

**APPLICATION FOR A DECLARATION OF NON-DOMINANCE IN THE
INTERNATIONAL CALL SERVICES MARKET
FOR NON-CHINA ROUTES
BY CABLE & WIRELESS HKT TELEPHONE LIMITED**

Statement of the Telecommunications Authority, Hong Kong

4 August 1999

EXECUTIVE SUMMARY

The Telecommunications Authority (TA) had received from Cable & Wireless HKT Telephone Limited (CWHKTT, previously called Hong Kong Telephone Company Limited) a request for reconsideration of his findings and conclusions on CWHKTT's previous applications for a declaration of non-dominance in the "international call services" market for non-China routes. In response to that, the TA, on 24 May 1999, invited views and comments on CWHKTT's application.

2. The TA received 7 submissions from operators in the telecommunications industry. The TA has considered and given due regard to all the representations made by all parties. He has also, where appropriate, made use of statistical or other information already in his possession. The TA, as previously stated in the consultation paper issued on 24 May 1999, considered whether he should accede to the application, accede to it in part or whether he should refuse it.

CONSIDERATIONS

Legal basis

3. The application had been considered under General Condition 44 of the Fixed Telecommunication Network Services (FTNS) Licence of Cable & Wireless HKT Telephone Limited, Cable & Wireless HKT International Limited and Cable & Wireless HKT CAS Limited. This gives the power to the TA when the licensee is

not in a dominant position, to exempt it from certain licence obligations such as obtaining the prior approval of the TA for the tariffs of new services and a prohibition on discounts from approved tariffs. At the same time, if the TA considers it appropriate he may impose conditions in doing so.

Market definition

4. The TA started by defining the services to be included in the relevant market. He has done so in the same way as during the last application by CWHKTT and confirmed that the market is that for “international call services” from Hong Kong. The definition included both voice and data services as operators and customers do not differentiate between the two when making a call.

5. However, he has also decided that the market for “international call services” is in reality subdivided into two markets. One of these relates to destinations where there are competitive routes at the wholesale level, that is to say those routes where the TA has declared as Category A routes¹. The other relates to destinations (excluding Mainland China) where the TA has declared as Category B routes.

6. He reached that conclusion after considering a number of factors including the substitutability of supply, and the elasticity of demand from both a consumers’ point of view and from a supply point of view.

7. These conclusions were also confirmed by the fact that Category A destinations and the Category B destinations (excluding Mainland China) have different characteristics. At the Category A level operators have more flexibility in pricing and can benefit by economies of scale where for Category B destinations no such flexibility exists. Also the two categories are having a price differentiation, which is not really justified by the real cost, demonstrates that the two markets are actually distinct. Product bundling, marketing plans, discounts, special promotions as well as advertising also demonstrated that Category A destinations are treated differently from Category B.

¹ This has the same meaning as in the TA’s statements of 25 November 1998 “Local Access Charge and Modified Delivery Fee Arrangements” and that of 24 December 1998 “Local Access Charge and the Modified Delivery Fee Arrangements – Classification of Routes into Categories A and B” and the list of destinations in the two categories as may be amended in part or in full by the TA from time to time.

8. The geographic market was also considered by the TA and he was satisfied that this is the whole of Hong Kong.

Assessment of Dominance

9. The TA having defined the relevant market then examined whether CWHKTT was in a position of dominance. Market share was used as the starting point. In the case of both the markets for Category A destinations and that for Category B destinations (excluding Mainland China), CWHKTT's market share was below 75% but above 25% and therefore no presumption of dominance or non-dominance could be made.

10. The TA based on actual figures supplied by licensed operators for external traffic for the period January 1999 to May 1999 (inclusive) has calculated - not estimated - each licensee's market share. In the case of CWHKTT for Category A destinations its market share (excluding calls through mobile telephones) was approximately 40% and for Category B destinations (excluding China) it was above 55%.

11. Equally important are the figures of the market shares of CWHKTT's competitors and the gap between them and CWHKTT. In the market for Category A routes operator X (name withheld) has a market share of above 20% but below 30% and operator Y (name withheld) a market share of above 10% and below 20%. The gap between CWHKTT and X is approximately 15%. In the case of the Category B market (excluding Mainland China) operator W (name withheld) has a market share of above 15% but below 25% and operator Z (name withheld) a market share of above 10% and below 20%. The gap however between CWHKTT and W is approximately 40%. The fact is that the gap in the Category A market is becoming smaller and the market is becoming more even.

12. The TA also examined the extent to which CWHKTT's behaviour in the market is constrained by the threat of new entry or of substitution into the market. This was considered as a significant factor in assessing the degree of competition in that market. The TA took into account the prospects arising after 1 January 2000

and the fact that regulatory restrictions concerning the operation of external circuits will be eased. He has also taken into account other barriers for new entrants that need to be surmounted in the short to medium term e.g. the need to set up correspondent relationships and how quickly entry and or substitution might occur. He has also taken into consideration the existing regulatory environment and safeguards, the number of operators offering external telecommunications services in Hong Kong, and the fact that many of them have already established a presence in the market and that many of the major ones have established household brand names.

13. The TA is satisfied that in all Category A destinations, it may be easy for a competitor of CWHKTT to switch to alternative connections in bypass of the CWHKTI gateway. The TA is also satisfied that many of the operators offering international call services in competition to CWHKTT have demonstrated, so far, that they have the ability and the expertise needed to establish themselves and to become equally well recognised both in the Hong Kong but also at overseas markets as international players. The TA is therefore satisfied that those destinations that are on a Category A route are fully contestable and thus ensuring that CWHKTT's prices are restrained by the prices that its competitors offer.

14. In the case of Category B destinations (excluding Mainland China) the TA is of the view that CWHKTI's dominant position is in the wholesale market and the fact that no effective alternative competitive routes are available to the destinations in Category B mean that CWHKTT's competitors have no option but to use CWHKTI's facilities with no possibility of setting their prices freely. The competitors can in Category A routes negotiate with the operators at the far end and obtain better prices. In the case of Category B routes, competitors have no direct alternative and thus is difficult if not impossible to negotiate prices.

Prices

15. In looking at the competitiveness of the market, the TA examined whether there is genuine independent price competition in the market. In this case, the TA is satisfied that competition in the retail markets for category A destinations is very intense. However, he is of the view that this is not the case for Category B

destinations where price competition is minimal.

Vertical integration

16. Vertical integration in itself does not imply that a firm is dominant. The potential, however, for vertical integration to lead to an abuse of a dominant position is a significant aspect of the analysis of market power in telecommunications markets. The TA therefore examined concerns expressed about the degree of vertical integration of CWHKTT and CWHKTI balanced by the existing safeguards for interconnecting operators in terms of accounting separation, competitive safeguard provisions in CWHKTT's licence, the ability for the TA to make interconnection determinations and the constraints still in place in markets where CWHKTI or CWHKTT are still dominant.

17. The TA agreed with the concerns expressed in some submissions that information available to CWHKTI in respect of the traffic of CWHKTT's competitors could be used by CWHKTT in an unfair manner. The TA however does not consider this to be an overriding factor in deciding on whether CWHKTT is dominant or not in a market. He considers that if necessary additional conditions could be imposed on the company in respect of the use and protection of information within the company.

CONCLUSIONS

18. The TA is satisfied that the CWHKTT is no longer dominant in the market for "international call services" where the destinations are within the Category A destinations. However, the TA maintains the view that CWHKTT is still dominant in the market for "international call services" to destinations that are within Category B destinations. Irrespective of the fact that for the group of Category A routes CWHKTT is no longer dominant, the TA is satisfied that CWHKTT still has significant market power and can influence the market in particular in combination with its sister company CWHKTI. This, combined with concerns about CWHKTT's ability to ensure its compliance with its licence obligations, its vertical integration with CWHKTI etc. has caused the TA to make the lifting of the dominance restrictions subject to conditions. This is to ensure that

proper compliance systems and robust pricing arrangements are put in place so that competition can be protected. They include the following requirements:

a) Pricing

- i) To establish systems and controls so as to ensure its compliance with its pricing obligations but also so as to monitor its behaviour on an ongoing basis;
- ii) To ensure that necessary information regarding the provision of the services declared to be non-dominant (i.e. breakdown of costs, business case, etc) be kept on file in full details so that CWHKTT could respond within 48 hours to requests for information by the TA in investigating complaints about pricing;
- iii) CWHKTT may not impose a minimum period of contract between itself, or any other affiliated company and the customer for offering any tariff or package of tariffs or discount to a customer;

b) Information

- i) CWHKTT and CWHKTI must establish systems and controls so as to ensure that any information concerning
 - a) the wholesale and retail traffic of CWHKTT's competitors;
and
 - b) the usage patterns and/or usage information of customers connected to CWHKTT's fixed network but who use CWHKTT's competitors for overseas calls

is not made available nor used by it in any way by CWHKTT so as to obtain, in the opinion of the TA, an unfair advantage.

19. The TA has also decided that the lifting of the restrictions should be dependent on the new safeguards being implemented first. The TA has therefore

made provision in the Direction issued by him today (Annex B) that one working day after Cable & Wireless HKT FTNS has notified him of how it has complied with the requirements of the Direction and has published a report of it, General Conditions 20(4) (prohibition of offering discounts to its published tariffs), 21(requirement for prior approval from the TA for tariff revisions) and 22 (tariffs for new services) of its fixed telecommunications network services licence will no longer apply in relation to the market that has been declared non-dominant. This will be effective until the Direction expires on 30 September 2000 or is revoked by the TA.

WAY FORWARD

20. In respect of the group of destinations that are not currently within Category A, the TA will not consider individual applications for declaration of non-dominance. Once a destination at the wholesale level has been declared as a Category A destination it will automatically be included in the group of destinations that CWHKTT is considered non-dominant.

21. The TA proposes to set a time limit to the Direction in Annex B. This will have the effect of acting as a “probationary” period over which Cable & Wireless HKT (CWHKT) as a group must demonstrate its compliance with its licence obligations as well as the conditions that the TA has today imposed through the Direction. The TA will commence his review of the whole structure in June 2000. However, if it can be demonstrated that between today and September 2000 there are major changes that justify the TA reconsidering this he will do so.

22. It should be kept in mind that the licence obligations of CWHKTT concerning abuse of dominance remain in place. If the TA was to find in the future that CWHKTT is dominant at the retail level of the Group that comprises the Category A routes and that it has abused its position he will act accordingly. A prior declaration of dominance is not a pre-requisite. The declaration is required where the TA wishes to impose additional conditions such as the requirement to obtain prior approval for price changes. Even where prior approval is not required, the licensee who is dominant in any market must comply with the requirement not to abuse its position. It is therefore a matter for each licensee to monitor, and

where necessary, adjust its behaviour depending on its market power.

23. The TA would like to stress that, like with all other markets, he will not hesitate to stamp out any breaches of licence obligations either in relation to pricing or other related anti-competitive behaviour and he will monitor closely CWHKTT's behaviour in the market.

Office of the Telecommunications Authority

4 August 1999

**APPLICATION FOR A DECLARATION OF NON-DOMINANCE IN THE
INTERNATIONAL CALL SERVICES MARKET
FOR NON-CHINA ROUTES
BY CABLE & WIRELESS HKT TELEPHONE LIMITED**

Statement of the Telecommunications Authority, Hong Kong

MAIN REPORT

BACKGROUND

1. On 28 November 1997, the TA, having considered an application from Cable & Wireless HKT Telephone Limited (CWHKTT, previously called Hong Kong Telephone Company Limited) for a declaration of non-dominance in the “International Business Call Market”, issued a report entitled: “Application from Hong Kong Telephone Company Limited for a Declaration of Non-Dominance in the “International Business Call Market” – Telecommunications Authority’s Findings”. The effect of that decision, as set out in the report, was to refuse the application of CWHKTT for such a declaration.

2. In response to that, CWHKTT submitted another application again seeking a declaration of non-dominance in the “International Call Services” market. On that second application, the TA consulted the industry in January 1998. On 23 May 1998, the TA published his findings in the report entitled “Application from Hong Kong Telephone Company Limited for a Declaration of Non-Dominance in the International Call Services Market - Telecommunications Authority’s Findings and Conclusions”. The application of CWHKTT for a declaration of non-dominance in the relevant market was again refused. (All reports mentioned above are available on OFTA’s web site at <http://www.ofta.gov.hk>.)

3. On 15 April 1999, CWHKTT requested the TA to reconsider his previous decision in relation to its past application for reconsideration of the company’s application for a declaration of non-dominance in the “International Call Services” market for non-China routes. The application of CWHKTT was

published by the TA (after the excision of such information as the TA considered commercially confidential) together with the consultation paper issued on 24 May 1999.

4. The TA in the consultation document stated that he was minded to apply to it the same tests as previously applied to past applications by CWHKTT subject to being satisfied that these tests were still valid and appropriate.

5. The TA therefore invited comments on some specific issues as well as any other issues that respondents wished to provide views or comments.

THE SUBMISSIONS

6. The TA received within the set deadline seven submissions, which he took into account. No late submissions or additional comments and/or withdrawals of comments were received. The comments and/or views came from the following (in alphabetical order):

- a) AT&T Asia/Pacific Group Limited (AT&T);
- b) City Telecom (HK) Limited (CTI);
- c) Global One Communications Limited (Global One);
- d) Cable & Wireless HKT Telephone Limited (CWHKTT);
- e) Hutchison Telecommunications (Hong Kong) Limited (HT);
- f) New T&T Hong Kong Limited (NT&T); and
- g) New World Telephone Limited (NWT).

7. The submissions received responded to the specific issues raised by the TA but also, in some cases put forward new or further arguments. Annex A is a list of the main arguments in the submissions received. This does not aim to be exhaustive nor does it mean to signify that the TA has accepted the arguments as correct. Comments are summarised without comments in a way that reflect as closely as possible the statements made.

8. Of the submissions received only CWHKTT supported the application it made. All other submissions – for different reasons and/or arguments – suggested that the TA should not accede to the application.

ANALYSIS

General

9. The TA in considering the application by CWHKTT has followed the same approach set out in the “Guidelines to Assist the Interpretation and Application of the Competition Provisions of the FTNS Licence” issued by OFTA in June 1995.

10. The analysis examined what was the relevant product and geographic market. Once the relevant market has been defined, the TA assessed whether CWHKTT was dominant in that market.

11. In considering whether CWHKTT was dominant the TA examined the market share of CWHKTT, the market concentration, as well as the surrounding market conditions to establish if the market was competitive and/or contestable. These included barriers to entry, pricing, vertical relationships etc.

12. Once the TA had established the position of CWHKTT (i.e. whether it was dominant or not) he examined whether its application for a declaration for non-dominance was justified. If he was satisfied that CWHKTT was no longer dominant then the TA would consider if any conditions should be applied to such a decision.

Legal basis

² This has the same meaning as in the TA’s statements of 25 November 1998 “Local Access Charge and Modified Delivery Fee Arrangements” and that of 24 December 1998 “Local Access Charge and the Modified Delivery Fee Arrangements – Classification of Routes into Categories A and B” and the list of destinations in the two categories as may be amended in part or in full by the TA from time to time.

13. General Condition 44 of the Fixed Telecommunication Network Services (FTNS) Licence issued to Hong Kong Telephone Company Limited, Hong Kong Telecom International Limited and Hong Kong Telecom CAS Limited (now re-named Cable & Wireless HKT Telephone Limited, Cable & Wireless HKT International Limited and Cable & Wireless HKT CAS Limited) - which is reflected in all FTNS licences - provides that if the TA forms the opinion that the licensee is not in a dominant position, with respect to any market for telecommunications services, he may exempt it from certain licence obligations. These obligations include the implementation of specified accounting practices, obtaining the prior approval of the TA for the tariffs of new services or the revisions of existing tariffs, and a prohibition on discounts from the TA approved tariffs. General Condition 44 also provides that the TA can lift any such obligations either completely or in part and for such period and on such conditions as he may determine.

14. The TA therefore in considering the application of CWHKTT had to determine whether:

- a) CWHKTT is dominant in respect of the market or markets under consideration;
- b) if it is not dominant, should he lift all, some or none of the licence obligations to which General Condition 44 applies; and
- c) any new conditions should be imposed and for what, if any specific, period.

Relevant Market

15. As the definition of the market could significantly affect the outcome of a dominance analysis, the TA invited comments on the appropriate definition of the relevant market. The TA, in reconsidering his previous market definition so as to be satisfied that it is still valid, started by looking at how customers would react if prices would rise by 5%-10%. If significant numbers of customers would switch to

substitutes, the market definition should be widened to include the substitutes. It is not necessary for all customers, or even the majority, to switch. The important factor is whether the number of customers likely to switch is large enough to prevent a “hypothetical monopolist” exercising market power.

16. Substitutes do not have to be identical products to be included in the same market. The products’ prices do not have to be identical. The important issue is whether the firm in question could maintain prices above competitive levels. The products will still be included in the same market if the delay before substitution takes place is so short that it would never be worthwhile to raise prices in the first place.

17. Supply Side Substitution. Substitution can also take place by suppliers. If prices rise, firms which do not currently supply a product might be able to supply it at short notice. This will prevent firms charging monopoly prices, so any supply-side substitutes should also be included in the market. Analysing supply-side substitution raises similar issues to the analysis of barriers to entry. In both cases the question is whether firms would start supplying a particular product if prices rose.

18. The TA accepts that like all other market definitions – in particular in a fast moving market like the telecommunications market – the definition can never be static and that in the future this may no longer be appropriate.

19. The TA has in the past defined the relevant market as: “...*the market for international call services (“International Call Services”) which exclude those provided by operators of mobile services and through Self-Provided External Telecommunication Systems (SPETS) but include ... International Simple Resale (ISR) services for fax and data and International Virtual Private Network (IVPN) services.*”

20. The TA having considered all representations made he is of the view that the previously used definition of the market – “international call services” market is still valid. He was not satisfied that it was appropriate to define the

market more widely than this. The detailed reasons for his views concerning what services should be included in the definition were set out in the previous reports concerning past applications by CWHKTT for a declaration of non-dominance.

21. The TA is satisfied that customers could and would switch between the different types of operators offering external telecommunications services from Hong Kong and for the bigger customers (i.e. big business) it could switch to Virtual Private Network services.

22. One other issue that the TA considered was whether external calls from Hong Kong through mobile telephones are now in the same market i.e. they are a substitute for calls through fixed line telephones. The arguments are finely balanced but there is certainly growing evidence that they are already a substitute, or if not yet, that they will be so in the very near future. The arguments that there is still a need for a separate subscription and contract for a mobile telephone, the need to pay an additional local call charge per minute for calls from mobiles, the need for a “security deposit” with the mobile operator so as to be allowed to make calls overseas and that calls through mobile telephones can be in cases more expensive than calls from fixed lines lean to a conclusion against including them. These arguments can however be countered by the high penetration figures of mobile telephones in Hong Kong, the special offers waiving the local call charges, deposits and in some cases even cheaper calls from mobile phones than from fixed lines. In this case as the conclusions reached by the TA were not affected in any significant way by the inclusion or exclusion of the calls from mobile phones he has decided that he would retain the same market definition of the services that he adopted during the last application by CWHKTT. However, in the future, the TA when called to consider similar issues he will give serious consideration to treating calls from mobile telephones as being possible substitutes for calls from fixed telephones.

23. Calls for data and voice are virtually indistinguishable nowadays and operators do not charge differently for say a minute call to country X to send a fax or a minute call to speak to someone. In this case the TA has included the voice and data calls in the same market, as the price for one would restrain the price for

the other.

24. However the issue of destinations remained. Having defined the general scope of the market, the TA also considered the “geographic” aspects of it. He had to consider and examine three views:

- a) the market consists of all International Call Services that originate from Hong Kong irrespective of where they terminate – which was the view supported by all respondents excluding AT&T and in part CWHKTT and Global One;
- b) the market consists of all International Call Services that originate from Hong Kong irrespective of where they terminate excluding Mainland China – which was the view supported by CWHKTT;
- c) the market consists of all International Call Services that originate from Hong Kong and terminate in a particular country (a *destination by destination* also known as a *route by route* approach) – which was supported by AT&T and in part by Global One.

25. The TA found the arguments for or against each definition finely balanced. However he also noticed from the way the market behaved that calls to countries that were also Category A Destinations were treated differently from calls to Countries that were Category B Destinations³. He therefore also considered whether Calls to Countries that are also Category A Destinations were a separate market from calls to countries that are Category B Destinations. The TA therefore looked at the following issues in deciding how the market should be defined:

- a) Cross elasticity of demand and supply;
- b) Product characteristics;
- c) Price difference;

³ This has the same meaning as in the TA’s statements of 25 November 1998 “Local Access Charge and Modified Delivery Fee Arrangements” and that of 24 December 1998 “Local Access Charge and the Modified Delivery Fee Arrangements – Classification of Routes into Categories A and B” and the list of destinations in the two categories as may be amended in part or in full by the TA from time to time.

- d) Judgement by participants;
- e) Distinct Sellers/Buyers.

Cross Elasticity of Demand and Supply

26. The TA examined if a price change for one product would cause the quantity sold of another product to change. Having examined the elasticity of demand he was satisfied that an increase in the price for Category A calls would not have an effect on the Category B calls. There was no substitutability between them. Therefore, from a demand viewpoint, Category B calls were not in the same market as Category A calls.

27. He also examined the same aspect of behaviour from a supply point of view. He was satisfied that within the Category A routes there was substitutability and if the price for delivering calls to destination X increased then the traffic could be diverted through (transit) destination Y. Therefore the routing of the calls in Category A was open to substitution and was price sensitive.

28. That was not the case for Category B traffic. Suppliers i.e. operators had no or very little option but to ask CWHKTI to deliver it for them. The charges here were fixed by CWHKTI (even though approved by the TA) and there was no flexibility available. There would be limited opportunity for substitution between the different routes.

Product Characteristics

29. The TA also examined the possible markets from a product characteristic point of view. He considered whether they have the same features and whether they provide the same uses for most buyers.

30. Looking at the Category A destinations and the Category B destinations the TA found that their characteristics were different because of the way by which traffic is being delivered and the resulting economies of scale that ensue.

31. In the case of Category A destinations, traffic is mainly delivered through International Private Leased Circuits (IPLCs). These are leased on a capacity basis and provided that the capacity that they can carry is not exceeded then the traffic that is delivered through it is not affected by a per minute charging at the wholesale level. On the other hand, traffic to Category B destinations is charged at the wholesale level on a per minute basis. This means that the operators at a Category A level have not only more flexibility in pricing but also are affected by economies of scale since the cost of the IPLC is fixed irrespective of the volume of traffic it carries. The opposite applies for Category B destinations where no such flexibility exists. Therefore wholesalers are restrained in the way they treat Category B destinations and thus the way they price or market them in the retail market.

Price difference

32. The TA also found that the two categories are having a price differentiation, which is not really justified by the real cost. In the case of Category A market in many cases the prices are low and in many cases they are offered at cost or even below cost as part of a bigger package. The same appears to happen in respect to calls to Mainland China. That is not the case for the other Category B destinations. In that case, calls are charged at a “premium” because operators do not have the flexibility in setting prices at the wholesale level but also they can not substitute between the different destinations. The opposite applies to the Category A destinations.

Judgement by participants

33. One of the other crucial areas that assists in considering the relevant market is what do the industry players see as the products that compete in. In the current case the TA looked at the following factors that tend to show Category A destinations as a separate market from Category B destinations. The factors that he looked at were: product bundling, marketing plans, discounts and special promotions as well as advertising.

34. The TA has observed from the way the market behaves that most

operators will offer bundles of destinations to their end customers. In some cases these are offered in such a way that once customers accumulate a level of spending that they can obtain a discount. Similar conclusions are reached by looking at the way operators market and promote external calls. In all cases the headline offers of all operators are based on Category A calls. They are the ones on which they can discount and offer attractive offers to customers so that they switch their calling habits through their company. A major exception however is Mainland China. Nearly all call packages will include offers for calls there even though it is a Category B destination. However, the TA is satisfied that Mainland China is an exception to the rule because of its importance to end customers and thus the marketing effect that a promotion with attractive prices would have. The package though is structured and financed by those routes that are Category A destinations.

Distinct Sellers/Buyers

35. The reality is that since external telecommunications services operators have to rely on CWHKTI to deliver their traffic at the Category B destinations and there is less price flexibility and economies of scale, they tend not to concentrate at nor promote Category B destinations again with the exception of Mainland China because of its importance to Hong Kong both in terms of volume of traffic but also because of the close ties between the two. These operators target their resources and marketing packages to those destinations that they are in a position to compete – i.e. the Category A destinations and Mainland China. This differentiates them from the existing FTNS operators who because of the nature of their relation with their customers they offer services to all destinations and in some cases they would bundle Category A and Category B destinations together. Even in that case they tend to concentrate on Category A destinations since the price differential that they are able to offer on Category B destinations is small and or is not profitable for them to do so.

36. To a certain extent we end up with CWHKTT on one hand offering calls to both Category A and Category B destinations and all the other operators concentrating on Category A routes. This is another indication that the two groups are separate and which is further reinforced by looking at the market concentration

in the two different markets. In the case of the Category A market the difference in the market share of CWHKTT and its second biggest competitor is approximately 15% for the period January to May 1999. However for the same period for the Category B market (excluding Mainland China) the gap between CWHKTT and its next biggest competitor is approximately 40%.

37. Therefore for the reasons set out above the TA concluded that in view of the behavioural characteristics of the suppliers as well as the consumers, product differentiation etc. the main market for international calls is subdivided into two markets, namely the market to those destination that have been liberalised at the wholesale level (i.e. Category A routes) and the markets that have not (i.e. Category B routes) excluding China. The TA considers that this is the most appropriate way to define the market in deciding whether CWHKTT is indeed dominant in either market.

Geographic Market

38. The geographic market is the area over which substitution takes place. Geographic markets are defined using the same process as that used to define the product market. Retailing markets are more likely to be defined on the demand-side, while wholesaling and manufacturing markets are more likely to be defined on the supply-side.

39. The Demand-side. As with the product market, the objective is to identify substitutes that are so close that they would prevent a “hypothetical monopolist” in one area from charging monopolistic prices. The process started by looking at a relatively narrow area and then it was broadened to consider whether consumers would switch to suppliers in neighbouring areas in response to a small increase in price. If substitution is potentially so significant that it would prevent an undertaking from raising prices, the area is added to the market definition. The evidence used to define geographic markets on the demand-side will usually be similar to the information used to define the product market.

40. The Supply-side. This entails looking at the potential for undertakings to

supply customers in neighbouring territories. As with product-market definition, substitution should be possible in the short run (for example, within one year). Supply-side substitution may not be possible within one year if undertakings need to spend significant sums on advertising or marketing, or if distribution channels are foreclosed.

41. In this case the TA was satisfied that in view of :

- a) the nature of the telecommunications services i.e. universal service to all Hong Kong residents,
- b) the need for a licence to be able to offer external call services in all of Hong Kong;
- c) that customers who wish to make an external call from Hong Kong do not have the option but to make the call from Hong Kong; and
- d) that they can select without any difficulty any operator of their choice irrespective of the operator that provides them with the fixed connection to the network;

that the geographic market should be the whole of Hong Kong.

ASSESSMENT OF DOMINANCE

Factors Relevant to Assessment of Dominance

42. There are a number of factors that need to be considered when assessing whether a firm – in this case CWHKTT - is still in a position of dominance. These include:

- a) market share;
- b) barriers to entry - contestability;
- c) prices;

- d) vertical relationships.

Market share

43. Although market share alone is a poor measure of market power, it is unlikely that a firm without a significant share of the relevant market would have sufficient market power to behave anti-competitively on its own. However, a large market share may not be sufficient to establish market power - for example, if entry into the market is easy, there may be a strong threat of competition from new entrants. Market shares are therefore used as a starting point in any analysis of this nature. The TA has already stated in the guidelines issued concerning the application of the competition-related provisions of the FTNS licences⁴ that certain levels of market share will create certain presumptions. Where the market share in a given market is below 25% then the licensee will be presumed non-dominant. Where the market share is above 75% the licensee will be presumed dominant. For shares between 75% and 25% no presumption will be made.

44. The presumptions made by the TA have the effect of placing the burden of proof on the person arguing that the presumption should not be followed. In the case of a market share between 25% -75% no presumption is made and the TA examines the market share of the firm together with the other relevant elements so as to determine if the firm is dominant or not. However, the TA has considered that if a firm has a market share persistently above 50% it is likely that it is dominant. Therefore when looking at the other market conditions he needs to satisfy himself that these demonstrate that the market is competitive and/or contestable before he would classify a firm with market share above 50% as non-dominant. The opposite applies where the market share is consistently below 50%. In these cases the TA will consider that it is more likely that the firm is not dominant and in examining the other market conditions he will look to see if these are such that make the market non-competitive and/or non-contestable before he would classify a firm with market share below 50% as dominant. This is not the same as the presumptions. Presumptions shift the burden of proof to those arguing against them. The 50% market share is simply used as a starting point for the TA to

⁴ “Guidelines to Assist the Interpretation and Application of the Competition Provisions of the FTNS Licence” June 1995

examine the market conditions and is based on the experience of other jurisdictions both in relations to the telecommunications related markets but also when applying general competition law.

45. All the above should however always be seen under the light of the fact that high market shares at a given point in time are not necessarily indicative of market power. There is thus a need to examine changes in the pattern of market shares over time and combine that with all the other relevant considerations.

46. The TA in examining market shares has done so based on volume of traffic. He has also considered whether he should examine the figures by revenue as well as by volume. However, he considers that in this case the volume measurement would be the most accurate. The retail prices vary substantially between operators. They also vary from month to month or even week to week. There are also discount plans that customers use and therefore it would be difficult and of little additional value to seek to establish the market share by value in relation to contestable routes.

47. The figures used to look at the individual shares was based on the figures for the traffic of each licensee as reported by it to the TA. These numbers are supplied to the TA each month and were not provided specifically for this application. In relation to the month of May 1999 some small firms that account for less than 2% of the overall volume had not supplied figures and those were estimated in line with other licensees in the same category. The figures for January to April 1999 do not include any estimates.

48. Therefore, the TA, having used the most appropriate market definition as well as the actual figures of traffic for each destination, has removed all major elements of estimation or guesswork that may be involved in such exercises.

49. Having examined the market shares of each group over a period of five months, CWHKTT had a market share of consistently below 50% for Category A destinations. The TA has therefore calculated that for the period of January – May 1999 (inclusive) in the case of CWHKTT for Category A destinations its market

share (excluding calls through mobile telephones) was approximately 40% and for Category B destinations (excluding China) it was above 55%.

50. It should be noted in the case of some small markets the market share fluctuated a lot because of the very small volume of traffic e.g. 20 minutes in a month. This meant that an individual telephone call could affect the market share of that route but because of their overall size they did not have a significant effect on the overall markets.

51. The TA has also examined the issue of market concentration. Concentration is the combined market share of the leading firms. This shows the degree of oligopoly/ concentration in a market but it does not provide a full picture of whether it is competitive or not. An oligopolistic market – even a duopoly - can be very competitive. However, the TA wishes to stress that, like the market share figures, the concentration in the market by itself does not carry any significance. When on this occasion the looked at CWHKTT's competitors shares he is satisfied that the gap between them and CWHKTT is not the same as during the last application. In the market for Category A routes where CWHKTT has been declared non-dominant the second biggest market players operator X (name withheld), has a market share of above 20% but below 30%. Operator Y (name withheld), the third biggest player, has a market share of above 10% and below 20%. The gap between CWHKTT and X is approximately 15%. In the case of the Category B market (excluding Mainland China) the second biggest player, operator W (name withheld), has a market share of above 15% but below 25% and the third operator, operator Z (name withheld), has a market share of above 10% and below 20%. The gap however between CWHKTT and W is approximately 40%. The fact is that the gap in the Category A market is becoming smaller and the market is becoming more even. In some individual routes CWHKTT is not even the bigger player in the market. However, even in the cases where the market has not evened out or where CWHKTT has a gap between itself and its competitors, that is not by itself sufficient to maintain that CWHKTT is dominant. The TA looked at this as one of the elements of the analysis that may or may not be neutralised by the other considerations.

Barriers to entry

52. Having established a starting point by the use of market share test the TA went on to examine the extent to which its behaviour in the market is constrained by the threat of new entry or of substitution into the market as a significant factor in assessing the degree of competition on that destination.

53. Where the market share is between 50% and 75% it is more likely that CWHKTT would be dominant unless other factors can show that the market is competitive and/or contestable. For those where the market share was between 25% and 50% it is more likely that CWHKTT is not dominant unless there are factors that demonstrate that the market is not competitive and/or contestable.

54. In the context of markets for telecommunications services there exist regulatory and/or technological barriers to entry and these barriers to entry may confer an absolute advantage on incumbent firms. When assessing market power, the TA took into account the prospects arising after 1 January 2000 and the fact that regulatory restrictions concerning the operation of external circuits will be eased. He has also taken into account other barriers for new entrants that need to be surmounted in the short to medium term e.g. the need to set up correspondent relationships and, if so, to establish how quickly entry and or substitution might occur. Also he took into account that many of the operators offering external telecommunications services in Hong Kong have already established a presence in the market and certainly all the major ones are household names.

55. In the current case the TA is satisfied that there are no regulatory restrictions on the number of operators that can offer external telecommunications services and this is evidenced by the number of licenses already issued – even if not all are active.

56. However, he is aware of the fact that all licensees offering international call services have to rely on CWHKTI for capacity to carry their traffic out of Hong Kong. The TA is also aware that the existing safeguards between CWHKTT and

CWHKTI should ensure that CWHKTT does not receive any unfair advantage over other licensees.

57. The TA is concerned that in all cases except where CWHKTI has been declared non-dominant (i.e. Category A routes) there is a possibility that CWHKTI could use its dominance to stifle competition in a downstream market i.e. retail or that it could in effect set the bottom price. It should however be noted that this affects all market players including CWHKTT.

58. The TA is however satisfied that in all Category A destinations, it may be easy for a competitor of CWHKTT to switch to alternative connections in bypass of the CWHKTI gateway. However, in cases where the wholesale market is not competitive it may not be easy to do so. This is not so in all cases. Where the destination is also a Category A destination (i.e. a route where CWHKTI is no longer dominant) this is certainly the case. Therefore if CWHKTT or CWHKTI was to try to abuse its position in any such destination, its competitors could easily offer competitive prices without having to fully rely on CWHKTI.

59. The TA is also satisfied that many of the operators offering international call services in competition to CWHKTT have demonstrated, so far, that they have the ability and the expertise needed to establish themselves and to become equally well recognised both in the Hong Kong but also at overseas markets as international players. There is no doubt that their management, sales, regulatory teams etc are equally well qualified – even if smaller in size – to ensure that they can compete as effective players. The fact that with the liberalisation of the external services market in January of this year and the demonstrated ability of the some operators to have in place correspondent relationships and to have acquired cable capacity to major markets on time in preparation for the forthcoming facilities liberalisation demonstrates their skill and determination to compete in the external call services market both at the retail but also at the wholesale level.

60. The TA is therefore satisfied that those destinations that are on a Category A route – i.e. where CWHKTI has been declared non-dominant – are fully contestable and thus ensuring that CWHKTT's prices are restrained by the

prices that its competitors offer.

61. This conclusion is further re-enforced by the fact that CWHKTT must be charged by CWHKTI the same price it charges other companies in a comparable position. Therefore the bottom price for CWHKTT should be the same as that for any other retail operator. However, the TA is aware of the concerns expressed about the ability of the HKT group to unfairly subsidise a specific route in such a way that it can have an effect on competition.

62. The TA is satisfied though that General Condition 15 of CWHKTT's and CWHKTI's joint licence makes it clear that if CWHKTI was to give CWHKTT an undue preference so that it had a significant detrimental effect on competition he could take action. This applies to financial as well as other advantages such as information. It is for this reason why the TA proposes to clarify the situation concerning information that is available within the companies. If CWHKTT and CWHKTI were totally separate companies and separately managed etc, these concerns would have been removed and CWHKTT could have been treated in the same way as any other operator offering external telecommunications services.

63. The TA is of the view that CWHKTI's dominant position in the wholesale market and the fact that no alternative competitive routes are available to the destinations in Category B mean that CWHKTT's competitors have no option but to use CWHKTI's facilities with no possibility of setting their prices freely. Admittedly a similar situation arises for those destinations that are served by Category A destinations in that CWHKTT's competitors have to obtain IPLC's from CWHKTI. However, IPLCs are only one of the cost elements. The competitors can in Category A routes negotiate with the operators at the far end and obtain better prices. In the case of Category B routes, competitors have no direct alternative and thus is difficult if not impossible to negotiate prices.

Prices

64. In looking at the competitiveness of a market and whether a firm is dominant the TA examined whether there is genuine independent price competition

in the market or whether pricing changes are, for example, better characterised in terms of a leader-follower situation.

65. The TA is satisfied that price competition in the retail markets for category A destinations is very fierce. In one of the submissions one of the respondent opposing CWHKTT's application has stated that “ ... *It is because the price has been driven down to cost⁵ in the competition and we do not see much development in the near future (at least in the coming six months before the external facilities liberalisation) that can drive the cost further*”. It went on to say “*More importantly, the facilities cost is in fact only a minor cost element in the overall cost structure of IDD services. For this reason, we expect to see that operators will start to compete with each other, instead of against CWHKTT only*”

66. The TA has also considered the arguments that CWHKTT is a price leader and or that it sets a pricing umbrella. The TA accepts that competitors in the market look at the prices charged by CWHKTT in setting their levels. However, the offers that appear daily in the newspapers for Category A destinations, the fact that competition to attract customers is fierce, advertising of new special offers and pricing packages are common, when at the same time CWHKTT's retail prices have been under the control and subject to the authorisation of the TA lead him to believe that CWHKTT is not necessarily the price leader. In many cases it is actually a price follower responding to offers and prices having obtained the TA's consent. In most cases it is responding to substantial reductions in prices by its competitors. That however is not the case for Category B destinations (excluding Mainland China) where price competition is minimal, non-real or non-sustainable.

67. Therefore, the TA is satisfied that the CWHKTT is no longer dominant in the market for “international call services” where the destinations are within the Category A destinations. However, the TA maintains the view that CWHKTT is still dominant in the market for “international call services” to destinations that are within Category B destinations.

⁵ Emphasis added.

Vertical integration

68. Vertical integration in itself does not imply that an undertaking is dominant. However, where an undertaking is dominant or has market power in one market and is vertically integrated into upstream or downstream markets around that market, then it may have the ability to affect adversely competition in the upstream or downstream markets. Consequently, the potential for vertical integration to lead to an abuse of a dominant position is a significant aspect of the analysis of market power in telecommunications.

69. In some cases, such as with international call services other operators and independent service providers rely on a vertically integrated company, which provides both the network and downstream services which are conveyed over it, for the provision of network inputs while at the same time competing with that vertically integrated operator in certain downstream markets. If the vertically integrated operator were dominant in the provision of certain network inputs there could be scope for it to leverage its position of dominance into the downstream market.

70. The TA therefore examined concerns expressed about the degree of vertical integration of CWHKTT and CWHKTI balanced by the existing safeguards for interconnecting operators in terms of accounting separation, anti-competitive provisions in CWHKTT's licence and interconnection determinations and also the constraints still in place where CWHKTI or CWHKTT are still dominant.

71. The TA has some concerns about the information that is available to (a) CWHKTI in respect of the traffic of CWHKTT's competitors and (b) the use that CWHKTT can make of information available to it about its fixed line customers who use competitors services for international calls and or their overall spending and call patterns. In particular the fact (a) that the major decisions of CWHKTT and CWHKTI concerning international call services are taken by the same team, (b) the failure of CWHKTI to protect and to withhold traffic information about other

operators from CWHKTT gives it a competitive and unfair advantage over its competitors who do not have access to them. The same applies for information that CWHKTT has about calling patterns, from the use of its fixed network access in which it is dominant. The TA therefore has decided that conditions must be imposed in respect of the use and protection of information within the company.

72. A specific requirement will be placed on CWHKTT that it does not use in a way that gives it an unfair advantage such information and can demonstrate that it complies with existing obligations about not making use of information it receives other than for the purpose it is supplied for – e.g. directing traffic to the switch etc. - in respect of the non-dominant routes. This is not a new requirement. CWHKTT and CWHKTI are already subject to obligations concerning the use of customer information but also that they should not give each other unfair advantage. However, the fact that CWHKTT's application for non dominance was prepared and presented to the TA by the same team that is responsible for the CWHKTI traffic and detailed traffic figures concerning CWHKTT's competitors were used to support its application (figures that belong to CWHKTI) demonstrated to the TA the fact that CWHKTI and CWHKTT are not sufficiently aware of their obligations in this area. CWHKTT and CWHKTI should have in place the necessary measures to protect the use and misuse of information. Since the use of the information was necessary for CWHKTT's application, it could have been supplied to persons within the company that are not in a position of conflict of interest e.g. regulatory team for them to compile the report.

73. Also, the fact that the FTNS licence is jointly held by CWHKTT, CWHKTI and CWHKTCAS means that at any stage they could be merged into one company, or that one of the three companies may take over the running of a service currently run by another. The decision made to separate the companies to run different services is a matter for the company. However, the TA wishes to ensure that the internal structure within the CWHKT group does not have a detrimental effect on competition.

Compliance

74. The TA in reaching his decision has been very aware of the fact that CWHKTT has in the past failed to comply with its licence obligations and on more than one occasion it has given cause to him to take enforcement action and impose financial penalties. In particular the fact that all the case involved unauthorised discounts and/or IDD calls makes this even more crucial to the decision by the TA.

75. In the light of CWHKTT's past performance and the fact that it is still to demonstrate that it has established a robust and effective internal compliance system and controls in respect of pricing issues but also protecting customer information – whether these are retail customers or competitors that rely on CWHKTT for services – and to ensure that any given flexibility will not be abused, the TA will only lift the existing restriction as soon as he can be satisfied that these concerns are met. Where the TA decided that it might be appropriate to declare CWHKTT non-dominant he has also considered if the existing safeguards are adequate to protect competition.

76. It is for each licensee to ensure that it has the necessary systems and controls in place to monitor its compliance with its legal and licence obligations. The proposed amendments to the Telecommunication Ordinance will make this even more crucial as the TA will have additional powers to deal with breaches much more severely. More crucially though each licensee should be concerned about the effect that its non-compliance has on its customers.

77. Effective but fair competition is what the TA wishes to see in the market. That is why the freedom to price in a flexible way to meet the needs of the market is crucial. But, there should be no doubt that the TA will not tolerate any abuse of the freedom that licensees are given. More so where restrictions are being lifted licensees are in effect required to demonstrate that they will not abuse the freedom that they are given.

78. Therefore, the requirement of the TA to see a fully effective compliance

system within CWHKTT as well as CWHKTI so as to protect consumers and competitors alike should not be seen as an easy option. CWHKTT and CWHKTI will be required to demonstrate their commitment to abiding by their obligations. The TA will also maintain its vigilance so that he can deal with any possible breach fast and effectively. This should not however be seen as a blank invitation for complaints every time that CWHKTT offers a competitive price. The TA will only entertain complaints that raise a prima facie case of a licence breach and provide adequate justification to merit an investigation. He will also require CWHKTT to maintain detailed records on the business case and details underpinning its pricing offers so that it can respond to detailed requests for information within two working days. These are information that should exist so as to demonstrate that the price on offer is compliant with its licence obligations. In addition the TA will from time to time proactively examine prices and offers so as to ensure that the systems to be implemented are functioning.

Future Applications

79. The TA considers that in view of the way that he has defined the market it may not be necessary and/or appropriate to entertain applications about re-classification of individual routes at the retail level. He proposes that the reclassification of a destination at the wholesale level should be used as an automatic trigger for moving it from the non-competitive market to the competitive one and thus lifting the constraints both at wholesale as well as the retail level.

80. It will always be open during the consultation for a reclassification of a route at the wholesale level for those responding to the TA's invitation to provide their views why a particular destination should be treated differently at the retail level. The TA will consider any views that he may receive and will reach his decision taking all factors into account.

81. The TA also does not propose to commence his review of the situation until June 2000 by which stage he would be in a position to examine the effects of the further liberalisation of the market. At that stage he will consider if the market has changed but also he will review the way that CWHKTT behaved over the 12

month period. He will then review the conditions he has imposed so that he can satisfy himself that these are still appropriate. The direction will therefore have a "Sunset Clause" i.e. an end date of September 2000. This is to allow for the review to take place and for any necessary amendments to be implemented in time before the expiry of the current direction.

CONCLUSIONS

82. Therefore, in view of the above the TA has reached the following conclusions:

- In respect of countries that are also Category A destinations CWHKTT is no longer dominant and he will lift some of the relevant obligations as soon as he is satisfied that CWHKTT's systems can ensure compliance with its existing licence obligations and conditions that he has imposed to ensure that competition is protected. These conditions will seek to ensure that CWHKTT:
 - a) will not abuse its vertically integrated position, its dominant position in other destinations;
 - b) not target customers of its competitors by using anti-competitive offers or methods; and
 - c) that it will institute a proper internal pricing vetting and information system for new prices.
- The TA has required CWHKTT to set up the necessary compliance systems on pricing, protection of customer information and information it obtains from CWHKTI. Once CWHKTT notifies the TA that it has set up the necessary controls and has produced and published a compliance plan for the above mentioned areas, General Conditions 20(4) (prohibition of offering discounts to its published tariffs), 21(requirement for prior

approval from the TA for tariff revisions) and 22 (tariffs for new services) of its fixed telecommunications network services licence will no longer apply in relation to the market that has been declared non-dominant.

- In respect of all other destinations he is not – at this point - able to accede to CWHKTT's application that it is non-dominant. He will therefore maintain the existing controls.

Office of the Telecommunications Authority

4 August 1999

SUMMARY OF SUBMISSIONS RECEIVED

(NOTE: The terms CWHKTT, CWHKTI and/or CWHKT used in this summary reflect the term used by the respondents.)

- a) **AT&T Asia/Pacific Group Limited** – does not support the application.
- Facilities based competition is necessary before such a declaration;
 - CWHKTT retains market power;
 - CWHKTT's prices for IPLCs set the floor for prices of competitors;
 - The comparisons with the FCC's decision of 1996 for AT&T is not relevant as other considerations taken into account other than market share;
 - CWHKTT controls bottleneck facilities
 - Dominance will continue after year 2000;
 - Analysis should be carried out on a route by route basis – a call to country X is not a substitute for a call to country Y;
 - Future evaluation of dominance should look at routes where there are both significant market share loss by CWHKTT and alternative facilities based capacity for traffic on that route.
- b) **City Telecom (HK) Limited**-does not support the application;
- Market definition must include the China traffic;
 - Competition on non-China route is a safeguard for the whole IDD market;
 - If application is approved, CWHKTT could timely and effectively offer parallel or even better services in all aspects on the non-China routes;
 - The decline of CWHKTT's market share is natural consequence of liberalisation. No sufficient evidence that the trend will continue;
 - The price of IDD calls has been driven down to costs;
 - Facilities costs is only a minor cost element in the overall cost structure of IDD services;
 - Expect operators to start competing with each other instead of against CWHKTT only;

- The IDD market is still highly concentrated;
 - From the ETS operators licensed (more than 100) only few actually active in the market – this is a good indication that no abnormal profit can be generated and the reduction in cost due to ISR liberalisation has been reflected in price;
 - Vertical integration of CWHKTT and CWHKTI cause for concern. Same parent company and run by same management team.
- c) **Global One Communications Limited** - does not support the application ;
- CWHKT is the primary supplier of retail international voice services;
 - CWHKT is the monopoly provider of the essential IPLC facilities;
 - Competition is fragile;
 - Market could be determined on a route by route basis;
 - Market definition is for the provision of international voice telephony and therefore TA should exclude non voice services;
 - Market could be determined on a route by route basis but would cause major issues on cost allocation;
 - Administrative easier to use a single geographic market approach – also taking into account the offerings of packages, overflow of dominance etc;
 - No reason why Hong Kong Chine route should be treated differently;
 - IDD market is dominated by CWHKT. Pricing offers should be seen for what they are – in cases they are short term and non-sustainable marketing efforts;
 - CWHKT is the pricing leader and creates a pricing umbrella;
 - CWHKT is incumbent in terms of customer loyalty, customer data, competitor data and branding;
 - The use of the FCC decision not a valid comparison due to difference in market shares, competitors had their own capacity on cables and or earth stations, agreed terms for access to cable stations and backhaul;
 - Barriers to entry exist – regulatory restrictions, facility based licenses, investment may be needed in other areas to build regional or global network to produce economies of scale.

d) **Cable & Wireless HKT Telephone Limited – supports the application;**

- Previously adopted market definition is still valid and in accordance with international practice;
- Voice over Internet should also be regarded as part of the relevant market
- Not appropriate to use route by route approach as carriers can hub or refile traffic;
- The use of headline price offers by competitors, the fact that customer do not select an operator for each destination and the discount packages irrespective of route also support a non route by route approach;
- CWHKTT's market share is below 50% for the non-China traffic;
- The application is made so that CWHKTT can compete fairly;
- With three FTNS operators and 109 ETS competitors the market share of any individual should not be critical to the health of the market;
- Loss of market share is of greater significance than whether one competitor can gain sufficient share to become dominant;
- Competitive process in the retail international market is firmly established;
- The existing spread of market shares of CWHKTT and its competitors mean that the market cannot be considered highly concentrated;
- Very competitive prices are available on the market;
- Existing safeguards on accounting separation, anti-competitive provisions mean that the TA should have no concerns about vertical integration;
- CWHKTT and CWHKTI remain as separate legal entities and there has not been any integration between the two.

e) **Hutchison Telecommunications (Hong Kong) Limited** - does not support the application;

- Refers to its previously made representations for the 1997 and 1998 CWHKTT application;
- Local and international markets should be regarded as a whole;
- Incoming and outgoing traffic should be take into account;
- CWHKTT and CWHKTI are a single licensee and control 99% of local infrastructure and 100% of international gateway facilities;

- Incoming traffic benefits the cost structure of CWHKT's outgoing traffic;
 - Calculation of CWHKT's market share should be based on its incoming and outgoing minutes;
 - CWHKT's competitors cannot price independently from CWHKT's prices for IPLCs;
 - Object to the division of China, non-China routes or a route by route definition;
 - Competition in the IDD market is slowly maturing
 - Very few new active ETS operators on the market;
 - Profit margin for IDD is very thin therefore unattractive market for new players;
 - CWHKT can also use the revenue from inbound traffic to bring prices down to level others cannot sustain business;
 - IDD services were very profitable with very high margins. Competition has successfully driven prices down;
 - Existing safeguards are inadequate and there have been a number of finding of anti-competitive contact by CWHKT;
 - ITBB proposes to introduce additional competitive measures but their success lies in their implementation and more heavy-handed approach towards non-compliance;
 - A ruling of non-dominance should only be considered after the full liberalisation of external facilities.
- f) **New T&T Hong Kong Limited** – does not support the application;
- The policy and regulatory context of this application is very different from the past due to the Framework Agreement signed by the Hong Kong SAR Government and the CWHKT group of companies. This agreement has changed the telecommunications environment of Hong Kong in a way that is detrimental to the new operators.
 - The market should be defined as the market for end user access and connectivity to international call services and should include “mobile” and “fixed” services, “voice” and “data” transmissions and China and non-China traffic;

- The market share of CWHKTT for the above mentioned market must be in excess of 75%. If the TA adopts the China/Non-China route approach he should rely on the basis of market data that he has or can collect and which would be reliable;
- Market share is only a factor; the market is highly concentrated and is unlikely that any competitor has more than 10% market share. If one accepts CWHKTT's claim that it has less than 50% of market on non China routes this creates an HHI index of 2400 which is in excess of the 1800 level used by the Department of Justice in the US as a benchmark for "highly concentrated" market;
- Here is asymmetry in market information and CWHKTT is the only company who has access to traffic information of competitors which gives it a competitive advantage; It can monitor traffic of operators, identify customers of competitors and monitor pattern of usage of its own and of competitors customers;
- The vertical integration between CWHKT and CWHKTI makes CWHKT group as the competitor of the local operators. It controls both ends of international traffic and can manipulate end user and inter-carrier pricing through internal transfer pricing arrangements;
- HKT still controls the supply of international facilities and the issues about the control of landing stations make it doubtful if the other FTNS operator will be able to offer any international facilities on 1 January 2000;
- CWHKTI has access to skill and recourses that new FTNS operators have to acquire and must now compete on an international level with the associated risks of international traffic volume forecasting, price settling, settlement transactions etc.;
- Service brand and reputation take time to build but also a significant investment. HKT's established brand gives CWHKTT an advantage;
- CWHKTT can maintain prices as part of its overall profitability from other services such as fixed lines, data services etc. Also HKT group is enjoying significant revenues from the leasing of IPLCs
- CWHKTT has the ability to implement decisions because of its market share, branding, access to competitors information and mature international business relationships;

- Although there are no prima facie regulatory barriers HKT's group advantages, its established customer base, customer inertia; economies of scale and number of operators present barriers to newcomers;
- The 1998 FTNS review has caused operators to re-examine their plans on the market and was a blow to FTNS operators. To declare CWHKTT non-dominant would be a further blow. A number of major milestones arising from the Framework agreement are still to be implemented;
- If the application was granted when CWHKTT has in the past been issued with three directions and was fined twice for breach of its licence would send the wrong signal;
- The controls that apply to dominant operators are comprehensive, but there are weakness in applying these in a timely manner. This weakness is not just a Hong Kong phenomenon.

g) **New World Telephone Limited** - does not support the application.

- The market should be defined as including China routes as well as incoming traffic;
- The overseas precedent quoted by CWHKTT is not applicable to this application. No routes were excluded from the applications there and proportionate return rules were already in place.
- The relevant market is still too unstable to make an accurate assessment of the market share of CWHKT;
- The market is concentrated and CWHKT can act independently of its competitors when they compete against each other;
- CWHKT can match competitors price reductions because of the profit from return traffic, the income of IPLCs etc;
- The control of the local access customers and the relation with CWHKTI gives CWHKTT information about competitors traffic;
- Local Access charges constitute an outpayment for CWHKT's competitors where in the case of CWHKT it is merely an internal transfer cost;
- CWHKT has been able to react to the market. From June 1998 to June 1999 it has launched more than 30 promotions/ discount schemes;

- The existing application should be rejected and only considered after January 200 when the external facilities monopoly ceases;
- The policy objective of 50% contestability in the residential line market is a key assumption for non-dominance but it has not been achieved yet;
- If the application is granted it will have a serious detrimental effect on the market. CWHKT will be able to regain substantial portion of the market; the TA will have little control over its pricing, any control will be after the price has been made available to the market. In addition, other safeguards concerning contractual terms, tying arrangements etc will also be lifted leaving competitors at the mercy of CWHKT.
