

Consolidation in UK mobile: the fat lady's not singing yet, but she's clearing her throat

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After months of speculation about consolidation in the UK mobile market, we finally know what the outcome will be. A takeover by each of the other big UK operators has been mooted at various points, as well as some more exotic possibilities such as an asset swap between T-Mobile in the UK and Vodafone in Turkey. But no-one saw this coming – or if they did, they kept very quiet about it. Deutsche Telekom and France Telecom are placing their UK mobile operations into a new joint venture, formed from "a merger of equals".

There's an awful lot to be worked out at the retail level. To start with, what brand will the new operator use? A new brand could succeed (as O2 has shown), but is risky and would incur heavy short-term marketing costs. Or they could keep one of the current brands – but then the "merger of equals" line immediately comes into question. And will the new operator retain Orange's heavy emphasis on multimedia content/services and handset branding, or will it adopt T-Mobile's more telecoms-centric marketing approach? What about T-Mobile's strong focus on wholesale business? These questions, and many more, are doubtless already the subject of vigorous discussion between the two executive teams.

One of the questions debated over the past months has been whether the RAN sharing deal between 3 and T-Mobile might stand in the way of any consolidation. From that point of view, today's outcome is a fairly clean one. Although some of the deal's terms are confidential, we do not believe that either party would have agreed terms that blocked or seriously impaired future M&A transactions. And following Vodafone's move to O2 as its RAN-sharing partner, Orange became the only UK operator not to be active in RAN sharing. Thus, it's even possible that the current 3/T-Mobile deal could be continued into the new joint venture.

Another big question has been whether any UK consolidation will be blocked by regulators on competition grounds. We think that's unlikely; there is plenty of recent European precedent for in-country mobile consolidation. However, it is more likely that Ofcom will apply some conditions to the merger, in order to remedy the reduction of competition in the UK market. In particular, we may see steps to boost the position of 3, in order to compensate for the removal of the other UK operator that has behaved as a "maverick" competitor on pricing in recent years (ie, T-Mobile). Possible areas in which remedies might be applied include divesting the merged operator's wholesale business – although that would be problematic in the long term. Another possibility might be compensation through asymmetrical termination rates. That would be politically contentious, but it has the advantage of enabling differential adjustment of the other three operators' competitive position with respect to the new merged JV.