JOINT ACQUISITION BY PHILIPPINE LONG DISTANCE TELEPHONE COMPANY AND GLOBE TELECOM, INC. OF VEGA TELECOM, INC., BOW ARKEN HOLDING COMPANY, INC. AND BRIGHTSHARE HOLDINGS CORPORATION
M-037/2016

Preliminary Statement of Concerns

25 August 2016

A. The Reference

1. On 8 July 2016, the Philippine Competition Commission ("Commission"), in exercise of its mandate under Section 12, 16 and 20 of Republic Act No. 10667, otherwise known as the Philippine Competition Act ("Act"), and Rule 5, Section 1 of the Rules and Regulations to Implement the Provisions of the Act ("IRR"), referred the joint acquisition by Philippine Long Distance Telephone Company ("PLDT") and Globe Telecom, Inc. ("Globe") of Vega Telecom, Inc. ("Vega") [the "Acquisition"], to the Mergers and Acquisitions Office ("MAO") for review and report to the Commission.

2. The MAO must determine whether the Acquisition may be expected to substantially prevent, restrict or lessen competition ("SLC") within any market or markets in the Philippines for goods or services.[1]

3. In this preliminary statement of concerns, we set out the main issues likely to be considered in our decision, having regard to the evidence gathered to date. This does not preclude consideration of other issues that may be further identified during the course of our review.

B. Background

B.1. The Parties

Philippine Long Distance Telephone Company

4. PLDT is one of the two largest telecommunications service providers in the Philippines. It offers a diversified range of telecommunications services including mobile, fixed broadband and fixed voice telecommunications and other value-added telecommunications services. It also operates the country's most extensive wired and wireless networks.

[1] *See* Section 20 of the Act; Rule 5, Section 1 of the IRR.

5. The company's principal shareholders are PCD Nominee Corporation, JP Morgan Hongkong Nominees Limited, Philippine Telecommunications Investment Corp., NTT DOCOMO, Inc., Metro Pacific Resources, Inc., and JG Summit Holdings, Inc.

6. PLDT's subsidiaries include Smart Communications, Inc. (“Smart”), ePLDT, Inc., Digital Telecommunications Phils., Inc. (“Digitel”), which PLDT acquired in 2011, and several other businesses that provide value-added telecommunications services.

7. PLDT offers its mobile telecommunications services through Smart, under the brands Smart and Talk 'n Text, as well as Digitel, under the brand Sun Cellular. PLDT itself offers fixed broadband and fixed voice telecommunications services.

8. The PLDT Group posted total revenues of Php171.1 billion for the year ended December 31, 2015.

Globe Telecom, Inc.

9. Globe Telecom, Inc. is one of the two largest telecommunications service providers in the Philippines. It offers a wide range of telecommunications services including mobile, fixed broadband and fixed voice telecommunications, and other value-added telecommunications services. It also operates its own wired and wireless networks.

10. The company's major shareholders are Singapore Telecom International Pte. Ltd., Ayala Corporation, and PCD Nominee Corporation.

11. Globe's subsidiaries include GTI Business Holdings, Inc., Innove Communications, Inc. (“Innove”), and Bayan Telecommunications, Inc. (“Bayantel”). Bayantel’s 98.26% shares was acquired by Globe in 2015.

12. Both Innove and Bayantel offer fixed broadband and fixed voice telecommunications services. Globe itself offers mobile telecommunications services under the brands Globe Postpaid, Globe Prepaid, and TM.

13. The Globe Group posted total revenues of Php120.0 billion for the year ended December 31, 2015.

Vega Telecom, Inc.

14. Vega Telecom, Inc. (“VTI”) is a telecommunications holding company with a franchise to engage in mobile, fixed voice, and fixed broadband telecommunications services.

15. VTI is a wholly-owned subsidiary of San Miguel Corp. (“SMC”). Its subsidiaries include Liberty Telecom Holdings, Inc. (“Liberty”), Bell Telecommunication Phils. Inc. (“BellTel”), and Eastern Telecommunications Philippines, Inc. (“ETPI”). ETPI offers enterprise-quality fixed voice and fixed broadband services in certain areas of the

country while BellTel is the holder of assigned frequency rights which allow it to offer mobile telecommunications services.

16. BellTel has no substantial revenue-generating commercial operations while ETPI reported total operating revenues of Php1.6 billion for the year ended December 31, 2015.[2]

Bow Arken Holding Company, Inc.

17. Bow Arken Holding Company, Inc. is a telecommunications holding company wholly-owned by Schutzengel Telecom, Inc. The company owns 99.6% of New Century Telecoms, Inc. which holds the right to operate 20 MHz of mobile telecommunications frequencies in the 700 MHz band. Based on publicly available information, New Century Telecoms, Inc. has no recorded commercial operation that generated substantial revenues, with only Php114,193.00 reported gross revenues for the year ended December 31, 2015.[3]

Brightshare Holdings Corporation

18. Brightshare Holdings Corporation is a telecommunications holding company wholly-owned by Grace Patricia W. Vilchez-Custodio. The company has only one subsidiary, eTELCO, Inc., which holds the rights to operate 15 MHz of mobile telecommunications frequencies in the 2500 MHz band. Based on publicly available information, eTELCO, Inc. has no recorded commercial operations that generated substantial revenues, with only Php177,932.00 reported gross revenues for the year ended December 31, 2015.[4]

B.2. The Transaction

19. On 30 May 2016, PLDT and Globe executed an agreement to jointly acquire SMC's telecommunications-related subsidiaries under VTI on a 50-50 basis. PLDT and Globe also entered into an agreement to jointly acquire on a 50-50 basis Bow Arken and Brightshare (collectively, the "Transaction"). These companies own telecommunications assets such as cell towers and radio antennas, franchises and the rights to use various radio frequencies. The total value of the Transaction is Php70 billion, split evenly between PLDT and Globe.

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[2] 2015 Annual Report of Bell Telecommunication Phils., Inc. and Eastern Telecommunications Philippines, Inc. submitted to the National Telecommunications Commission.

[3] 2015 Annual Report of New Century Telecoms, Inc. submitted to the National Telecommunications Commission.

[4] 2015 Annual Report of eTELCO, Inc. submitted to the National Telecommunications Commission.

20. Upon consummation of the Transaction, PLDT and Globe acquired control of VTI, Bow Arken and Brightshare, giving PLDT and Globe ownership of the above firms and their subsidiaries.

21. As of date, PLDT Regulatory Affairs and Policies Head Ray Espinosa and Globe Senior Vice President Gilbert Simpao have been elected as Co-Chairmen and Co-Presidents of Liberty, a VTI subsidiary, at the 18 August 2016 annual stockholders meeting of said company.[5] Liberty's new board of directors include PLDT Chief Finance Officer Anabelle Chua, PLDT Executive Vice President Ernesto Alberto, Globe Vice President Jan Lester Olaño and Globe shareholder Ramon Nonato C. Aesquivel, Jr.[6] Shortly thereafter, on 24 August 2016, Liberty submitted its Petition for Voluntary Delisting of Liberty's common shares from the Philippine Stock Exchange.[7]

C. Market Definition

22. The Transaction presents several horizontal and vertical overlaps in several markets. The MAO has focused its preliminary investigation and review on the following markets: (a) retail supply of mobile services; (b) retail supply of fixed broadband services; (c) retail supply of fixed voice services; (d) wholesale supply of mobile services; and (e) wholesale supply of fixed broadband services.

23. Based on the available information to the MAO, it finds that the above mentioned are the affected markets. However, this does not preclude the MAO from identifying other affected markets following the receipt of additional information.

C.1. Retail Supply of Mobile Services

C.1.1. Product scope

24. Retail supply of mobile telecommunications services refers to the provision of mobile telecommunication services to end-consumers. It includes services for national and international voice calls; short message service ("SMS"), including multimedia messaging service ("MMS") and other messages; mobile internet data services; and international roaming services.

25. For the purpose of the PSOC, the MAO did not further subdivide the market for the provision of mobile telecommunications services. It notes, however, that the following segmentations may also be relevant for the competitive assessment: (a) by

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[5] Liberty Telecoms Holdings, Inc. PSE Disclosure Form 4-24-Results of Annual or Special Stockholders' Meeting, available at http://edge.pse.com.ph/companyDisclosures/form.do?cmpy_id=27#viewer

[6] PLDT's SEC Form No. 17-A, Annual Report for 2015; Globe SEC Form No. 17-A, Annual Report for 2015.

[7] Letter dated 24 August 2016 from Liberty Telecoms Holdings, Inc. to the Philippine Stock Exchange.

customer (corporate or private); (b) by plan (prepaid or postpaid); and (c) by technology (2G, 3G and 4G).

C.1.2. Geographic scope

26. The MAO currently holds that the relevant geographic market for retail mobile services is national in scope. The MAO will also consider smaller geographic markets if necessary.

C.2. Retail Supply of Fixed Broadband Services

C.2.1. Product scope

27. Fixed broadband services consist of the provision of a fixed telecommunications link to the internet.

28. For the purpose of the PSOC, the MAO did not further subdivide the market for the provision of retail fixed broadband services. It notes, however, that it may be necessary to further divide the market into, e.g., enterprise and residential customers.

C.2.2. Geographic scope

29. The MAO currently holds that the relevant geographic market for retail fixed broadband services is national in scope. The MAO will also consider smaller geographic markets if necessary.

C.3. Retail Supply of Fixed Voice Services

C.3.1. Product scope

30. Fixed voice services provide consumers with access to the public switched telephone network for the transmission and switching of voice, data, and video where the call is made from a fixed customer location.

31. For the purpose of the PSOC, the MAO did not further subdivide the market for the provision of retail fixed voice services. It notes, however, that it may be necessary to further divide the market into, e.g., enterprise and residential customers.

C.3.2. Geographic scope

32. The MAO currently holds that the relevant geographic market for retail fixed voice services is national in scope. The MAO will also consider smaller geographic markets if necessary.

C.4. Wholesale Supply of Mobile Services

C.4.1. Product scope

33. Wholesale mobile services provide a customer access to a mobile network operator's ("MNOs") radio access network ("RAN"), which in turn allows the customer to provide retail mobile telecommunications services to end-users. An example of this is a mobile virtual network operator ("MVNO") arrangement.

C.4.2. Geographic scope

34. The MAO currently holds that the relevant geographic market for wholesale mobile services is national in scope. The MAO will also consider smaller geographic markets if necessary.

C.5. Wholesale Supply of Fixed Broadband Services

C.5.1. Product scope

35. Wholesale fixed broadband services cover different types of access that allow internet service providers ("ISPs") to provide services to end-consumers. It includes physical access at a fixed location, such as local loop unbundling ("LLU"); non-physical or virtual network access, such as bitstream access; and the resale of a fixed incumbent's internet offering.

C.5.2. Geographic scope

36. The MAO currently holds that the relevant geographic market for wholesale fixed broadband services is national in scope. The MAO will also consider smaller geographic markets if necessary.

D. Counterfactual

37. The MAO will assess the effect of the Transaction on competition relative to the situation that would prevail prior to the Transaction (i.e., the counterfactual). The counterfactual guides the MAO's analysis in establishing whether the Transaction will lead to an SLC.

38. While there exist several possible scenarios, the MAO ultimately uses as counterfactual that which is the most likely scenario absent the Transaction, based on the facts available to the MAO.

39. In establishing the most likely scenario absent the Transaction, the MAO has opted not to make any assumptions on who will operate or end up controlling VTI, Bow Arken, and Brightshare or their existing assets. It may be the case that VTI, Bow

Arken and Brightshare may be sold to another third party, other than the incumbents.

40. In this regard, the MAO determines that the most likely scenario is the prevailing conditions of competition prior to the Transaction. It is therefore critical to examine the market conditions leading up to the Transaction to properly define said status quo.

41. First, the MAO notes that SMC positioned itself as the third player, challenger, and threat to the incumbents in the telecommunications industry. SMC had plans to enter the telecommunications industry as early as 2009 when it acquired thirty-three percent (33%) of the outstanding capital stock of Liberty, and subsequently acquired BellTel in 2010. It subsequently invested in more telecommunication assets and brought in consultants from Telstra Corp., Ltd. ("Telstra") on board to assist in rolling out the network. Entry plans intensified in 2015 as talks of a partnership with Telstra emerged.[8] This was confirmed by SMC with the Philippine Stock Exchange on 1 September 2015[9]. SMC set out a target launch date within 2016.

42. Second, the MAO considers the likelihood of VTI to enter and compete in the market. As early as July 2015, VTI acquired the entire interest and participation of Qtel West Bay Holdings S. P. C., Wi-tribe Asia Limited, and White Dawn Solution Holdings, Inc. in Liberty, and acquired Express Telecommunications, Inc. and High Frequency Telecommunications, Inc.[10] The MAO finds that all SMC telecommunication assets were consolidated under VTI including spectrum rights, network infrastructure, and network backbone. Moreover, the cumulative assets under VTI would allow its owner, whether SMC or another third party, the capability to enter and compete in the telecommunications industry.

43. Third, the MAO took into account the timeliness of VTI's entry in considering it as a credible threat to the incumbents. It finds that VTI was poised to launch its mobile business under the brand Bell Telecommunications sometime between the second and fourth quarter of 2016.

44. Therefore, the MAO determines that the counterfactual is a situation where VTI's presence and entry into the market(s) are likely to have an impact on competition in a timely and substantial manner. Actual and potential competition exist through the competitive constraint that VTI's mere presence imposes on the market.

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8 Transcript from Investor Day, 29 October 2015, available at http://www.asx.com.au/asxpdf/20151030/pdf/432m56r1z2jbyg.pdf

9 PSE Disclosure Form 4-13 - Clarification of News Reports

10 San Miguel Corporation ("SMC") Letter dated 16 July 2015 to the Philippine Stock Exchange relating to the acquisition by VTI of Liberty shares; SMC Letter dated 15 July 2015 to the Philippine Stock Exchange relating to the acquisition by VTI of Express Telecommunications, Inc. and High Frequency Telecommunications, Inc.; PSE Disclosure Form 4-2 - Acquisition/Disposition of Shares of Another Corporation by SMC; Sale and Purchase Agreement dated 30 May 2016.

E. Theories of Harm

45. A key consideration in the MAO's assessment of the Transaction is the potential harm it may inflict on the market due to a substantial prevention, restriction or lessening of competition. The theories of harm detail the possible ways in which these may arise relative to the counterfactual and provide the framework for the analysis of the competitive effects of the transaction. The MAO has identified at least seven (7) theories of harm that it intends to investigate further, which will be discussed in more detail below:

    a) Unilateral effects from loss of potential competition in the retail supply of mobile services;

    b) Dynamic loss of competition in the retail supply of mobile services;

    c) Unilateral effects from loss of existing and potential competition in the retail supply of fixed broadband services;

    d) Unilateral effects from loss of existing and potential competition in the retail supply of fixed voices services;

    e) Input foreclosure in the wholesale supply of mobile services;

    f) Input foreclosure in the wholesale supply of fixed broadband services; and

    g) Coordinated effects in the supply of telecommunications services.

46. However, the MAO may revise its theories of harm as the inquiry progresses. The identification of a theory of harm does not preclude another being identified following further work done or the receipt of additional evidence.

E.1. Retail Supply of Mobile Services

E.1.1. Unilateral effects from loss of potential competition

47. The concern under this theory of harm is that the Transaction would remove the constraint on PLDT and Globe that VTI would have exercised in the counterfactual. The loss of VTI as a competitive constraint could allow PLDT and Globe to raise prices, reduce quality or innovation in the retail mobile service market, relative to the counterfactual.

48. The Transaction effectively terminates VTI's potential as a third major player in the mobile market along with the potential competitive constraint it can impose on the incumbents. The MAO has found evidence to indicate that VTI was ready to launch BellTel's services within the National Capital Region ("NCR") by the end of 2016. The acquisition eliminates it as a credible threat to the incumbents along with its promise of delivering improvements in service quality.

49. Potential competition is beneficial to the public because it prevents the incumbents from abusing its market power. The threat of entry may sometimes be enough to encourage incumbents to offer prices and quality as if there were an actual additional player.

50. Potential competition creates a momentum for the market players to invest, innovate and improve service quality, as well as exerts a downward pressure on prices so that they can maintain or capture the market. The departure of VTI nullifies these beneficial effects and preserves the sub-optimal market inertia set by the incumbents.

51. The MAO has found strong evidence to support the notion that VTI is a credible threat and has potential to affect competition in a significant way. VTI has (a) substantial spectrum holdings; (b) access to ETPI's backbone; (c) surmounted the major barriers to entry; and (d) amassed the required radio access network to operate in NCR.

52. Due to these attributes, VTI stands out as a strong potential competitor in the market. Initial evidence suggests that even as a new entrant, VTI has the potential to be a disruptive competitive force and may be regarded as a maverick firm.

53. Accordingly, the MAO currently believes that the transaction may raise significant competition concerns due to unilateral effects in the retail mobile telecommunications market.

E.1.2. Dynamic loss of competition

54. The concern under this theory of harm is that the Transaction will weaken any potential competitors to PLDT and Globe such that they will impose less competitive constraints than they would have done in the counterfactual. The MAO has considered whether the Transaction will result in either or both PLDT and Globe having substantial advantages such that it will not be possible for other operators to match and effectively compete with the incumbent firms. This may then allow PLDT and Globe to set higher prices or lower quality in the medium to long term.

55. The MAO identifies two potential advantages that accrue in favor of the incumbents as a result of the Transaction: (a) the amount and type of spectrum that will be held by PLDT and Globe; and (b) PLDT and Globe's ownership of VTI's telecommunications infrastructure and facilities.

56. Spectrum is an essential input in mobile telecommunications. The amount of spectrum rights held by a firm dictate the number of subscribers it can sustain, as well as the quality of service it can provide. The pre- and post-transaction spectrum holdings of the Parties are set out in Tables 1 and 2.

Table 1. Pre-Transaction Spectrum Holdings

	700 MHz FDD	850 MHz FDD	900 MHz FDD	1800 MHz FDD	2100 MHz FDD	2300 MHz TDD	2500 MHz TDD	3500 MHz TDD	Total
PLDT	-	20	15	75	50	30	35	60	**285**
Globe	-	-	35	45	20	-	50	60	**210**
Vega	70	10	20	30	-	30	80	40	**280**
Brightshare	-	-	-	-	-	30	15	-	**45**
Bow Arken	20	-	-	-	-	-	-	-	**20**
Others	-	-	-	-	-	-	-	40	**40**
Vacant	-	-	-	-	50	-	5	-	**55**
Total	**90**	**30**	**70**	**150**	**120**	**90**	**185**	**200**	**935**

Table 2. Post-Transaction Spectrum Holdings

	700 MHz FDD	850 MHz FDD	900 MHz FDD	1800 MHz FDD	2100 MHz FDD	2300 MHz TDD	2500 MHz TDD	3500 MHz TDD	Total
PLDT	35	20	25	90	50	45	75	60	**400**
Globe	35	-	45	60	20	15	90	60	**325**
Brightshare*	-	-	-	-	-	30	-	-	**30**
Others	-	-	-	-	-	-	-	40	**40**
Vacant	20	10	-	-	50	-	20	40	**140**
Total	**90**	**30**	**70**	**150**	**120**	**90**	**185**	**200**	**935**

Acquired by PLDT and Globe but not subjected to a co-use agreement.

57. The Transaction will leave a limited amount of spectrum to a potential third player. The MAO has found cause to believe that the amount of available spectrum post-transaction may not be sufficient for a new player to exert competitive pressure on PLDT and Globe.

58. First, it is apparent that PLDT and Globe will have a substantial advantage over other potential competitors in terms of spectrum bandwidth. The Transaction will leave 180 MHz of spectrum available to a third party, whereas PLDT and Globe will hold 400 MHz and 325 MHz, respectively.

59. Second, the MAO notes that given the current technical constraints, there will be no usable 2G bands available to provide basic mobile telecommunications services such as SMS and voice. Without access to 2G frequencies, it would be extremely difficult, if not impossible, for a new player to enter and challenge the incumbents.

60. Third, expanding a network with a limited frequency spectrum requires considerably more investment, as more cell sites are needed to create the same capacity. This means that a new player will need a long time to build and expand its network and will incur considerable expense.

61. Fourth, a potential new entrant's capacity will be severely restricted and its ability to expand will be limited. The limited spectrum that would be available significantly

reduces a third player's incentive to attract new customers. A competitor will have little incentive to reduce prices to attract customers as they will be capacity-constrained.

62. The MAO also considers that the terms of the co-use entered into by Smart, Globe and BellTel, particularly for the division of the 700 MHz band, is structured in a way that creates a disadvantage for a third player. The co-use arrangement dictates that 17.5x2 MHz of the 700 MHz band will each be allocated to PLDT and Globe, while 10x2 MHz will be returned to the government to be used by a potential new entrant. However, the 700 MHz band only supports channel bandwidths of 1.4 MHz, 3 MHz, 5 MHz, 10 MHz, 15 MHz and 20 MHz. Thus, it appears that neither PLDT nor Globe would be able to use the 17.5x2 MHz efficiently. The MAO therefore finds that the circumstances point towards a possible object by the incumbents to foreclose access to essential inputs.

63. Aside from spectrum holdings, the Transaction will transfer the ownership of VTI's telecommunications infrastructure to PLDT and Globe. After the Transaction, PLDT and Globe will fortify their hold over the entire backbone network in the country. Due to the lack of a national broadband network as well as a mandatory infrastructure sharing policy, a new entrant will have to build its own backbone and infrastructure in order to successfully compete against the incumbents. The Transaction will thus result in significantly higher costs for potential third players.

64. The advantages that will accrue to PLDT and Globe by the acquisition of VTI's telecommunications infrastructure and spectrum may further entrench their dominant position in the market for mobile services. In the long term, consumers will likely face higher prices and reduced choices as the incumbent firms will have minimal incentives to pass on cost savings to consumers given that it will unlikely face strong competitive constraints.

65. Accordingly, the MAO currently believes that the Transaction may raise significant competition concerns due to dynamic loss of competition in the retail mobile telecommunications market. The MAO considers that post-transaction, no other firm will be able to impose competitive constraint on the incumbents, resulting in an SLC in the provision of mobile services in the Philippines.

E.2. Retail Supply of Fixed Broadband Services

E.2.1. Unilateral effects from loss of existing and potential competition

66. The concern under this theory of harm is that the Transaction eliminates an actual competitor, ETPI, which is engaged in providing both fixed broadband and fixed voice services. Actual competition produces two effects to the benefit of the public. First, it gives consumers access to an alternative service provider which may offer better and cheaper services. Second, it applies a competitive constraint on the price and quality offerings of the incumbents as it creates downward pressure on prices

such that incumbents are either forced to match the new entrant's prices or offer even lower prices altogether.

67. ETPI is an active player which currently provides business-grade internet services, network solutions, and voice services in Makati, Ortigas, Manila, Caloocan, Cebu, Baguio, and the industrial zones of Laguna and Cavite. It also offers its services to residential customers. Though small in size compared to the incumbents, the loss of a competitor may further increase market power.

68. ETPI currently owns a backbone network which is capable of servicing NCR and adjacent areas including Pampanga, Batangas, and Laguna. The MAO notes that ETPI could potentially expand and operate its fixed broadband business across the country. As VTI has the incentive and capacity to expand the coverage of its mobile telecommunications network across the country, ETPI would have benefitted from VTI's investment as the same infrastructure can be used to operate its fixed line business. The Transaction may therefore potentially foreclose a player that would be able to provide a competitive constraint on nationwide carriers, PLDT and Globe.

69. Accordingly, the MAO currently believes that the Transaction may raise significant competition concerns due to unilateral effects from loss of existing and potential competition in the retail supply of fixed broadband services.

E.3. Retail Supply of Fixed Voice Services

E.3.1. Unilateral effects from loss of existing and potential competition

70. The concern under this theory of harm is that the Transaction also eliminates ETPI as a fixed voice service provider and would remove the constraint on the incumbent operators that ETPI would have exercised in the counterfactual. The fixed voice market is highly concentrated. The loss of ETPI as a competitive constraint could allow PLDT and Globe to degrade their service to businesses and consumers, because the acquisition would reduce the number of customers that could switch away from them.

71. Accordingly, the MAO currently believes that the Transaction may raise competition concerns due to unilateral effects from loss of existing and potential competition in the retail supply of fixed voice services.

E.4. Wholesale Supply of Mobile Services

E.4.1. Input foreclosure

72. The concern under this theory of harm is that the Transaction may allow PLDT and Globe to restrict access to the wholesale supply of mobile services. MVNOs are not able to deploy their own network infrastructure and are thereby dependent on

wholesale access to provide mobile services to end consumers. As direct competitors in the downstream market, the MAO notes that PLDT and Globe may have incentive to foreclose the active MVNO (*i.e.,* ABS-CBN Mobile) as well as future potential MVNOs.

73. The Transaction may leave MVNOs in a weaker bargaining position, making it harder for them to obtain wholesale access under similar prices and conditions as in the counterfactual. This could reduce the competitiveness of MVNOs at the retail level and, due to the loss of competitive constraint, lead to higher prices of retail mobile services.

74. Accordingly, the MAO currently believes that the Transaction may raise significant competition concerns due to input foreclosure in the wholesale supply of mobile services.

E.5. Wholesale Supply of Fixed Broadband Services

E.5.1. Input foreclosure

75. The concern under this theory of harm is that the joint acquisition will give PLDT and Globe complete control of the backbone network necessary to provide fixed broadband services. Telecommunication infrastructure owners lease out access to their backbone networks to ISPs, which offer services to end consumers. The Transaction increases the market power of PLDT and Globe since the number of end-to-end infrastructure owners is reduced.

76. The Transaction may change the incumbents' incentive to grant access to its infrastructure and may result in higher costs for ISPs, relative to the counterfactual. This eventually leads to higher prices because there is less competitive constraint in the industry. The MAO notes that PLDT and Globe have the incentive to foreclose the market because they are active players in both the upstream and downstream industry. They can then raise prices as an attempt to limit the ability of an ISP to offer better packages (in terms of speed, quality, and price) compared to what PLDT and Globe offer their customers.

77. Accordingly, the MAO currently believes that the Transaction may raise significant competition concerns due to input foreclosure in the wholesale supply of fixed broadband services.

E.6. Coordinated effects in the supply of telecommunications services

78. The concern under this theory of harm is that the Transaction may enhance the likelihood of coordination or strengthen existing coordination in a manner that harms competition significantly.

79. To determine if the Transaction will enhance the likelihood of coordination or strengthen existing coordination, the MAO assessed: (a) whether market conditions are conducive to coordination; and (b) whether the acquisition would affect market conditions and the firms' ability or incentives that would make coordination more likely.

80. In its initial assessment, the MAO took note of the following characteristics of the Philippine telecommunications industry: (a) there are only two (2) dominant players in the market; (b) telecommunication services are fairly homogenous; (c) PLDT and Globe are generally similar in terms of market shares, cost structures, and level of vertical integration; and (d) there is a good degree of price transparency amongst competitors.

81. The MAO has taken into account the past behavior of the incumbent firms, as indications of previous coordination may serve as evidence that conditions for successful coordination are present. Recent events suggest that it may be easy for PLDT and Globe to cooperate and coordinate their actions. For instance, during the announcement of the agreement to jointly acquire SMC's telecommunications businesses on 30 May 2016, PLDT Regulatory Affairs and Policies Head Ray Espinosa made the following statement: "The story on when we started dating is not important because we are already married." This is further confirmed by the disclosure to the Commission during its 8 July 2016 meeting with Globe, that Globe Chief Executive Officer Ernest Cu ("Mr. Cu") communicated directly and arranged with Mr. Manny V. Pangilinan on the joint acquisition of SMC's telecommunication assets, shortly after the former received an informal offer to sell the subject assets from SMC's Ramon Ang. The nature of the formation of the joint acquisition suggests the existence of coordination between the two firms, which may be further enhanced by the Transaction.

82. The MAO notes that the joint acquisition may reduce PLDT and Globe's incentives to compete and may facilitate collusion between the two competitors. For instance, the terms of the Transaction involve a 50-50 sharing between PLDT and Globe. As such, if no corporate reorganization is made, it is expected that PLDT and Globe will each have directors sitting in the boards of the acquired corporations. This is already demonstrated in the recent election of the board of directors in Liberty. The structure of the joint acquisition legitimizes coordinated and strategic behavior in the management and operations of the acquired firms. This setup increases the risk associated with cartel-like behavior.

83. The acquisition of VTI, being a maverick firm that has a different competitive strategy, may eliminate a significant constraint to effective coordination and make coordinated interaction more likely and more successful.

84. Accordingly, the MAO currently believes that the Transaction may raise significant competition concerns due to coordinated effects.

F. Entry and Expansion

85. The MAO considered whether the lessening of competition may be mitigated by the expansion or entry of competitors. The threat of entry or expansion can be an important competitive constraint on the conduct of firms. However, the MAO currently holds that entry or expansion in the relevant markets will not be timely, likely, nor sufficient, due to the considerable structural, legal, and artificial barriers.

86. Barriers to entry and expansion to compete in the Philippine telecommunications markets are inherently high. The lack of mandatory infrastructure sharing policy or a national broadband network in the country means that a new entrant wishing to enter the market needs to overcome significant structural barriers to entry. This includes high fixed and sunk costs associated with building a network infrastructure.

87. Legal barriers include the difficulty in securing necessary franchises, licenses, and permits, as well as the Constitutional requirement that public utilities such as telecommunications be sixty percent (60%) Filipino-owned. Incumbent firms have also complained of bureaucratic red tape at the local government unit level, which increases the burden and costs of building infrastructure.

88. A new entrant would also need to surmount artificial barriers to entry such as high switching costs and the threat of protracted legal battles posed by PLDT and Globe. For instance, the country still has no number portability which impede customer switching. Both incumbents also have a history of issuing legal threats against the sector regulator, other players, and against each other.

89. In addition, a new entrant would have to face other barriers resulting from the practices of firms with significantly higher bargaining strength. These practices may include price squeezing, constructive refusal to deal, tying and bundling, anti-competitive cross-subsidization, and the imposition of other barriers to entry such as the charging of prohibitive interconnection fees.

90. The MAO therefore currently believes that there are slim prospects of new entry or expansion to constrain the behavior of PLDT and Globe after the Transaction. Notwithstanding the foregoing, the MAO notes that VTI has demonstrated that it has the ability to overcome certain significant barriers to entry. In this light, the elimination of VTI as a potential competitor raises significant competitive concerns.

G. Conclusion

91. At this point, the preliminary competitive assessment has found a realistic prospect of a substantial lessening of competition within the relevant markets. The MAO expects that the Transaction will result in a substantial prevention, restriction or lessening of competition in relation to: (a) the retail supply of mobile services; (b) the retail supply of fixed broadband services; (c) the retail supply of fixed voice

services; (d) the wholesale supply of mobile services; and (e) the wholesale supply of fixed broadband services.

92. The joint acquisition involves the elimination of important competitive constraints and the reduction of competitive pressure on already concentrated markets. The MAO is therefore concerned that the Transaction may cause significant harm to consumers, in the form of higher prices and reduced choice and quality of services, relative to the counterfactual.

93. Based on the information obtained as of date, the MAO believes that SMC's telecommunications businesses would have significant potential to be important drivers of competition in the industry. The joint acquisition of SMC's telecommunications businesses is likely to further entrench the dominant position of PLDT and Globe, in markets where outcomes have not traditionally served consumers well.

94. The MAO therefore currently believes that the Transaction is likely to substantially prevent, restrict or lessen competition within the relevant market(s) in the Philippines.

95. In view of the foregoing, the MAO considers that it is under a duty to proceed to a more detailed review of the Transaction that will allow the MAO to further examine and analyze the competitive effects of the Transaction in the relevant market(s), and make a more conclusive recommendation to the Commission.

96. Should it finally conclude that the Transaction will substantially prevent, restrict or lessen competition in any relevant market(s), the MAO will consider whether its implementation should be prohibited, or otherwise require remedies thereon, and if so, what remedies might be appropriate for the Transaction, with due regard to what will be the benefits to customers and which customers will benefit.

Mergers and Acquisitions Office
25 August 2016