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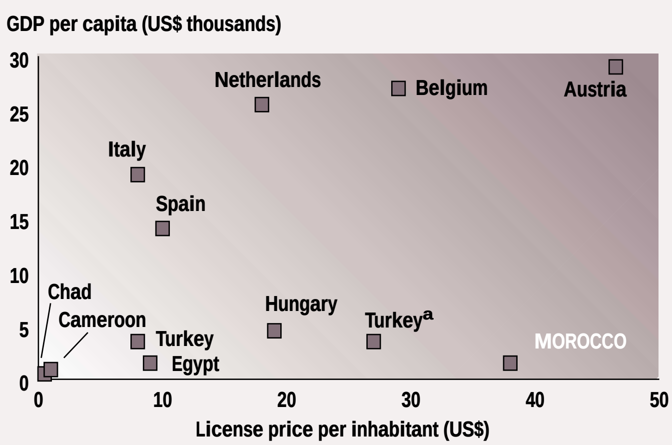
Introducing Telecommunications Competition through a Wireless License

Lessons from Morocco

Björn Wellenius and Carlo Maria Rossotto

In August 1999 the Moroccan government awarded a second mobile telecommunications license through international tender. All bidders made commitments on quality, coverage, and tariffs that would significantly expand and improve telecommunications services. The winning bidder was Medi Telecom, a consortium of Telefónica of Spain, Portugal Telecom, and Moroccan investors. Medi Telecom paid about US$1.1 billion for the fifteen-year license to operate under relatively unfettered competition—one of the highest prices ever paid for a mobile license relative to population size. Just as impressive is that the price was offered in a country not usually on the radar screen of foreign investors. The fiscal and development impact will be far reaching. The strong competition from reputable bidders was the payoff to Morocco's decision to set up a credible, pro-competitive regulatory environment before the transaction and to conduct open, professional bidding for the license. This Note examines why Morocco was able to reap these big rewards.

FIGURE 1 PRICES PAID FOR SECOND GSM LICENSES IN RECENT TRANSACTIONS, 1994–99



a. Net present value.
Source: ANRT and World Bank data.

The liberalization of Morocco's telecommunications sector formally began with the Parliament's passage in 1996 of a telecommunications law (effective June 1997) that lay the foundations for an increasingly competitive, private-led sector. The law enabled competition in all segments of the market and set up an independent regulatory agency, Agence Nationale de Réglementation des Télécommunications (ANRT). The law also envisaged privatizing Itissalat-al-Maghrib (IAM), the incumbent state-owned telecommunications monopoly, but set no timetable. IAM operates fixed and mobile services, including the first Global System for Mobile Communications (GSM) network.

The award of a GSM license to a second operator in August 1999 was the first major step in introducing competition in the telecommunications market. As the process of tendering and awarding the license unfolded, the agenda for

TABLE 1 THE BIDDERS AND THEIR BIDS

Bidding consortium	Composition	Financial offer (US$ millions)
Medi Telecom	Telefónica, Portugal Telecom, and others	1,140
Badil Com	France Telecom, Motorola, and others	915
TIM Maroc	Telecom Italia Mobile	634
Orange Communications Maroc	Orange Plc. and others	529
Marphone	Vivendi (CGSAT), SBC International, and others	526
Vodafone Maroc	Vodafone, Air Touch, and others	441
Maghreb Cell	GTE, Bell Atlantic, and others	296

Source: Press releases.

privatizing IAM accelerated. By the time the license was issued, the government had set the first quarter of 2000 as the target for opening IAM to private capital and had hired financial advisers to prepare the transaction.

Preparation

The successful issue of the second GSM license can be attributed largely to three features: a credible regulatory framework, the transparent tender process, and the attractive terms of the license.

Clear rules and roles

A legal and regulatory framework, including ANRT, was in place before the tendering of the second license started. The framework could have used improvements, such as simplified licensing, the addition of modular penalties, and ex post rather than ex ante financial control of ANRT. Nevertheless, coupled with the government's sustained commitment to telecommunications reform, it gave investors sufficient confidence and a basis for reliable business decisions.

The law set out the principles for licensing and competitive award. It also ensured that throughout the process the bidders had a clearly identified, independent counterpart, ANRT, with explicit responsibilities and functions. And by giving ANRT a broad mandate and clear authority (putting it in charge of managing and allocating spectrum, for example), the law helped reduce regulatory risk.

The law was complemented by several subsequent implementation decrees. One of these established general interconnection principles, defined a dispute resolution mechanism, specified the essential elements of the interconnection contract, and provided technical and cost principles for interconnection. Another established the legal regime for leased lines.

ANRT sought expressions of interest from prospective investors once it had drafted the second license and IAM had published a default interconnection offer. These elements helped investors forecast the net cash flow and the breakeven point, the main drivers of the financial offer.

Transparent tender

ANRT, which was responsible for conducting the licensing process, asked qualified bidders to offer commitments matching or exceeding targets for service quality, coverage, and tariff plans. These three elements form the core of the technical offer; the financial offer, the amount the bidder intends to pay for the license, is separate. Seven bidders made offers (table 1). In determining the best bid, ANRT weighted the price 60 percent and the technical offer 40 percent. Medi Telecom submitted the highest financial offer and the second highest technical one.

The process for awarding the license was transparent and conducted fairly and professionally by ANRT, and it stayed on schedule. The criteria for evaluating bids were set out in the tender documents, including the weights to be given each part of the technical offers. How marks would be assigned within each part to reflect offers above minimum requirements, however, was left to the evaluating committee. This balance between predictability and uncertainty is consistent with practice in some European countries, and ANRT believes it encouraged bidders to offer better than minimum performance. To enhance transparency, ANRT published a bid evaluation report on its Website disclosing the marks given to each part. But at the bidders' request the offers were not disclosed, so as to protect commercial information.

Nor have the technical offers of the winning bid been made public or reflected in the license. In some countries, such as Italy and the United Kingdom, the license includes the main technical parameters in the winner's bid, since their disclosure is not judged a violation of confidentiality. Other countries, such as Belgium, follow the same approach that Morocco has. If Medi Telecom fails to meet the minimum requirements published in the tender, anybody can complain to ANRT, including IAM or consumers. But if it fails to meet the technical commitments in its bid, it will be up to ANRT to enforce compliance.

Commercially attractive license

The license was particularly appealing to investors because, in addition to the usual features of a mobile license, it conferred embedded rights that mitigated the risks posed by IAM's initial market dominance, enhanced the expected cash flow, and signaled the authorities' willingness to allow effective competition. In particular, the license allowed the new operator to:

- Build its own long-distance infrastructure, bypassing the network of the incumbent operator, or build its own infrastructure up to the point of interconnection.
- Build and, after January 1, 2002, operate its own international gateway to provide services to its clients.
- Offer fixed wireless services in rural, suburban, and industrial areas, subject to ANRT approval.
- Serve as the sole licensed cellular communications operator, other than IAM, for four years.

The first two features give Medi Telecom much flexibility to invest in and develop its network and to overcome possible capacity and pricing bottlenecks in IAM's network. The third allows Medi Telecom to extend access outside the core markets at marginal cost, and to develop potential sources of additional revenue in industrial areas where advanced applications (such as wireless) can be launched. These features enable Medi Telecom to position itself well for building up a wide range of services once IAM's exclusive rights expire.

The last feature, which establishes a duopoly in mobile communications for four years, is more controversial. Hindsight suggests that restricting entry was unnecessary to attract serious investors. Moreover, it added little to the price paid for the license. The three highest bids came from consortia led by major European companies that had a strategic rather than a purely financial interest in the Mediterranean Basin. Whether the somewhat higher bid price justifies slowing the liberalization of mobile services is questionable. Experience in other countries suggests that a third operator is needed for competition to bring further big cuts in retail prices and innovations in service.

Impact

The new license has already prompted the incumbent to improve service and reduce prices. It also promises to deliver big benefits to customers and new revenues to the government.

The bid evaluation report shows that the bidders' average growth forecasts for the mobile market in Morocco envision it expanding from 170,000 customers today to about 5 million in 2010. While the technical commitments of the winning bidder are confidential, the average commitments bid greatly exceed the minimum targets for the population share and road length to be covered in the first five years. Service is expected to reach 90 percent of Morocco's population during the fourth year, compared with the minimum requirement of 60 percent by the end of year three and 75 percent by year five. Moreover, because the winner committed to matching IAM's mobile coverage when it launches the new service, all current customers will have a choice from the start. These commitments are in line with the aggressive rollout programs in other countries. In Turkey, for example, Telsim agreed to cover 50 percent of the population in two years and 90 percent in five.

From the start of service, tariffs are likely to fall about 30 percent below those at the time of bidding, or to less than half what they had been before the tender was issued. That will bring retail prices within the range for the region, but still 20 to 30 percent higher than the best international prices, about US$50 for 360 minutes of GSM service.

Performance of the incumbent

As in other countries, the imminence of competition alone prompted big improvements in the incumbent's service:

- Between March and November 1998, as the tender was being prepared and expressions of interest were being sought, IAM reduced mobile service prices by about 25 percent, partially rebalanced tariffs for fixed telephone service, and committed publicly to expanding mobile and fixed networks.
- In December 1998, shortly after the tender was issued, IAM again reduced its mobile charges by about 25 percent and introduced the ability to receive short text messages.
- Although IAM introduced GSM service in 1994, it connected most of its customers (and considerably improved service quality) while the second license was being processed. Its customers increased by 57 percent in 1998 and by another 30 percent in the first half of 1999, reaching more than 170,000 in July 1999.

Fiscal impact and jobs

At about US$40 per inhabitant, the license price exceeds by 50 percent or more what operators recently paid for mobile licenses in most other countries (figure 1). These include other middle-income countries in the region (Egypt, Turkey) and elsewhere (Hungary), mature economies where operators expect to build up large customer bases with high purchasing power (Italy, Spain), and small but very high-income markets (Belgium, the Netherlands). Among recent transactions, only Austria did better than Morocco.[1]

The US$1.1 billion license fee increased Morocco's fiscal revenue for 1999 by about 13 percent. The government could use the proceeds—equal to about half a year's public capital expenditures or two years' capital inflows (portfolio and direct foreign investment)—to finance new public sector investments or to reduce the foreign debt stock by about 6 percent.World Bank estimates suggest that the total fiscal impact of the second license (including future taxes and research and development) will be much larger—in present value terms, more than US$2 billion by 2008, and perhaps as much as US$3.5 billion. Moreover, Medi Telecom expects to employ about 3,000 people, and its operations may generate 20,000 additional jobs, mainly in sales, distribution, and network installation and maintenance.

Conclusion

The 1990s have seen an unprecedented pace of telecommunications reform around the world, but some developing countries have moved more cautiously. Reform has been particularly slow in the Middle East and North Africa, where such countries as Algeria, Syria, and Tunisia have maintained closed markets. Elsewhere, as in parts of Africa and South Asia, unclear regulatory frameworks, lack of process transparency, and indefinite reform timetables have made private investors hesitant and prevented end users from getting the full benefits of competition. Morocco shows that a middle-income developing country can quickly become attractive to major international investors. Its reform sets a quality benchmark for the region and the effects are thus likely to extend beyond Morocco to many of its neighbors.

In the 1980s and early 1990s the World Bank financed modernization and expansion of IAM's network. An April 1999 telecommunications sector adjustment loan of US$100 million supported initial liberalization, including the issuing of the second GSM license.

1 Revenue sharing in Lebanon probably has a higher present value but is not readily comparable, as mobile replaced the destroyed fixed network and the future was more uncertain.

Björn Wellenius (bwellenius@worldbank.org) and Carlo Maria Rossotto (crossotto@worldbank.org), Telecommunications Division