

Personal Contribution from Prof Stephen Temple CBE

Response to the notice of possible remedies for the anticipated JV between Vodafone and Hutchison 3G UK

INTRODUCTION

My earlier contributions to the Phase 2 Terms of Reference concluded that the CMA decision on the proposed merger would be a watershed moment for the future quality of the UK's mobile network infrastructure. It is therefore encouraging that the CMA provisionally considers the merger, in principle, could lead to rivalry enhancing efficiencies, subject to an effective investment commitment. I have just finished a piece of research on how Ofcom's Annual License Fees can be paid for in *qualifying investments* rather than in cash to the Treasury. This has a direct read-across to what the CMA may be seeking. I have also added below some informative comments on two other areas the CMA propose to explore.

BEHAVIORAL REMEDIES - Investment Commitment

The CMA has set down in paragraph 30 what it is looking for from an investment commitment. It is all very straight forward except the way the deliverable has been expressed. The JNP/JBP contains a technology outcome for ten years hence and a linked investment of £11 billion. Trying to monitor and enforce a technology outcome ten years hence is hugely complex, problematic and resource intensive. Doing the same for £11 billion of investment over ten years is very simple and not requiring much resource beyond a firm of auditors.

Since this is not a public procurement nor regulatory coverage obligation, the case for simplicity is compelling. Start from the £11 billion over ten years, list the areas from the JNP/JBP where the investment is to be directed as "qualifying investments" (eg mobile network data capacity, extending standalone 5G coverage and faster average network speeds) and what gets delivered after ten years will be £11 billion's worth of better network capacity, standalone 5G coverage and average network speeds).

Why it does not have to be any more complicated than this is that the merged entity is spending its own money to improve its own network to meet its customers' needs and therefore it has sufficient incentive to spend that money efficiently and wisely. The remedy's purpose is to ring fence the £11 billion as a capital investment into its mobile network infrastructure and not paid out as dividends.

The broad approach would an amendment to merged entities spectrum licence whereby its Annual License Fees would be increased by the agreed investment amount over the agreed period

The new license condition should give them a choice to pay the amount due each year in cash to the Treasury (as happens today) or in "qualifying investments." Fees owed that cannot be accounted for in the audits of "qualifying investments" will be paid in cash to the Treasury. That meets the CMA need to be assured the investments will happen *in full*.

Monitoring is then simplified down to an annual audit by a qualified firm of auditors. Ofcom has all the powers and experience to enforce Annual License Fees. The outcome for consumers is likely to be far better because it allows more fine tuning by the merged entity along the way. Ten years is a long "time horizon." To this end, it would be wise to add to the areas of qualifying investments: "and other attributes of a "best-in-class 5G network for the future" approved by Ofcom.

At the end of the agreed period the level of Annual License Fees reverts to the prevailing level Ofcom has set for that spectrum range. That meets the CMA need for the remedy to be time limited

Wholesale market remedies

The CMA's further study in this area might usefully include the implications of VMO2 extraordinarily successful role in the MVNO market. The table below gives some very approximate data for all the MVNOs not wholly owned by the host MNO:

Host Mobile Network Operator	Total number of customers being supported on the host network	Independent and partially independent MVNOs being supported (but excluding MVNOs wholly owned by an MNO)
VMO2	~4.5 million ~ 5 million	Sky Mobile & Lycamobile Tesco Joint Venture
Vodafone	~1.9 million	Lebara Mobile ASDA Mobile Lidl Connect
Three	~1.1 million	ID Mobile, Superdrug Mobile
EE	110 thousand	1pMobile, To The Moon

VMO2's strategy is ensuring:

- **Economies of Scale:** More customers on the network, including those from MVNOs, allow VMO2 to operate more efficiently, spreading costs across a larger user base.
- **Additional Revenue Streams** from reaching different market segments.
- **Attracting Strong Brands as partners.** Better having them as partners than competitors

If the merger is approved, then VMO2 displaces Three as the smallest player in the market. Holding onto their leading MVNO customers then becomes critical to VMO2's own survival, as they need them to spread the cost of their infrastructure *to remain competitive with their two larger MNO competitors*. VMO2's competitors will be aware of this. This gives VMO2's existing MVNO partners a lot of negotiating power when contracts come-up for renewal. *In the light of this, the argument that the successful MVNO's, like Sky and Lycamobile, will be disadvantaged by the merger looks marginal.*

POSSIBLE STRUCTURAL DIVESTITURE REMEDY

The evidence below confirms the CMA initial view that a partial divestiture remedy would not work:

- Low band spectrum is essential to the commercial viability of a mobile operator. That was the findings of Ofcom at the time when Three struggled to achieve viability when it only had 2.1 GHz spectrum and before it obtained low band spectrum at the 4G auction. *But Vodafone and Three together do not have a surplus of low band spectrum to divest.* If it is forced to divest low band spectrum already loaded with customer traffic – this would cause serious and immediate harm to the service of millions of consumers.
- Forcing the parties to divest mid band spectrum (3.6 GHz) would place the new entrant in an even more disadvantaged position than Three struggled with at 2.1 GHz, as its transmission range is shorter.

A far more efficient way to protect the neediest from price rises is through a time-limited retail protection of *social tariffs* than to seek to achieve this through a failing new entrant proxy. It remains my view that a three-player market will remain sufficiently competitive so the industry shifts from the current state of delivering ever more data for a lower price to a more sustainable "delivering ever more data *for the same price* (in real terms)." What the country needs for economic growth is the *ever more data*.