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## THE WATERBED EFFECT

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**Have you ever tried lying down on a waterbed? It can be a disconcertingly bumpy experience, push down the water in one section and it pops up somewhere else to compensate. The “waterbed effect” is what economists use to describe an effect that happens in some markets when a price is forced down, another price rises to compensate.**

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**T**he waterbed effect happens in “two-sided” markets, when a business has two distinct kinds of customers. Telecommunications is a two-sided market, there are the consumers who pay to make and receive calls on the one side, and all the operators who share traffic on the other side.

Recent regulations from ICASA, under heavy pressure from Parliament have brought down the interconnect fee that operators may charge each other to pass calls between their networks. In theory, this should have brought down prices to users of those services. In fact, the opposite has happened, we’ve been treated to a first-hand, live demonstration of the waterbed effect.

An example is that a big mobile operator has brought down its average call rate by a small amount, but at the same time eliminated the difference between peak and off-peak call rates, so some callers are paying much more.

The problem is that ICASA doesn’t have the power to regulate retail telecommunications rates, only interconnect fees. Some politicians seem fixated on the idea that this will magically lead to lower retail rates, but costs in the telecommunications industry aren’t that simple. Operators have fixed their budgets on certain assumptions, and when an important part of those budgets changes by 50% in six months, something else has to change to balance things out.

Telkom, to its credit, has passed on the interconnect reduction directly to its customers: When the price it paid to the mobile operators to pass calls to their networks dropped from R1.25 to 89c, customers got the full 36c saving. But the mobile operators, who have lost that revenue, although they are paying less to each other at the same time, haven’t done the same.

The mobile operators, incidentally, have always paid Telkom far less to accept their calls than they get paid by Telkom when calls go in the other direction. This asymmetry dates back to 1994, when the first mobile operator licences were granted. The operators successfully argued that Telkom had the advantage of existing infrastructure, whereas they had to build everything from scratch so they should, in effect, enjoy a subsidy so that they could compete fairly. Sixteen years later, that argument can’t be made, yet the asymmetry persists. ■