

PRESS STATEMENT:

**DETERMINATION ON RETAIL AND INTERCONNECTION RATES
AMONG THE FIXED AND MOBILE TELECOMMUNICATIONS
NETWORKS IN KENYA**

INTERCONNECTION DETERMINATION NO.2 OF 2010

Member of the media,
Ladies and gentlemen,

You will recall that the Commission in February 2007 issued a determination stipulating cost-oriented interconnection rates for the industry with a declining three-year glide path for mobile termination rates ending in early 2010 and a four-year glide path for fixed termination ending in next February. The Commission also undertook to conduct a review of the interconnection framework before the end of the glide path in order to accommodate new developments in the industry.

I am glad to inform you that the Commission has just concluded a study that was undertaken to review the 2007 position, taking into consideration the prevailing market situations in the communication industry in the last three years. The study has also developed pricing models for infrastructure sharing and co-location as well as a broadband interconnection framework.

This study, which commenced on 22nd March 2010, was being undertaken a globally acclaimed consultants, Messrs Analysys Mason. The Commission has reviewed the study report and agreed with the findings. Consequently, CCK issued a determination on 16th August 2010 (Determination 2 of 2010) that gave guidelines on retail and interconnection rates for fixed and mobile telecommunications network in Kenya. The determination effective date is 1st July 2010.

In the determination, the Commission has imposed price caps on mobile and fixed termination services with a three-and-half year (3.5)year declining glide path to attain the efficient cost levels determined using the pure Long Run Incremental Cost (LRIC) methodology.

Considering the large discrepancy between the existing mobile termination rates of Ksh.4.42 per minute and the termination rates estimated using the pure LRIC methodology for 2010 of Ksh.0.87 per minute, an immediate reduction of the termination rate to the pure LRIC cost could potentially cause disruptions to the business plans of operators. Consequently, the glide path adopted by the Commission imposes an immediate 50% reduction in mobile termination rates from the current level of Ksh.4.42 per minute to Ksh.2.21 per minute and then progressively decline by 35%, 20% and 15% annually in 2011, 2012 and 2013 respectively with a view to attaining fully cost-oriented levels by 2014. We believe the glide level will provide an acceptable balance between the regulatory objective of attaining efficient cost levels as soon as possible while maintaining stability in the business plans for the operators.

The Commission adopts a similar approach with respect to fixed termination rates by immediately aligning the tariffs for single-tandem termination from tandem exchange on the tariff for local termination to arrive at a new fixed termination rate and gradually declining the rates with a view to converging with the mobile termination rates by 2013.

At the retail mobile and fixed markets, the Commission has noted that the large on-net-off-net tariff spread is being used by large operators to curtail competition at the retail level by entrenching and sustaining a “club” effect. This phenomenon is a common practice in telecommunications markets where operators with large subscriber bases price their off-net services (calls outgoing to other networks) onerously in order to discourage their subscribers from calling other networks. This pricing mindset is offensive to competition as it entrenches traffic imbalances in favour of large operators and makes other networks net payers to large networks.

In addition, this behavior entrenches the “club” effect by influencing the choice of network by consumers to subscribe to large networks even when pricing and other quality service standards are not in their favour. This lack of effective competition at the retail voice markets together with product differentiation have largely contributed to the increased market concentration in these markets despite the wholesale interventions undertaken in 2007.

In order to remedy the competition problem at the retail mobile and voice markets, the Commission intends to apply a price cap on the off-net tariffs of dominant operators in mobile and fixed voice markets to the level of their on-net tariffs. In making this decision, the Commission is convinced that the intervention of reducing the off-net price for large operators in the mobile and fixed voice markets will only have a limited negative impact on their voice revenues, since the bulk of their traffic volumes are on-net.

In addition, in terms of cost burden, the Commission has considered that the cost for providing a one minute off-net service by large operators is lower than the cost of providing a one minute on-net service. This is an affirmation that the high off-net tariffs relative to on-net tariffs imposed by large operators is not motivated by the desire to recover prudently incurred costs and returns, but is rather a strategic approach which impacts negatively on competition.

Finally, the improvement of the competitive landscape arising from this intervention including potential retail price competition would generate significant market efficiency dividends to the entire industry. The effective date for implementation of this intervention will be immediately upon designation by the Commission of dominant/large telecommunication operators in the retail mobile and fixed voice markets in line with the existing laws and regulations.. The Commission will soon be releasing the findings of a

comprehensive competition assessment study in the telecommunications markets that will inform regulatory policy interventions towards creating a more vibrant and competitive telecommunications sector.

Moreover, the Commission has confirmed glaring distortions in the pricing of mobile and fixed SMS services in the country. At the pure LRIC cost of less than Ksh.0.01 for terminating an SMS on both the mobile and fixed networks, the Commission considers the wholesale termination rate of Ksh.2.00 per SMS negotiated by the operators extremely high. The high termination rate has adverse consequences on the market as it reduces the scope for operators to reduce the SMS retail prices which erodes consumer welfare. The Commission has, therefore, determined that all operators renegotiate lower mobile and fixed SMS termination rates and file the new rates with the Commission within three months.

The Commission further notes that mobile money transfer is an important value-added service that significantly differentiates other services such as voice. While noting the strategic importance of this service to general public and the economy at large, the Commission is aware of the ability of this service differentiation in entrenching the “club” effect. In addition, the Commission has noted the very high charges the mobile money transfer service providers are imposing on the non-registered users and users from other networks. In line with the evolution of a converged environment in the telecoms market, the Commission has determined that the mobile money transfer service providers pursue the interconnectivity options for the service in line with regulatory obligations and review the charges accordingly.

Meanwhile, the Commission intends to continue with discussions with the Central Bank of Kenya in order to develop a fairly inclusive regulatory framework that delivers the benefits of this service to the public at cost-effective rates.

With regard to infrastructure sharing and co-location; and the interconnection framework for the broadband market, the Commission has decided to monitor the developments in these markets and allow pricing and other agreements to be reached through commercial negotiations and only intervene if such negotiations do not generate optimal results.

Thank you for your attention.

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