



**INDEPENDENT CONSUMER AND COMPETITION COMMISSION**

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**DETERMINATION**

**APPLICATION FOR CLEARANCE OF THE  
ACQUISITION OF DALTRON ELECTRONICS  
LIMITED**

**BY**

**DATEC (PNG) LIMITED**

## **DETERMINATION**

### **Background**

Datec (PNG) Ltd (**Datec**) and Daltron Electronics Limited (**Daltron**) have submitted a clearance application in respect of the proposed merger of Datec and Daltron. For the purposes of section 81 of the *Independent Consumer and Competition Commission Act 2002* (**the Act**), the proposal would be an acquisition of Daltron by Datec or its owners.

### **Parties and Acquisition Proposal**

**Datec** is jointly owned by Steamships Limited and Generic Technology Pty Ltd and sells a range of computer and telecommunications related products and services in PNG. Datec says that its primary focus is towards corporate customers in government and business in PNG, though it also sells products and services to small business and private consumers.

**Daltron** is a private company under the control of Bruce and Marcie Dahlenburg. Daltron also sells a range of computer and telecommunications related products and services in PNG, though on the information available to the Commission, it appears that Daltron's business is somewhat more focused than Datec on the consumer market rather than on the large corporate customers.

The application<sup>1</sup> states that Datec is considering a merger with Daltron. In subsequent discussions with Steamships Limited, it was said that if the acquisition proceeded, Datec would continue to operate Daltron as a separate business, in competition with Datec and other technology suppliers. While this is at odds with what is said in the application, it does not matter. For the purposes of a clearance under the Act, if the acquisition is allowed to proceed, there is nothing to stop the successful acquirer from merging the two businesses, even if the original intention were to maintain the businesses as separate operations. In any event, even if the businesses are operated separately, the fact of their common ownership is, in competitive terms, little different from a merger between the businesses, because of the influence the common owner can have on the operation of the individual businesses.

### **Elements of a Clearance**

Datec has applied for a clearance under section 81 of the Act. Section 81(3) of the Act provides that the ICCC shall either –

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<sup>1</sup> Clearance application received 10 August 2004

- (a) if it is satisfied that the acquisition will not have, and will not be likely to have, the effect of substantially lessening competition in a market.....give a clearance for the acquisition; or
- (b) if it is not satisfied that the acquisition will not have, and will not be likely to have, the effect of substantially lessening competition in a market.....decline to give a clearance for the acquisition.

The test for a clearance under section 81 of the Act is a positive one – in order to grant a clearance, the Commission must be satisfied that the acquisition would not have or be likely to have the effect of substantially lessening competition in a market. If the Commission is not so satisfied, it must refuse to grant clearance.

### ***The market***

The applicant has broken down the computer technology market in PNG into seven broad market segments<sup>2</sup>. The Commission agrees with that segmentation, so that there are, for the purposes of this clearance application, seven different markets. It would not be appropriate to classify the market as broadly as “computer technology” since each of the market segments comprises products or services which are not substitutable with those in another market segment. The seven identified markets are:

- Personal computers and peripherals
- Office consumables
- Uninterrupted power supplies and power solutions
- Photocopiers
- Software applications
- Networking and communication services
- Internet service providers

Datec has provided estimates of market shares of each participant in each of the identified markets. The Commission has not been able to verify those market shares, but with the exception of the PC and peripherals market (as to which, see below), the Commission has received no contrary information to suggest the market shares estimated by Datec would be inaccurate.

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<sup>2</sup> Clearance application, page 3

## ***The Effect on Competition***

### **General Characteristics of Technology Markets**

Rapid developments and innovation in technology means that technology based markets such as those under consideration here tend to be very dynamic, often with reducing unit prices from the availability of more efficient and advanced machinery and technology. Those markets are, as a result, frequently characterised by low market barriers and vigorous competition on price and on technological advances, with relatively frequent entry and exit of participants. However, while that is true of most of the seven identified markets, all of these characteristics do not apply across the board to all of those markets.

### **PCs and Peripherals**

This is an important market for both Datec and Daltron, particularly Daltron where it comprises at least 53% of sales<sup>3</sup>, while for Datec computers and peripherals, including PCs and larger computing equipment, amount to upward of 40% of total sales<sup>4</sup>. Datec estimates that the top four competitors in this market have about a 53% combined market share, with direct imports accounting for a further 15% of sales, and 12 other companies supplying the remaining 32% of the market. Datec says its share of the market is about 13%, with Daltron as the market leader with 16%.

If these figures are correct, the combined market share of Datec and Daltron would be about 29%, with the rest of the market spread among 14 other competitors, plus direct imports. However, one company<sup>5</sup> claims that the combined Datec/Daltron share in this market would be around 80%. This is a major discrepancy, but the Commission has been unable to assess with any accuracy what the respective market shares are. The Commission thinks it likely that the combined Datec/Daltron market share would be somewhere between those two figures, perhaps nearer 50% of the total market. What is clear is that Daltron and Datec are two of the market leaders, perhaps the two biggest, and their combined market share would be substantially larger than anyone else, perhaps three times the size of their next largest competitor.

On the basis of market share alone, the combined size of Datec and Daltron in this market would suggest that those companies had significant market power, which would be enhanced after the merger, with a consequent risk of a substantial lessening of competition resulting

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<sup>3</sup> Datec estimate, presentation to ICCO October 2004

<sup>4</sup> *ibid*

<sup>5</sup> Data Nets Limited letter, 20 August 2004

from the acquisition. However, there are a number of other relevant factors. Barriers to entry in this market are low. The market has numerous competitors with vigorous competition between them. Direct imports are a significant portion of the market and provide a strong competitive constraint on excessive pricing or other anticompetitive conduct. The market is dynamic and constantly benefiting from advances in technology, which also brings pricing constraints and promotes vigorous competition.

### **Bundling**

Both Datec and Daltron appear to bundle their PC products as a marketing technique. Bundling occurs where a supplier “bundles” two products together, in effect requiring a purchaser of one product, to take another product as well, for one inclusive price. This can have a disadvantage for the consumer who is, in effect, paying for two products when he may only really want one of them, or may disadvantage competitors who may not have access to the second product, or are not able to offer it at no additional cost, and thus are at a competitive disadvantage.

Datec and Daltron are both internet service providers, and have a practice of supplying purchasers of their PCs with internet connection for the first month at no extra charge. While there may be an incentive for those purchasers to continue to use Datec or Daltron as their internet service provider, for example, because they will have a Datec or Daltron email address, there is no obligation on the purchasers to continue to use Datec or Daltron after their first “free” month, nor do they have to take up the ISP offer at all if they don’t want to. The other ISPs in PNG also sell PCs and, it is understood, may also bundle their PCs and ISP connections.

While PC suppliers who do not have an association with an ISP may feel they are disadvantaged because they do not have the capacity to bundle PC sales with an ISP connection, that applies to more than just Datec and Daltron, and more particularly, the merger of Datec and Daltron would neither increase nor decrease their capacity to bundle ISP connection with PC sales. In other words, any lessening of competition which might occur from bundling would not be as a result of the acquisition.

In those circumstances, it is considered that the acquisition would not have the effect or likely effect of substantially lessening competition in the PC and peripheral market.

### **Office Consumables**

Consumables are a significant contributor to Datec's and Daltron's businesses, comprising the third largest and second largest proportions respectively of their overall businesses<sup>6</sup>. However, according to Datec's submission, the market is led by Supreme Industries with the largest market share at 25%, Datec and Daltron being the fourth and second largest firms in the market with 7% and 10% market share respectively. Datec says there are over 20 firms in the market. The Commission has no independent assessment of the state of that market, but has no information which would disagree with the Datec assessment.

In the circumstances, the Commission considers that the acquisition would not have or be likely to have the effect of substantially lessening competition in the office consumables market.

### **UPS and Power Solutions**

The UPS and power solutions market is serviced by nearly 20 companies, mostly competing vigorously at the lower (consumer) end of the market, including Daltron, with Dalco, Datec, Esco and Lae Battery competing in the high value, high end of the market. Datec says it has 15% of the market and Daltron has 5%. On the basis of those market shares, in a market with a large number of competing firms, the Commission considers the acquisition would not have or be likely to have the effect of substantially lessening competition in the uninterrupted power supply and power solutions market.

### **Photocopiers**

According to Datec<sup>7</sup>, this market is dominated by Remington, with about 14 other firms competing in the market. Each firm tends to represent one specific manufacturer. Datec and Daltron are the third and fifth largest firms, respectively, with 10% and 5% market shares.

On the basis of those market shares, in a market with a large number of competing firms, the Commission considers the acquisition would not have or be likely to have the effect of substantially lessening competition in the photocopier market.

### **Software Applications**

Datec claims that the predominant source of software applications for the PNG market is overseas companies, with, in Datec's estimation, about 70% of the market. Among the dozen or so companies supplying the market locally, Datec claims to have 4% and Daltron 3% of the total market. That combined market share of 7% is not significant, and even

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<sup>6</sup> Datec presentation, October 2004

<sup>7</sup> Clearance application, page 5

if their combined share of the locally supplied market were considered excluding imports, it would still be less than 25%.

On the basis of those market shares, in a market with a large number of competing firms, and particularly where imports comprise the bulk of the market, the Commission considers the acquisition would not have or be likely to have the effect of substantially lessening competition in the software applications market.

### **Networking and Communication Services**

Datec and Daltron both compete in the network and communications market sector with, in Datec's estimation, 14% and 8% of the market respectively. Datec claims that a significant portion of the market is serviced by companies outside PNG, about 20% of the total market, according to Datec<sup>8</sup>. Hitron, Data Nets and Global all appear to be major participants in this market, which is also serviced by a number of other firms.

On the basis of those market shares, in a market with several competing firms, and where imports comprise a significant part of the market, the Commission considers the acquisition would not have or be likely to have the effect of substantially lessening competition in the networking and communication services market.

### **Internet Service Providers**

Unlike the other markets in which Datec and Daltron compete, the ISP market is characterised by high concentration and few participants, with Datec and Daltron having a combined market share of nearly 50%<sup>9</sup>, and 4160 of the 7936 commercial internet customers<sup>10</sup>, or 52.4% of the total internet customers. By any measure, Datec and Daltron are major participants in the ISP market. In addition, the barriers to entry in the ISP market are almost impossibly high.

There are four firms providing commercial ISP services in PNG, Datec, Daltron, Data Nets and Global. In addition, Unitech supports an academic network, but this is not a direct competitor with the commercial ISPs. All commercial ISPs compete in the same market, though Datec points out that a large proportion of its ISP business is used to support Datec's provision of switched private network services for its large corporate commercial and government customers. By contrast, Daltron and the other commercial ISPs principally provide dial-up

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<sup>8</sup> Clearance application page 11

<sup>9</sup> *ibid*, page 10

<sup>10</sup> Datec presentation, October 2004

internet services for individual (primarily small business and private) internet and email users<sup>11</sup>.

Internet operations in PNG are controlled through Tiare, a subsidiary of Pacific Mobile Communications Ltd, which is itself a wholly owned subsidiary of Telikom PNG Limited. Tiare operates the international telecommunications gateway for PNG and, through that gateway, the international data connections to the rest of the world. Tiare insists that all ISP's must route their traffic through the international gateway, even purely domestic traffic, with the result that there is no reason for an ISP to have various points of presence (POP) in different parts of the country to provide local call service to its customers, as occurs in most other parts of the world.

The outcome produces very high internet usage charges by world standards, exacerbated by the high charges imposed by Tiare on ISPs, which of course the ISPs pass on to their customers. For example, the price for 10 hours of internet in PNG is around K70, compared with a charge of about AU\$10 for 10 hours of internet connection in Australia. From the point of view of the ISP market, Datec maintains that the high charges from Tiare mean that the profit margins of all ISPs are very tight, with buyer resistance to having prices for consumers any higher than they are now.

A further important issue for ISPs is the severe shortage of bandwidth made available by Tiare for international data transmission. All ISPs require international data access if they want to give their customers access to the internet; an ISP without international data access would be confined to offering their customers domestic email only.

There are currently 8 megabits (Mb) of bandwidth made available for international data transmission to and from Papua New Guinea. This bandwidth is allocated among the four existing ISPs, with some capacity also being used by Unitech, and also Tiare for its small number of dial-up customers. In addition, some international bandwidth is used by Telikom itself for its own purposes.

That 8Mb is fully utilised – according to Datec, it is overutilised as the total amount of bandwidth utilised consistently exceeds the recommended maximum usage by a sizable margin. This is exemplified by the fact that in April 2004, when the available bandwidth was increased by 33%, from 6Mb to 8Mb, the extra bandwidth was immediately fully utilised.

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<sup>11</sup> Datec presentation, October 2004

Datec maintains that Telikom (or Tiare) could make extra bandwidth readily available for international data traffic, either by activating unused satellite capacity or by adopting some relatively low cost technical solutions to provide greater bandwidth using the existing links. The Commission has not been able to confirm with Telikom whether this is correct. However, the reality is that Telikom has not, to date, made extra capacity available above 8Mb.

### **Barriers to Entry**

The unavailability of international data bandwidth poses a virtually insuperable barrier to entry for any new ISP. As indicated above, any new ISP will need access to international bandwidth, and according to Datec, no bandwidth is available. Thus there appears to be little or no opportunity for any new ISP to set up in PNG in competition with the 4 existing ISPs.

The information provided by Datec about the lack of availability of bandwidth is consistent with what the Commission had heard from others in the internet industry, to the effect that there could only be four ISPs in PNG, without room for any more. As against that, some time ago the Commission heard suggestions that Telikom was considering starting its own ISP, in competition with the 4 existing ISPs. If that were to occur, Telikom could presumably find some additional international data capacity to satisfy the requirements of its own ISP, either from the bandwidth currently used by, or reserved to, Telikom and Tiare, or by utilising one of the techniques suggested by Datec as being available to Telikom to increase the existing 8Mb bandwidth.

Nonetheless, Telikom has not, to date, set up its own ISP. It is possible that one reason why Telikom has not started its own ISP is that, notwithstanding what Datec says, Telikom is not capable of finding sufficient bandwidth available on its international data circuits to give adequate bandwidth to its own new ISP.

### **Substantial Lessening of Competition**

In assessing whether the acquisition would or would be likely to result in a substantial lessening of competition, consideration should be given to factors such as those enumerated in section 69(5) of the ICCA Act and their application to the ISP market. Thus:

- Import competition is not relevant.

- Barriers to entry are, as outlined above, very high or even virtually insurmountable, unless one of the existing ISPs relinquishes some of its bandwidth, or a new entrant just acquires one of the existing ISPs.
- With only four firms in the ISP market, it is fairly highly concentrated and the merger of Datec and Daltron would result in there being only three left. In addition, the merged Datec/Daltron would have a share of about half the market, more or less, a high level of market power.
- Countervailing power in the market is limited. Small customers, who comprise most of the ISP market, have little countervailing power and with only four competitors, little alternative choice. Also, since changing ISP generally means changing email addresses, that is a constant disincentive to customers to move from one ISP to another. The large corporate customers which Datec specialises in have some countervailing power, but their options to move to a competing ISP are also limited.
- Substitutes are not realistically available.
- While the market is dynamic in some respects, it is not in others. The lack of bandwidth and the fact that the existing bandwidth is fully utilised, means that there is probably little incentive for the existing ISPs to aggressively compete to expand their customer base and market share, because the ISP would not be able to expand its existing allocation of bandwidth to accommodate those new customers.
- There is currently some vertical integration in the market through the ISPs all having association with computer sales, though the sort of vertical integration which might occur if Telikom were to enter the ISP market, has not occurred.
- As far as the Commission can tell, notwithstanding the serious constraints imposed by Tiare's limited allocation of bandwidth, the level of competition in the ISP market is reasonably good, though not perhaps in comparison to other countries where bandwidth is not a problem, where there is generally intense competition in the ISP markets. The Commission notes that Datec says that it proposes to operate Datec and Daltron as separate businesses, and this would certainly be the case with their ISP businesses. This is particularly so because Tiare will not permit ISPs to combine their

bandwidth<sup>12</sup>, which effectively means that, the Datec and Daltron ISPs must continue to be separately operated. While the Commission acknowledges that Datec may well continue to operate Daltron's ISP separately from Datec's that does not necessarily mean that they will have to continue to vigorously compete with each other. Firms under the same ownership rarely do. Datec has explained that its current ISP business is largely directed at large corporate customers, and is used principally to enable Datec to supply those customers with switched private network services; Telikom will not allow switched private networks to be operated by anyone other than ISPs. In this respect it does not compete directly with Daltron's ISP, which is directed principally at dial-up customers, not those seeking switched private networks. Overall, the Commission considers that the acquisition would, to some extent at least, be likely to remove a vigorous competitor.

In light of the matters discussed above, what would be the likelihood of the acquisition resulting in Datec being able to significantly and sustainably increase prices or profit margins?

On one hand, Datec would have significant power as the largest competitor in the market and would certainly be able to be the price leader. There would be no fear of additional ISPs coming into the market, with the possible exception of Telikom, and the other existing ISPs probably have all the customers that their bandwidth allocation can handle. Customers require ISP services and would have little countervailing power to resist price rises.

On the other hand, Datec points out that the high costs charged by Telikom mean that the opportunity for high margins in ISP business is not there because of customer resistance to higher prices, and the acquisition would not be likely to change that. Datec operates largely in a separate segment of the market, corporate private networks, which would be unaffected by the acquisition, so prices for that sector would not rise as a result. While the ISP market would be reduced to only three, the two remaining competitors would be expected to continue to provide a competitive constraint on any attempt by Datec to significantly increase its prices or margins.

## **Summary and Conclusion**

Datec and Daltron are competitors in a number of technology related markets. If Datec were to acquire Daltron, the merged firm would have a significant share in a number of those markets, and would be the largest

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<sup>12</sup> Steamships Ltd letter of 7 October 2004.

firm in some of them. That particularly applies to the PC and peripherals market. However, in all but the ISP market, there are factors, including the number of competing firms, the dynamic nature of the markets, ease of entry, import competition (in some markets) and the current level of competition, which indicate that the acquisition would not be likely to have the effect of substantially lessening competition in those markets.

In the ISP market, the barriers to entry are very high, because of the lack of availability of additional bandwidth. Thus one constraint on anticompetitive behavior is not available in the ISP market. That may be exacerbated by the remaining competitors utilising all of their available bandwidth, and thus perhaps having little incentive to aggressively compete to expand their market share. In that market, the merged firm would have at least a 50% market share, in a concentrated market of three firms only.

As against that, the existing ISPs do compete with each other, notwithstanding the bandwidth limits, and would be likely to do so after the acquisition also. The possibility of Telikom setting up its own ISP remains, especially since it can apparently overcome the lack of available bandwidth if it chooses. The lack of available international data bandwidth, which places an artificial competitive constraint on the ISP market, is an issue which the Commission will be raising with Telikom in the context of the likelihood in the near future of ISPs being required to obtain Value Added Services licenses under the *Telecommunications Act*. If additional capacity can be made available by Telikom, new ISPs will have the opportunity to enter the market.

The unavailability of bandwidth for new ISPs is likely to lessen competition. However, that lessening of competition occurs as a result of action by Telikom, not as a result of the acquisition of Daltron by Datec. In addition, much of Datec's ISP business is related to its provision of switched private networks for large corporate clients. This is a different market segment from the mainly dial-up internet customers which are the principal focus of Daltron and the other ISPs.

Having considered all the information available to it, the Commission considers that the acquisition would be likely to have the effect of lessening competition in the ISP market. Whether that lessening of competition would amount to a substantial lessening of competition, the Commission is at this stage unable to determine. As indicated earlier, the test for a clearance under section 81 of the Act is that if the Commission is not satisfied that the acquisition will not have, and will not be likely to have, the effect of substantially lessening competition in a market.

Based on the Commission's assessment of the competition effect of the proposed acquisition in all the relevant markets; and taking into account the non-exclusive factors under section 69(5) of the ICCA Act, the Commission is not satisfied that the acquisition will not be likely to have the effect of substantially lessening competition. Accordingly, the Commission must decline to give a clearance under section 81(3)(b) of the Act for the acquisition by Datec of Daltron.

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**Thomas Abe**  
**Acting Commissioner**

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**Paul Baxter**  
**Associate**  
**Commissioner**

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**Chris Gideon**  
**Associate**  
**Commissioner.**