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21st January 2014

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Office of the Communication Authority  
29th Floor, Wu Chung House  
213 Queen's Road East  
Wan Chai, Hong Kong

Attention Dr. Gary Shiu  
(Principal Regulatory Affairs Manager)

Dear Dr. Shiu,

**Application for Prior Consent Under Section 7P of the Telecommunications Ordinance In  
Respect of the Proposed Acquisition of  
CSL New World Mobility Limited by HKT Limited**

The Consumer Council (CC) notes that the Communication Authority (CA) is considering, under the Telecommunications Ordinance (TO) whether the proposed acquisition by HKT Limited (the parent company of carrier licensee HKT) of CSL, another carrier licensee, would have, or be likely to have the effect of substantially lessening competition in a telecommunications market.

Notwithstanding

- the views expressed by industry;
- the concessions made by HKT regarding preservation of the status quo in the wholesale market via MVNO resale access (which continues China Mobile's network sharing arrangement with HKT's 3G network); and
- the agreement not to bid for additional 3G spectrum upon expiry of its 3G licence in 2016,

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CC is of the view that the acquisition still raises concerns regarding the future development of competition and the long term interests of consumers in the Hong Kong mobile telecommunication services market.

HKT has offered the view that the proposed transaction results in a market share of only 31.2% which is below the 40% market share accepted in the CA's Merger Guidelines, which states at Para 2.13:

*"In any event where the post merger market share of the parties to the transaction is 40% or more, it is likely the Telecommunication Authority (now the CA) will wish to make a detailed investigation of the transaction."*

HKT suggests therefore that a detailed investigation by CA into the proposed transaction is not necessary.

It is understood that the effect of the transaction on competition is highly subject to CA's views about the relevant market. CC finds that the effect of the transaction on the market share of HKT in terms of spectrum capacity is very different, increasing from 10.9% to 28.1% in a narrowly defined market of 3G/4G mobile data services or increasing from 13.8% to 35.1% in a broadly defined market of any mobile telecommunications services. The effect of the transaction cannot be concluded unless the relevant market is well defined and analysed.

CC is also of the view that determining whether the proposed transaction will have the effect or likely effect of substantially lessening competition requires CA to take into consideration the market power of all firms operating in the relevant market rather than simply the market power of the entities involved in the transaction.

CC considers that a more appropriate means of measuring potential concern is to determine the relative size and distribution of the remaining firms in the relevant market (i.e., the levels of market power that will exist across all firms) post transaction. A suitable methodology for these purposes, used extensively by many competition authorities such as the United States Department of Justice, is the Herfindahl-Hirschman Index (HHI). CC suggests that this method is a more appropriate means of assessing the effect of the proposed transaction on the question of market power.

CC notes that some competition authorities adopting the HHI as a measure consider that a merger that results in a change in the HHI of more than 100 points in a moderately concentrated market (i.e., one that is defined with a HHI measure between 1500 and 2500 points) potentially raises significant competition concerns.

CC is inclined to measure market share or market concentration by using the number of subscribers instead of the spectrum capacity unless there is a clear limitation that will constrain the parties' ability to take on additional customers in the future. For the purposes of determining the relevant HHI measure for this proposed transaction, CC considers it is appropriate to use the data submitted by industry on the number of subscribers for each service provider in the mobile telecommunications market in June 2013, with regard to the Application to CA under 7P of the Telecommunications Ordinance Regarding the Acquisition of all the Shares in CSL New World Mobility Limited by HKT Limited.

Using this data it is calculated that the pre-transaction market has a HHI of 1769, i.e., it is a moderately concentrated market, and the post-transaction market has a HHI of 2223. The HHI therefore increases from a moderately concentrated market by a factor of 454, which would raise concerns under the established procedures used by other competition authorities. Having regard to this more problematic outcome, by using the HHI as a measure, CC suggests that CA may need to conduct a detailed investigation to assess the potential effect of the transaction on competition and the likelihood that the transaction will increase prices and lower service quality in the mobile telecommunication services in Hong Kong.

Apart from HHI thresholds set in various overseas authority guidelines, many competition authorities are highly concerned with the number of operators remaining in the relevant market after the transaction because the possible tactical coordination between firms should become easier with less players (reducing from five to four players if the transaction happens). It is understood that there could be serious coordinated effects on competition even if the resulting entity holds less than 40% of market share. Although there are many overseas precedent cases of approved four-to-three or five-to-four mergers in telecommunications industry, CA is urged to consider the potential coordination between mobile carriers in view of precedent case of price coordination happened in Hong Kong in 2000.

CC is aware of the commitment by HKT to honour the agreement with China Mobile, after the proposed transaction, which allows China Mobile to access up to 50% of HKT's 3G network capacity. One effect of the proposed transaction is that HKT will expand its network (25% of the total 3G spectrum by combining the spectrum held by CSL and HKT after deducting the spectrum return back to the Government). CC views this as a potential detrimental effect on the future development of the market. It is possible that a successful outcome by China Mobile in auction bidding on the reassignment of the 25% of the 3G spectrum could mean China Mobile would have access to a total market share of 37.5% (by adding on the benefit of the network sharing arrangement with HKT's 3G spectrum) and with its holding of a 25% share of the total 4G spectrum, China Mobile could in five years' time easily become the biggest and possibly dominant player in the market.

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CC invites the CA to demand the parties of the transaction to provide more evidence as they have firm view that the transaction will not result in an increase in prices and will not have an adverse effect on competition. At the best interests of consumers, CC holds the view that with more information provided, CA could better gauge and assess the potential impact of the transaction and make a robust judgment.

In conclusion, the CC considers that

- the increase in market concentration with subsequent increase in market power of some carriers as a result of the merger between HKT and CSL;
- the potential coordination effect of the transaction
- the network sharing arrangement between HKT and China Mobile, with the prospect of China Mobile succeeding in bids for 3G spectrum in coming years,

and means that the CA needs to monitor closely the development of the sector and to take necessary measures to safeguard competition in the market with ultimate long term benefits to Hong Kong consumers.

Should you wish to discuss this matter further please feel free to call Victor HUNG, the Chief Trade Practices Officer at the Council on 2856 8554 or myself on 2856 8585.

Yours sincerely,

A handwritten signature in black ink, appearing to read 'Gilly Wong', is written over a faint circular stamp or watermark.

Gilly WONG  
Chief Executive  
Consumer Council