CONVERGENCE AND THE EVOLVING TELECOM LANDSCAPE

We continue to see a number of deals where operators are scaling up in core market segments at the country level. Pure-play consolidation in a single market remains popular. Additionally, in the face of the evolving telecom landscape and intensive price competition/increased churn and reduced ARPU across core businesses, operators are also looking to find ways to innovate and develop their offering, including entry into new markets and, for this reason, convergence-oriented deals where communications companies expand their traditional model to include other services and capabilities are also popular. We expect these "convergence" deals to remain popular provided debt and equity markets continue to remain buoyant and there is sufficient regulatory stability and certainty to spur these kinds of transactions.

Competition authorities understand of course that convergence deals can provide real benefits for consumers. Where there is overlap in the parties' activities, as a general proposition, competition authorities will want to ensure that there is real competition going forward, both in terms of pricing pressure from competitors and incentives to continue developing new and innovative products and services. Even where there is no overlap in activities, competition authorities will still want to check that the combination of services will not give the merged entity so much market power that it becomes very difficult for other (non-integrated) market players to compete effectively.

Sometimes a competition authority concludes that a particular proposal goes too far. Earlier this year the Commerce Commission in New Zealand declined to grant clearance for the proposed merger of Sky Network Television and Vodafone New Zealand. As a pay-TV and full service telecommunications provider in New Zealand, the merged entity would have also owned all premium sports content. The Commission was concerned that the potential popularity of the merged operator's offers could result in competitors losing or failing to achieve scale to the point that they would reduce investment or innovation in broadband and mobile markets in the future. More often however, competition authorities will conclude that their competition concerns can be dealt with through commitments offered by the parties to the transaction.

This article considers the various commercial motives for convergence deals, lists some notable examples and also comments on the general trends seen in commitments, in cases where they do need to be agreed with competition authorities in order to secure competition clearance.

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MOTIVES FOR CONVERGENCE DEALS

The motives for convergence deals are numerous and will depend on the operator's business objectives and the specific market dynamics, but may include:

- Offer the full range of communications services (fixed telephony, broadband, pay-TV and mobile) and complementary products to the combined customer base and thereby stabilise and/or increase ARPU/ overall share of customers' wallets.
- Increase customer satisfaction:
  1. Customers benefit from having all services on a single bill, plus the bundled price is usually offered at a discount to the combined standalone price of the included services which represents value for money for customers.
  2. Customers benefit from having all forms of communication and delivered seamlessly across platforms.
- Meet increasing consumer demand for service bundles.
- Increase customer 'stickiness'/reduce customer churn.
- Offer operators the means to upgrade and create products and services for their customer base and develop new revenue streams.
- Increase ability to compete against the scale Internet companies which have been able to embed many of the traditional telecoms services into their offerings, often at little or no cost to their customers (eg, Facebook Messenger, WhatsApp, Skype, Viber etc.).
- Respond to bundled offerings of competitors in the market eg, in the UK recently there has been a market shift towards a quad-play environment with BT's acquisition of EE, Vodafone's plans to offer broadband and TV and Sky's response in the form of launching its own MVNO.
- Achieve network efficiencies and cost efficiencies by eg, accessing fixed networks for mobile backhaul (for themselves and other operators) and data offload to increase capacity across the network.
- For fixed operators, increase the usage level of their fixed networks and therefore the efficiency of the deployment and optimisation of the investment.
- Achieve operating cost and capex synergies (and therefore improve margin) from consolidating sales and marketing operations; procurement savings; IT and network savings through consolidation of IT and network development/operations and phased migration away from duplicate customer support systems; customer service savings from insourcing overseas and third party contact centre resources and expanding online/self-service facilities; and other savings from not duplicating head office functions and property. It is argued that these synergies will give a merged entity increased investment capacity to further develop and deploy new networks and services, including converged offerings, to consumers.
- Access expertise for converged fixed-mobile product development.

RECENT CONVERGENCE DEALS

There have been numerous multi-sector mergers across the EU in recent years, reflecting a convergence strategy of some of the leading global operators.

UK-based Vodafone has pursued a market-by-market convergence strategy, acquiring cable assets in recent years. Vodafone's high speed data networks in Europe in 2017 can reach 315 million people with 4G mobile and 96 million households with fixed broadband. "*Today, consumers are increasingly taking bundles of mobile, landline, broadband and TV services. For the consumer this provides the benefit of simplicity – one provider for multiple services – and better value. For operators this provides higher customer loyalty as well as operational efficiencies*." (Vodafone Annual Report, 2017).

Orange is adopting a similar strategy. In relation to the Jazztel acquisition, Orange CEO Stephane Richard said in 2015: "*We are doing this deal to accelerate our growth in Spain, particularly around fixed-mobile convergent offers*."

Table 1 below shows a selection of recent multi-sector mergers, both in developed and developing economies, including a description of each transaction and its status.

TABLE 1: Selection of recent multi-sector mergers including a description of each transaction and its status

DATE	COUNTRY	PARTIES	SUMMARY	STATUS
2017	Italy	Vivendi and Telecom Italia	Telecom Italia provides voice and data services through mobile and fixed technologies, digital content services and IT services. Vivendi is active in the music, TV, cinema, video sharing and games businesses.	Complete Cleared by the European Commission, subject to Telecom Italia selling its stake in a JV providing wholesale access to digital terrestrial networks for the broadcast of TV channels.
2017	Malta	Melita and Vodafone Malta	Melita is a quad-play operator, offering cable television, internet and mobile and fixed telephony. Vodafone Malta offers mobile phone services and nationwide Wi-Fi internet coverage.	Proposed In July 2017, the Maltese competition authority began a phase 2 investigation; a decision is expected by the end of November.

DATE	COUNTRY	PARTIES	SUMMARY	STATUS
2017	UK	Three and UK Broadband	Mobile operator Three (owned by Hong Kong- based CK Hutchison) acquired UK Broadband which is a fixed operator providing broadband access to 15,000 customers across the UK.	Complete Cleared by the UK's competition authority, the CMA.
2016	New Zealand	Sky and Vodafone New Zealand	Combination of telecom and media assets to create leading integrated provider of telecoms and media.	Abandoned The New Zealand competition authority blocked the merger because the combined entity would control the rights to broadcast all New Zealand premium live sports content.
2016	Netherlands	Vodafone and Liberty Global (Ziggo)	Merged their Dutch operations to form a 50:50 joint venture to create an integrated fixed and mobile provider across broadband, video, fixed telephony and mobile.	Complete Cleared by the European Commission subject to Vodafone divesting its consumer fixed line business in the Netherlands.
2016	UK	BT and EE	Incumbent fixed communications operator BT (voice, broadband and pay TV) acquired mobile operator EE.	Complete Cleared by the CMA.
2016	India	Vodafone India and YOU Broadband	Mobile operator Vodafone acquired You Broadband to boost Vodafone's fixed line offering. You Broadband has around 3,000km of fibre and 6,000 km of last mile cable serving homes in 12 cities.	Complete Approved by the Foreign Investment Promotion Board.
2016	Vietnam	MobiFone and AVG Vietnam	MobiFone acquired a 95% stake in local pay-TV operator AVG to boost its offerings in advance of the digital switchover in 2020.	Complete
2016	Moldova	Orange Moldova and Sun Communications	Incumbent operator Orange acquired cable provider Sun Communications as part of plans to offer converged packages of fixed line and TV services.	Complete Cleared by the Moldovan competition authority.
2015	Belgium	Liberty Global (Telenet) and BASE	The transaction brought together BASE, one of Belgium's three mobile network operators, with Telenet, a Belgian cable operator controlled by Liberty Global that also offers mobile services as a mobile virtual network operator.	Complete Cleared by the European Commission subject to Liberty Global and BASE agreeing to sell part of their customer base to a new virtual mobile operator.
2015	Spain	Telefónica and DTS	The transaction involved the purchase of the remaining 56% of shares of DTS.	Complete Cleared by the Spanish competition authority, subject to Telefónica offering competitors wholesale access to its premium channels and various internet / pay per view commitments designed to ensure that customers can also use competitors' services.

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DATE	COUNTRY	PARTIES	SUMMARY	STATUS
2014	Spain	Orange and Jazztel	Incumbent operator Orange merged with Jazztel which provides telecoms services in Spain through a subsidiary. Orange and Jazztel both provide fixed telecommunications services in Spain.	Complete Cleared by the European Commission subject to Orange divesting its Fibre-To-The-Home network as well as granting that purchaser wholesale access to Jazztel's national ADSL network and wholesale access to its mobile network, to enable a fourth operator to enter and compete effectively.
2014	Netherlands	Liberty Global (UPC) and Ziggo	Liberty Global and Ziggo are both cable TV operators and provided fixed and mobile telecommunications services to end consumers in the Netherlands. The merger brought together the first and second largest cable TV networks in the Netherlands.	Complete Cleared by the European Commission subject to Liberty Global divesting a premium film channel and agreeing not to prevent broadcasters from offering their channels and content over the Internet.
2014	Spain	Vodafone and ONO	ONO is a Spanish pay TV and fixed telecommunications company which Vodafone (mainly active in mobile telecoms) acquired, providing an integrated communications provider in Spain.	Complete Cleared by the European Commission
2014	France	Altice (Numericable) and SFR	Numericable is a cable operator and telecoms services company which acquired Vivendi's SFR mobile telecoms affiliate.	Complete Cleared by the French competition authority subject to Numericable agreeing to give competing operators access to its cable network and divest its copper network and an overseas mobile business. Numericable also agreed that no strategic information would be provided to Vivendi, which retained a minority stake in Numericable.
2014	Belgium	Liberty Global (Telenet) and De Vijver Media	Liberty Global took a 50% stake in De Vijver Media alongside an additional cash investment. De Vijver was a private Belgian broadcaster and Telenet was a cable company.	Complete Cleared by the European Commission subject to De Vijver agreeing to license its channels to TV distributors in Belgium under fair, reasonable and non-discriminatory terms.
2014	Portugal	Altice and Portugal Telecom	Altice provides pay TV, fixed internet access and fixed telephony services to residential customers. PT provides telecoms and multimedia operations to residential companies as well as a range of business services.	Complete Cleared by the European Commission subject to Altice selling its corporate telecoms and cable company in Portugal.
2014	South Africa	Vodafone and Neotel South Africa	Planned acquisition of Neotel by Vodafone, to gain fixed network assets and additional spectrum.	Did not complete due to regulatory issues
2013	Germany	Vodafone and Kabel Deutschland	Global operator Vodafone acquired Kabel which owns and operates cable networks in most of Germany providing TV and telecoms services over the cable network.	Complete Cleared by the European Commission

DATE	COUNTRY	PARTIES	SUMMARY	STATUS
2013	UK	Liberty Global and Virgin Media	Created second biggest pay-TV business after Sky and at the time the world's biggest broadband company.	Complete Cleared by the European Commission
2013	Germany	Deutsche Telekom and GTS	Incumbent operator Deutsche Telekom acquired GTS which was one of the top infrastructure-based providers of telecommunications services in Central and Eastern Europe, owning and operating an extensive fibre optic and data centre network throughout the region.	Complete Cleared by the European Commission
2012	UK	Vodafone and Cable and Wireless Worldwide	Cable Wireless Worldwide was acquired by Vodafone in order to add a UK fixed line network to Vodafone's existing mobile network.	Complete Cleared by the European Commission

GENERAL THEMES BEHIND COMMITMENTS/REMEDIES

Regulatory scrutiny has obviously increased as markets have become more concentrated. But regulators have also recognised the consumer benefits of having multi-play operators. For this reason we see many conditional decisions, with the parties agreeing (or sometimes not agreeing) to commitments to get the deal through. These commitments fall broadly into the following two categories:

1. **Divestments** – the most clear-cut remedy to deal with competition concerns. Divestments are traditionally preferred by competition authorities, and there has been an increasing trend to require the parties to find a purchaser for the relevant assets up-front. For example, we have seen divestment remedies in network infrastructure (an optical fibre network in the Orange/Jazztel merger, and a copper DSL network in Numericable/SFR merger), content providers (selling a pay TV/fixed line subsidiary in the Altice/PT Portugal merger), businesses dealing with market segments such as business customers (in the Altice/PT Portugal merger) and brands/customers (transferring to a third party customers of a particular mobile brand in the Liberty Global/BASE merger).

2. **Access remedies** – these are always more complex to set up but have been adopted to give network access to third parties on fair and reasonable terms. We have seen access remedies such as wholesale access to a national ADSL network for a fixed period of time in the Orange/Jazztel merger, and wholesale access to a cable network in the Numericable/SFR merger to enable competitors to provide their own very high speed fixed telecom services. Access to premium TV content was also agreed in the Telefonica/DTS and Liberty Global/De Vijver Media mergers. These remedies also need an effective monitoring mechanism to be implemented to ensure there is no distortion of competition. Sometimes other safeguards are also built in such as restrictions on providing information to shareholders who have competing activities (eg in the Numericable/SFR merger firewalls were put in place to prevent certain strategic business information from being passed to Vivendi).

CONCLUSION AND PRACTICAL CONSIDERATIONS/TIPS

From a practical perspective, competition clearance will of course be harder to secure the more consolidated the market, both within and across multi-play sectors, so the advice is to get in early.

In especially complex deals where there is a real risk that the proposed transaction will give rise to substantive competition concerns then it is recommended that time is built into the transaction timetable for strategic planning with legal advisors/economists and holding detailed, confidential pre-notification talks with the relevant competition authorities. Clean teams and integration planning teams should be set up from the outset to ensure that commercially sensitive information is handled correctly. Any third parties who object to the proposed transaction will try to lobby the authorities as soon as the deal is announced. It is important, therefore, to understand the scope of any competition concerns as early as possible so that you are well placed to rebut them with evidence in the formal merger filing.

If the competition authority is likely to insist on remedies it is good to have early notice of this – again to try to rebut the need for any remedies but also to consider what you are prepared to offer up if this is the only way to get the deal through. This approach may save you time later on in the merger filing process and will also need to be reflected at least to some extent in the transaction documentation. With the increasing trend for "fix it first" remedies, it is also worthwhile starting to think about third parties which are likely to be suitable and interested purchasers. Contacts between the purchaser and the target/possible remedy-takers all need to be handled carefully, to protect commercially sensitive information and ensure that the purchaser does not "jump the gun" by exercising too much control over the target business before securing merger clearance.

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We also recommend ensuring that all company documents (external and internal) reflect the realities of the competitive market pressures you face. In our experience, competition authorities are likely to put more weight on a company's contemporaneous views on their competitors, rather than legal submissions in a merger filing. In the more detailed merger investigations the European Commission in particular is developing a reputation for requesting huge numbers of internal documents (ie, hundreds of thousands of internal documents and emails) to check the company's own view of the market in which it is competing – it makes sense therefore to talk realistically about the market and the companies you are competing with, directly and indirectly.

OTHER OPTIONS TO ACCESS INFRASTRUCTURE FOR CONVERGED OFFERINGS

Whilst this article has looked at acquisitions of and mergers with competitors so far, there are of course other options available to operators to access infrastructure. For fixed operators, they can achieve this by launching their own MVNO - negotiating a wholesale national roaming agreement with a mobile network operator. For scale mobile operators who have a strategy of securing access to high speed broadband infrastructure, they can achieve this in a variety of ways - building their own fibre (either alone or co-investing), wholesaling (renting from incumbent operators) or as described above through acqusitions or mergers.

The approach mobile operators will adopt will usually be determined on a market-by-market basis, taking into account the mobile operator's business objectives, the cost of building their own fibre, the economics of wholesale terms on offer, and the availability of good quality businesses to acquire.

Table 2 below briefly describes some of the issues associated with each such infrastructure access model.

TABLE 2: Some of the issues associated with each infrastructure access model

INFRASTRUCTURE ACCESS MODEL	COMMENT
Acquisition	Acquire stand-alone business with fibre or cable infrastructure. Regulatory uncertainty and possible competition concerns/requirement for commitments. Usual M&A risks eg, integration risk.
Own investment	Invest in building own fibre network (typically FTTH/P but can be FTTC). There are not many examples of own investment most likely due to cost and capability concerns, however in the mid-term, cloud technologies such as network virtualization and software-defined networks could significantly reduce fixed-line costs resulting in more own investment in fixed infrastructure. Cost mitigation – access to/re-use of fixed incumbent's passive infrastructure (ducts and poles) or a utility network for purposes of build. Regardless, there will be a long pay-back period eg 20 years.
Co-investment/JV/ strategic collaboration	Invest with utility companies eg, Vodafone and ESB in Ireland. Invest with other operators eg, Vodafone and Orange in Spain. Regulatory issues if eg, one party has significant market power.

INFRASTRUCTURE ACCESS MODEL	COMMENT
Wholesale access	Can take a number of forms: ◦ Resale – operator resells fixed incumbent's capacity eg, recently Telefónica and Vodafone España agreed a deal that will give the latter access to the telecom incumbent's fibre optic network to extend the reach of Vodafone's fixed network and offer ultra-high-speed broadband and TV services to a wider potential base of customers. ◦ Bitstream access – operator develops and sells own products utilising incumbent's infrastructure and equipment. ◦ Local loop unbundling – operator develops and sells own products using its own equipment installed in incumbent's infrastructure. Ability to obtain regulated or equivalent access to infrastructure of fixed incumbent – access typically regulated under the EU telecoms regulatory framework, but access terms vary across markets and in some cases may not facilitate the entry of a new competitor on the market who can replicate or undercut existing retail prices.
	Will require access to backhaul connections – to backhaul broadband traffic from incumbent's exchanges (where they have co-location equipment to aggregate unbundled local loops) to their core networks. The capacity and price of those connections affects the speed and cost of downstream mobile and asymmetric broadband. Can be through wholesale leased lines or through commercial or regulated dark fibre. In addition to wholesale access to the infrastructure of scale providers of communications infrastructure, wholesale access can also be gained to NGA networks of smaller alternative providers (altnets) who have built FTTP/H, fixed wireless or satellite networks.

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