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Analysis: NZ's mobile regional "monopolies"

Is New Zealand's mobile market a series of discrete monopolies? 2degrees says it is. The cellular newcomer used exactly those words in its July 2009 submission on the Commerce Commission Draft Report on MTAS. And it provided evidence to back up this view.

Buried deep in the mountain of documentation accumulated during the Commerce Commission's long-running investigation into mobile termination rates is a May 2009 study by Phoenix Research. The analyst company quizzed university and high school students in Auckland and Dunedin during late 2008 and early 2009 about their mobile phone use.

Phoenix's sample size wasn't huge, just 120 interviews in each city at a handful of schools. The study found 97% of Auckland students were on the Vodafone network, while 89% of the Dunedin students were Telecom NZ mobile customers. Phoenix also found the overwhelming majority of calls made by students and as many as 97% of text messages stay within their home network.

2degrees financed the survey, and in return was provided with powerful ammunition illustrating how New Zealand's high mobile termination rates allow the two big mobile carriers to lock-in customers. They ensure calls made between users on their own networks are significantly less expensive than calling rival networks: a process known as 'on-net' discounting.

According to 2degrees this proves MTRs artificially raise the cost of calling one net from another. They do. But it's not the whole story.

Telecom NZ and Vodafone offer their customers huge discounts when calling others on the same network. Both operators offer a variety of plans which, in effect, often reduce the marginal cost of some onnet calls and texts to zero or almost zero. These plans are carefully structured to ensure traffic stays within one walled garden or another.

When the plans are coupled with relatively high MTRs, the overall effect leads communities of users to self-select one network or another. Economists would call this a tariff-mediated network externality.

I can provide personal anecdotal evidence of how this works in practice. My teenage daughters, now at Auckland University, but previously at a North Shore high school, are both on the Vodafone network. So are all their local friends. We use a Vodafone family plan allowing unlimited calls and texts between the four of us for just under

$20 a month. It simply doesn't make financial or social sense for any one of us to switch networks – even though Vodafone reception is lousy in our immediate neighbourhood. Moving all four to, say, 2degrees would increase our phone costs. But more importantly, moving away from Vodafone would result in social exclusion for the teenagers.

In its various submissions to the Commerce Commission, 2degrees used the Phoenix research data to assert these calling communities make it hard for customers to switch networks.

A document produced by Canberra-based Concept Economics for 2degrees put it this way: "To do so is to face high (off-net) costs in calling those friends, and to impose on those friends high (offnet) costs if they wish to call back. In fact, to the extent that people are price sensitive, switching networks will reduce the contact one once would have had with those customers left behind on the other network."

Vodafone submitted a document to the Commerce Commission prepared by Covec on August 18 2009 which critiqued the Phoenix study. Most of the criticisms pick holes in the methodology and the assumptions made about the market.

Neither Phoenix nor 2degrees appear to argue the small sample size can be extrapolated to say Vodafone operates a virtual monopoly over the entire Auckland region or that Telecom rules the roost in Dunedin. Instead the focus is on a series of discrete monopolies.

However, that's not the wider market perception. Rightly or wrongly there is a general acceptance in New Zealand mobile circles that Vodafone dominates Auckland and Telecom NZ enjoys a greater market share outside of New Zealand's largest city. There's some background to this. Vodafone has always been based in Auckland. Until recently Wellington was Telecom NZ's home. The drift north started in earnest about five years ago, but was only cemented when Paul Reynolds joined as CEO and decided to stay up north.

During a recent private conversation with a major analysis organisation I once again heard the possibly apocryphal story that Vodafone's influence diminishes and Telecom NZ's increases the further south one travels. The idea is widely accepted as fact, even in the absence of hard evidence.

The regional nature of New Zealand's mobile market came to the fore recently when Telecom NZ's XT network repeatedly failed in the area "south of Taupo" – that is, in the company's home territory. To make matters worse, the epicentre of the failure was Dunedin, which both Phoenix Research and conventional wisdom suggest is Telecom's strongest region.

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