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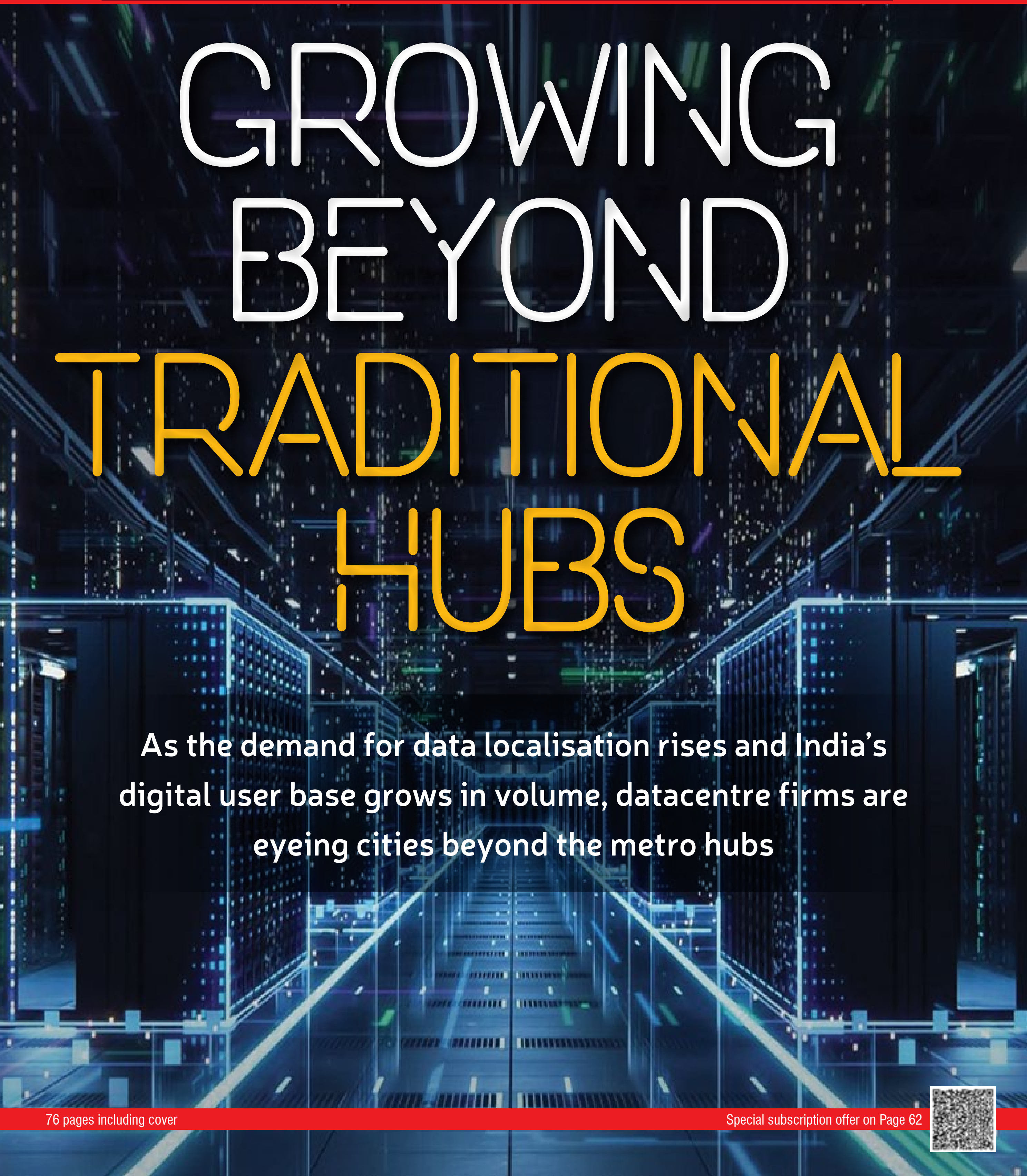


GROWING BEYOND TRADITIONAL HUBS

As the demand for data localisation rises and India's digital user base grows in volume, datacentre firms are eyeing cities beyond the metro hubs

Special subscription offer on Page 62

Two sides of the story

Their dispute over revenue split is a cliffhanger that continues season after season. A look at the issues at stake and possible happy endings

BY PRATIMA HARIGUNANI

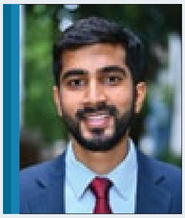
The debate between telecom companies and OTT players keeps brewing over and over. Even when data consumption is exploding – and will break the roof when 5G arrives. Telcos have, on some occasions, suggested a revenue-sharing model – something like a usage charge for the traffic that OTT players carry on the networks of telcos. Their argument is simple: You generate this money because of the networks we have built, so we deserve a slice. After all, the 'same service, same rules' model applies when OTT platforms also allow a bundle of services, such as voice calling, video calling and communication avenues. But only telcos bear the weight of fees, licences, and other infrastructure investments.

Things are not that simple. Walk a bit to the other side and the argument made by OTT players holds some water too. If it were not for what OTT platforms offer, telcos would not enjoy all the sky-kissing data consumption that they see now.

Quite a conundrum. But one that telcos cannot put on the back-burner for long, especially when their average revenue per user (ARPU) has been suffering a lot of pressure in recent times. All the ARPUs have shown a dip between the June 2013 quarter and the December 2022 quarter, as per the TRAI paper. ARPU rose only about 41%, from Rs 123.77 to Rs 146.96, during that period. The share of revenue calls also slipped to Rs 14.79 or 10.1% in ARPU of Rs 146.96, from Rs 72.53 or 58.6% in that period. Not just that, revenue share from SMS declined from Rs 3.99 or 3.22% of ARPU to 23 paise or 20%.

IN THE PREVIOUS SEASON

Let us first understand the two sides with more clarity on where they are coming from.As Sudhir Kunder,



> "The regulations must be based on the nature of functions performed and services provided. A square peg in a round hole will stifle innovation."

Purushotham Kittane
Technology Lawyer, Nishith Desai Associates

Country Director, DE-CIX India, dissects it, the discourse surrounding the request made by telcos for tech players to bear a portion of the expenses related to content delivery and data is multifaceted, encompassing issues of net neutrality, equitable competition, and the sharing of costs.

These discussions have been brought into the mainstream discourse for several years now, observes PurushothamKittane, Technology Lawyer, Nishith Desai Associates. "TRAI had as early as 2015 considered in a consultation paper whether to regulate OTT services within a licensing framework. While the discourse then was a carriage vs. content debate, it is now a debate of OTT apps replacing functionalities of traditional telecom services. The telecom industry's case is that it is already affected, taking a hit in revenues over the years while still paying licence fees, which the OTT players donot. The OTT industry feels a licensing framework is unfair as they should not pay licence fees for infrastructure the telecom service provider operates."

Advocates of telcos charging tech players for content delivery and data argue that telcos invest significant resources in building and maintaining the communication infrastructure, such as fibre optic cables, cell towers, and datacentres, explains Nitin Singhal, Managing Director, Sinch India. "They argue that tech players benefit from using these well-established networks and should contribute to their upkeep. Also, data-heavy content and services from tech players can contribute to network congestion. By charging tech players, telcos can manage network traffic and ensure quality of service for all users."

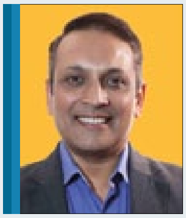
There is more to the story. This issue is quite fragile given its natural collision with the net neutrality debate as well.

"Charging tech players can also prevent an unfair advantage for large content providers, ensuring smaller content providers can compete on an equal footing. On the other hand, charging tech players for content delivery and data could violate the principles of net neutrality, which advocates for equal treatment of all Internet traffic. Net neutrality argues that ISPs should not discriminate against different types of data or content providers," Singhal reasons.

Sourav Gupta, Telecom Analyst at Omdia, says that it will be an ongoing competition until the regulator of

THE TELCO POV

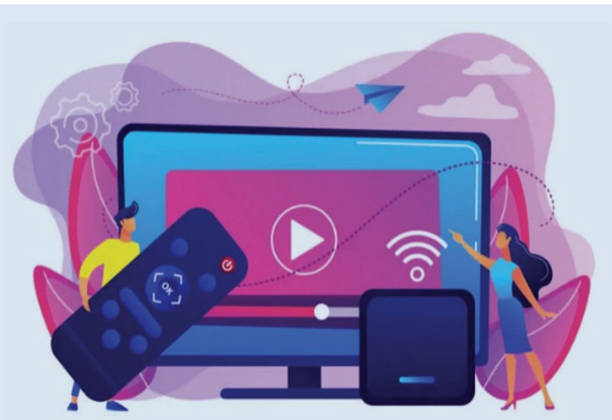
- Telcos invested heavily in network infrastructure
- They argue OTT platforms benefit from this infrastructure
- Telcos seek a share of OTT revenues as compensation
- Declining ARPU adds urgency to revenue-sharing demands
- Telcos aim to manage network congestion and ensure quality
- Potential benefits include fair competition and network sustainability



"Charging tech players can also prevent an unfair advantage for large content providers, ensuring smaller content providers can compete on an equal footing."

Nitin Singhal
Managing Director, Sinch India

the country steps in with any kind of regulations for the OTT players. "Currently in India, TRAI is working on the consultation process and carrying out comparative studies on how OTTs are regulated in other countries. One of the models being discussed is a revenue-sharing mechanism between OTTs and telcos. Video consumption comprises 70% of the overall traffic flow on telecom networks, and this would grow further with 5G services. Similarly, telcos would have to increase their spending on carriage capacity and backhaul networks, which entails investments."



THE OTT STORY

- OTT platforms claim they've driven telco data consumption
- They argue licensing fees for infrastructure are unfair
- Concerns about violating net neutrality principles
- Worries about increased costs for consumers
- Fear of stifling innovation and smaller player entry
- Belief in a symbiotic relationship with telcos

The Cellular Operators Association of India (COAI) had suggested levying a usage charge for actual traffic carried by OTT on telecom networks. The usage charge would be a mutual decision between OTT players and telecom service providers. Furthermore, OTT players must contribute towards developing and creating digital telecom infrastructure in India in exchange for using the services.

Telcos already charge their customers for data usage and Internet access, experts note. Adding charges to tech players might increase costs for consumers, leading to potential backlash and dissatisfaction. Imposing fees on tech players could also stifle innovation and limit the entry of new smaller players into the market. Tech players also bring value to telcos by driving demand for high-speed Internet and data services. A symbiotic relationship exists, where both parties benefit from each other's offerings.

Roslyn Layton, VP Roslyn Layton, Strand Consult, brings an avid gaze about the importance of broadband to transform India's economy, drive its IT industry and enable leadership. She has worked for TCS Innovation Labs Hyderabad and attests to the gravity of this whole debate. "Globally, there is a USD 2 trillion shortfall in broadband network investment. Over half of the world is offline for the reasons of lack of affordability. The UN Broadband Commission recognised in 2021 that the largest global OTTs need to be incorporated financially into business models for network rollout to the end user ina rational, predictable, transparent, and sustainable way. Finding solutions for India is worth tens of millions of dollars and will help millions of people get online."

Layton also tries to bring some attention back to the arguments that Big Tech uses globally to say that these models are "harmful". "Alphabet, Amazon, Meta, Netflix, Apple and others organise collectively to lobby against governments' exploration of these models. They use reports by Analysys Mason and the lobbying arm of the CCIA and Incompas. However, Strand Consult has debunked these reports and arguments. The UN also

"TRAI is working on the consultation process and carrying out comparative studies on how OTTs are regulated in other countries."

Sourav Gupta
Telecom Analyst, Omdia

rejects these views. In the USA, Commissioner Brendan Carr of the Federal Communications Commission has called for ending Big Tech's Free Ride. Moreover, there is bipartisan support in the US Congress to bring OTTs into a cost recovery scheme."

The debate has no relationship to net neutrality, according to Layton. "Net neutrality is about the broadband provider and the end user. Cost recovery is about the broadband provider and the OTT. Under this scheme, there is no blocking, throttling or prioritisation of traffic. Cost recovery enables the free and open Internet because it reduces the cost burden on consumers and makes networks more affordable and accessible."

She further adds that the country with the most robust regime, South Korea, is rated the world's top broadband market for the highest percentage of next-generation rollout of broadband (fibre and 5G). "South Korea is the world's seventh-largest content producer and competes globally with its OTTs. Moreover, Google and Netflix booked record profits in South Korea at the same time as they paid network usage fees. Simply put, if you have faster networks, there are more opportunities to show ads and sell movies."

VIEW FROM THE OTHER SCREEN

While telcos have a lot of reasons to worry about the way the cake is cut now, there are many reasons that OTT and Big Tech players also insist on. Like how they help telcos in cost recovery or increased data demand or how the models they suggest are fair and square.

Interestingly, the Strand Consult'snew report 'Fact Check on Analysys Mason's Claims on Big Tech Investments and Arguments against Broadband Cost Recovery' reviews the claims made by Analysys Mason in its 2022 report, 'The impact of tech companies' network investment on the economics of broadband ISPs'.Ask Layton about how Analysys Mason's claims about the level of Internet infrastructure investment by edge providers appear credible and consistent with the size and scale of the leading Internet giants (called "edge providers" in the US parlance), and she talks of how these numbers come from that agency's calculations.

"Moreover, the type, purpose, level, regulatory treatment and location of the infrastructure investments in the comparisons do not cohere. Plus, these investments largely reflect the requirements and profit-driven decisions of edge providers for their businesses and 'direct investment in their infrastructure'. By contrast, broadband providers as a class invest far more in the Internet infrastructure to connect end users to the Internet than both in nominal amounts and as a percentage of their revenue, compared to Analysys Mason's figures of edge providers. The investment by Internet giants on infrastructure amounts to 1% of their revenue."

Parveen Mittal, Vice President and General Manager, Celigo, reflects on how telcos, especially in Europe, are lobbying with regulators to get a policy that makes Internet companies, including social media which send traffic over their networks, pay for the infrastructure used.

"Telcos are spending billions on laying cables and installing towers to meet increasing data demand necessitated by increasing consumption of online content. Telcos reason that if Google and Apple can charge a cut of sales in their app stores, why can telecom service providers get a similar cut? Tech players reason that any service-provider-specific payment affects net neutrality and, in any case, telcos get paid by the customer for the data services used."

However, given that tech companies have benefitted disproportionately from the increased data usage, as is evident in the relative market capitalisation of tech companies and telcos, a strong case can be made for the former to pay for the traffic generated, Mittal reasons. "Even in India, social media, e-commerce and fintech companies are much higher valued than telcos."

Listen to how Layton slices the problem. “Strand Consult’s microeconomic analysis of 50 rural US FTTH providers demonstrates that broadband providers have increasing costs from growing video streaming entertainment traffic. Not only can rural broadband providers not recover costs, but they have no data exchange relationships with Big Tech giants anyway, and their attempts to negotiate fall on deaf ears. Few, if any, broadband providers have been able to raise prices meaningfully in the face of growing costs.”

She strongly reckons that even if policymakers believe that Big Tech has no obligation to pay or negotiate for the use of broadband providers’ networks (as Netflix has argued in a South Korean court), there is still a valid case for Internet giants to support universal service obligations and affordable connectivity programs which provide vouchers and broadband subsidies directly to end users. “If Big Tech wants accolades as infrastructure providers, they should also shoulder the burdens.”

The challenge is that the “pipes” are priced uniformly for end users (this makes them more expensive for the poor), but the usage of the pipes is highly disproportionally consumed by video and advertising data, Layton adds. “Moreover, the social and private values of the services are not equal. Hence the pricing model needs to evolve. There are also issues of competition, regulation, and market entry for services which are presently dominated by platforms.”

SOLVING THE STALEMATE

- Universal fixed fee
- Revenue sharing
- Market-based cost recovery
- Telcos with their content bundles
- OTT with their infrastructure
- Telcos as resellers of OTT bundles
- Telcos using content as an acquisition tool
- Telcos adopting MVNO and asset-light models
- Telcos-OTT partnership for a win-win business

SKIP THE ‘POPCORN SCENE’ PLEASE

Answers have to come. And they can have a different narrative than the one we are used to.

Layton offers some solution ideas. “Broadband cost recovery is the process to enable design and implementation of these models with the following steps: accounting, accessibility, affordability, augmentation. There are at least five models of broadband cost recovery: market-based (e.g., usage fees in South Korea), regulated (the proposed Universal Service Fee as in the USA, the existing Affordable Connectivity Program), technological (e.g., multicasting), philanthropic (grants, donations) and financial (bank loans). The upside for society is to make broadband networks more affordable and available with contributions from OTTs whether to governments, clearing houses, operators, end users or other actors. Significantly, we can also see how Australia and Canada have proceeded with a News Media Bargaining Code and received some AUD 200 million in fees for Google and Facebook. This covers 20% of journalists’ salaries in Australia.”

Many alternatives are possible. What is important to remember is that achieving a harmonious equilibrium that is mutually advantageous to all parties involved and guarantees the long-term viability of the ecosystem will be of utmost importance, Kunder stresses. “The establishment of open and transparent communication channels, as well as the engagement in negotiations characterised by transparency, are of utmost importance to identify mutually advantageous resolutions that facilitate the expansion of digital services, while simultaneously upholding a just and equitable environment for all parties involved.”

According to Gupta, plausible solutions include telcos bundling their services with OTT, telcos developing their own OTT platforms, and telcos just partnering with established and highly demanded OTT platforms having

"If Big Tech wants accolades as infrastructure providers, they should also shoulder the burdens."

Roslyn Layton

VP Roslyn Layton, Strand Consult

a good customer base. Telcos would be able to make profits from the heavy traffic such OTT platforms attract and may do so by improvising the broadband package plans for customers.

Telcos should, of course, be seeking tech companies to share some revenue with them for content and data delivery. However, the question of whether telcos should ask tech players to pay some of the cost of content delivery and data is a complex and debated issue. Different stakeholders hold various perspectives on this matter, and the answer depends on the specific context, regulations, and market dynamics.

In Kittane's opinion, there is a middle ground although it is industry-led and not regulator-led. "The ITU had suggested in 2020 that OTT providers could enter into voluntary commercial arrangements with telecom service providers. These arrangements can allow OTT providers to invest in Internet infrastructure without falling under the licensing requirement."

It is interesting how this issue could impact branding and advertising, notes Gaurav Gulati, a seasoned advertising expert and branding consultant.

"This partnership could change how companies talk about themselves and their ads. For example, they might say, 'We work together to make your videos load faster and your apps work better.' This could show how they are a strong team, focusing on a better experience for you."

But if this model becomes a reality, Gulati cautions that tech companies might need to change their branding strategies to highlight their value to users and telcos. "They could emphasise how their services contribute positively to the network ecosystem and user experience. Just as a McDonald's burger finds its perfect companion in a refreshing Coke, the Netflix experience shines with Vodafone. Telecom and tech unite, spotlighting mutual strengths."

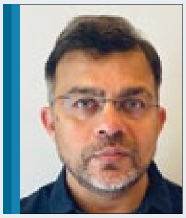
Layton discounts the question that this debate might not matter five years from now, when hyperscalers, satellite Internet, decentralised networks and so on might have become a reality. "Yes, it will matter." She maintains her concerns. "India must still evolve from 2G to 5G. Today there is limited revenue to make those infrastructure investments. Many locations in India will also roll out fibre. Those networks will not be built if it is expected that 100% be covered by end users. OTTs which get the benefit of the networks must also contribute to the building of the networks to the end users. Satellite Internet also faces the same cost challenges and will want to access cost recovery models."

As for software-definednetworks and so forth, she remarks that these are not one-to-one substitutes for hardware: the actual servers, routers, wires, base stations, towers, antennas and so on are needed to deliver data. That is, software only comes into play once the 5G network is installed. There is no shortcut for the purchase of spectrum licences, towers and base stations.

Eventually, the decision to charge tech players for content delivery and data is a policy matter that involves balancing the interests of various stakeholders, Singhal sums up. "Governments and regulatory bodies often play a role in determining the rules and regulations on these types of practices to ensure a fair and competitive digital ecosystem."

Kittane agrees, and adds, "Ultimately, consumer demand gives direction to how either of these service providers function and the regulations also should evolve keeping that in mind. These regulations must be based on the nature of functions performed and services provided. A square peg in a round hole will stifle innovation."

He has a word of advice for telcos too. "They are into enabling voice and data requirement of the businesses and users and telcos need to clear their positioning in the market. They need to focus more to improve on user



"Telcos need to continuously educate consumers as well as regulatory bodies and policymakers to build their case."

Parveen Mittal

Vice President & General Manager, Celigo

experience by providing best-in-class networks for each user at every location in the country. This will increase their pie chart on usage of the network and can have more innovative commercialmodels basis the same. We should not try to take share from the content producer and go on the path of impacting the creativity."

Indeed. This debate is not a negotiation table-stop but a wake-up call for telcos to make that big 'pivot'. According to a report by Straits Research, the global OTT market size was at USD 276.02 billion in 2021 and would be USD 2838 billion by 2030, with Asia Pacific as the fastest-growing market. It is time for telcos to look beyond low-hanging fruits. A 2022 KPMG report, titled 'Future of Telco', pointed out that when we look at the factors that have the greatest potential to change the landscape for the telecommunications industry, we see the development of revenue-generating solutions that exceed the cost of network upgrades at the top (29%) followed by funding for network upgrades and modernisation (at 23%).

Telcos that can flip the script would be the ones to enjoy a new negotiation advantage at the tables that will emerge in future.

The KPMG report also showed that compared with followers, future-focused telcos are 2.5x more likely to develop compelling customer value propositions on price, products and services to engage some of the most attractive customers and drive profitable growth. They are also 3.1x more likely to engage, integrate and manage third parties to help increase speed-to-market, reduce costs, mitigate risk and close capability gaps to deliver on the customer promise. And 4x more likely to harness data, advanced analytics and actionable insights with a real-time understanding of the customer and the business to shape integrated business decisions.

The report also explains how today's market conditions are creating challenging times for telco players. It states – Traditionally, telcos have made their money by moving bits through the air and across wires in their networks. And while doing so is still central to their mission, telcos need to figure out ways to diversify and make their businesses more profitable, because continually investing in infrastructure can limit profitability.

Meanwhile, the OTT revenue dead-end can, hopefully, be addressed through a regulatory GPS. And if not, telcos can find a new and bigger highway they would not have to fight upon.

"I believe that it is finally a policy decision to find a fair and balanced approach that is essential to ensure a sustainable and equitable Internet ecosystem," Mittal says. "Telcos need to continuously educate consumers as well as regulatory bodies and policymakers to build their case."

Regulatory consultation papers have been in progress, not just in India but in a global arena like GSMA and EU too, but we need more clarity and more action – and sooner rather than later.

Gupta surmises that the OTT-telco revenue debate will not end till the telecom watchdog comes up with any regulation model for OTTs or a revision in tariffs is made.

Overall, as Gulati sees it, the telco-OTT debate can shape branding and advertising strategies by fostering collaboration between telecom and tech companies. "This collaborative approach could emphasise the mutual value they bring to each other's services, highlighting telecom companies as reliable content delivery platforms and tech companies as innovative creators. Additionally, it could lead to campaigns emphasising enhanced user experiences, innovations resulting from collaboration, transparency in cost-sharing and data usage and alignment with privacy-focused messaging to build consumer trust."

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