Hypothetical on Margin Squeeze

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Market Players

• AlphaTelecoms
  – Incumbent, enjoyed a legal monopoly until end of 2004
  – Is the only owner of a nationwide fixed electronic communications network; offers broadband connections

• Smaller competitors
  – e-Entrant and Innovator offer broadband services based on access to AlphaTelecoms’ network
  – 7 cable operators operate own networks in certain cities enabling them to offer broadband services
Broadband Market Structure 2010

Access network
Wholesale market

Retail market

Retail market shares

67%
12%
6%
15%
Regulation Imposed on AlphaTel. by TelReg

- Obligations imposed since 1 January 2005
  - Access, interconnection, non-discrimination (inter alia) relating to *voice telephony only*
  - Cost accounting system: long-run incremental costs

- Access obligation valid from 1 January 2009
  - Unbundled access to the local loop; price cap based on cost estimations of AlphaTelecoms and forecasts of costs for the provision of access to the local loop
  - Note: AlphaTelecoms voluntarily provided unbundled access to the local loop from 2007 until the end of 2008
Complaint and Investigation of Highcomp (1)

- e-Entrant’s complaint of 1 January 2010
  - Dominant AlphaTel. conducts margin squeeze since 2007

- Investigation results of Highcomp
  - 2007/2008: negative spread between the wholesale and retail prices of AlphaTelecoms’ broadband offerings
  - 2009 - today: spread was insufficient to cover product-specific costs for providing own retail broadband services
  - Product-specific costs for retail broadband services of e-Entrant and Innovator 20% higher than AlphaTelecoms’
Investigation of Highcomp (2)

• Two e-Mails found at AlphaTelecom‘ offices
  – AlphaTel. knew that the regulated wholesale rate was too high since TelReg´s cost accounting methodology was flawed
  – It decided to use the upper price cap set by TelReg anyway

• Promotional christmas offers in 2008/09 by the competitors had no impact on AlphaTelecoms´ retail market share or price setting policy
Arguments by AlphaTelecoms (1)

• No liability until end of 2008
  – No duty to provide unbundled access to the local loop until end of 2008

• Justification for its conduct from 2009 on
  – Wholesale prices for the regulated local loop access were set in compliance with the TelReg price regulation
Arguments by AlphaTelecoms (2)

• There was no margin squeeze
  – Highcomp wrongfully allocated to broadband retail services costs common to the provision of various telecom services
  – It was normal and inevitable for its downstream division to incur losses because broadband investments need time to yield profits

• Margin squeeze had no effect on the market
  – AlphaTelecoms lost market shares to competitors
  – Cable operators do not need access to unbundled loops
  – Retail prices for broadband access have in fact decreased
Thank you!
Have a good discussion!