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5. Author (s)

1. Idris F. Sulaiman
2.

6. Contributing Organization (s)

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During the first three quarters of 2003, the issues surrounding the new product *Telkom Flexi* ("TF" or "FLEXI") suggest that it is increasingly posing a serious threat to the competitiveness of non-incumbent telecommunication operators in Indonesia. FLEXI appears to not only aggravate further the already unlevelled playing field but also brushes aside the existing regulation and warnings from the regulator. There is every indication that the FLEXI rollout planned for urban areas is aimed mainly as a complementary product. Some announced pricing schemes for the Internet access are clearly giving FLEXI an added advantage and the rules governing local traffic will determine future competition. If this status quo is allowed to prevail, the likely outcome may not too different when Telkom introduced its Internet access "*Telkomnet Instan*" (or *T-Instan*) in 1999, in that such a new product will seriously affect its competitors. In the cellular market, FLEXI could rapidly reduce the market share of other GSM operators, particularly in Greater Jakarta and Surabaya Metropolitan areas. In the Internet access market, FLEXI could exert further pressure on the remaining ISP operators who have already lost much of their market shares as a result of T-Instan. Any failure to thwart it must mean that Telkom will increase its dominance over its GSM competitor further as well as threaten some ISP competing services. The real tragedy is that Indonesia's tele-density will not be significantly increased either, contrary to the regulator's expressed wishes in ironically allowing the introduction of FLEXI.

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C. Stuart Callison, Chief of Party
e-mail: stu@pegasus.or.id

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***Is Telkom-Flexi the new Telkom-Instan:
Can it level the playing field and bridge the digital divide?***

Paper presented at Telecommunications Committee Meeting, American Chamber of Commerce- Jakarta on September 18, 2003, part of several meetings towards a position paper on the “Telkom Flexi” product launch by PT Telkom and its Implications for the Telecommunications and IT Industries in Indonesia.

By Idris F. Sulaiman, USAID/PEG¹ ICT Advisor to the Ministry of Communications and Information and a member of Indonesia Info-Com Society, MASTEL <idriss@indo.net.id, idris@pegasus.or.id>

Summary

During the first three quarters of 2003, the issues surrounding the new product *Telkom Flexi* (“TF” or “FLEXI”) suggest that it is increasingly posing a serious threat to the competitiveness of non-incumbent telecommunication operators in Indonesia. FLEXI appears to not only aggravate further the already unleveled playing field but also brushes aside the existing regulation and warnings from the regulator. There is every indication that the FLEXI rollout planned for urban areas is aimed mainly as a complementary product. Some announced pricing schemes for the Internet access are clearly giving FLEXI an added advantage and the rules governing local traffic will determine future competition.

If this status quo is allowed to prevail, the likely outcome may not too different when Telkom introduced its Internet access “*Telkomnet Instan*” (or *T-instan*) in 1999, in that such a new product will seriously affect its competitors. In the cellular market, FLEXI could rapidly reduce the market share of other GSM operators, particularly in Greater Jakarta and Surabaya Metropolitan areas. In the Internet access market, FLEXI could exert further pressure on the remaining ISP operators who have already lost much of their market shares as a result of T-instan. Any failure to thwart it must mean that Telkom will increase its dominance over its GSM competitor further as well as threaten some ISP

¹ The Partnership for Economic Growth (PEG) is a United States Agency for International Development (USAID)-funded Project with the Government of Indonesia. The views expressed in this report are those of the author and not necessarily those of USAID, the U.S. Government or the Government of Indonesia.

competing services. The real tragedy is that Indonesia's tele-density will not be significantly increased either, contrary to the regulator's expressed wishes who ironically is allowing the introduction of FLEXI in the first place.

Regulations falling by the wayside

There is no doubt that Telkom is steaming ahead with its FLEXI roll out despite some regulatory challenges. A recent Communications Ministerial Decree (Keputusan Menteri Perhubungan KM 27/PR301/MPPT-98, 2003) stated that the maximum radius for wireless cellular is set at 50 Km such that this becomes the basis for the local zone area charge. While FLEXI clearly operates with the roaming facility outside this radius, Telkom knows that other cellular operators in practice are also setting their local zones wider than 50 Km. Hence, what is needed here is for the telecommunications regulator, the Directorate General of Post and Telecommunications (DGPT) to clearly define the local zone standard and fully enforce it such that all operators comply to a common set of standards.

Telkom appears to be enjoying special treatment notwithstanding the recent warning from the DGPT in a letter dated July 4, 2003². This letter stated that FLEXI cannot continue to have the roaming facility across base stations (Base Transceiver Stations, BTS). But Telkom seems to be able to continue the practice by arguing that FLEXI needs to be given special treatment because it is a fixed wireless product.

But the basic principle of fixed wireless is that the operator must apply the rule that a local zone charge will be set for a single BTS and that the local area limit fixed wireless is defined for an area of no more than 5-10 Km surrounding that BTS. While another small CDMA operator Ratelindo is forced to follow this rule, Telkom claims that because FLEXI is running the CDMA 2000-1X technology that is superior to both Ratelindo's

² Telkom is arguing that a number of other implementing regulations are required to enforce the letter from DGPT of July 4, 2003. The DGPT has also reiterated that the main purpose for introducing the Fixed Wireless Access is to increase the country's low tele-density.

older CDMA and other GSM operators' technology as well an overwhelming consumer demand, the special treatment for FLEXI can be justified.

To prove that there is a strong demand, Telkom claims that as of July 15, 2003, there are a total of about 45,000 FLEXI subscribers and 18,250 of them reside in Divre II (West Java areas surrounding Jakarta). Around 9,000 FLEXI lines are connected in Jakarta, 20,000 lines in East Java and 2,700 lines in Bali with 125 BTS are installed in Jakarta, 47 BTS in East Java and 7 BTS in Bali (Teknotel, Koran Tempo, July 16, 2003).

Serving the Urban Consumers' Interest

A strong urban focus of FLEXI is evident particularly for metropolitan Jakarta and Surabaya. Mr. Alex Sinaga, the Head of the Fixed Wireless Division of Telkom suggested that Telkom is planning to add 29 BTS to the installed 178 BTS by end of October 2003. Mr. Garuda Sugardo, Telkom's Director of Business Services announced however, that there is an even stronger focus on the Greater Jakarta area with 500 BTS (both micro for indoor and macro for outdoor) service will ideally be installed in this area (Bisnis July 16, 2003).

Actually, Telkom claims that since the rollout in Bali commenced earlier, the waiting list for FLEXI has reached 80,000 in Bali. Prior to its rollout in Jakarta, FLEXI has been promoted in Surabaya, Balikpapan, Batam, Makassar and Malang. Telkom is further planning to introduce FLEXI in Palangkaraya-Riau, Banjarmasin-Kalimantan, Medan and Palembang-Sumatra, Bogor, Bandung and Semarang.

It is a little wonder that Telkom can be very optimistic in setting a target of 727,000 lines by the end of 2003. By precisely using the argument that there is great consumers demand, Telkom can afford to take a very "Flexi ble" attitude toward any regulation or warnings from the regulator.

However, if Telkom and the regulators really want to take a good look at "consumer interests" then they should really spell out which consumers is FLEXI serving. What

Telkom is doing with FLEXI is really only adding the number of connected lines while not really significantly increasing the tele-density of each region where the rollout occurs.

The reason for this is not that there are current shortcomings in terms of technical problems such as a lack of coverage in some areas. FLEXI service will be improved with the wider coverage from the installation of more BTS and with the offer Internet connection. If we take a closer look at Telkom's strategy, it is clear that it is mainly targeting bigger cities for the FLEXI roll-out. Telkom is mainly aiming this product at people from the middle-class and above who already have cellular phones. As such TF, particularly in its current form as yet without some facilities (such as voice-messaging and the lack of SMS capability to other GSM cellular operators), is mainly a complementary, not the main cellphone for most of its new customers.

The new customers are not going to be located in the villages. As the total fixed lines (SST) installed by Telkom have now reached 7.8 million lines with 7.4 million subscribers and assuming Indonesia's population of 210 million people, the current tele-density stands at 3.7%. But in Indonesia, there are 72,000 villages outside the main cities with 43,000 of them (or 59.7% of the total) not even having access to a public phone. If most of BTS for the FLEXI service is mainly planned for the main cities where it is mainly being taken up as a second phone, then, there won't be any significant improvements in Indonesia's tele-density as a result of the introduction of TF. However, even if Telkom can come up with statistics to the contrary, not many of the 43,000 villages will be enjoying the benefits of TF.

However, Telkom need not worry too much because Indosat, the other telecom (formerly-state owned) company is also planning to make a foray into the lucrative CDMA market. Indosat is planning to launch its fixed-wireless CDMA product (in November delayed from August 17, 2003) in Jakarta and Surabaya. The company, which is now partly owned by ST Technologies of Singapore, is targeting 450,000 lines in Jakarta and 250,000 lines in Surabaya to be built by its 10-company consortium called Mega Asia Communications led by Bakrie Communications Corporation.

Other GSM operators will have to face tough competition as they are facing an increasingly unlevelled playing field. They have to pay roaming charges while FLEXI roams free. The GSM operators still have to abide by strict pricing rules while Telkom can charge FLEXI “Flexi bly” as it pleases with impunity. The regulator, the DGPT and the Business Supervisory Commission (KPPU - the independent government authority to implement and enforce the competition law) seem ineffective in curbing Telkom from practicing monopolistic acts in the past are unlikely to do so with respect to TF now.

Internet Services – entrenching Telkomnet Instan service?

There is no country in the world that offers mobile services for a fixed telephone price but in Indonesia this is made possible by FLEXI with an added bonus of cheaper mobile Internet access. Testing of TF’s Internet capabilities is already under way. Telkom announced that from July 10, 2003 the Internet access charges for FLEXI would be set at Rp 15 per kilo bit data transferred. The service will have the maximum speed of 150 kbps, about three times the standard theoretical maximum of 56 kbps enjoyed by the GPRS cellular operators. Operators such as the Indosat’s Multimedia Mobile service are currently charging Rp 20 – Rp 30 per kilobit data transferred data, almost twice of what FLEXI subscribers have to pay.

Meanwhile, ISP operators have been seeking clarification, but in vain, from Mr. Alex Sinaga, Head of FW Division on which specific ISP operators allowed to be connected to the TF’s Internet service.

Up until now, only Telkom’s Telkomnet Instan dial-up service enjoys instant billing access without the need to subscribe to Telkom’s ISP.³ While other ISPs have also been allowed to have instant billing access, their subscribers have to pay monthly fees. The

³ Note that Telkomnet Instan access is now charged at Rp. 165 per minute but the effective speed varies from around 20-45 kbps which contrast sharply with TF’s Internet effective speed of 128-153 kbps charged at Rp 15 per kilobit data transferred.

case of unfair competition filed against Telkomnet Instant to the KPPU and the Supreme Court by the ISP Association (APJII) met with little success.

Notwithstanding the announcement made by Mr. Sinaga, TF's Internet service is now already offered in the urban areas such as Jakarta. While the number of FLEXI subscribers who are accessing the Internet can now purchase a handset⁴ or PC-card (which provide their high speed broadband access at an average of 128 kbps) is now relatively small. But when the FLEXI subscriber base reaches significant level, if subscribers can have the existing advantages of Telkomnet Instan, then, this will only reinforce Telkoms' dominance of the ISP market (APJII estimates that to be over half of the total access to Internet are through Telkomnet Instan or T-Instan). ISP operators and would-be Wifi operators are fearing that what happened earlier to them as they watch a significant decline in their market share after the introduction of T-Instant could be repeated in the case of the introduction of Telkom Flexi with respect to the cellular operators.

Telkom is also offering another advantage to its FLEXI subscribers with the ability to SMS to 7.5 million Telkomsel subscribers which is currently under testing stage. With the exception of free SMS within the Division of Jakarta (Divre II), FLEXI subscribers will be charged Rp225 per SMS from July 2003. As of July 15, 2003, there are 45,000 FLEXI subscribers and 18,250 of them reside in Divre II.

Tariffs and Pricing – “Wolf in Sheep’s Clothing”

There are various ways to lower the cost of telephone calls besides TF. Competition among cellular operators has led to lower prices. Various operators, particularly those using GSM, are competing by widening the local zone area to increase their traffic.

⁴ Not all handsets can be used for Internet access for Telkom Flexi as Nokia and other handsets users have experienced difficulties.

Most however are targeting the local traffic and by using their own specific characteristics of their subscriber base, these GSM operators are widening their local zones in different ways. As an example, there is no operator who offers both Jakarta and Bandung under one local zone because there is heavy traffic between these two cities. FLEXI is also aiming to increase their share of the local traffic. By making one area code as home location register (HLR), FLEXI is hoping that many subscribers from other cellular operators will take up TF. The reason for this is that 80 % of cellular revenue comes from the local traffic. Based on 2002 earnings, the local traffic revenue came to a total of Rp. 10.4 trillion (or around \$1.2 billion).

FLEXI is not an economical option for long-distance (SLJJ) calls however. If a FLEXI subscriber is Jakarta-based but makes a call to Bogor which is outside his/her HLR, then SLJJ charges will apply which will certainly be higher than that if he/she uses a GSM cellular phone. According to the new tariff charges, SLJJ to Bogor is set at Rp. 1,789.70 per minute. This is higher than the new GSM charge of only Rp. 800-900 per minute. The operators are now treating Jakarta-Bogor as one local zone.

Within the new system, the cellular operators are looking at the inter-city SLJJ market. Estimates of this market segment are around 21 %. This means that the total revenue from fixed line subscribers of around Rp 15 trillion, Rp. 3.15 trillion comes from the SLJJ source. This may be targeted by cellular operators. Therefore, if they can withstand the competition from Flexi and if the DGPT enforces its warning (in the letter cited above) about the need to enforce higher roaming charges on TF, there is prospect of an improved competition not only in price but also in cellular service. But the current condition has been described by Dr Onno Purbo, a well-known commentator as patently “unfair and not gentlemen-like”. He describes FLEXI as “wolf in sheep’s clothing”.

Will the introduction of Telkom Flexi together with other CDMA services from Indosat and Ratelindo affect the competitiveness of GSM operators? This depends very much on whether the Government through the DGPT can issue clear regulation and enforce their directives. According to the published figures on the development of CDMA lines (SST)

planned by the three main operators, Telkom is targeted to build 1.2 million lines by 2007 while Indosat is to build 750,000 by 2010 and Ratelindo is to build 1.2 million by 2006.

It is approximated that by the end of 2003, the optimistic estimates of GSM operators claimed that there will be around 16-17 million cellular subscribers but the additional FLEXI CDMA lines could as much as produce a downward “correction” to around 15 million if there are no changes in the existing regulatory environment.

These are some major issues that need to be clarified on the eve of open competition in international (SLI) and inter-city (SLJJ) on August 1, 2003. Four key issues are Telkom-Indosat compensation, non-subsidized tariff scheme, Universal Service Obligation (USO) scheme and the fixed wireless regulation.

Conclusion

Without a firm regulator and transparent regulatory environment, some non-incumbent GSM (and even ISP) operators could see a significant reduction in their market share, particularly in the major cities. As the revenue of GSM operators fall, so too will be the non-tax earnings for the government collected through the licensing and frequency fees. As eighty percent of government’s earning in telecommunications comes from the local traffic source, there will be less revenue for the Government. While the target of Telkom Flexi and other CDMA operators appears to be existing GSM cellular subscribers in the main cities, there is little chance that Indonesia’s tele-density will be significantly increased, particularly in areas currently without access to telephony. Hence, unless the government steps in real soon to improve the competition regime, the scenario is set to further un-level the playing field and widen the digital divide.