

Zero-rating controversy in India – a storm in a teacup



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I have been watching the launch of Airtel Zero and the visceral reaction of a million netizens in India with curiosity. With 240M+ internet users and ubiquitous use of social media, I guess it is not hard to whip up a million citizens into frenzy!

Having led strategy for a zero-rating pioneer and having the unfortunate experience of dealing with the alarming side-effects of an activist regulatory regime, I believe this reaction is misplaced and any supportive actions by the telecom regulators will only serve to keep the digital divide in India up for longer.

The term zero-rating was yet to be coined, when in late 2009, we at MTS launched our high-speed data product in India. As an upstart trying to disrupt the telecom landscape, we introduced numerous innovations to the market – data on prepaid for the 1st time in India, zero-balance recharge, unlimited data and differential charging (launched with an offer of 5 free websites and later allowed customers to customize their choice of 5 sites). The last innovation is in essence zero-rating! We were among the first in the world to work with websites and vendors to figure out the technology to make this happen. Figuring out how to have content on websites not count towards your data allocation was one thing, but we went further to make sure the ads on these sites did not either.

Why did we do this? We believed trialing was an important step towards growing the internet population in India and allowing subscribers to surf their favorite sites for free was our way of making this happen. While we did not strike revenue arrangements with these websites and chose to give away this data for free, we believed this was a way for us to differentiate ourselves in the market. This along with the other innovations we brought to market drove the market for high-speed wireless data to double every 12 months and in the process, MTS became the leader for high-speed wireless data subscriber additions.

Our data ARPU was depressed, we continued to bleed cash, but we nevertheless thought this was a worthwhile investment to acquire customers and establish MTS as a data-market leader. However, both due to the lack of overwhelming scale in the market and the fact that we left it to the consumer to choose the 5 free sites, we do not believe we caused any monopolistic or anti-competitive situation and neither did we stifle innovation and most of all, we did not cause a million netizens to vent their fear and anger about net-neutrality!

Now, looking at the market as a whole, though Internet and broadband usage in India has grown at a fast clip in the past 5 years, it has trailed the government's targets by a wide margin time and again. At the end of 2014, only 19% of Indian citizens were connected to the Internet behind countries such as [Bhutan](#), [Iran](#), [Libya](#) and [Syria](#) and nowhere near the other BRIC countries which average approximately 53%! While we can debate the reasons for this, I believe the lack of incentives for private players to drive growth, lack of affordable devices and the lack of affordable tariffs are all driving factors.

While the top-3 telcos are profitable at an EBITDA level, 9 other private and public operators in the market have consistently lost money since 2009, 3 more have exited the market after racking up significant losses and the industry as a whole has been unprofitable and has had abysmal return on capital. Additionally, with the government's near-term focus on maximizing revenues, the auctions since 2010 in India have led to some of the highest spectrum cost compared to global benchmarks in terms of cost per MHz-Pop. And now, informed netizens and regulators want these operators to spend billions more on infrastructure but allow over-the-top players to appropriate all the profits.

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While those agitating for “net-neutrality” have some legitimate concerns that need to be addressed, I believe they are trumped by the pressing need for more affordable services to bring 100s of millions of Indians onto the Internet. Also lost in the melee is an understanding of the economics underlying the industry. Let’s take a look at a couple of Internet pioneers in the US. Vonage, a VOIP pioneer has 2.5M subscribers and offers a world plan with unlimited calling within the US and to 60 other countries for \$25.99 per month, but surcharges and government mandated taxes and fees adds a whopping 53% more for a total of \$39.84. Will the calling feature on WhatsApp stand a chance if the government imposed these taxes and fees on these calls? Amazon, a poster-child for Internet success drove numerous brick and mortar businesses into bankruptcy due in part to consumers being able to [avoid sales tax while purchasing online](#). If net sales were taxed from day one, would Amazon have become the behemoth it is today?

In the long-run, India's vision of half a billion citizens connected to the web will happen only if the operators spend tens of billions more on expanding high-speed data coverage and also provide the lowest data tariffs in the world. The economics of the data business is very much unlike the voice business and there are hardly any network effects and greater scale for sure begets greater costs, but not higher profits. As a first-mover in this market, we at MTS understood this all too well and were struggling to figure out how to become profitable, five years after launch. The other operators understand this now and have been dragging their feet in making more investments in their network without any line of sight to profitability. The onus is on the regulators to incent the industry to make these investments. What can they do?

- For a period, **exclude data revenues in calculating adjusted gross revenue** used for calculating license fee and spectrum usage charges. Telcos, ISPs and others will have a greater incentive to drive adoption of data.
- **Lightly regulate the OTT players** so they are required to either invest in the infrastructure themselves or defray the costs borne by others. I am sure no one finds it reasonable that a private party can setup a toll booth on a highway without paying a substantial part of it to the government. The OTT players are collecting the tolls, not necessarily from the users, but from other businesses and getting away without paying anything to anyone. If you can generate revenues with almost no costs, no wonder these companies sport obscene valuations.
- **Allow telcos to offer differential charging.** Yes, there will be some winners and some losers. But in what industry the world has known, have incumbents and upstarts alike not marketed and-or discounted their wares to gain a competitive advantage. This does not mean innovation will not happen

Microsoft, the undisputed leader in Technology was upended by Google, Amazon and Facebook not because the US and EU punished Microsoft for abuse of its dominant position in the market, but because these companies innovated faster and better!

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