on a five-year glide path. Specifically, the regulator proposed that smaller operators with less than 20% market share would be able to charge dominant players an asymmetric rate of ZAR0.44 until March 2014, that will be then reduced to ZAR0.39 until March 2015.

MTR asymmetric rates will further decrease to ZAR0.33 in March 2015, to ZAR0.26 in March 2016, to ZAR0.20 in March 2017, and to ZAR0.14 in March 2018. MTR asymmetry rates will be aligned at ZAR0.10 by 2019. These further reductions would increase competitive pressure and lead to lower prices across all operators.

Despite dominant operators' concerns about the impact of the MTR on their profitability, and their warnings that the size of the proposed reductions would inhibit their growth and ability to invest in much-needed next-generation networks and services to the poor; currently they remain highly profitable businesses. They warn however, that the lag in investment would only reflect in future investment decisions so negative effects on investment may not yet be apparent.

While this is clearly an important caution, references to the millions of Rands lost in interconnection revenues often fail to reveal significant reductions in interconnection costs, leaving net revenue generally positive when other parts of the business are healthy. Further, from a benchmarking point of view, a reduction in the termination rate towards a cost-based price, brings the MTR closer to some of the best termination rates on the continent, which have successfully driven down prices elsewhere, for

**Table 1: Cost of cheapest products for the OECD's 40 calls/60 SMS basket in USD**

| Country name | Ranking by: Dominant operator | | Cheapest in country | | % cheaper than dominant |
|---|---|---|---|---|---|
| | USD | Rank | USD | Rank | |
| Egypt | 3.20 | 1 | 3.20 | 3 | Dominant is cheapest |
| Ghana | 3.20 | 1 | 3.20 | 3 | Dominant is cheapest |
| Sudan | 3.20 | 1 | 1.20 | 1 | 63% |
| Ethiopia | 4.01 | 2 | 4.01 | 4 | Dominant is cheapest |
| Mauritius | 4.05 | 3 | 4.05 | 5 | Dominant is cheapest |
| Kenya | 4.30 | 4 | 1.48 | 2 | 66% |
| Guinea | 5.96 | 5 | 5.96 | 10 | Dominant is cheapest |
| Tunisia | 6.01 | 6 | 5.83 | 9 | 3% |
| Algeria | 6.27 | 7 | 6.27 | 11 | Dominant is cheapest |
| Libya | 6.94 | 8 | 6.94 | 13 | Dominant is cheapest |
| Rwanda | 7.24 | 9 | 5.24 | 8 | 28% |
| Nigeria | 7.36 | 10 | 4.65 | 6 | 37% |
| Congo Brazzaville | 8.16 | 11 | 8.16 | 16 | Dominant is cheapest |
| Sierra Leone | 8.28 | 12 | 8.28 | 17 | Dominant is cheapest |
| Uganda | 9.72 | 13 | 7.22 | 14 | 26% |
| Namibia | 9.86 | 14 | 9.86 | 18 | Dominant is cheapest |
| Mozambique | 10.67 | 15 | 10.67 | 21 | Dominant is cheapest |
| Liberia | 11.30 | 16 | 11.30 | 22 | Dominant is cheapest |
| Botswana | 11.41 | 17 | 10.37 | 20 | 9% |
| Benin | 11.45 | 18 | 11.45 | 23 | Dominant is cheapest |
| South Africa | 12.06 | 19 | 5.20 | 7 | 57% |
| Mauritania | 13.01 | 20 | 12.58 | 25 | 3% |
| Cote d'Ivoire | 13.30 | 21 | 13.30 | 26 | Dominant is cheapest |
| Senegal | 13.32 | 22 | 13.32 | 27 | Dominant is cheapest |
| Central African Republic | 13.74 | 23 | 13.74 | 28 | Dominant is cheapest |
| Sao Tome and Principe | 14.43 | 24 | 14.43 | 31 | Dominant is cheapest |
| Malawi | 14.95 | 25 | 14.50 | 32 | 3% |
| Tanzania | 15.40 | 26 | 7.34 | 15 | 52% |
| Burkina Faso | 15.60 | 27 | 15.36 | 33 | 2% |
| Mali | 15.84 | 28 | 15.84 | 34 | Dominant is cheapest |
| Togo | 16.20 | 29 | 16.20 | 35 | Dominant is cheapest |
| D.R. Congo | 17.10 | 30 | 10.10 | 19 | 41% |
| Chad | 17.54 | 31 | 17.54 | 38 | Dominant is cheapest |
| Seychelles | 18.02 | 32 | 18.02 | 40 | Dominant is cheapest |
| Cameroon | 18.08 | 33 | 18.08 | 41 | Dominant is cheapest |
| Lesotho | 18.13 | 34 | 13.83 | 30 | 24% |
| Zambia | 18.72 | 35 | 17.55 | 39 | 6% |
| Swaziland | 19.85 | 36 | 19.85 | 42 | Dominant is cheapest |
| Niger | 20.20 | 37 | 17.05 | 36 | 16% |
| Angola | 22.13 | 38 | 19.92 | 43 | 10% |
| Madagascar | 22.55 | 39 | 21.83 | 45 | 3% |
| Zimbabwe | 22.75 | 40 | 21.78 | 44 | 4% |
| Cape Verde | 31.57 | 41 | 31.57 | 46 | Dominant is cheapest |
| Morocco | 46.62 | 42 | 12.25 | 24 | 74% |

[1] In order to capture the dynamic pricing structure of MTN Zone, RIA makes the following assumptions for dynamic pricing across Africa: On-net prices at 40% discount during peak time, 50% discount during off peak time and 60% discount during off-off peak time for on-net calls. For off-net calls RIA assumes a 10% discount. These assumptions are the same across Africa.

example Kenya, Ghana, and Namibia. In these markets, as with the first glide-path in South Africa, the reduction in MTRs has reduced prices, increased the number of subscribers, increased traffic flows, and incumbents have remained profitable. South Africa still has considerable room for improvement.

With retail prices having come down, the total number of subscribers has continued to grow, though the rate at which this has occurred has historically slowed down for the dominant operators. However, as Vodacom indicates in its December 2013 quarterly report, its lower prices, that were induced as a result of price competition, were offset by a growth of more than 23% in high voice traffic. It is reported that the prepaid average price per minute has been reduced by 25% during 2013.

MTN has been challenged the most by the pricing pressure from the smaller operators, losing a significant number of subscribers when it did not adjust its prices in the second quarter of 2013 following the reduction of the MTR and the introduction by Cell C of their ZAR0.99 offering, which Vodacom met. By the end of their third quarter (September 2013) and after some adjustment to their product offering - including revision of their dynamically priced product MTN Zone - its subscriber base increased by 233 000. Cell C was rewarded for its price reduction reporting in October 2013, that it had achieved 1.2 million gross connections, with 400 000 net additions in October 2013.

## South Africa prepaid mobile prices

Figure 1 displays the cost of the cheapest prepaid mobile product available in South Africa, and in Africa, for the OECD[2] 40call/60 SMS basket between the fourth quarter of 2010 and the forth quarter of 2013.

The South African cheapest operator basket price dropped between the second quarter of 2013 and the third quarter of 2013, from USD10.9 to USD5.3[3]. This price is nearly 4.3 times more expensive than the cheapest product in Africa and 1.66 times more expensive than the cheapest product available from a dominant operator in Africa (MTN Ghana, Vodafone Egypt and Sudani (Sudan) had a basket price of USD3.2; see Table 1 or Figure 2).

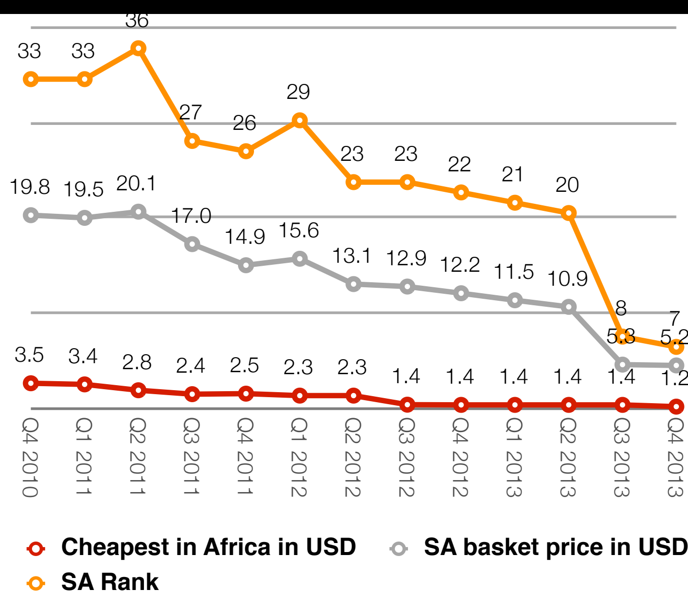


***Figure 1: Ranking and cost of cheapest prepaid mobile product available in South Africa and Africa for the OECD's 40 calls and 60 SMS basket***

South Africa's ranking for the cheapest product in the country dropped from 20th in the second quarter of 2013 to 7th in the forth quarter of 2013. The detailed ranking for all countries for the forth quarter of 2013 is displayed in Table 1.

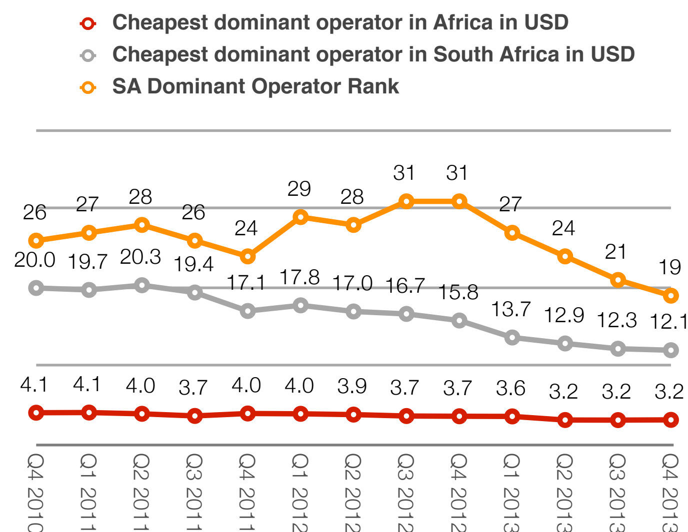


***Figure 2: Ranking and cost of cheapest prepaid mobile product available from dominant operators for OECD 40 calls and 60 SMS basket***

Figure 3 depicts that in the third quarter 2013, only Telkom Mobile seems to be engaged in the price battle, as it significantly reduced both on-net and off-net tariffs. In the fourth quarter of 2013, Virgin Mobile reduced its tariffs to ZAR0.99 reaching the same basket as Cell C but being a virtual operator with a limited subscriber base it is not a price setter. Cell C had last cut its tariffs in the second quarter of 2012. Both MTN South Africa and Vodacom have not reduced tariffs since first quarter 2013, when they both introduced a flat tariff set at ZAR1.20.

2 OECD (2010), Revision of the Methodology for Constructing Telecommunication Price Baskets, OECD Working Party on Communication Infrastructures and Services Policy.

3 The reduction is also affected by the USD/ZAR exchange rate that increased from 8.94 in Q1 2013 to 10.14 in Q4 2013. This translates in a reduction of the cost of the OECD basket in USD.

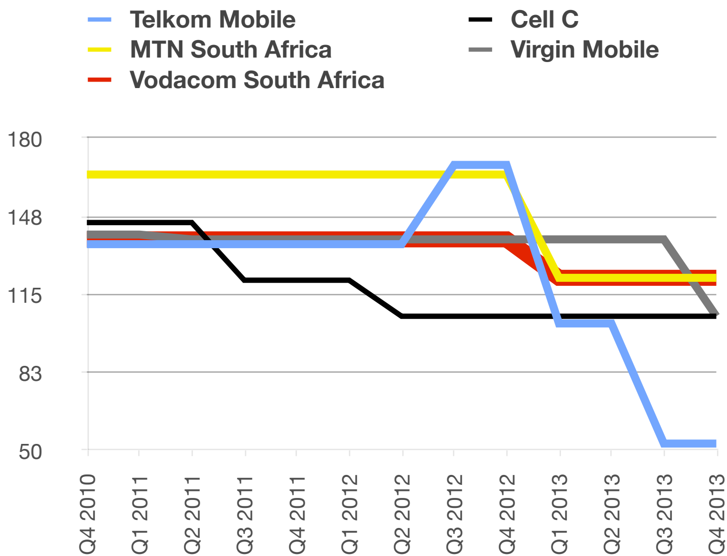


***Figure 3: Cost of cheapest prepaid mobile product for the OECD 40calls/60SMS basket by operators in ZAR***

This supports further reductions in the MTR as prescribed by ICASA for March 2014, though the asymmetry in the rates proposed seem unprecedentedly high.

| Draft call termination regulations | | | |
|---|---|---|---|
| | MTR | MTR for operators with less than 20% market share | Difference |
| March 2013 | 0.4 | 0.44 | 10% |
| March 2014 | 0.2 | 0.39 | 95% |
| March 2015 | 0.15 | 0.33 | 120% |
| March 2016 | 0.1 | 0.26 | 160% |
| March 2017 | 0.1 | 0.2 | 100% |
| March 2018 | 0.1 | 0.14 | 40% |
| March 2019 | 0.1 | 0.1 | 0% |
| Source | http://goo.gl/7QX2Ts | | |

The proposed MTR will bring South Africa into line with some of the leading markets in Africa, in terms of cost-based and wholesale prices, laying the foundation for lower and more competition retail prices.

The asymmetries in the termination rates will provide a boost to the cash flow of smaller network operators, if MTN and Vodacom do not increase their off-net prices. The changes may have no consequences if they do increase their off-net prices. Revenue is a function of price multiplied by quantity. Higher off-net prices may lower off-net traffic and Telkom Mobile and Cell C may actually not see any benefit.

The general lowering of MTRs will, however, reduce what net-payers pay and net-receivers receive.

Evidence from the rest of Africa suggests that reductions in termination rates enable competition and result in price reductions, but also that this increases traffic flow, grows subscriber bases, improves revenues and profitability (in many cases driving investment) and increases company tax streams for the state.

Asymmetrical regulation of operators is an extreme intervention in the market and is only justifiable when dominant positions in the market have become entrenched over a long period of time - as ours have.

ICASA appears to have recognised that in order to challenge dominant operators small players require a certain and sustained, but defined, period in which they can exert pricing pressure on dominant operators to attract subscribers and grow their networks.

The caution is that asymmetrical termination rates have the potential to distort the market as well as investment incentives and, at a certain point, may undermine the competitive incentives of the beneficiaries of asymmetrical rates. For this reason, asymmetry should be imposed only for a limited period, needs to be closely monitored, and should be withdrawn as soon as the intended competitive outcomes kick in, or if they fail to succeed within the specified period.

The new glide-path suggests a leveling out of the significant asymmetries in MTRs within three years and, in line with global trends, also indicates moving towards greater symmetry in mobile and fixed termination rates.

The degree and speed to which this should be done, or the degree of asymmetry required to boost small players, is impossible to ascertain independently without the traffic and cost data that the regulator has presumably used to set the proposed tariffs.

## Assessing prices going ahead

What is clear from the financial quarterly reports of the country's operators, and particularly the dominant operators over the last year is that data is emerging as the fastest growing area of their business in parallel with global trends. While voice and SMS remain a significant source of revenue and important communications services for the poor, who either do not have smart-devices due to cost or are constrained by illiteracy or e-literacy shortcomings, their contribution to total revenues are diminishing. Data is where operators and service providers are now re-focusing. In fact, there is already such extensive bundling and use of airtime for both voice and data that it has become increasingly difficult to separate them in order to make pricing transparent and indeed determine the required point of regulation.

Vodacom reported a 3.4% growth in service revenue for its South African operations in the forth quarter of 2013, driven by 31.7% data revenue growth, which now constitutes nearly a quarter of total services revenue.

Vodacom's data revenue from international operations has more than doubled with data traffic now three times higher than a year ago and makes up more than 22% of total services revenue. Group active data customers grew 27.9% compared to voice customers which grew by 12.3%. This is also reflected in the boost from equipment revenue as a result of significant take-up of smart devices required for data services.

While MTN's fourth quarter results for 2013 were not available at the time of preparing this brief, its third quarter report confirms these trends. Its September 2013 report indicates that data remains the largest contributor to revenue growth with an increase of 16.6% year-on-year.

## Conclusions

The implementation of the MTR in March 2013 resulted in a reduction of prices of dominant operators. However, by the fourth quarter of 2013, prices had become static with no further reductions by the incumbents after the second quarter. At the same time, following three years of mobile termination rate reductions, eighteen countries in Africa had cheaper prices than South Africa as measured by their dominant operator.

Although a comprehensive assessment is only possible once the detailed annual financial results of companies are released, it appears from quarterly reports and press statements that the reduction in MTRs implemented during the three year glide-path, did not have the disastrous impact on the financial performance of the dominant operators that was predicted by the operators and some investment analysts. Overall, the sector grew, prices came down, subscriber numbers grew, and EBITDA of the incumbents remained healthy.

The rate at which MTR reductions were made have not been sufficient for smaller players to place enough pressure on incumbent operators to get them to significantly reduce their tariffs. Dominant mobile operators prices have been static since the first quarter of 2013 despite some significant reductions by Telkom Mobile. South Africa's position on the Africa Pricing Transparency Index has thus not shifted significantly.

The introduction of the 'Sim-SONKE' tariff by the latest market entrant, Telkom Mobile, in the third quarter of 2013 and that of the new '1, 2, Free' Virgin Mobile tariff in the fourth quarter of 2013 did not put sufficient pressure on the dominant operators to change their prepaid price structure. This suggests that further regulatory adjustments are required in the market.

The termination rates proposed in the new three-year glide-path will bring South Africa's termination rates into line with the leading countries in Africa and with global trends towards cost-based termination rates, in conjunction with symmetrical rates for all operators whether fixed or mobile. The degree of asymmetry between terminating calls on the networks of dominant players and on that of the smaller players is unprecedentedly high. This will hopefully provide the smaller players with the kickstart they need to claw onto some of the market share which appeared to be so intractable until now.

While there are real asymmetries in the costs of termination between large and smaller players due to economies of scale and scope, the regulator will need to monitor the hidden effects of asymmetry very closely to guard against unintended outcomes from highly asymmetrical termination rates.

Understanding the viability of operators and their business models together with the changing demands of customers will require a far closer examination of data prices and wholesale access to networks and facilities. While data prices have come down considerably over the last year, the measurement of data prices and ways in which to make pricing transparent are far more complex than with voice packages. RIA has begun the quarterly collection of data prices for the African Pricing Transparency Index and will report on these in the next quarter - this is going to become a critical issue for the regulator going forward.

Operators are adapting their business models to the migration that is taking place from voice to data. This will become increasingly intense as they are able to rely less and less on voice revenues for their profitability. Mobile operators' abilities to attract users and subscribers will be shaped by their data offerings and by their capacity to provide reliable and affordable data services. To enable mobile operators to adjust their business to these shifting global trends, the Ministry of Communications and ICASA need to urgently release high demand spectrum, which is necessary for the development of 4G (LTE) services in South Africa, and to the growth and development of the mobile broadband operators.

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