



Mobile Matters.

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RETHINKING MOBILE DATA PRICING

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‘Our customers appreciate they now have a choice of data plans. From the feedback we have had, the classic one-size-fits-all approach doesn’t make sense any more.’

Mark Siegel

Executive director of media relations, AT&T

Offering customers unlimited use of data for a fixed monthly fee is looking like bad economics for many mobile operators, but there are also dangers in abandoning this pricing model.

Flat-rate pricing is usually a good thing for customers – provided, of course, the rates are low enough. There are no nasty surprises on the monthly bill, which is simple to understand. A service that customers might otherwise have been cautious about using (and paying for) suddenly becomes more attractive.

This has certainly been the case for mobile data services, particularly with the introduction of unlimited data for a fixed monthly fee – the ‘all-you-can-eat’ deal. True, many mobile operators (particularly in Europe) have placed caps on data use, but these are usually set so high that, in most cases, the customer can happily use the mobile phone for such things as web browsing, video, music downloads and photo-sharing without having to worry about the monthly bill. The result has been a mobile data boom. According to Heavy Reading, a market research firm, data traffic volumes on some 3G mobile broadband networks are now increasing, year on year, by a factor of 10.

Flat-rate pricing is not the only reason for the mobile data explosion. Faster mobile networks have also been a major factor, serving to drastically reduce waiting times for downloading. Another is the growing popularity of attractive and advanced end-user devices in the shape of smartphones (such as Apple’s iPhone). USB dongles, devices that plug into laptops and can access data from mobile networks, have also been an ingredient in the data surge.

77%

of respondents agree that pricing mechanisms will play a more important role in mitigating future traffic management issues.

64%

agree that, in developing markets, the less complex the voice and data pricing plans, the better.

In association with

Economist Intelligence Unit

The
Economist

Freshfields'
perspective

‘Traditionally, operators’ competitive concerns tended to drive pricing strategies, but we now increasingly see pricing used as a tool to manage traffic and data consumption. We expect this approach will have an impact on a number of regulatory issues, such as net neutrality or wholesale regulation.’

Thomas Tschentscher
Partner, Freshfields

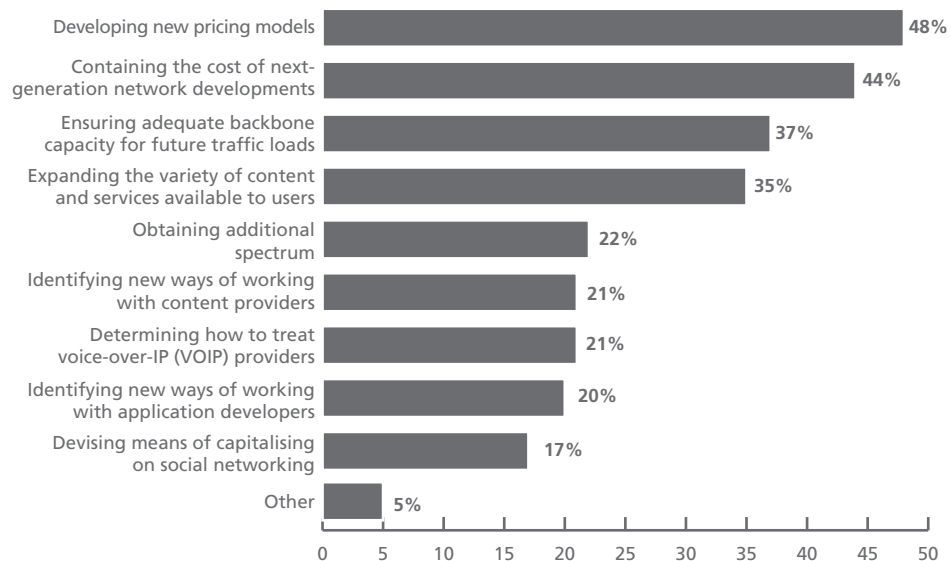
But what is good for the consumer is not always good for the operator. While flat-rate pricing has helped persuade customers to sign up to mobile data packages, many mobile operators are beginning to view flat-rate tariffs as having outlived their usefulness. The data traffic volumes have been a boon for network use – and revenue – but costs must be incurred to increase capacity. If operators do not make this investment to meet capacity demand, there is a danger that network performance may deteriorate.

Meanwhile, data retail prices have tumbled. When Vodafone first started offering flat-rate data deals in the UK in June 2007, pricing started at £7.50 per month for 120MB of data transfer (with additional charges for use above that limit). Through a mixture of competitive and regulatory pressures, Vodafone UK’s flat-rate 3G data deals now start at £15 for a monthly download limit of 5GB. This means that, in little more than three years, Vodafone has dropped its megabyte price two-hundredfold.

Will it all end in tiers?

If their networks are becoming overly congested, and the economics of delivering increasing amounts of data do not stack up, then operators need to find new pricing models that can alleviate the strain. One possible solution is to move away from all-you-can-eat and flat-rate tariffs (with generous usage caps) to a pricing scheme that more accurately reflects use. One is the so-called tiered-pricing approach: the more data the customer uses, the more he or she pays. This would have the advantage of curtailing the small minority of heavy users who chew up a disproportionate amount of the network’s capacity. According to Telefónica, a major mobile operator in Europe, 0.1 per cent

In your view, which of the following are the three most critical challenges facing mobile operators over the next three years?



Source: Economist Intelligence Unit survey, June 2010.

of customers use nearly 30 per cent of network capacity. Stefan Wiessmeier, senior vice president, strategy and development with Telekom Deutschland, the parent of T-Mobile, says that his company 'warmly welcomes the general market trend towards tiered pricing, especially as it ends cross-subsidisation of heavy users by medium and low-volume users'. (T-Mobile operators in the US, UK and Germany have recently announced the introduction of tiered data plans.) The danger of moving to tiered pricing is that it may hand over a competitive advantage to rivals that hold on to their all-you-can-eat deals, at least in terms of acquiring and retaining customers.

Mobile operators therefore have tough decisions to make on pricing strategies, but as yet there appears to be no clear consensus on the optimal route. In a recent survey of 391 international mobile industry executives conducted by the Economist Intelligence Unit, nearly half cite the development of new pricing models among the three most critical challenges operators will face over the coming three years. And although 55 per cent of all survey respondents agree that tiered pricing is the way forward in mature markets, that still leaves a sizeable minority who either have no strong views on this matter or even disagree. Moreover, 47 per cent of respondents say that all-you-can-eat data tariff plans are damaging operators' ability to increase revenue, but a larger percentage either disagree with this notion or remain neutral about it. This suggests that a good number of mobile operators are still reaping the benefits of this type of pricing when it comes to attracting new data customers.

You first: AT&T

One major operator that has decided to make the shift from all-you-can-eat to tiered pricing is AT&T, the first to do so in the US. Since June 2010, new AT&T smartphone users have no longer had access to unlimited data use, which had been priced at \$30 per month. Instead, there are cheaper monthly deals available with data use caps that, says AT&T, more accurately reflect customers' needs: \$15 for 200MB per month and \$25 for 2GB per month, with extra charges for customers who exceed those amounts. According to the operator, 98 per cent of its customers use, on average, less than 2GB of data per month and 65 per cent use less than 200MB.

'Our customers appreciate they now have a choice of data plans,' says Mark Siegel, executive director of media relations at AT&T. 'From the feedback we have had, the classic one-size-fits-all approach doesn't make sense any more.'

If what AT&T is saying is true in terms of customers' actual data needs, then the overwhelming majority of its smartphone customers will benefit from cheaper mobile data packages. 'The upside for us is that we should be able to persuade more customers to sign up to our mobile data packages, who may have balked previously at the \$30 price tag,' adds Mr Siegel. And with

Sweden: unlimited data v caps

Sweden has led the way in commercial services using next-generation long-term evolution (LTE) mobile technology. Launched in December 2009 by TeliaSonera, the largest fixed and mobile broadband provider in Sweden, the LTE network offers customers downlink speeds ranging between 10Mbps and 80Mbps. TeliaSonera has evolved its mobile data pricing from a single tariff of SEK599 per month, with a data cap of 30GB, to a range of tiered packages involving different combinations of data speeds and volume limits.

By contrast, two LTE competitors to TeliaSonera in Sweden – Tele2 and Telenor – have opted for unlimited data deals, both of which are cheaper than the top-end SEK599 tariff offered by their great rival. Using a shared network, they launched LTE in November, so they have substantial mobile broadband ground to make up and clearly feel that unlimited data is more effective at attracting customers than tiered pricing.

Tele2 and Telenor risk attracting a lot of very heavy data users. And unlimited data may not turn out to be an effective customer acquisition strategy if most users prefer the cheaper options that come with tiered pricing, even if it means accepting some constraints on speed and volume. How long Tele2 and Telenor persist with unlimited data will reveal how useful that pricing strategy really is.

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users of smartphones, which are much more data-friendly than ordinary mobile handsets, operators have greater potential to increase revenue from additional applications that are paid for on a per-download basis.

The big question is how comfortable customers are with restrictions placed on data use, even if most aren't affected by them in practice. AT&T does not disclose the number of previous smartphone users on the \$30 all-you-can-eat deal who have switched to one of the tiered pricing options, nor whether the rate of smartphone adoption has increased since June. Knowing this information would go a long way in helping operators in developed markets work out the pros and cons of tiered pricing.

But there are other factors at play in AT&T's decision to opt for tiered pricing (other than boosting the smartphone subscriber base). Mr Siegel reports that wireless data traffic volumes have increased by 5,000 per cent in three years in the US and that AT&T carries half that total today. 'No-one has had to face the challenges that we have had in handling in terms of wireless data,' asserts Mr Siegel. This may help explain why AT&T has suffered from a number of network outages in recent months. By applying the brakes on its very heavy data users through tiered pricing, AT&T can help keep the majority of its customers happier.

As mobile operators move to next-generation networks, the economics tilt more in favour of all-you-can-eat pricing, because the cost of providing much greater capacity is reduced. Operators that are holding back on tiered pricing today may well have that in mind.

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