

by Gita Sorensen

What shape competition in a bundled services market?

Consumer preference for buying bundles may threaten the viability of single or dual-service providers of electronic communications, but it could also be the vehicle for true inter-platform competition. Current regulatory frameworks and principles are challenged by the increase in triple and some quadruple-play service bundles in the market.

The pace of service bundling in the electronic communications sector is picking up. It is popular with providers as well as consumers and looks to be here to stay. Yet many regulators view service bundling with unease for a number of reasons, including concerns about anticompetitive pricing, tying of competitive and non-competitive services, and margin squeeze. However, it is important to recognise that service bundling is popular with consumers who value cost savings and the possible reduction in administration. This article explores the potential market impact of increased service bundling.

The electronic communications sector comprises four groups of providers: fixed network operators, mobile network operators, entertainment platform operators, and providers without networks or platforms. Four service groups can be combined to form double, triple, or quadruple-play service bundles (see Table 1).

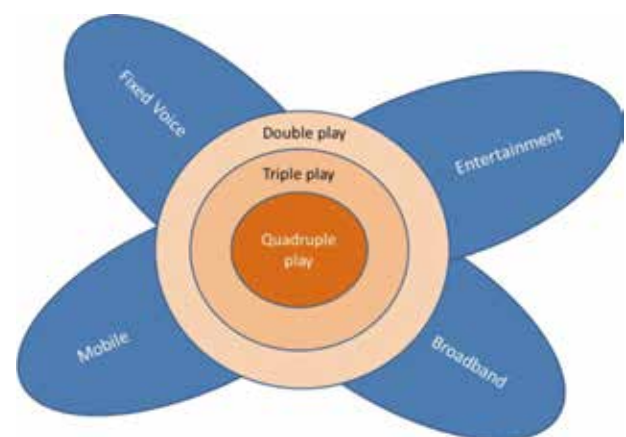
Each single-service provider seeks access to the other three services in order to offer the largest and most attractive bundle to existing and prospective customers (see Figure 1).

In contrast to service-specific analogue networks, digital networks are multi-service. Operators can therefore add services to their portfolios at relatively low incremental costs, achieving economies of scope and indeed scale through increased network utilisation. The increased provision of Voice over Internet Protocol (VoIP) and IPTV services are examples of this technological development.

Table 1 Service bundle options

| Double-play | Triple-play | Quadruple-play |
|-------------------------------|---|---|
| Fixed voice and broadband | Fixed voice, broadband, and mobile | Fixed voice, broadband, mobile, and entertainment |
| Fixed voice and entertainment | Fixed voice, broadband, and entertainment | |
| Fixed voice and mobile | Mobile, entertainment, and broadband | |
| Entertainment and broadband | | |
| Entertainment and mobile | | |
| Mobile and broadband | | |

Figure 1 Combinations of services



In Europe, the regulation of fixed telecommunications network operators has made wholesale access to fixed networks available to other operators. Therefore, the provision of bundles including fixed voice and fixed broadband can be offered by a large number of providers.

The importance of bundling to the consumer can be seen in these UK data:

- In July 2012 Ofcom, the regulator, reported for the first quarter:
 - o 57 percent of UK consumers purchased electronic communications services as part of a bundle
 - o 19 percent purchased a bundle of fixed voice, broadband, and multichannel TV services
 - o 27 percent purchased a bundle of fixed voice and broadband.
- Virgin Media, the cable operator, reported in October 2012 that 81 percent of its customers purchased triple or quadruple-play bundles: 65 percent purchased triple-play, and 16 percent purchased quadruple-play.
- BSkyB, the satellite operator, reported that its customers purchased an average of 2.7 services. As BSkyB only offers three services (fixed voice, broadband, and multichannel TV), this suggests that the vast majority of its customers purchased bundles.

Why do providers bundle?

A customer’s switching decision is believed to be more complex when buying several services from the provider. Comparing service bundles can be complex, as few are identical in content or contractual terms. Further, if the services in the bundle are sold at a price below the sum of the stand-alone charges, the stand-alone services become unattractive. Service bundling increases the “stickiness” of the services included in the bundle.

Providers may also experience economies of scope and scale from bundling, reducing the unit cost, which could make them more competitive in both bundled and stand-alone service markets.

Why do customers buy bundles?

Research suggests that customer preferences for service bundles lie in two areas: cost savings and convenience. Research by the Finnish regulator FICORA confirmed that pricing is the strongest driver, closely followed by convenience (see Figure 2) (OECD, 2012). This is confirmed by Ofcom (see Figure 3).

Figure 2 Reasons consumers cite for wanting a bundled package (2009)

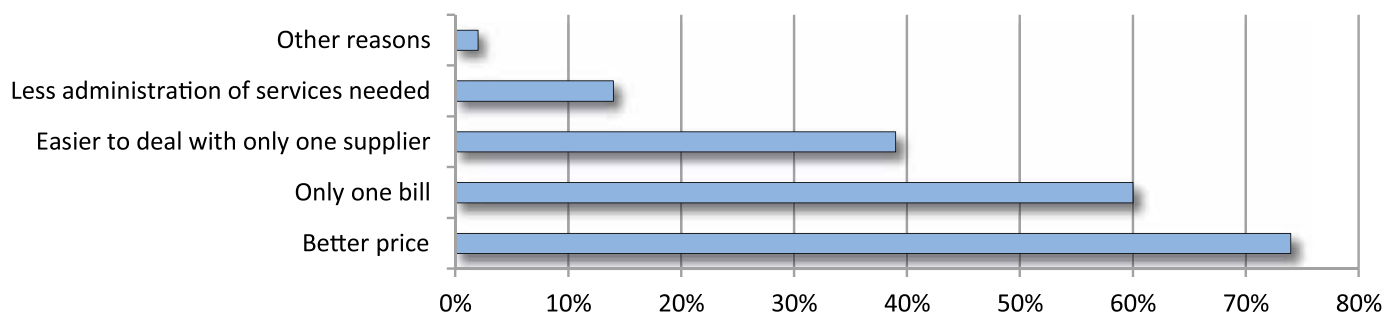
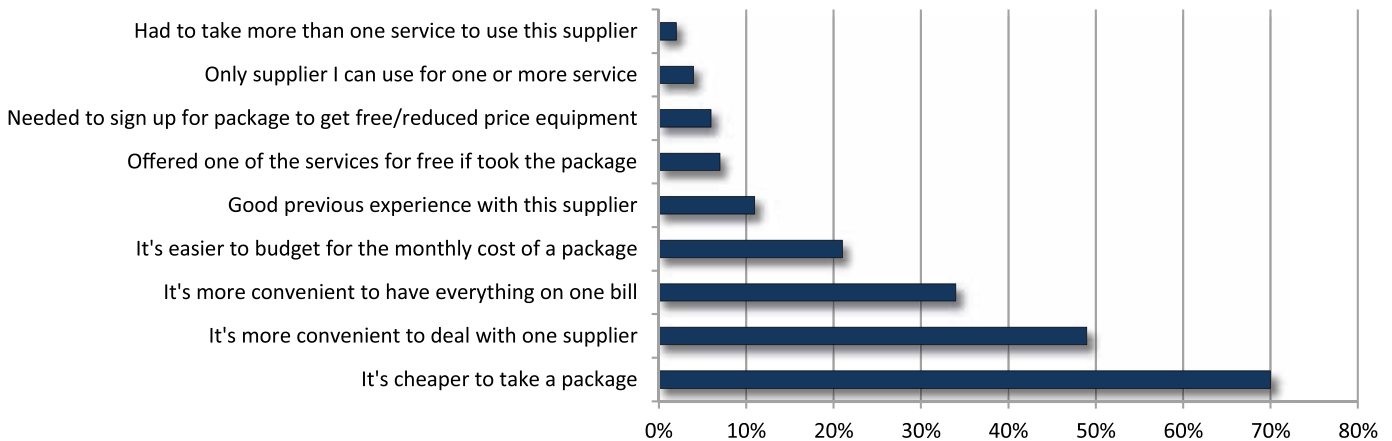


Figure 3 Reasons for deciding to take a bundle of services



Source: Figure 47, Saville Rossiter-Base, 2010

How does service bundling impact the different market players?

The four groups of providers mentioned above have an important recent addition: over-the-top (OTT) providers (e.g., *Skype and Spotify*).

Of the four conventional provider groups illustrated in Table 2, the three that control networks or platforms would need to add services from the others' networks/platforms in order to enter the triple-play market; the fourth group (those without networks or platforms) depends on purchasing access to networks/platforms for all its services.

OTT providers offer their services over the internet. Broadband access is conventionally purchased by consumers, so OTT providers have not depended on access to networks. However, they frequently use content delivery networks (CDNs) to ensure consumers have easy access to their offerings

Fixed network operators already offer fixed voice and broadband services. The SMP providers (those with Significant Market Power) typically have near-ubiquitous coverage and would not need to purchase access to other fixed networks. However, providers with only partial geographic coverage would need access to fixed voice and broadband services from the SMP provider. This is often facilitated through regulated wholesale access services.

Many SMP fixed operators also operate mobile networks. Therefore, in principle, they should be able to offer a triple-play bundle of fixed voice, broadband, and mobile services. Those that do not operate mobile networks would need to purchase access to mobile services to offer triple-play. In most countries, there is no regulated wholesale access to mobile services; therefore, access needs to be on a commercial basis.

Many fixed SMP operators are also developing entertainment services in the form of IPTV. To a limited extent, smaller fixed network operators are also developing IPTV services. The attractiveness to consumers of IPTV services depends critically on the availability of premium content, including sport, movies, and premium television news and entertainment programs. Content rights are heavily guarded commercial property and may only be available to a small group of providers. IPTV could, in principle, enable some fixed network operators to offer a quad-play service bundle.

Mobile network operators need to access fixed networks for broadband services in order to offer the triple-play bundle. Many countries regulate wholesale access to fixed networks, so many mobile network operators should be able to offer the triple-play bundle.

Few mobile network operators have developed IPTV services, although the advent of 4G/LTE networks facilitates IPTV. To offer quad-play, mobile operators would therefore need to negotiate commercial access to content platforms.

PayTV providers fall into two categories:

- *Satellite operators* own and aggregate content and operate the PayTV platform. To provide triple/quad-play bundles, they would need to purchase access to other networks. They could use regulated wholesale broadband services to offer a triple-play bundle of PayTV, fixed voice, and broadband services. Access to a mobile network to offer quad-play would be on a commercial basis.
- *Cable operators' networks* are designed to distribute both entertainment and telecommunications services. Content is typically purchased from satellite operators and other sources. Cable operators do not typically have ubiquitous geographic coverage, but concentrate around larger conurbations. Where they have networks, they could (and many do) offer a triple-play bundle. Outside their network areas, they would need to purchase access to fixed-network wholesale products, and even then would only have a double-play service bundle. To make this a triple/quad-play bundle, the cable operator would need to negotiate access to a mobile network or find a way of offering content services using regulated wholesale broadband access.

Non-network providers operate no infrastructure and need to purchase access to all services. Fixed-network access is typically regulated and should present limited problems. Access to mobile services and/or PayTV services would be on a commercial basis.

OTT providers offer services across internet connections purchased by the consumer, or have so far. In a recent agreement, Google has agreed to pay Orange in Africa for delivery of content (Spence, 2013).

In summary, provision of service bundles is heavily reliant on regulated wholesale access to fixed networks, and many current providers face significant challenges in developing triple-/quad-play bundles (see Table 2).

Table 2 Current regulation of access

| | Fixed voice | Broadband | PayTV | Mobile |
|-------------------------|-----------------------------|--|---|--|
| Fixed network operator | Yes | Yes | Only via IPTV or commercial arrangement | Sometimes; otherwise by commercial arrangement |
| Mobile network operator | Yes, using regulated access | Yes, using regulated access | Only by commercial arrangement | Yes |
| PayTV platform operator | Yes, using regulated access | Yes, using regulated access | Yes | Only by commercial arrangement |
| Non-network provider | Yes, using regulated access | Yes, using regulated access | Only by commercial arrangement | Only by commercial arrangement |
| OTT provider | N/A | N/A, although challenged by Orange/Google deal | N/A | N/A |

What - if anything - could and should regulators do?

The flip side to the positive service stickiness for providers, from a regulator's perspective, is that it increases barriers to switching (e.g., makes it less likely for consumers to switch supplier). Finding a comparable bundle may prove difficult. Only a few providers can offer triple-play bundles, and most would rely on regulated wholesale access and commercial negotiations.

The fixed voice and broadband markets have multiple providers in most developed economies as well as in many developing economies. Many of these do not operate networks and could not offer triple-/quad-play unless successful in commercial negotiations for mobile and/or PayTV. Network and platform operators have few, if any, commercial incentives to provide commercial access and so enable increased competition in the market for triple- and quad-play service bundles.

Should regulators intervene? The European Union framework for electronic communications regulation (used extensively around the world) is based on defining relevant markets and imposing regulation if one or more parties are found to hold significant market power in such a market.

- If consumers prefer to purchase electronic communications services in bundles, should regulators start to define markets of bundled services?
- If so, if SMP is found in the relevant markets, should the EU extend current regulatory interventions to include access to PayTV services and mobile (e.g., mobile virtual network operator access) in order to enable replicability of the triple-/quad-play bundles? Do they have the power to do so?
- Or, alternatively, should regulators reduce or remove current regulations of fixed networks to encourage commercial inter-platform negotiations and competition?
- If so, what would be the future for providers without networks?

These are critical issues that face the sector now - not in three or five years. Inter-platform competition is in many ways a positive development, but should it be to the exclusion of service competition? The EU has built its regulatory framework to encourage infrastructure investment, but it has embraced service competition as a stepping stone to infrastructure competition and as a permanent market feature, presenting continued price competition to infrastructure operators.

Whether bundling represents an opportunity or a threat is likely to be a matter of perspective. Whether consumers' interests are best served by bundles is yet to be seen.

How markets are defined and regulated could determine the future shape of competition. The European Commission is currently reviewing the relevant markets that national regulatory authorities in member states must review; the outcome could be critical in this regard.

The views expressed are those of the author and not intended to represent those of Research Group or other experts at BRG.

Gita Sorensen is a director at Berkeley Research Group (BRG), specialising in economic and strategic advice in the electronic communications sector. Ms. Sorensen provides consultancy service as well as expert opinions in disputes, arbitrations, and litigations.

Contact details: gsorensen@brg-expert.com,
+447789 004509

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