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# Determination

## Voyage Digital (NZ) Limited, Orcon Holdings Limited and Two Degrees Group Limited [2022] NZCC 3

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| **The Commission:** | Sue Begg<br>Elisabeth Welson<br>Tristan Gilbertson |
| **Summary of application:** | An application from Voyage Digital (NZ) Limited seeking clearance to acquire 100% of the shares in each of Orcon Holdings Limited and Two Degrees Group Limited. |
| **Determination:** | Under section 66(3)(a) of the Commerce Act 1986, the Commerce Commission gives clearance to the proposed acquisition. |
| **Date of determination:** | 14 March 2022 |

Confidential material in this report has been removed. Its location in the document is denoted by [ ].

## The proposed merger

1. On 5 January 2022, the Commerce Commission registered an application for clearance (the Application) in relation to a transaction that would result in the merger of the New Zealand operations of Vocus Group Limited (Vocus) and Two Degrees Group Limited (2degrees) (the Proposed Merger).

2. The Proposed Merger involves a newly incorporated Vocus company, Voyage Digital (NZ) Limited (Voyage, the Applicant), acquiring all of the shares of Orcon Holdings Limited (formerly known as Vocus (New Zealand) Holdings Limited (Vocus NZ)) and then acquiring all of the shares in 2degrees from its shareholders, Trilogy International New Zealand LLC and Tesbrit B.V.. Voyage seeks clearance from the Commission to acquire 100% of the shares in each of Vocus NZ and 2degrees.

## Our decision

3. The Commission gives clearance to the Proposed Merger because it is satisfied that the acquisitions will not have, or would not be likely to have, the effect of substantially lessening competition in a market in New Zealand.

## Our framework

4. Our approach to analysing the competition effects of mergers is based on the principles set out in our Mergers and Acquisitions Guidelines (our guidelines).[1]

5. We assess mergers using the substantial lessening of competition test. We determine whether a merger is likely to substantially lessen competition in a market by comparing the likely state of competition if the merger proceeds (the scenario with the merger, often referred to as the factual), with the likely state of competition if the merger does not proceed (the scenario without the merger, often referred to as the counterfactual).[2]

## The parties

6. Vocus and 2degrees are both telecommunications providers that primarily supply retail fixed and mobile services to consumers and small business customers.

7. Vocus NZ is the New Zealand subsidiary of Vocus. It owns and operates a national fibre telecommunications network, which it uses to supply fixed-line and other telecommunications services (on both a wholesale and retail basis). It retails telecommunication services to residential, business and government customers under brands that include Orcon, Slingshot, Flip and Vocus. It also retails energy to residential customers, bundled with telecommunications services. It does not own any mobile network infrastructure, and instead operates as a mobile virtual network operator (MVNO).

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[1] Commerce Commission, *Mergers and Acquisitions Guidelines* (July 2019).

[2] *Commerce Commission v Woolworths Limited* (2008) 12 TCLR 194 (CA) at [63].

8. 2degrees owns and operates a national mobile telecommunications network. It retails fixed, mobile and other telecommunications services to residential, business and government customers. It also provides wholesale services, including for fixed-line and mobile.

## Market definition

9. Market definition is a tool that helps identify and assess the competitive constraints that a merged entity would face.[3] Determining the relevant market(s) requires us to judge whether, for example, two products or services are sufficiently close substitutes to fall within the same market.

10. We define markets in the way that we consider best isolates the key competition issues that arise from the proposed acquisition. This may not require us to precisely define the boundaries of a market. What matters is that we consider all relevant competitive constraints, and the extent of those constraints. A relevant market is ultimately determined, in the words of the Commerce Act 1986, as a matter of fact and commercial common sense.[4]

11. In the Application, the Applicant submitted that the markets relevant to our assessment of the Proposed Merger are national markets for the retail supply of:[5]

    11.1 fixed-line voice and broadband services to consumers and small business customers; and

    11.2 mobile phone services.

12. We consider that the relevant markets in this case include markets at both the retail level and wholesale level, as this reflects the functional levels at which the Parties provide services. In reaching a decision on the Proposed Merger we did not need to identify the precise boundaries of the relevant markets. While multiple markets at the wholesale and retail level may exist for different services (including those identified by the Applicant at [11]), we were able to reach a decision simply by considering the impact of the Proposed Merger generally on retail and wholesale competition.

## With and without scenarios

13. The Applicant submitted that absent the Proposed Merger, Vocus NZ and 2degrees are likely to proceed with separate initial public offerings.[6]

14. We have assessed the Proposed Merger against a counterfactual of the status quo, where Vocus NZ and 2degrees would continue to exist as separate suppliers and

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[3] Commerce Commission v New Zealand Bus *Limited* (2006) 11 TCLR 679 (HC), at [123]. *Brambles New Zealand Ltd v Commerce Commission* (2003) TCLR 868 (HC) at [137].

[4] Section 3(1A). See also *Brambles v Commerce Commission* (2003) 10 TCLR 868 at [81].

[5] The Application at [120].

[6] The Application at [39].

competitors (in those markets where they overlap and compete). We consider that this is the likely counterfactual.

## Competition analysis

15. We assessed whether the Proposed Merger would be likely to substantially lessen competition in any relevant retail or wholesale markets by assessing whether any horizontal unilateral, vertical, conglomerate or coordinated effects might result from the Proposed Merger.

    15.1 *Unilateral effects.* Unilateral effects arise when a firm acquires or merges with a competitor who would otherwise provide a significant competitive constraint (particularly relative to remaining competitors) such that a merged entity can profitably increase price above the level (or reduce quality or innovation below the level) that would prevail without the acquisition without the profitability of that increase (or reduction) being thwarted by rival firms' competitive responses.

    15.2 *Vertical or conglomerate effects.* A merger between suppliers (or buyers) who are not competitors but who operate in related markets can result in a substantial lessening of competition due to vertical or conglomerate effects. This can occur where a merger gives a merged entity a greater ability or incentive to engage in conduct that prevents or hinders rivals from competing effectively.

    15.3 *Coordinated effects.* An acquisition can substantially lessen competition if it increases the potential for a merged entity and all or some of its remaining competitors to coordinate their behaviour and collectively exercise market power or divide up the market such that output reduces and/or prices increase. Unlike a substantial lessening of competition which can arise from a merged entity acting on its own, coordinated effects require some or all of the firms in the market to be acting in a coordinated way.

16. For the reasons set out below, we consider that the Proposed Merger will not have, and would not be likely to have, the effect of substantially lessening competition in any relevant market.

### The Applicant's submissions

17. In the Application, the Applicant submitted that the Proposed Merger would not be likely to substantially lessen competition in any relevant markets due to unilateral, coordinated or vertical/conglomerate effects. The Applicant submitted that:[7]

    17.1 Vocus NZ and 2degrees are not each other's closest competitors in the relevant markets;

[7] The Application at [11]-[15], [137], [167]-[168] and [170]-[171].

17.2 the Proposed Merger would only result in limited to minimal aggregation in the relevant markets;

17.3 a range of existing competitors would remain in the relevant markets to constrain the merged entity;

17.4 in the retail supply of broadband services, further constraint would be provided by potential competition, as barriers to entry and expansion are not significant;

17.5 the relevant markets do not appear vulnerable to coordination and the Proposed Merger would not enhance the ability for the merged entity and other competitors to coordinate their behaviour; and

17.6 the merged entity would not have the ability or incentive to foreclose competitors in respect of access to wholesale services or customers by bundling energy, broadband and mobile services.

18. The Applicant further submitted that the Proposed Merger would have pro-competitive effects because, in the Applicant's view, it would:[8]

18.1 create an integrated fixed-line and mobile business of scale, with the ability to provide better services to customers (both in terms of enhanced choice, as well as complete solutions and new bundles of services);

18.2 enhance competition in the relevant markets by leveraging the existing positions of Vocus NZ and 2degrees (and combined scale) to create a stronger number-three player and stronger challenger to compete with its largest competitors, Spark and Vodafone; and

18.3 create a merged entity with the scale required to enable further investment in network capacity and sustain the anticipated network investment required for 5G, as well as sufficient capital to accelerate investment in 5G.

**Our assessment**

19. Vocus NZ and 2degrees overlap mainly in the retail supply of fixed-line voice and broadband services. The parties face competition, including from several large and well-resourced competitors, for the supply of these services.

20. We consider that these and other competitors are likely to constrain the merged entity and prevent a substantial lessening of competition due to unilateral effects in all relevant retail and wholesale telecommunications markets. We further consider that the Proposed Merger is unlikely to cause a substantial lessening of competition due to vertical, conglomerate or coordinated effects in any relevant telecommunications markets.

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[8] The Application at [7]-[9] and [29]-[35].

*Unilateral effects: competition at the retail level*

21. The Proposed Merger is unlikely to cause a substantial lessening of competition due to unilateral effects in any relevant retail telecommunications markets.

22. The evidence indicates that Vocus NZ and 2degrees are not each other's closest competitors in any retail markets, and that any competition at the retail level lost as a result of the Proposed Merger is unlikely to be substantial.

    22.1 There is minimal overlap between the parties in the supply of retail mobile services. Whereas 2degrees is an established competitor with its own network and an estimated 19% share of mobile connections, Vocus is an MVNO operator with a share of the 2% of connections accounted for by all MVNOs.[9]

    22.2 In terms of fixed-line broadband services, Vocus is a vertically integrated network owner/retailer and has an estimated 12% share of broadband connections, while 2degrees does not own its own network and has a share of 7% of connections. The merged entity's share will be around 19%.[10]

    22.3 Our enquiries showed that existing competitors such as Spark and Vodafone (who both retail fixed-line and mobile services), and also the large number of retailers offering only fixed-line services (eg, Trustpower), would constrain the merged entity in all relevant retail markets.

    22.4 The bundle of telecommunications products that the merged entity will be able to offer will face significant competition from the bundles offered by competitors.

23. Because we were satisfied that existing competitors would constrain the merged entity in all relevant retail telecommunications markets, we did not assess the constraint provided by potential competition.

24. The Proposed Merger is therefore unlikely to result in reduced competition on price, quality or innovation in any relevant retail markets.

25. Some parties submitted to us that the Proposed Merger would create a stronger third player and competitor in retail markets.[11] We noted these and the Applicant's submissions on the pro-competitive effects of the Proposed Merger but have not needed to reach a view on these submissions in deciding the Application.

*Unilateral effects: competition at the wholesale level*

26. The Proposed Merger is unlikely to cause a substantial lessening of competition due to unilateral effects in any relevant wholesale telecommunications markets.

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9 Commerce Commission "Annual Telecommunications Monitoring Report 2021" (17 March 2022).

10 Commerce Commission "Annual Telecommunications Monitoring Report 2021" (17 March 2022).

11 Submission from WISPA to the Commerce Commission (14 February 2022) and submission from TUANZ to the Commerce Commission (24 February 2022).

27. The evidence indicates that Vocus NZ and 2degrees are not close competitors in any wholesale markets. This is because they do not compete to offer the same wholesale services. Vocus NZ wholesales mainly fixed-line services and 2degrees largely wholesales mobile services. Any competition at the wholesale level lost as a result of the Proposed Merger is unlikely to be substantial.

*Vertical or conglomerate effects*

28. For the reasons set out below, we consider that the Proposed Merger is unlikely to substantially lessen competition due to vertical or conglomerate effects in any relevant telecommunications markets.

29. The Proposed Merger would result in the largest existing MVNO (Vocus NZ) becoming vertically integrated with the mobile network operations of 2degrees. MVNOs currently account for a small proportion of retail mobile connections,[12] and with the Proposed Merger this share will decrease.

30. The Commission considers that MVNOs are likely to influence the further development of competition in mobile services,[13] and the Proposed Merger could be of concern if it affected mobile network operators' collective willingness to offer wholesale access to MVNOs on competitive terms.[14]

31. Some concerns were raised about how the Proposed Merger might change the incentives of the merged entity and its rivals to wholesale access to MVNOs, which could raise vertical or coordinated concerns.

32. We received two submissions raising concerns that the Proposed Merger could reduce the extent or choice of wholesale offerings available to MVNOs, or negatively impact on innovation in wholesale offerings. Submitters considered that further development and a workable MVNO model are needed.[15]

33. While the Proposed Merger would result in vertical integration, on balance, we do not consider it is likely to significantly change the incentives of the merged entity (or its competitors) to supply wholesale access on competitive terms. The merged entity, like other wholesale suppliers, is likely to be incentivised to compete for wholesale customers in order to utilise spare capacity on its fixed and mobile networks, both of which have high fixed costs. In addition, the merged entity would supply no 'must have' products or services and would not have market power at the wholesale or retail level.

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12 Customers of MVNO made up 2% of the mobile connections in 2021. Commerce Commission "Annual Telecommunications Monitoring Report 2021" (17 March 2022).

13 Commerce Commission "Mobile Market Study Findings" (16 September 2019).

14 This could also be characterised as a vertical concern because it relates to the potential for MVNOs to obtain access on acceptable terms.

15 Submission from WISPA to the Commerce Commission (14 February 2022) and submission from TUANZ to the Commerce Commission (24 February 2022). In terms of a workable MVNO model, WISPA further submitted that it would like to see MVNO access evolve to the point where MVNOs are able to offer mobile services that are truly competitive (meet the retail market), while allowing a fair margin for MVNOs.

34. While we have no issues with the Proposed Merger in terms of the substantial lessening of competition test, we acknowledge the concerns that have been expressed. The Commission has previously noted the importance of wholesale access arrangements to the development of competition in telecommunications markets. We have an obligation under the Telecommunications Act to monitor and report on the performance and development of telecommunications markets, including at the wholesale level, and the ability to address any competition issues that may arise going forward.

*Coordinated effects*

35. For the reasons set out below, we consider that the Proposed Merger is unlikely to cause a substantial lessening of competition due to coordinated effects in any relevant retail or wholesale telecommunications markets.

36. The relevant retail telecommunications markets do not appear especially vulnerable to coordination. Competitors vary significantly in terms of size and business model. The prevalence of bundled deals reduces price transparency while also making rival suppliers' offers less immediately comparable in terms of quality, service and innovation. These factors would complicate the efforts of any providers attempting to coordinate on, and maintain agreements about, price or other aspects of their offers. The Proposed Merger is unlikely to result in a significant change to these dynamics in a way that would allow competitors to coordinate their behaviour.

37. While the Proposed Merger would result in vertical integration (as discussed above under vertical effects), on balance, we do not consider that coordinated effects are likely in any relevant wholesale telecommunications markets. We consider that the Proposed Merger is unlikely to change conditions in wholesale telecommunications markets such that coordination between wholesale suppliers is more likely, more complete or more sustainable. While the Proposed Merger would decrease the combined market share of MVNOs, we do not consider it is likely to significantly change the incentives for the merged entity or its competitors to wholesale services (including to MVNOs). The merged entity, like other wholesale suppliers, is likely to be incentivised to compete for wholesale customers in order to utilise spare capacity on its fixed and mobile networks, both of which have high fixed costs.

## Determination on notice of clearance

38. Under section 66(3)(a) of the Commerce Act 1986, the Commerce Commission determines to give clearance to Voyage Digital (NZ) Limited to acquire 100% of the shares in each of Orcon Holdings Limited and Two Degrees Group Limited.

Dated this 14th day of March 2022

Sue Begg
Deputy Chair