

UPDATE: State of prepaid market in South Africa Submission to the Parliament of South Africa on “The Cost to Communicate in South Africa”

- Vodacom, MTN and Cell C are competing more and more on customised products for subscribers instead of strict service pricing.
- Telkom fails to exert pressure on other operators despite undercutting competitors' voice tariffs and monthly data prices.
- Cell C's strategy to champion best-value products, cheapest voice and SMS products, and subsidising an exclusive zero-rating strategy with a global social networking platform makes it the leader of the prepaid pack.
- Customised products from service providers may result in reduced cost of communication but this requires high levels of consumer awareness to check the terms and conditions of such services which may have time or product limitations.

Introduction

Pent up demand for internet service has driven strong growth in data revenues for operators throughout Africa. Traditional voice and SMS revenues have, in turn, been shrinking but still make a significant contribution to operator revenues.

Operators are launching promotional and personalised data products as a means of retaining and gaining revenue.

With Over-the-Top (OTT) services increasingly acting as substitutes for the traditional voice and SMS services, operators are opting not to raise prepaid prices on their cheapest tariffs as a means of making up for lost revenues. Regulatory interventions such as cost-based termination rates have created consumer expectations of continued price reductions in voice offerings.

Although some operators called for regulation of OTTs in the South African mobile market at Parliamentary hearings held earlier this year, their innovative new pricing strategies suggest responsiveness to this fast-changing environment.

South African operators, in line with operators in other markets, have responded to disruptive OTT services by introducing new products such as bundled data, voice and SMS, or service-specific promotions. Are these new products easier on the pockets of consumers and are they transparent enough for consumers either to understand their value or their conditions?

Pricing trends in South Africa

Research ICT Africa (RIA) measures the cost of communication by mapping African mobile prepaid pricing trends with a Voice and SMS basket, the RIA 1GB data basket and the Bundled Value for Money Index. Both, the Voice and SMS basket

and the 1GB basket methodology calculate the minimum price for consumers in the South African market.

Methodology:

Voice/SMS basket (OECD basket): 30 voice calls for a total of 50 minutes and 100 SMSs per basket per month.

1 GB basket: monthly cost of 1GB data based on prepaid data top-ups or bundled top-ups. Both baskets are converted to USD for comparison across African markets.

Voice and SMS basket

Using the second quarter benchmark analysis South Africa is ranked 10th out of 49 other African countries for the voice and SMS basket. South Africa falls behind Kenya and Egypt of better priced voice and SMS products.

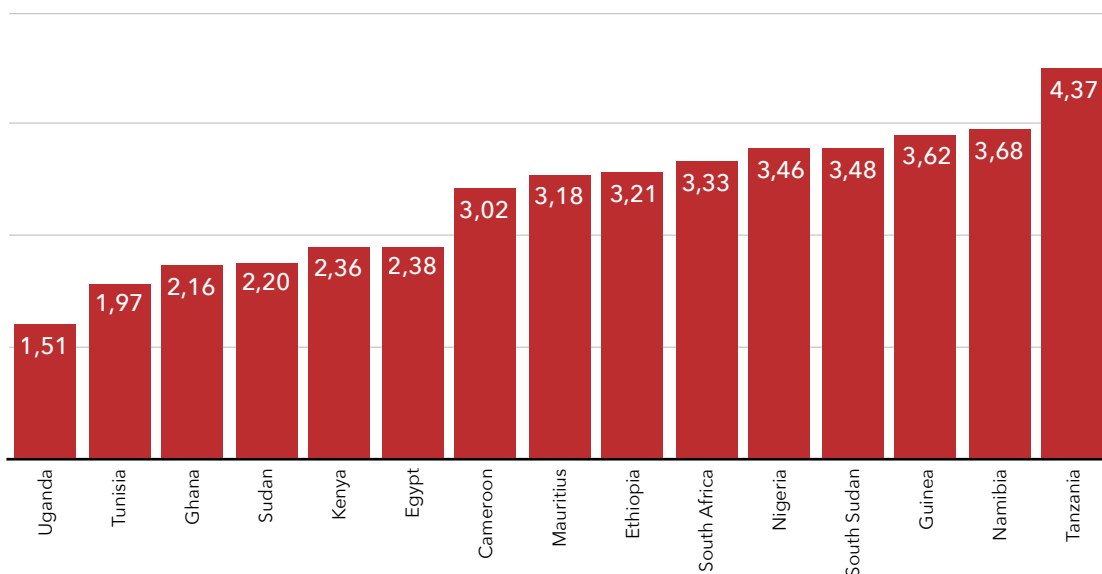


FIGURE 1: Top 15 countries on OECD based index in (USD) Q2 2016

Source: RIA African Mobile Pricing (RAMP)Index

Telkom Mobile, which has traditionally had the cheapest voice and SMS basket in South Africa, has been dethroned by Cell C (see Figure 1). The cheapest Voice and SMS basket would be satisfied by the Mega Bonus R5 reward product. The customer gets R10 extra for a R5 recharge leaving them with R15's worth of value (but valid for three days). As the Voice and SMS basket calculation is based on a monthly recharge calculated for 30-day validity, the Mega Bonus product has an airtime value of R150, which costs only R50 for the customer. For consumers willing to recharge R5 every three days for this value, this would be the cheapest product for Voice and SMS basket in South Africa. However, when looking at voice tariff prices, subscribers pay a higher tariff of R1.50 in comparison to R0.66 on Cell C's cheapest tariff.

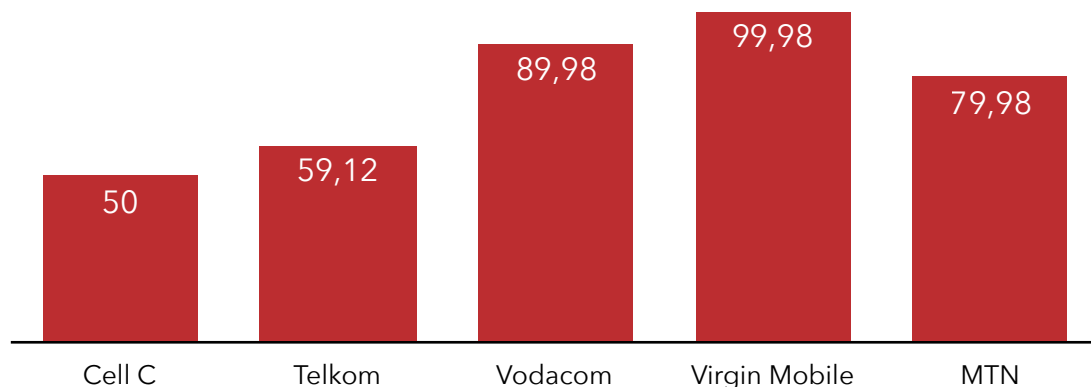


FIGURE 2: VOICE AND SMS BASKET COST TO CONSUMER (ZAR)
SOURCE: RIA AFRICAN MOBILE PRICING (RAMP) INDEX

Cell C's 66cents product has the cheapest flat tariff in comparison to MTN's and Vodacom's cheapest flat tariffs of R0.79. Vodacom's R0.79 is a promotional product¹. While the cheapest flat tariffs are the same, MTN's cheapest voice and SMS products, Signature R35 monthly, comes with R45 inclusive value.

Telkom's strategy on the prepaid market has been to undercut on-net and data prices to swing subscribers in the growing prepaid market to?????. Its Sim-Sonke product, with the cheapest on-net tariff of R0.29, makes it the second cheapest operator in the Voice and SMS basket comparison (Figure 1). It also has the cheapest 1GB product on the market at R99 per 1GB (see Figure 3 and Table 3). At the same time, its 2GB is even cheaper than the price of 1GB offered by other operators at R139. This has resulted in a 37% increase in data revenue due to a large growth in mobile data traffic².

Telkom Mobile experienced a 24% growth in total number of subscribers for the financial year ending March 2016. However, low-price strategy does not appear to be drawing subscribers in significant numbers.

1GB data basket

Regionally, data prices remain expensive. South Africa's cheapest 1GB data places it at 16th of out 47 African countries assessed by RIA. Tanzania has the cheapest 1GB for USD0.89 in comparison to South Africa priced at USD 5.26 (see figure 3). In comparison to other large markets, Egypt, Kenya and Nigeria have better data prices compared to South Africa.

¹ Vodacom 79c Ts&Cs: <http://www.vodacom.co.za/vodacom/terms/promotions/vodacom-prepaid-79c>

² RIA Policy Brief no. 2 2016: SA mobile operators wake up as 2020 draws closer <http://goo.gl/D5ihdB>

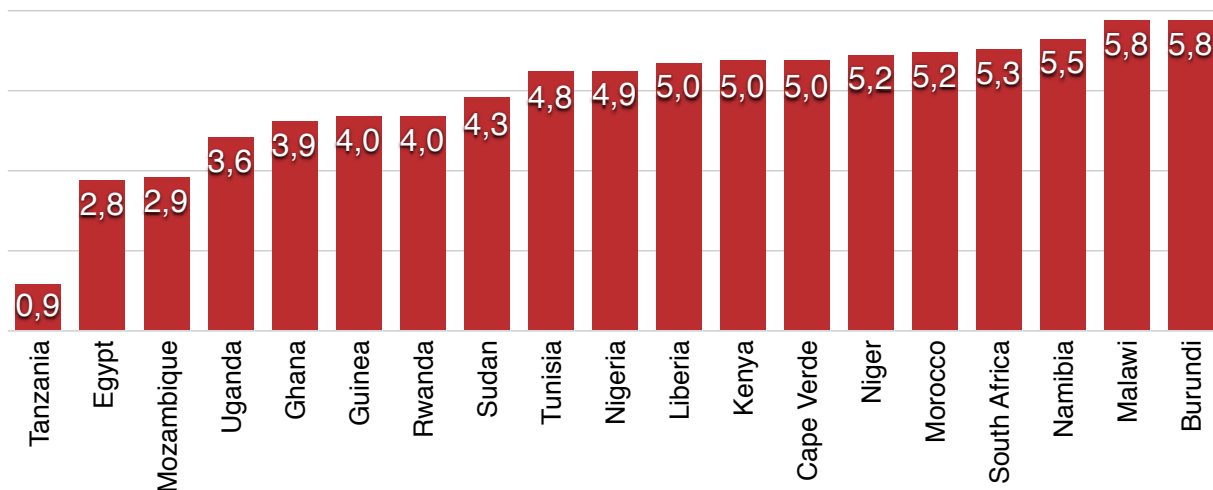


FIGURE 3: 1GB COST TO CONSUMER TOP 20 COUNTRIES IN USD. SOURCE: RIA AFRICAN MOBILE PRICING (RAMP) INDEX

The 1GB data basket in the South African market has not seen much change with operators either introducing competitively priced smaller data packs; running promotions that differentiate their data offerings or changing prices for lower or higher data volumes³. All operators, except for Telkom Mobile and MTN, advertise 1GB of mobile data for prices around the R150 mark (see Table 1).

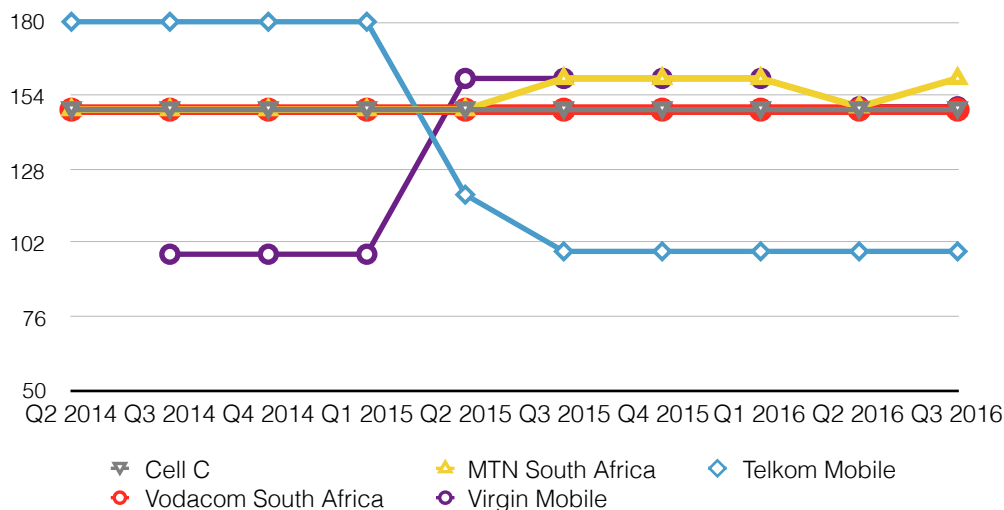


FIGURE 4: 1 GB DATA BASKET (ZAR) Q2 2014-Q2 2016; SOURCE: RIA AFRICAN MOBILE PRICING (RAMP) INDEX

MTN introduced a daily bundle in the last quarter which, purchased daily for a month, would work out cheaper than their monthly 1GB, which drove its cheapest 1GB to R150. The promotional price which had been R5 went up to R6 which if purchased daily would cost R180 a month. Thus MTN’s standard 1GB bundle priced at R160 a month, is the most expensive of the ‘cheapest priced bundle’ on the market but, it offers prepaid customers 50% give-back on that data valid for 15 days. A customer who pays for 1GB will be given back 500MB. Therefore whilst it is the most expensive 1GB, the reward component offsets the highest price. However this benefit comes with a limited time validity of 15 days.

³ Cell C data price increases: <http://mybroadband.co.za/news/cellular/167090-cell-c-data-price-increases.html>

| Table 1: Operator monthly 1GB prices in Q3 2016 | Price (ZAR) |
|---|-------------|
| Telkom Mobile | 99 |
| Cell C | 149 |
| Vodacom | 149 |
| Virgin Mobile | 150 |
| MTN | 160 |

Vodacom's 1GB offered under the "Just 4 You" promotion has an advertised price of R79, almost half the price of their 1GB product - incredible value for those using data primarily as text and voice substitutes. As the validity of "Just 4 You" products is customised for consumers, validity cannot be determined for the purposes of basket measurement and is therefore excluded.

Product re-creation in the prepaid market

As the above indices show, the cheapest products on the market are not simply based on the tariff or once-off cost, but rather product features that seem designed for different customer needs based on validity, volume or price.

Vodacom introduced the "Just 4 You" promotion customised for individuals with offerings that change constantly. For example, one could get a promotional pack for data or for making voice calls or for a combined service top-up with minutes and data based on the menu selection for the day. Vodacom reserves the right to vary offers therefore customers will not always have the same offer available.

Customers need to be aware of the time sensitivity of these offers, knowing that they might not find the same offer again. Vodacom also introduced the "NXT LVL" tariff package for users not older than 25, seemingly designed to entice those users into the market. The package carries certain benefits and rewards such as zero-rated career service sites and Vodacom's e-school.

With significant investments in infrastructure development, as in the case of Vodacom and MTN, it is clear that the dominant operators will also be seeking to distinguish themselves on quality and their ability to keep up with growing demand for data⁴.

Bundled Value for Money Index

New pricing innovations that include multiple services that are bundled together and discounted are also new to the market⁵. RIA created the Value Money Index (VMI)⁶ as a means to capture the value of combined data, SMS and voice packages on offer. Given the complexity and high number of products on the market, only bundles offering data, or application specific data, combined with voice and/or Sases are captured.

Product types:

Combined-service top-ups or bundles

Buying two or more volumes of service combinations e.g. minutes+data; SMS+data; minutes+SMS+data+application.

Rewards plans

Customers receive activity-based rewards such as airtime or redeemable points after using a service.

⁴ RIA Policy Brief no. 2 2016: SA mobile operators wake up as 2020 draws closer <http://goo.gl/D5ihdB>

⁵ RIA Policy Brief No. 3 2015: Bundling up – new pricing strategies in the African prepaid market <http://goo.gl/LFu4kb>

⁶ Refer to RIA website for methodology: http://www.researchictafrica.net/fair_mobile.php

Vodacom, Cell C and MTN offer combined bundles (see Table 2) often in product families such as MTNSky and MTN Boosta. Cell C offers the Infinity range with a flat price and the SupaCharge that ranges from R5 to R500.

Cell C's Supacharge products dominate the BVI, with Supercharge 500 having the best BVMI. Cell C's Supacharge volumes and validity increase as one recharges with between R5 and R500 airtime. The highest and lowest priced bundles both offer the best value compared to other South African products on the BVMI with Cell C's Supacharge R5 product offering the second-highest value on the market.

However these benefits are only possible on airtime recharge; that means data recharges or bundle purchases do not qualify one for the Supacharge bonus.

MTN has the third most valuable bundle on the Index: MTN's Sky Unlimited Uncapped product. However, a fair use policy limits daily minutes, SMS and data as stated by the operator (See Table 1 for limits).

| Table 2: Bundled Value Index (Q2 2016) | | Price (ZAR) | Validity | Free on-net Minutes | Free all minutes | Free SMS | Free MB | BVI |
|--|---------------------------------|---|----------|---------------------|------------------|----------|---------|------|
| CellC | Supercharge R500 | 500 | Month | 7200 | 0 | 1000 | 1000 | 1,55 |
| CellC | Supercharge R5 daily (30 times) | 5 | Daily | 120 | 0 | 120 | 120 | 1,14 |
| MTN | MTN Sky Unlimited Uncapped | 1799 | Month | 4500 | 4500 | 12000 | 10000 | 1,05 |
| MTN | Boosta 79 | 79 | 10 days | 600 | 0 | 600 | 1500 | 1,02 |
| MTN | Boosta 339 | 339 | Month | 700 | 0 | 700 | 2000 | 0,95 |
| Voda com | Just for you 60 | 60 | Other | | 60 | 0 | 60 | 0,9 |
| MTN | Boosta 189 | 189 | 15 days | 1000 | 0 | 1000 | 2000 | 0,87 |
| MTN | Boosta R39 | 39 | 5 days | 600 | 0 | 600 | 1200 | 0,85 |
| MTN | MTN Sky Absolute 2GB | 599 | Weekly | 4200 | 4200 | 12000 | 8000 | 0,65 |
| MTN | MTN Sky Super Uncapped | 999 | 15 days | 4500 | 4500 | 12000 | 6000 | 0,64 |
| MTN | MTN Sky Super 1GB | 999 | Month | 4500 | 3000 | 12000 | 1000 | 0,49 |
| MTN | MTN PAYG R35 | 1599 | Month | 462 | 308 | 700 | 525 | 0,43 |
| CellC | Infinity | 1000 | Month | 0 | 7200 | 1000 | 1024 | 0,38 |
| MTN | MTN-to-MTN Sky Daily | 25 | Daily | 4500 | 0 | 0 | 300 | 0,27 |
| MTN | MTN Sky Daily | 79 | Daily | 4500 | 4500 | 12000 | 600 | 0,20 |
| MTN | MTN PAYG R7 | 7 | Daily | 180 | 120 | 75 | 75 | 0,18 |
| | | *Data, Voice minutes and SMS indicated above are monthly volume calculation | | | | | | |

MTN has the widest range of bundled products on the market. This is an effective strategy against OTTs because unlimited calls, data and SMSes means that the relative value of OTTs to consumers decreases. The only factor that might undermine this strategy is the people they are communicating with are using OTT substitutes only or primarily.

Vodacom's "Just 4 You" combined bundle is based on the advertised product on the Vodacom site. It is the 6th best product available on the BVI market. However its customisation means validity and availability is only determined if it is offered to the customer on the "Just 4 You" menu.

Zero-rated services

Zero-rating is a relatively new tactic for South African operators. Cell C became the first mobile operator to offer South Africans access to the globally controversial internet.org (subsequently Freebasics) at the end of August 2015. Cell C is the only South African operator subsidising an exclusive zero-rating strategy with a global social networking platform by partnering with Freebasics. As in most other jurisdictions where zero-rating of this kind is occurring this is a late-entrant strategy to attract new customers onto their network and compete for customers with their much bigger rivals.⁷ Cell C was also the first mobile company to discount data use for WhatsApp. It is the only operator that zero-rates WhatsApp with its Trace Mobile Pack. It also has a R7.50 unlimited WhatsApp pack that excludes voice calling for customers.

| Operator | Product | Features |
|----------|-------------------------|--|
| Cell C | Freebasics | internet.org application |
| | WhatsApp | Free WhatsApp on Trace Mobile |
| Vodacom | Vodacom e-school | Educational learning app. Also zero-rated on NXT LVL plans. |
| | Career sites | Zero rated on NXT LVL. |
| MTN | Twitter | |
| | Wikipedia | Only when accessed on Opera Mini. |
| | D6 communicator service | Allows schools to communicate with parents. (100MB data cap) |
| | MTN play | Selected sites are zero rated. |
| | MTN Vu | Video streaming service Max Vu subscribers only. |

Vodacom and MTN South Africa have vehemently opposed OTT players in the mobile broadband market that compete with their voice and text services. This opposition arose as a reaction to the prominence of Facebook Mobile, Messenger

⁷ See Gillwald, Chair, Futter, Koranteng and Walubengo (2016) Much Ado About Nothing? Zero rating in African Context. http://www.researchictafrica.net/publications/Other_publications/2016%20RIA%20Zero-Rating-Much%20ado%20about%20nothing_Policy_Paper.pdf

and WhatsApp. Both operators clearly see OTTs as a threat to their traditional business. It appears that now their strategy is to counter it by offering attractive combined bundles and a wide range of their own zero-rated products.

The OTT services that the dominant operators do offer, either do not compete directly with their traditional services or are products that they have developed with local partners. For example, Vodacom zero rates their e-school application for all users while MTN zero rates entertainment sites. This helps demonstrate the dynamism in the mobile market and the strategies required by operators to remain relevant and profitable.

Conclusion

New pricing strategies and products available on the market have clearly moved away from a single tariff or price for a single service to variable value bundles of services to meet the diverse needs of users. This tariff innovation makes the effective price of products way below the price of IGB as advertised for particular customer and increasing difficult to measure and compare.

Consumer awareness

For a customer to get the best product, they need to determine what it is they value and what works best for them from the options that service providers are pushing. Although prepaid products are flexible, this dynamic market makes it important for the consumer to be aware of the terms and conditions of all services in order to determine eligibility for a package and the conditions attached to changing to apparently beneficial packages.

Leveraging global platforms

Operators generally with a smaller voice market share are entering into relationships with global social network platforms to attract customers to data services from where their revenues will increasingly come. Cell C is leading the pack in terms of products targeting price sensitive users by offering higher-value bundled products, cheaper-priced products and price-cutting products such as zero-rated Freebasics and an unlimited WhatsApp bundle (with no calling).

More than price

Though Telkom offers considerably cheaper on-net tariffs and data prices, it has not been able to exert pressure on its competitors to reduce prices, particularly in the data segment. As its market share of only 2.6% indicates even price sensitive users are not selecting the operator on price alone. The perceived lack of ubiquity of the network, the quality of service, the cost associated with moving to a new operator and brand perception are possibly the issues deterring price-sensitive customers from responding positively to the high-value product.

Valuing broadband

RIA found with these dynamic new tariffs and bundles that its approach of benchmarking voice and SMS prices used in the past to compare countries (as in the Voice and SMS basket and 1GB data basket) failed to explain the dynamism

and innovation in the mobile sector. New strategies to retain revenues and shore up subscribers are continually being tested, compelling RIA to revise its measures. The BVI is a critical tool in evaluating operator strategies in this dynamic market. A combination of the Voice and SMS user basket, the 1GB data basket and the BVI provides insight into which strategies are working for operators as well as the potential opportunities for smaller operators. Promotions have not been included in the valuation. Incumbent operators are using these to retain customers and defend their products from OTT services that are acting as substitutes for voice and SMS services.

Voice-text substitution

The supply-side assessment of pricing highlights the shift in operator revenues from voice to data. This is reflected in the rise of bundled voice and data packages that seek to retain traditional voice and text users in the face of data-based substitution of these services.

With the increasing availability of alternative means of connectivity, such as public WiFi and high speed broadband access at schools and colleges, there is need to understand the impact of such aggregated demand points have on user strategies to access and use services affordably.

Recommendations

While the effective prices of data may be well below the advertised price of the 1GB measure used internationally, users, especially those in the lower income category, are spending significant portions of their income (around 20%), on relatively small amounts of data (1GB). This is due to data prices remaining relatively high, as well as consumers' extensive use of a wider range of services. This is forcing operators to build out next-generation networks, increase their international and local capacity to meet this demand, and retain the quality of their networks.

As a result, operators are collectively investing billions (over ZAR20 billion between Vodacom and MTN in the current financial year alone) in network extension and upgrades which they need to justify to shareholders with robust rates of return. Doing so ensures future investments. Without a comprehensive cost analysis of the businesses – and indeed the long overdue market review – it is difficult to determine the existence and extent of dominance in the market, *abuse* of said dominance and whether operators are price gouging.

The cost of rolling out next-generation broadband networks, both the backbone and wireless access networks, is high. This is true all over the world, but particularly in Africa and parts of South Africa, where complementary investments in electrical and road infrastructure are required to support network extensions to poorer communities where returns on investment are not guaranteed.

An enabling regulatory environment that supports the rollout of broadband services effectively is determined, to a significant degree, by the administrative and regulatory costs of securing licences, spectrum and sector-specific levies. These inputs costs must be kept as close as possible to the actual costs associated with the administration of these regulatory activities; not used to generate income for

the national fiscus. As we saw with the 3G auctions in the UK, the short-term gains for the Government from high auction prices resulted in operators having little capital left to operationalise their 3G networks, arresting the development of the mobile broadband market in the UK and compromising its position as a world leader.

Urgently releasing the currently available 2.6GHz spectrum that is most suitable for LTE is imperative. Optimally, it should be allocated together with the digital dividend spectrum, which will only be available after the migration of television broadcasters from analogue to digital. At least auctioning the spectrum now would make some of it deployable immediately.

Rather than the intention of the auction being to secure the maximum price for the spectrum, the winners of such auctions should be required to roll out services to areas that do not yet have broadband coverage, before they can deploy the desirable LTE spectrum in the more lucrative urban areas. This is likely to reduce the demand for the spectrum, and therefore the price, but will still attract serious, long-term players. Conditional auctions of this kind have been successfully implemented in several jurisdictions, including Sweden. They more efficiently and equitably allocate national resources compared to the extraction of high prices for spectrum – the surpluses from which are supposed to be used for social or economic redistribution, whether at the sectoral (universal service levies) or at the national level.

The costs of not enabling the evolution of broadband services, not only to operators and end-users but also to the economy, is significant if one considers the extensive empirical evidence linking broadband penetration and economic growth.

Together with the lag in less tangible network effects that result from improved efficiencies in information flows in the economy and society, policy and regulatory failure to enable the evolution of such broadband technologies is also causing South Africa to lag on international rankings.

Enabling service-based competition and self-provision of services

Mechanisms that ensure service-based competition through access to wholesale networks must be a regulatory priority. This does not have to be as extreme as mandatory structural separation of some or all networks and services, or single mandatory open access networks. It can be enabled through cost-based access by service providers and MVNOs to networks (including a fair rate of return), transparent infrastructure sharing and facilities-leasing arrangements, with the regulation of wholesale pricing if necessary. Regulatory interventions need to ensure that they do not impact negatively on the massive investments required to roll out and maintain next-generation networks.

Further, where opportunities exist to fill the gaps in the availability of competitively priced broadband either because monopoly providers exist in a particular geographic area or none at all, self-provisioning of services should be permitted. Remote communities are not currently served affordably and pay a premium on airtime and power for their devices simply by being in remote areas. Self-

provisioning must be permitted to improve this situation and the processes for doing so expedited.

Public Wi-Fi

With the cost of rolling out networks and service prices likely to remain beyond the means of many people for some time, prioritising the roll out of public Wi-Fi at all public buildings as required by SA Connect, especially outside of the larger and wealthier metropolitans, is essential. There is considerable evidence that citizens are able to use such aggregated demand points to complement their otherwise relatively limited use of internet, providing some potential for reducing the increasing digital inequality in the country.

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**The RIA African Mobile pricing portal is available here <http://www.researchictafrica.net/pricing/ramp.php>*