

South Africa: Will Telkom's Monopoly Strangle E-commerce?

by Arthur Goldstuck

The latest edition of the biannual Internet Domain Survey, the world's most elaborate measure of Internet connectivity, put South Africa in 20th place in the world in terms of the number of computers connected to the Internet. This ranking, measured at the end of July 1998, ought to have been a cause for rejoicing since it placed what is in reality a Third World country squarely within the arena of major league players in Internet utilization.

The reaction, however, was entirely the opposite: great consternation and mutual recriminations. The reason? South Africa ranked number 14 in January 1996. By July 1997 it had fallen to 18. The most recent announcement prompted Telkom, the monopoly telecommunications provider which is 70% owned by the government, and the Internet Service Providers Association which represents 30 major and minor ISPs, to trade accusations as to which one was responsible for the continuing ebb in South Africa's ability to compete globally via the Internet.

In late 1997 the South African Telecommunications Regulatory Authority (SATRA) cited this drop in rankings when it denied Telkom the right to exclusivity of Internet service provision in South Africa. Telkom has taken this decision to the courts, arguing that its five-year monopoly status over telephone services included a monopoly over Internet or Internet protocol (IP) connectivity. The government had granted Telkom a monopoly over telephone services in re-

turn for requiring it to deliver lines to under-serviced areas throughout the country. While the issue concerning extending Telkom's monopoly remains pending, the Internet industry faces business as usual, but with the shadow of a more restrictive regulatory framework hanging over it.

The perils of a monopoly

Were Telkom to be granted its sought-after IP monopoly, the Internet industry—now worth an estimated \$333 million—might be forced to abandon its subscriber base of more than 250,000 individuals and small companies and more than 2,000 corporate clients. Clearly, this would be a major setback for the industry as well as for its clients.

Furthermore, e-commerce has grown tremendously in recent years, and it is the driving force behind the expansion of the Internet. However, the legal battle for exclusive monopoly rights may conclude by imposing a regulatory framework that will retard the potential of more explosive growth of e-commerce.

South Africa is an instructive case study because it exemplifies a dilemma facing many policymakers in developing countries. Some are considering granting monopoly status to a company in return for requiring it to extend telephone services to rural or poor areas that do not have telephone access. In doing so, the government may also eventually encounter a creeping monopoly that wants to assert its authority over the Internet, an

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area that thrives in an unregulated, entrepreneurial environment. Allowing the monopoly to extend its authority over the Internet may provide the rope that will ultimately strangle e-commerce.

The Internet's unforeseen growth

The Internet appeared in South Africa in the early 1990s, a time when the authorities had no interest in it. It entered on the back of electronic bulletin board systems (BBSs), which were computers that allowed an individual to dial in via modem and to exchange messages or download and upload files. Many BBSs were connected to computer networks set up by hobbyists, enthusiasts, academics, and researchers, while the networks were linked to the Internet via "friendly insiders" at academic institutions. As a consequence, any BBS user in South Africa could exchange electronic mail via the Internet. In the short period between 1992 and 1994, a strong core of Internet users emerged in South Africa under the nose of an unsuspecting Telkom.

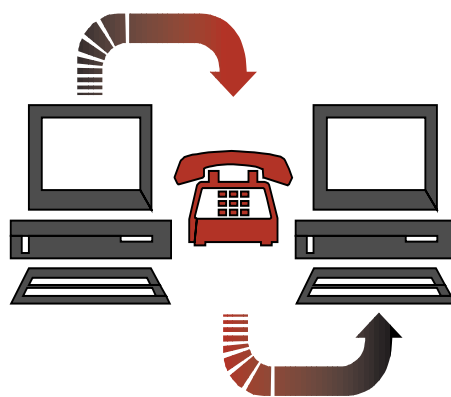
The first commercial ISP emerged in 1994 to an already existing audience. However, that year Telkom finally awoke to the presence of both the user community and the industry. It briefly threatened to close down this industry, partly by refusing to install additional telephone lines that were desperately required by the ISPs. This threat coincided with South Africa's transformation to a democratic society and proved a great embarrassment to the company that was trying to shrug off its roots in an apartheid society. An apparent iron-fist approach to small operators was an uncomfortable reminder of the all-too-recent era of tight control and aggressive suppression of dissent. The threat was withdrawn, the hold order was taken off the new telephone lines, and an industry that had been holding its breath prepared to explode.

Telkom moves in

It was not until 1996 that Telkom announced that it was entering the fray as an ISP. After testing its ability to provide this service, both in terms of infrastructure and access services, Telkom revealed

its underlying motive: it applied to have the private provision of Internet services declared illegal.

Telkom justified this proposal by arguing that its monopoly status over telephone services entitled it to a monopoly over the Internet as well. The government had granted Telkom a monopoly over telephone services but in return required it to deliver 2.8 million new lines by March 2002, most of these going to under-served or "disadvantaged" areas. South Africa has a population of 40 million people, but only 4 million currently have access to telephone lines. Another



120,000 lines will be installed as public telephones, primarily in rural areas. By March 2005, it is projected that 8.3 million lines will be connected.

The consequences have not been all that Telkom could have anticipated. It had assumed that its "new South Africa" credentials, along with its mission to connect the entire country, would have been enough to convince the regulators to accept its proposal to become the sole Internet provider. At the same time, it expected that its challenge to the independent ISPs would put a halt to their further expansion and drive subscribers to Telkom's subsidiaries and partners.

Instead, the ISP industry has continued to grow at a dramatic pace. In March 1998 the number of dial-up subscribers exceeded 250,000, up from 154,000 in September 1997, while the user base continues to expand by roughly 10% a month.

However, as indicated by the Internet

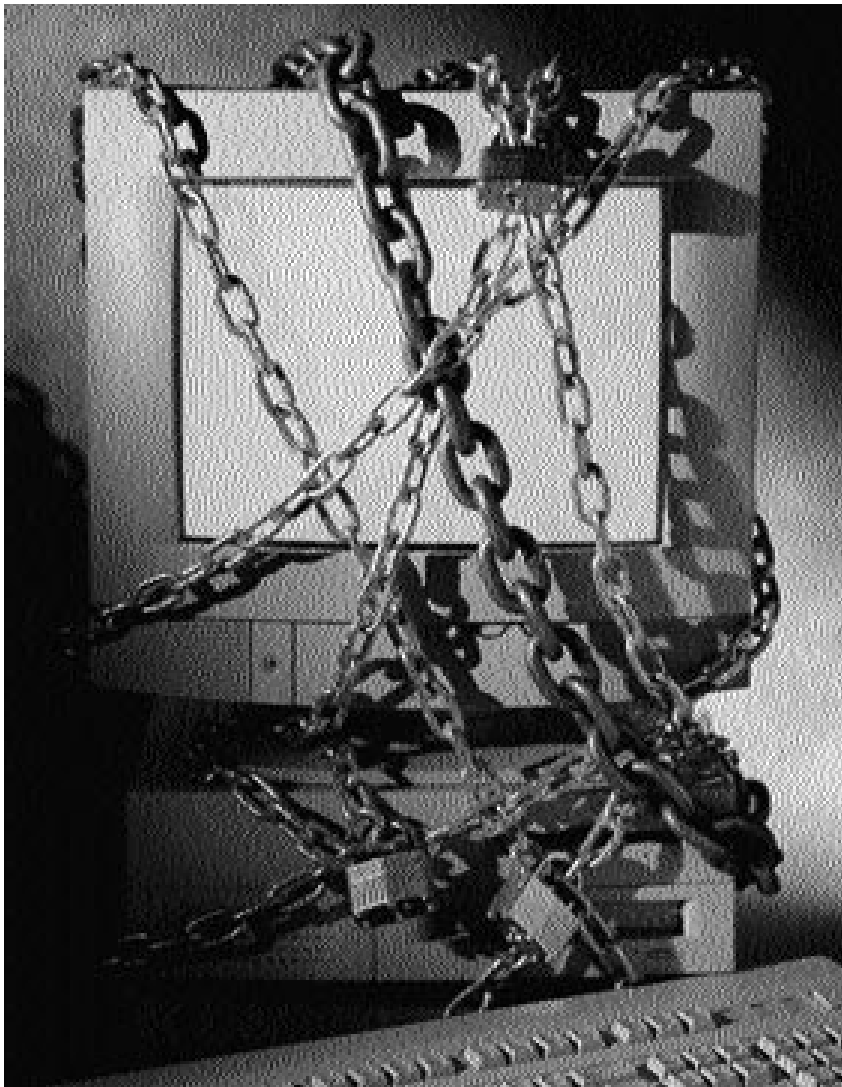


Photo: PhotoDisc, Inc.

Does monopoly help or hinder the Internet?

Domain Survey, investment in infrastructure has slowed, due to uncertainty among ISPs about the outcome of Telkom's court challenge to their business as well as Telkom's reluctance to encourage their growth. As a result, while the number of subscribers continues to grow, Internet users are encountering ever-slower and less efficient access to the Internet.

Can e-commerce be harnessed?

E-commerce has been the driving force behind the expansion of the Internet in South Africa, and it will continue to grow whether or not Telkom is successful in its legal battle for exclusive monopoly rights. In 1998 consumers are expected to spend \$166 million via e-commerce, up 100% from \$83 million in 1997, according to a 1998 web commerce survey by Media

Africa. While this represents less than 1% of GNP, if taken with roughly \$333 million invested by the ISPs and the value of new Internet-oriented corporations that are being formed through mergers and acquisitions, the Internet industry is quite significant. Furthermore, by 2002 spending on e-commerce will reach \$2.5 billion, according to BMI-Techknowledge, South Africa's main information technology research organization.

As the monopoly battle drags on, the Internet in South Africa will have grown from a fledgling industry into an economic force. This Internet economy has grown to the point where any attempt by the government to control or regulate it will certainly damage the economy.

If Telkom becomes the sole ISP or licensing authority for ISPs, it could also control the flow or nature of transactions across the network. Over the years Telkom has earned a reputation of offering lethargic service and inefficient billing, and consumers and the private sector are already suspicious of Telkom's ability to deliver business-critical services beyond telephony. The intrusion of a parastatal into the control of transactions would certainly undermine the growth of online transactions and reduce public confidence in the Internet economy.

Digging whose grave?

A telecommunications irony may shape the future of the Internet and e-commerce in South Africa. Telkom views the independent Internet industry as a threat to its monopoly, while the regulatory authorities have demonstrated a deeper appreciation for competition. Telkom's obligation to roll out universal telephone access will provide the platform on which ISPs will be able to offer universal Internet access. This would certainly ensure continued economic benefits of the Internet and e-commerce. However, if the government grants Telkom the right to be the sole Internet provider, the future of electronic commerce as a robust force in South Africa may be less certain. ☹☹