

Telco consolidation - where next after Three and O2?

Blog post by Adviser Conan D’Arcy, 12 May 2016

The EU’s Competition Commissioner Magrethe Vestager announced yesterday she had blocked the proposed merger of Hutchison’s Three and Telefonica’s O2 in the UK. This marks a clear departure from the policy of her predecessor, Joaquin Almunia, who had approved a series of mergers which reduced the number of mobile competitors in national markets from four to three. In contrast, Vestager asserted that only having three mobile competitors in the British market would have had a negative impact both on investment in mast infrastructure and on retail prices for British consumers.

While Vestager has insisted that the Commission will “assess each case on its own merits”, telcos looking to consolidate will take little comfort. They will be acutely aware that regulatory approval from the Commission will come with significant remedies attached, potentially undermining the commercial incentives of deals as happened in Denmark last October when the Telenor and Teliasonera merger collapsed. Next up in the Commissioner’s in-tray is Hutchison’s proposed joint venture with Vimpelcom in Italy, which would likewise see a reduction from four to three competitors and, therefore, is vulnerable to the same charge as Three/O2 that it will increase consumer prices.

With in-market consolidations increasingly unlikely to receive regulatory approval at this level of concentration, the options for companies looking to consolidate market share and profitability are cross-border consolidation or convergence between fixed-line and mobile. Following a period of cross-border expansion within the EU mobile market in the late 1990s and early 2000s, the trend in cross-border market entry has reversed with Deutsche Telekom and Orange pulling out of the UK, KPN leaving the German market and Telefonica exiting Ireland and looking to do the same in the UK.

Instead, it is tie-ups between fixed-line and mobile operators - known in industry terminology as “convergence” - that is attracting both commercial and regulatory approval. BT’s merger with mobile operator EE in the UK was approved earlier this year while Liberty Global and Vodafone have announced a partnership in the Netherlands. Regulators have so far taken a softer stance to cross-industry convergence with the UK’s Competition and Markets Authority judging that the BT/EE merger did not threaten competition despite consolidating an estimated 45% of British mobile spectrum. Commercially, competition in the fledgling “quad-play” market of fixed-line broadband, mobile, TV and fixed-line telephone offers is driving potential deals. With in-market mergers failing the regulatory test and cross-border mergers losing commercial appeal, the impact of Vestager’s decision is that the future of consolidation is “convergence”.