

Covid-19, pricing regulation and big player profitability

- ❖ **In line with global trends towards rising demand for mobile data and services during the Covid-19 pandemic mobile data and services usage has risen dramatically.**
- ❖ **This appears to be supported by data price reductions last year mandated by the Competition Commission following the Data Services Market Inquiry. MTN and Vodacom reduced their 1 GB monthly data bundle from R149 to R99, in 2021_Q2 representing a 34% decrease in the price. MTN further reduced its data to R85 monthly GB during 2021_Q3.**
- ❖ **South Africa's data pricing remains prohibitively high compared to other African countries. In 2021_Q3, South Africa ranked 34th out of 47 countries on the RAMP Index, with the most expensive mobile data in the region.**
- ❖ **MTN and Vodacom have performed well despite regulatory pressure.**
- ❖ **High demand spectrum needs to be urgently released to enabling alternative providers with more cost-effective business models to enter the market with minimal regulatory transaction costs, together wholesale access regulation to remedy market dominance and enable smaller players to compete would go a long way to enabling the alternative delivery of services.**
- ❖ **In South Africa, the cost of 1GB is USD 5.78, while in countries like Sudan and Tanzania, mobile data costs USD 0.68 and USD 1.51 per monthly gigabyte, respectively. In countries where MTN and Vodacom operate, South Africa also ranked in 10th place out of 14 countries.**

Introduction

South African Mobile Network Operator's (MNO) performance has remained resilient despite the recommendations from the Competition Commission (Commission) to review data pricing within the country. While the Commission's recommendations are meant to facilitate greater access and affordability, the reality is that South Africa's data pricing remains prohibitively high compared to other African countries (Chinembiri, 2020). Furthermore, the onset of the COVID-19 pandemic has driven demand for data services as goods and services shifted to digital channels, workplaces implement working from home policies, and the public sector has had to accelerate the e-government and digitisation initiatives. Besides these challenging and uncertain business environments, the COVID-19 pandemic has catalysed demand for data services. This policy brief aims to analyse the impact of Covid-19 and changes in data pricing on operators' performance.

COVID-19 pandemic has been a catalyst for the demand for data services which has accelerated the need for digital services.

The pandemic has driven demand of data services

The Covid-19 pandemic has highlighted the importance of having a connected society and brought to light the need to have digital services that are available, reachable and affordable to all. Demand for data has grown with the lockdowns associated with the COVID-19 pandemic, which has accelerated the growth of digital services. Data traffic has increased as companies adopted work from home strategies; consumers used social media to communicate and consume entertainment online; schooling and tertiary education switched to remote learning; and those that could, met their retail needs online.

One of the very few sector that have flourished under these conditions, is telecommunications, particularly the dominant operators with the capacity to offer high quality, always on broadband. MTN South Africa's data revenue grew 15,3% at ZAR 14,6 billion in 2020. Vodacom South Africa did not report data revenue in 2020 and 2021; however, it grew from ZAR20.7 billion in 2017 to ZAR24.3 billion (accounting for 45.3% of service revenue) in the year ending March 2019. Furthermore, Vodacom and MTN's customer bases grew by 6,8% and 7,3% for Vodacom and MTN SA, respectively, representing a combined market share of 73,3%.

With regards to EBITDA, MTN's Earnings before interest, taxes, depreciation and amortisation (EBITDA) margin for 2020 was 39%, MTN said the solid EBITDA margin was possible due to cost efficiencies and channel optimisation, reductions in device volumes and device subsidies. EBITDA grew 5.7%, while margins contracted 1.7ppts in the year. Vodacom's EBITDA margins have been relatively flat, but high, over the past few years and stood at 41.8% (in the year ending March 2020) and 40.1% (in the year ending March 2021), respectively. Vodacom's EBITDA growth was supported by solid growth in service revenue while operating profit grew by 4.2%.

These represent extremely profitable businesses and EBITDA at these levels would be the envy of most other sectors, somewhere between 10% (retail) and 20% (tourism) prior to COVID. Only the drug industry historically gets high margins above 50% consistently.

Vodacom and MTN experienced increases in the revenue and solid EBITDA margins, despite the pandemic's uncertainties and in challenging macroeconomic conditions such as slow economic growth and the weakening of the Rand against the US dollar. Furthermore, during 2021_Q2, in response to the Data Services Market Inquiry, MTN and Vodacom reduced their 1 GB monthly data bundle from R149 to R99, representing a 34% decrease in the price. MTN further reduced its data to R85 monthly GB, during 2021_Q3.

Regulatory pressures decreased the cost of data prices and spurred demand

South Africa's mobile market has historically comprised four mobile operators and 20 mobile virtual network operators (MVNOs)¹. In 2020, Vodacom and MTN dominated the mobile market (see Figure1), which collectively had just over 73% of the subscriber market share (98,6 million subscribers). Cell C and Telkom Mobile are trying to build their growth on data services but are struggling to do so, given

Both Vodacom and MTN's customer bases grew by 6,8% and 7,3% for Vodacom and MTN SA, respectively, representing a combined market share of 73,3%.

¹ Competition Commission (2019). Data Services Market Enquiry: Final Report: Available from <https://www.compcom.co.za/wp-content/uploads/2019/12/DSMI-Non-Confidential-Report-002.pdf>

Vodacom and MTN's first-mover advantage. It is believed that South Africa has 20 Mobile Virtual Network Operators, who account for a subscriber market share of 1,9%¹.

In 2019, the mobile operators implemented the revised end-user and subscriber service charter regulations issued by ICASA, enabling subscribers to roll over unused data, avoid the automatic out-of-bundle data usage, and transfer data between customers. This measure impacted the out-of-bundle (OOB) data revenue for MTN and Vodacom.

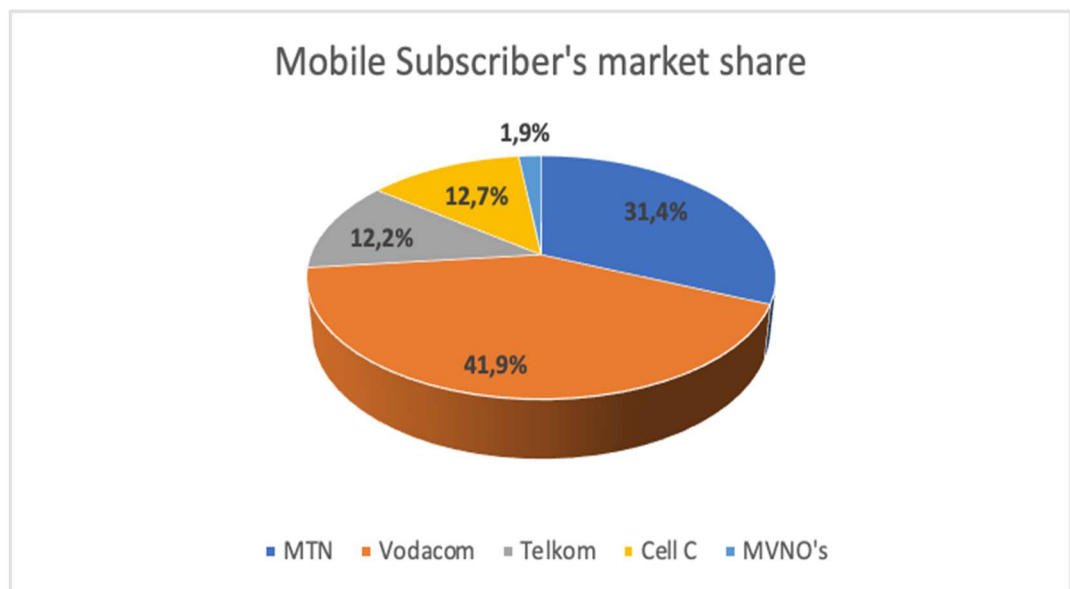
In December 2019, the Commission released the findings of its two-year data services market inquiry, which raised market power and competition concerns. In 2015, MTN and Vodacom did not adjust their 1GB bundle prices when Telkom reduced them by 45% to ZAR99. Furthermore, the findings also indicated that the mobile data pricing structure is anti-poor, and as a result, the Commission requires the two dominant mobile operators¹:

- to reduce their prepaid data bundles between 30% and 50%.
- to standardise the cost per MB for sub- 500MB 30-day prepaid data bundles so that it is the same as 500MB 30- day bundle, and
- to stop implementing price discrimination strategies that do not benefit the lower-income consumers.

The recommendation for all mobile operators is to:

- offer all citizens access to life-line data connectivity.
- provide zero-rating of content for public organisations and educational units, and
- to inform each subscriber of the price for all data consumed by the customer monthly.

Figure 1: Subscriber Market Share in South Africa



Source: Annual Reports for MTN (2018, 2019 and 2020), Vodacom(2020), Telkom (2021) and Cell C (2019 and 2020); and Competition Commission (2019). Data Services Market Enquiry: Final Report

Overview of Vodacom and MTN's performance

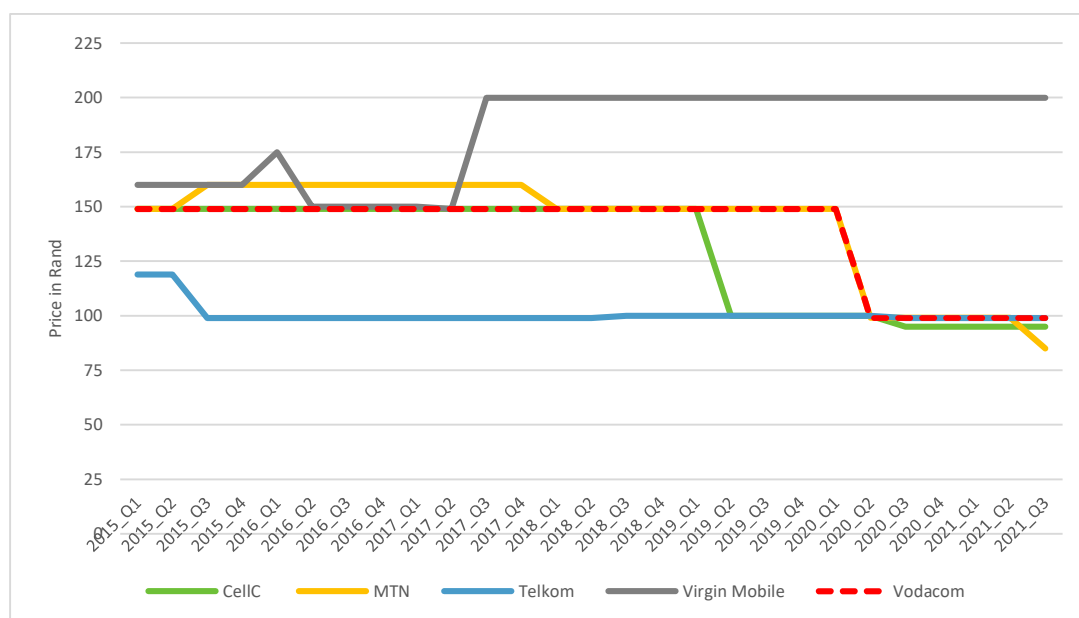
Over the past three years, several factors have impacted MTN and Vodacom's performance, including low economic growth which has constrained consumer spending, and regulatory pressures to address data pricing. Despite these conditions persisting and in fact intensifying under the COVID-19 pandemic, the lockdown has driven demand for data services and impact positively on their bottom lines. The RAMP index data reflected in Figure 2, shows Vodacom's quarterly prices for 1GB remained constant at ZAR150 until the Competition Commission ruled that the prices should come down in the first quarter of 2020. MTN's prices have plummeted three times since 2017_Q4, with the recent one in the third quarter of 2021.

Data pricing transformation for Vodacom

In the year ending March 2019, Vodacom's data revenue grew by 3.9% to R24.3 billion, accounting for 43.5% of service revenue. Vodacom started implementing ICASA's data regulations by cutting out-of-bundle rates by 50%, resulting in a decline in effective rates by 37.3%. Furthermore, Vodacom migrated 75% of their customers to smart integrated plus plans, offering more value mostly in data. The reduction in data bundles spurred demand for data bundles, and data traffic grew by 35.6%.

In 2020, Vodacom embarked on a data transformation strategy following recommendations from the Competition Commission. Vodacom reduced pricing across monthly data bundles and provided zero-rated access to government websites in education, internet search, jobs, social and internet services, health and wellness, safety and security and emergency services, among others. The data transformation strategies, including a further reduction of out-of-bundle rates, resulted in a 9.7% increase in data customers and 66% in data traffic in 2020. In 2021, data traffic grew by 55.6% off the back of a decline in data bundle prices in 2020.

Figure 2: 1GB Data trend in South Africa's Mobile Network Operators 2015-2021



Source: RIA RAMP Index 2021_Q3²

² The RAMP Index data portal is available here: https://researchictafrica.net/ramp_indices_portal/. The methodology is given in Box 1 below. Virgin Mobile has ceased its operations in South since the beginning of November 2021: <http://www.virginmobile.co.za/>

Data pricing transformation for MTN

In 2020, MTN's service revenue increased by 1,6% to ZAR 37,0 million, and the data revenue grew by 15,3% to ZAR 14,6 million. The increase in traffic by 70% and the 1,5 million active data subscribers led to growth in the data revenue. This significant growth uptake by MTN was made possible by the temporary assignment of the high demand spectrum that ICASA permitted due to the pandemic. In the same year, MTN reduced the effective data tariff by 35%, led by the adoption of mobile broadband, student and SME deals. These price reductions were in line with Competition Commission recommendations made on the DSMI.

MTN's EBITDA margin for 2020 was 39,0%. Besides the growth in the service revenue, the solid EBITDA margin was possible due to cost efficiencies and channel optimisation, reductions in device volumes, and device subsidies.

With the release of temporary spectrum by ICASA in 2020, to facilitate COVID-19 increased data demands, MTN offered zero-rated services to 1 000 health, education and job websites, thus helping more than five million financially vulnerable South Africans to cope during this pandemic. The temporary spectrum is now available until November 2021.

MTN's mobile subscribers grew by 7,3%, reaching 31,0 million subscribers in 2020, compared to 28,9 million subscribers in 2019.

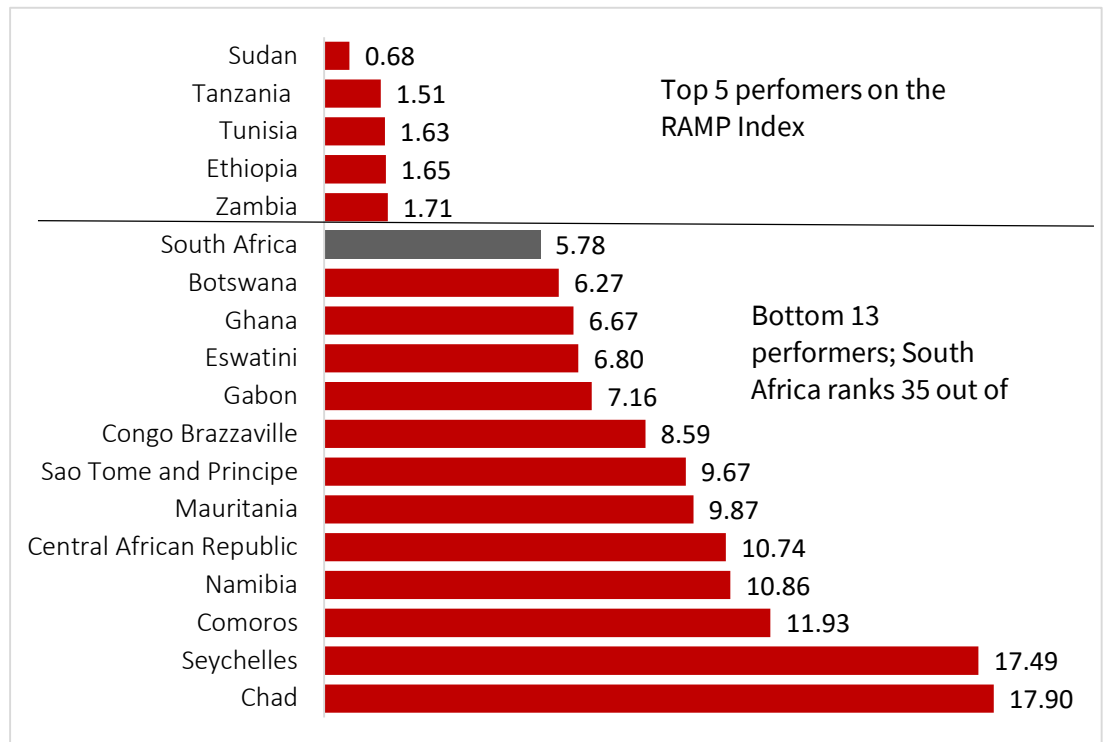
MTN SA recorded 140 million smartphones used on their network, and the effective rate per megabyte was reduced by 32,9%. Additionally, the average data usage rose by 60% to 4,4 GB per month.

In terms of 5G, MTN SA launched this high-speed network in June 2020 and has over 150 sites across various spectrum bands across the leading South African cities. If the 3500MHz high demand spectrum is allocated, MTN SA will be able to connect more than 1000 sites with 5G connectivity

South Africa's 1GB data price is relatively high compared to other countries in the region

According to the RAMP Index (see Figure 3), the top five countries in the continent with the cheapest mobile data is Sudan at USD 0.68 per 1GB, followed by Tanzania, Tunisia, Ethiopia and Zambia. What the Index does not reflect however is the quality of service of the different operators in the 50 countries monitored. MTN provides the cheapest data in Sudan, but the connectivity is reportedly weak and has limited network coverage. South Africa is in the bottom 13 performers on the RAMP, ranking 35 out of 47 countries, charging USD 5.78 per GB, equivalent to R85, the cheapest 1GB data price offered by MTN. In past continental quality assessments undertaken by RIA, the two operators have had by far consistently the highest quality and together with several other countries most extensive coverage. Chad and Seychelles have the most expensive data charges, currently above USD 17 per 1GB. In 2020, Vodacom and MTN reduced the 1GB data price to ZAR 99, responding to the Commission enquire.

Figure 3: South Africa’s ranking compared to all countries on the RAMP Index (2021_Q3)

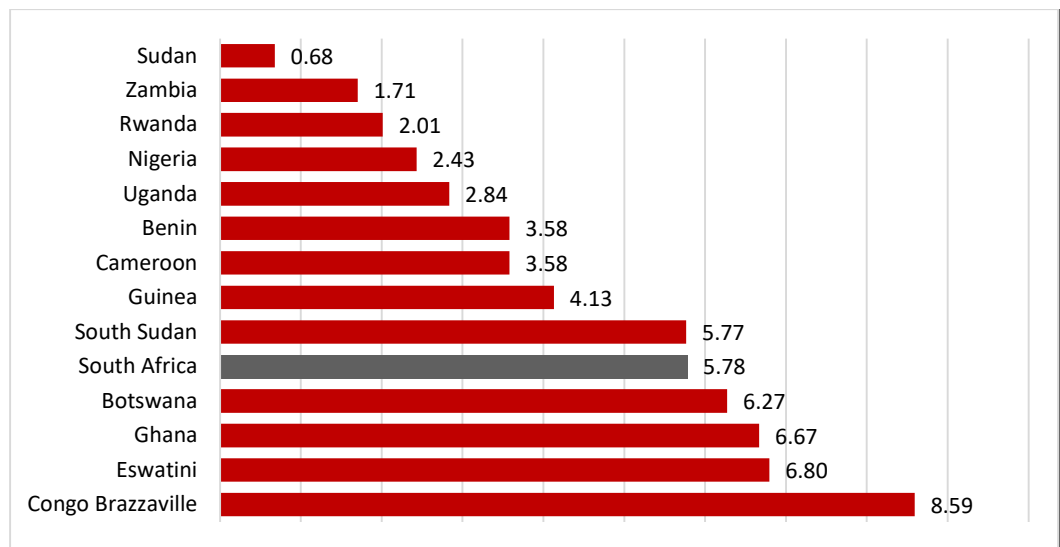


South Africa is on the bottom 13 performers on the RAMP, ranking 35 out of 47 countries in Africa. It ranks 10th out of 14 selected countries where MTN and Vodacom have operations

Source: RIA RAMP Index, 2021Q3

Based on the countries where MTN and Vodacom are present (see Figure 4), South Africa still ranks 10th out of 14 selected countries. With the long-delayed spectrum allocation expected to take place next year (TechCentral, 2021), data price should come down in South Africa, with the possibility of making the internet affordable and accessible for more South African's to use the internet and for newer people to come online. For the dominant operators to maintain their profitability, they have to change their business models to maximise other services, such as improving the quality of services on mobile money and internet speeds by utilising the 5G, which MTN has already rolled out.

Figure 4: South Africa’s ranking compared to countries where MTN or Vodacom have operations on the RAMP Index (2021_Q3)



Source: RIA RAMP Index, 2021Q3

Conclusion

The policy brief examines the performance of the dominant mobile network operators in South Africa, MTN and Vodacom, by highlighting the data pricing transformation strategies adopted before and during the COVID-19 pandemic.

Although the Commission's recommendations to lower the data price were only confirmed towards the end of 2019, the actual reduction in price from ZAR 150 to ZAR 99 took place in 2020_Q2, which was in the middle of the pandemic in South Africa.

Despite regulatory pressure and reduced prices, both operators have increased their revenue throughout the period, partly due to the upsurge in demand for data services. Furthermore, Vodacom recovered from the data price cuts in the second quarter of 2020.

However, as the RAMP Index indicates, prices remain high in South Africa compared to other countries as does the profitability of the dominant players MTN and Vodacom. They have continued to invest extensively in network extension – from past analysis the recipe to their success as consumer demonstrate a willingness to pay a premium for quality service if they are able to. The data pricing in Sudan is relatively cheap, although the quality of service needs to be improved. Operator price reductions and data transformation over the years is a welcomed development. However, RIA calls for further price cuts to accommodate the poor and facilitate digital inclusion by bringing more people online since the cost of data has been one of the main reasons cited as to why a significant proportion of the population is still offline. The expected allocation of spectrum will allow for competition and bring prices down where most people will be online due to the dominance of MTN and Vodacom.

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RIA calls for further price cuts to accommodate the poor as well as facilitating bringing more people online

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