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“Is Safaricom losing its grip?”

Part 4: Mobile Data - “Losing its byte”

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Executive Summary

- **Mobile Data “Losing its byte”** is the 4th part of our 6 part series report titled **“Is Safaricom losing its grip?”**
- In the 1st part - **“Pricing Power Explained”** we explained the concept of “pricing power” which we defined as the ability of a company to raise prices over time without reducing demand for its products.
- We used the Herfindahl Hirschman Index (HHI) theoretical framework to determine each business line’s concentration levels and mentioned in brief the services in which Safaricom has or does not have pricing power.
- The HHI Index for mobile data has been on the decline over the last one year as a result of competitive threats.
- From our tariff analysis we observe that Safaricom is the most expensive mobile data provider and this has a negative impact on its market share.
- The report concludes that Safaricom **does not have pricing power** in the mobile data business as mobile data customers are highly price sensitive.
- In spite of loss of market share, we expect data service revenues to increase but at a declining rate, a trend that will force Safaricom to devise strategies aimed at countering the trend.

“Is Safaricom losing its grip?”	Report Title
Part 1	“Pricing Power Explained”
Part 2	Voice Calls - “Dialing the Wrong Number”
Part 3	SMS – “No one’s texting”
Part 4	Mobile Data - “Losing its byte”

Mobile Data–Safaricom Losing its byte

- Although the HHI index for the mobile data market remains high at 5,270.27 (Table.1), we observe a declining trend over the last one year as Safaricom faces strong competition in the mobile data business (Fig.1).

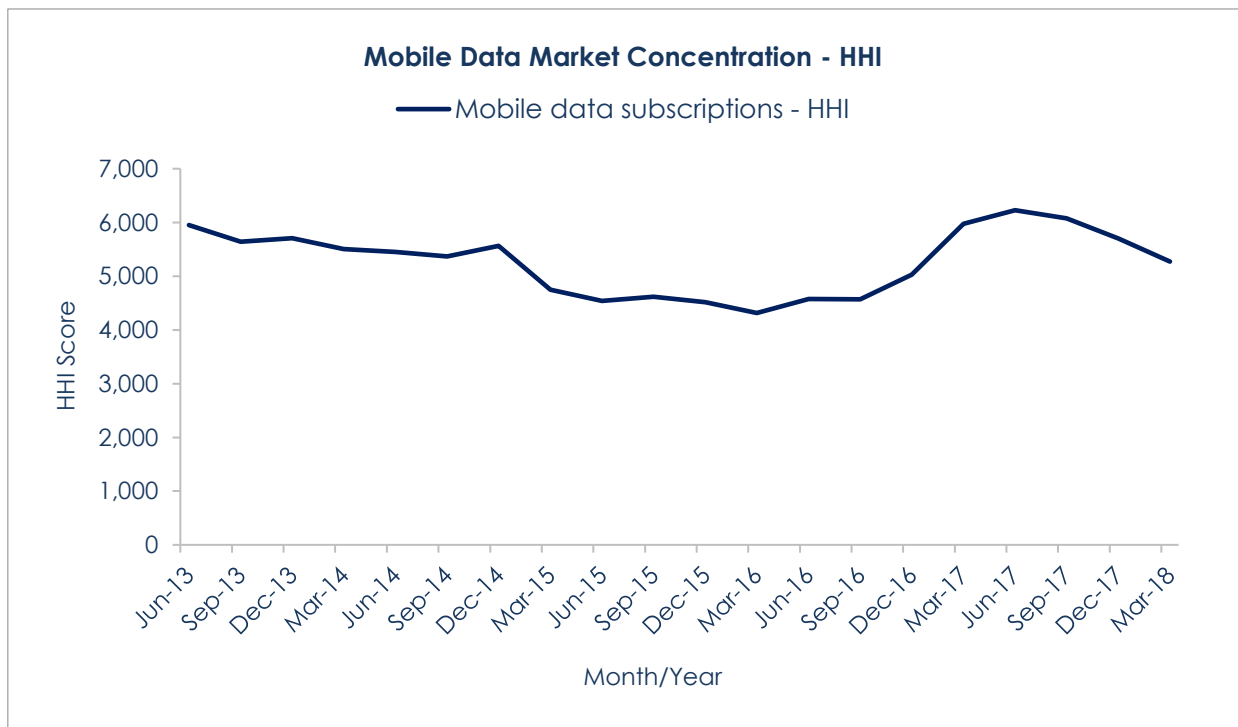
Table.1: High market concentration levels for mobile data

Mobile data/internet subscription by operator	Jan 2018 - March 2018
Safaricom Limited	68.4
Airtel Networks Kenya Limited	23.1
Telkom Kenya Limited	7.6
Finserve Africa Limited	0.5
Mobile Pay	0.3
HHI Index	$68.4^2+23.1^2+7.6^2+0.5^2+0.3^2=5270.27$

Source: Communications Authority of Kenya (CA) & Sterling Research

- An analysis of historical mobile data subscription market shares (Fig.1) indicates declining market concentration especially over the last 1 year.
- This is a direct result of the growing competitiveness of the mobile data business with both Airtel and Telkom increasing their share of mobile data subscribers following downward revisions of mobile data tariffs and aggressive marketing thereafter.

Fig.1: Mobile data market concentration declining as competition intensifies

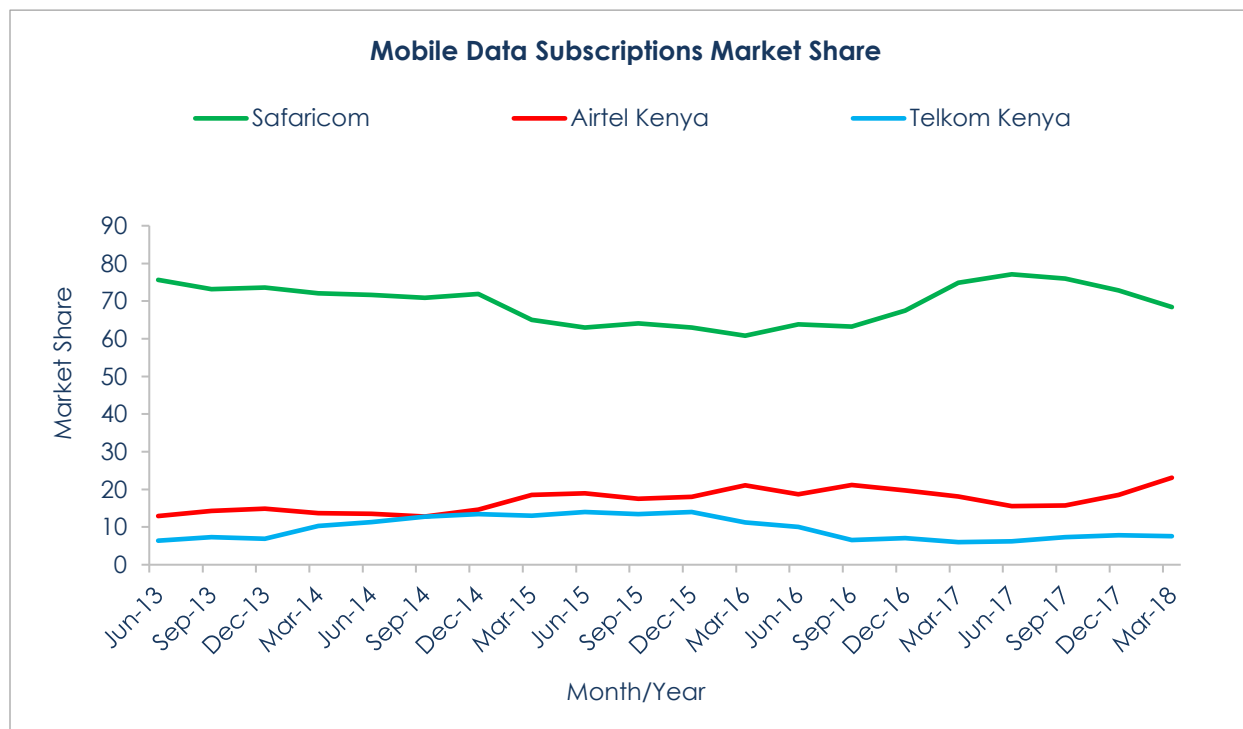


Source: Communications Authority of Kenya (CA), Sterling Research & CFA Institute

Mobile data - Safaricom losing the byte

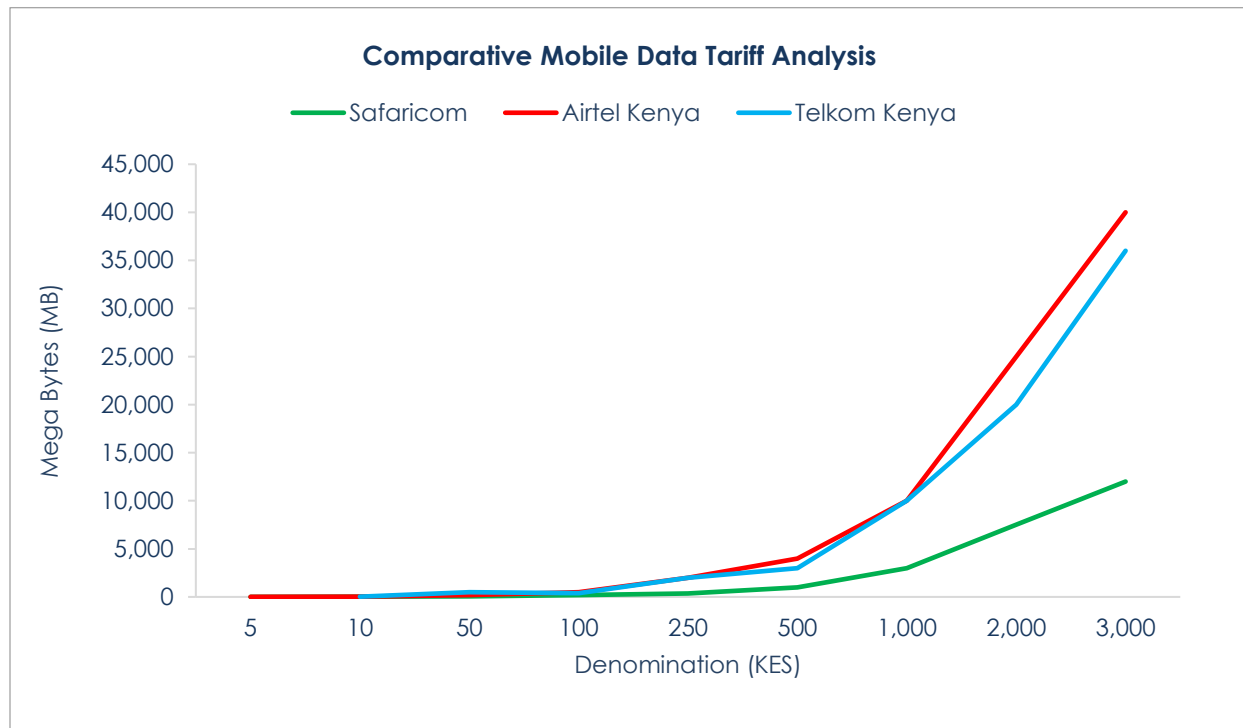
- We observe that Safaricom loses mobile data subscriber market share whenever Airtel and Telkom Kenya adjust their tariffs downwards (Fig.2).
- In spite of a 29% drop in Safaricom's effective mobile data tariffs in March 2018, they remain comparatively higher than Airtel and Telkom (Fig.3).
- This means mobile data demand is highly price sensitive and customers can easily switch mobile data providers whenever tariffs are revised downwards.
- On the basis of the effect of price adjustment on market share, we conclude that Safaricom **does not have pricing power** in mobile data business.
- Safaricom's introduction of new mobile data tariffs in September 2018 in our opinion is a move to counter this loss of market share.
- In October, Safaricom announced an upward revision of mobile data tariffs following the increase of excise duty on internet services from 10% to 15%, thus putting it in a difficult position considering it had revised its tariffs downwards in September 2018.
- High customer price sensitivity however means that this increase could potentially result in a loss of market share in the event other operators choose to maintain their existing tariffs.

Fig.2: Price competition in mobile data has seen Safaricom lose market share



Source: Communications Authority of Kenya (CA)

Fig.3: Safaricom mobile data tariffs higher than the competition

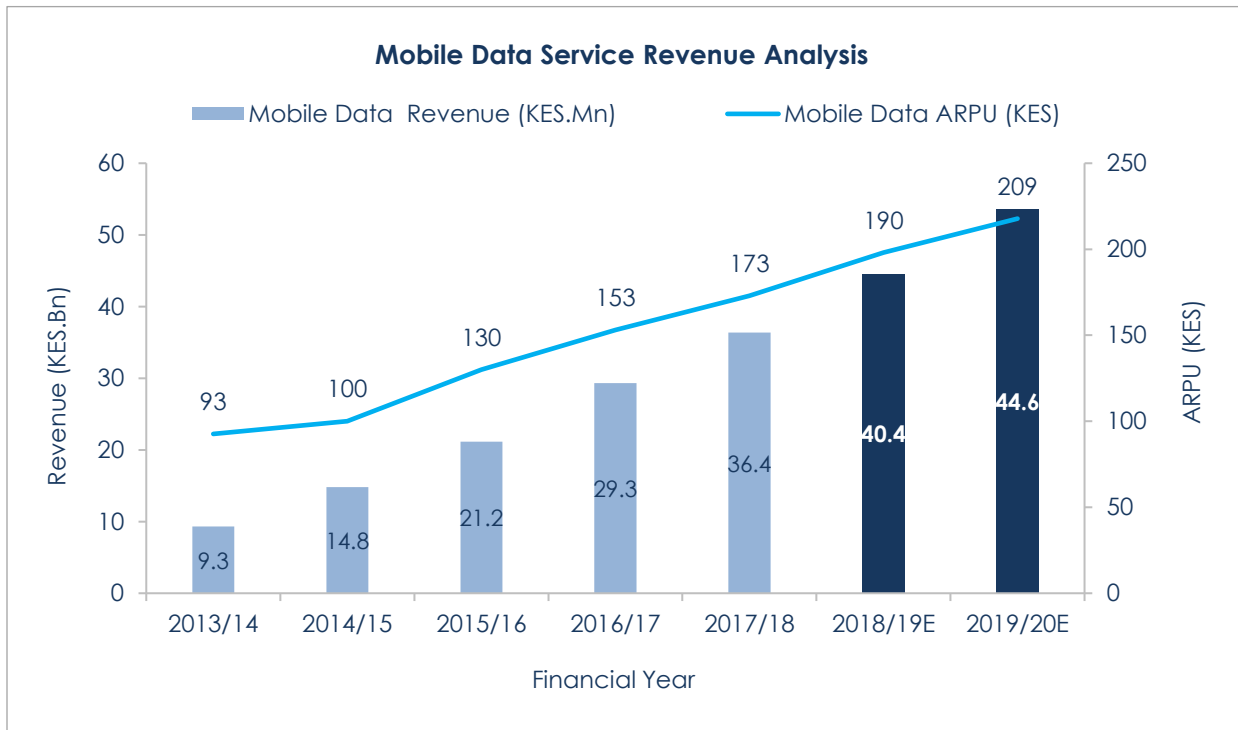


Source: Company tariff guides

Will loss of pricing power have an impact on mobile data service revenues?

- We forecast a positive but declining mobile data revenue growth rate for Safaricom as a result of loss of market share.
- FY2018/19 mobile data service revenues estimated at KES.40.4Bn a 11.1% growth over the previous year (Fig.4).
- Mobile data service revenues forecasted to account for 16.8% and 17.5% of total service revenues FY2018/19 and FY2019/20 respectively.
- Revenue growth will be supported by its competitive advantages including brand strength, wider network coverage (4G) and faster internet speeds.
- Data revenue growth will also be supported by an industrywide growth in data consumption from OTT services.
- The competitive advantage that Safaricom enjoys in the medium term also means that we do not see market share levels dropping low enough to call for a revision of tariffs below that of its two main competitors.
- In the long-term we should expect almost uniform mobile data pricing amongst the main mobile data service providers.
- Other mobile data service providers are unlikely to lower data tariffs significantly as current tariffs and new taxation on mobile data keep them below profitability thresholds.
- Safaricom will shift focus away from pricing to driving data consumption through smart phone sales and promotion of data driven social media applications.

Fig.4: Mobile data revenues positive but growth rate expected to decline



Source: Company filings & Sterling Capital estimates

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