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For the Week Ending October 13, 2006

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LATIN AMERICA ADVISOR | Telecom

Featured Q&A *With Our Board of Advisors*

Q Mexico last week implemented a plan allowing companies to offer so-called "triple-play" communications services of voice, television, and high-speed Internet. Do you think the plan will successfully spur greater competition in Mexico's telecom markets to the benefit of consumers? Why/why not?

A Board Comment: Janet Hernandez & Victor Mulas: "The secretary of Communications and Transport issued the 'Convergence Accord' to allow 1) Telmex and other minor local (wireline and wireless) exchange carriers to provide subscription television; and 2) subscription service providers (*e.g.*, cable, wireless, and satellite television operators) to offer local fixed-telephone service. Operators may offer these new services by requesting an expansion of their current licenses, provided that they implement number portability and comply with certain other conditions. Telmex, for example, cannot offer subscription television services until it has interconnected with any subscription television provider that seeks to provide fixed local services. These obligations are intended to foster multimodal competition by allowing subscription television operators to enter the fixed market, currently dominated by Telmex. However, this Accord does not address certain crucial issues. First, it does not establish any safeguards to prevent big players, such as Telmex, from using their market power and financial capabilities to obtain exclusivity rights over premium content (such as sport channels) to the detriment of small subscription television operators. Second, the Accord does not include mobile operators, thereby maintaining a technology-discriminating regulation (especially with regard to trunking operators that are unable to obtain full interconnection). Finally, the Accord does not establish the amount that Telmex must pay to the government for eliminating the prohibition to provide subscription television services from its license. The government has indicated that these issues require further study. The outcome of these studies will be crucial for the success or failure of a competitive market in convergent services. This Accord is a good measure insofar as it eliminates certain artificial entry barriers in Mexico's fragmented telecommunications market. However, it does not eliminate the exist-

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PHOTO OF THE WEEK

Brazilian Communications Minister Helio Costa announced that after six years the government would finally start spending its universal service fund. See story on page 2.

Photo: Agencia Brasil.

Inside This Issue

INDUSTRY BRIEFS

Cofetel: Mexican Telecom Sector Grew 17.9 Percent YoY in Q2

Mexico's telecommunications sector grew 17.9 percent in the second quarter of this year compared to the same period of 2005, telecom regulator Cofetel said Tuesday. Cofetel said trunking grew 33.3 percent year-on-year during the quarter. Mexico had more than 51 million mobile subscribers and 19.9 million fixed lines at the end of the second quarter, Cofetel said.

Telefonica Names New Head of Operations in Argentina

Spain's **Telefonica** announced Wednesday that Eduardo Caride would replace Mario Vazquez as head of its operations in Argentina. In a press release, Telefonica said Vazquez, who is stepping down from the post at the end of this year, will continue as a member of the board of **Telefonica Latinoamerica** and other affiliated companies, as well as president of **Fundacion Telefonica** in Argentina. Caride, who has served as president of the southern cone for **Telefonica Moviles** for the past two years, will also head Telefonica's operations in Uruguay.

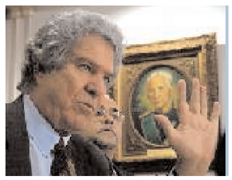
Judge Grants Bankruptcy Protection to Mexico's Iusacell

A Mexican judge on Wednesday granted bankruptcy protection for **Iusacell**, the country's third-largest mobile operator, as part of the company's debt restructuring, Iusacell said in a press release. The mobile operator said the judge's declaration brings it closer to executing the restructuring of some $416 million in debt. Iusacell, which was bought by Mexican tycoon Ricardo Salinas in 2003, is focused on corporate customers and higher-income subscribers.

Industry News

Brazil to Spend $352 Million on Universal Service Projects

Brazil will invest 757 million reais ($US 352 million) over four years in social programs that expand telecom services to low-income groups, the country's first dip into its 5 billion-real Telecommunications Universal Service Fund (FUST), Communications Minister Helio Costa announced Wednesday, according to state news service Agencia Brasil. Costa said that FUST monies, collected via a 1 percent tax on telecom providers' gross income, would be disbursed through a government agency, the Tribunal of Accounts, which is responsible for overseeing official spending. Service providers in Brazil have long complained about the government's failure to disburse the universal service funds. In January, the country's biggest fixed-line service providers sought an injunction against an increase in the universal service tax, partly on the grounds that since the FUST's creation six years ago not a cent had been spent on projects. Analysts told the *Telecom Advisor* in January that the government may have been reluctant to use FUST monies for several reasons, including the desire to keep the money in fiscal accounts and help reduce the government's overall fiscal deficit, and the lack of viable programs on which to spend the funds [Editors' note: see related Q&A in the January 20, 2006 issue of the *Telecom Advisor*]. Costa said Wednesday that seven projects were chosen for the funds, divided into two groups. The first group will receive 512 million reais for programs that expand fixed-line access, divided among programs for health care, schools, and institutions that work with people with disabilities. The second group will receive 245 million reais for programs expanding broadband access, divided among programs for municipalities, schools, and job training for people with special education needs. Social programs that expand high-speed Internet access are a good use of this type of government-controlled fund "because they target customers that existing operators have largely abandoned," Wally Swain, principal analyst for Latin America at **The Yankee Group** and a member of the *Telecom Advisor* board, told the *Telecom Advisor* in January. However, Swain also noted that there is debate about the effectiveness of direct subsidy programs. "Some suggest that the explosive growth of mobile communications has already done more for universal access than any government-sponsored program, and so the public good would be better served by lowering mobile prices through elimination of the universal service tax," he said.



Costa

Photo: Agencia Brasil.

Service providers in Brazil have long complained about the government's failure to disburse the universal service funds.

Mexico's Cofetel Says 11 Service Providers Agree to Calling Party Pays

Mexican telecom regulator Cofetel said Wednesday that 11 fixed-line and mobile operators had agreed to implement a national "calling party pays" system. In a press release, Cofetel said the fixed-line and mobile operators, which include fixed-line giant **Telmex** and its dominant mobile affiliate, **Telcel**, had agreed to implement calling party pays starting on November 4. The operators account for more than 90 percent of the combined fixed and mobile customers in Mexico, according to the regulator. Last month, five Mexican fixed-line operators—**Alestra**, **Bestel**, **Axtel**, **Protel**, and **Maxcom**—won an injunction against the implementation of a national calling party pays system. The five companies say they are not opposed to the idea of calling party pays, but that fixed-mobile interconnection rates being implemented in tandem with the system are unfairly high. Last month, Cofetel announced a gradual reduction in the rates Telcel—which has about 80 percent of Mexico's 51 million mobile subscribers—could charge fixed-line operators Alestra, **Avantel**, and Axtel to terminate calls on Telcel's network, from a current rate of 1.54 pesos ($US 0.14) per minute to 0.90 pesos by 2010. One of the companies, Alestra, said the rates were still too high and that they should be set at less than half the lowest rate that mobile companies charge their own customers. Alestra said that the scheme established by Cofetel is discriminatory because fixed-line customers have to pay twice as much—or about two pesos—to call mobile customers as it costs mobile customers to call each other. In its press release on Wednesday, Cofetel said that the operators agreeing to implement calling party pays had also agreed to the 1.54 pesos per minute fixed-mobile interconnection rate.

Telecom Italia to Transfer its Stake in Brasil Telecom to Blind Trust

Telecom Italia said Monday it plans to transfer its stake in **Brasil Telecom** to a blind trust as a prelude to an eventual sale of the stake, Dow Jones reported. In a plan submitted to Brazilian telecom sector regulator Anatel, Telecom Italia said it would transfer its 38 percent stake in **Solpart**, a holding which in turn has 51 percent control of Brasil Telecom, into a newly created blind trust called Brasilco S.r.l. The blind trust will be managed by **Credit Suisse**, which will be charged with selling the stake to a third party, according to Dow Jones. A blind trust is a financial arrangement through which an individual or a company can avoid a possible conflict of interest by ceding control of the assets to a fiduciary while at the same time giving up the right to information about the status of the assets. Anatel has given Telecom Italia until October 28 to shed its stake in Brasil Telecom to comply with rules barring one company from having interests in competing mobile operators. Brasil Telecom's mobile unit competes with Telecom Italia's mobile affiliate in Brazil, **TIM Brasil**. Last month, Brazilian conglomerate **Grupo Algar** said its telecom subsidiary, **CTBC**, was in talks to buy Telecom Italia's stake in Brasil Telecom. Also last month, the board of debt-ridden **Telecom Italia** approved a plan to separate its fixed-line and mobile operations, giving rise to speculation that TIM Brasil, Brazil's second-largest mobile operator, would be sold. However, analysts say financial and regulatory issues represent important hurdles to a potential sale [Editor's note: see related Q&A in the September 22, 2006 issue of the *Telecom Advisor*].

Alcatel to Support Telefonica's LatAm Broadband Transformation

French communications equipment provider **Alcatel** announced Monday it will support a broadband network transformation project in Spanish **Telefonica**'s Latin American markets. In a statement, Alcatel said it will help Telefonica offer higher bandwidth capacity to clients in Latin America based on each country's stage of broadband deployment. Alcatel will provide solutions for Telefonica's access, Metro Ethernet, IP edge and optical transport networks that will enable personalized multimedia services such as video on demand, high-definition TV, and IPTV for both residential and enterprise customers. Telefonica recently selected Alcatel to undertake a similar network transformation in Spain. Financial details of the agreement were not disclosed. Paris-based Alcatel has operations in 130 countries. The group posted second-quarter revenue of 3.38 billion euros ($US 4.24 billion), up from 3.15 billion euros for the same period of 2005.

Brazil's Net to Acquire Main Local Rival Vivax

Brazil's biggest cable TV operator, **Net Servicos de Comunicacao**, announced Thursday it had concluded an agreement to buy a minority stake in and later take control of its main rival, **Vivax**. The two companies said the acquisition would have to be done in two phases because the second phase involves a change in control and therefore must be approved by the government telecom sector regulator Anatel. Vivax is estimated to be worth around 1.45 billion reais ($US 672 million), according to sources cited by Reuters. Net, which is controlled by the **Globo** media group and by long distance operator **Embratel**, said that as a result of its acquisition of Vivax its share of the pay TV market in Brazil would rise to 45 percent from 38 percent, while its part of the broadband sector would rise to 14 percent, from 12 percent, according to Reuters. As of June 30, the companies had a combined 1.98 million pay TV customers, 638,000 broadband subscribers, and 49,300 fixed line telephone customers. Net said the purchase of Vivax, whose main market is in Brazil's wealthiest state, Sao Paulo, would expand its coverage to 8.4 million homes in the richest parts of Brazil. Vivax is the sole cable TV operator in 32 out of the 34 cities in which it has concessions.

Net and Vivax Combined Assets as of June 30

Pay-TV Subscribers (thousands)	1,975
Broadband Subscribers (thousands)	638.4
Voice Subscribers (thousands)	49.3
Revenues (millions of Brazilian reais, H1 06)	1,060
EBITDA (millions of Brazilian reais, H1 06)	306.3

Source: Net.

Media Industry News

Televisa to Sell its 11 Percent Stake in Univision

Mexican broadcaster **Televisa** plans to sell its 11 percent stake in US Spanish-language broadcaster **Univision**, Televisa Chairman Emilio Azcarraga said Tuesday, according to Reuters. The announcement follows Televisa's decision late last month to abandon its efforts to bid for Univision through a consortium, saying it could not beat a rival group's $12.3 billion offer. In June, Televisa had offered $12.1 billion for Univision. Televisa provides 90 percent of the US broadcaster's programs as part of a deal that expires in 2017, but the relationship between the two countries has been marred by accusations and lawsuits. Despite failing to offer the winning bid for Univision, analysts expect Televisa will still seek to enter the US market, just as US-based and other companies are seeking to enter Mexico's television market. Asked what Televisa planned to do with the proceeds from the sale, Azcarraga said "we have been very careful with money and obviously our Televisa shareholders are the most important to us," according to Reuters. Azcarraga said the funds could be used for a dividend. Analysts estimate Televisa would receive at least $1 billion from the sale of its stake in Univision.

Political News

Correa Heads Into Sunday's Vote in Ecuador with Strong Lead

Left-leaning Ecuadorean presidential candidate Rafael Correa heads into this Sunday's election with a strong lead over his rivals, although he may not garner enough votes to avoid a run-off. The latest poll, by **Informe Confidencial**, found that 30 percent of intended voters support Correa, versus 23 percent for banana magnate Alvaro Noboa and 19 percent for center-left Leon Roldos, according to Reuters. As much as a third of voters are still undecided. To win in the first round outright, a presidential candidate must have either 50 percent plus one of the eligible votes or at least 40 percent of the valid votes and a 10 percentage point margin over the the second-place candidate. "Our information is confirming the election will be resolved in just one round," Correa was quoted as telling reporters. However, he hinted there could be attempts to block his victory in the first round through fraud. Investors are worried about the possible election of Correa, who has said he would consider restructuring the country's debt. However, some analysts say the US-trained economist's policies will likely be more moderate than his populist rhetoric. [Editor's note: look for a Q&A on the outcome of Ecuador's presidential election next week in the *Advisor*.]

Peru's Garcia Meets with Bush; Leaders Discuss Trade, Drugs

Peruvian President Alan Garcia met with US President George W. Bush at the White House on Tuesday, with both leaders expressing support for a proposed bilateral free trade agreement and continued cooperation in the war on drugs. "The central issue facing us right now is the passage of a free trade agreement," Bush told reporters, according to a transcript posted on the White House's Web site. "I assured the president that I will work with Congress as soon as possible to get this agreement passed." US and Peruvian negotiators concluded talks for a free trade agreement last December. Peru's legislature has approved the deal, but US congressional leaders have signaled that it, and a separate free trade agreement with Colombia, will not see a vote in Congress until next year. US trade preferences for exports from Peru, Colombia, Bolivia, and Ecuador will expire at the end of this year unless they are renewed by Congress. Garcia said Tuesday he was "very satisfied" to hear Bush's promise to work toward passage of the trade agreement, which he said Peru would use to fight poverty, strengthen equality, and achieve security through democracy. The Peruvian leader also said that his government would "at some point" propose a high-level meeting on drug eradication efforts. The meeting's purpose would be "to relaunch the fight against drugs, in terms of offering other alternatives, such as alternative development, and the free trade agreement is one of these tools," Garcia said.

Garcia and Bush at the White House

Photo: White House.

Chavez Vows to Defend Bolivia's Morales from Coup

Venezuelan President Hugo Chavez vowed Wednesday to come to the defense of his Bolivian ally, Evo Morales, if Morales were to be ousted in a coup, the Associated Press reported. "Venezuela will not keep its arms crossed if the Bolivian government and people are attacked from outside or within," Chavez said in a televised speech, without elaborating on what actions he might take. The Venezuelan leader repeated allegations that the US was backing efforts to unseat Morales. He has accused the Bolivian opposition, the media, and the US Embassy in La Paz of trying to foment unrest in Bolivia to justify Morales' removal. US officials have denied that they are plotting coups against either Chavez or Morales, both of which have been staunch critics of the Bush administration. Chavez's warnings follow a threat last week by leaders in Bolivia's four wealthiest provinces that are opposition strongholds to disregard proposed constitutional reforms. The leaders in Santa Cruz, Tarija, Beni, and Pando provinces said they would disobey the Constitution if reforms currently being debated by a constitutional assembly were passed by a simple majority, rather than a two-thirds majority, or if the new Constitution implied a total reshaping of the state.

Striking Teachers in Oaxaca Reject Return of Police to City

Striking teachers in the Mexican city of Oaxaca have rejected a proposal to allow police back into the city, dashing hopes for a quick end to five-month-old protests in the city, the Associated Press reported on Thursday. The teachers said they would not consider the proposal to allow local police back into the city under federal command until Mexico's Senate rules on their main demand—the resignation of Oaxaca state Governor Ulises Ruiz, who they accuse of rigging his election in 2004 and unleashing armed gangs against his opponent. A group of senators are expected to visit Oaxaca today to determine if the state government has lost control, a finding that could allow the Senate to remove Ruiz from office, according to the AP. However, the Senate group may postpone the visit amid a resurgence in violence in the city. Yesterday, gunfire broke out when protesters, armed with clubs and rocks, tried to seize the offices of a public safety agency. Four protesters suffered gunshot wounds when police inside the agency building fired at them, local daily *El Universal* reported. Protesters have taken to the streets of Oaxaca since May to demand Ruiz's removal, setting up barricades, seizing media outlets, and burning buses in the city, which has reportedly lost millions of dollars in tourism revenue because of the unrest.

Economic News

Mexico's Calderon Presents Long-Term Economic Strategy

Mexican President-elect Felipe Calderon on Tuesday outlined an ambitious long-term vision for Mexico, saying that Mexico could become one of the 10 most powerful countries in the world by the year 2030 if economic reforms are adopted. "If we undertake the task of our generation, we could achieve by 2030 income close to $30,000 per person, comparable to what the world's developed economies have today," Calderon told an audience at Mexico City's World Trade Center, according to a transcript of his speech posted on his official Web site. "But if we do nothing, even without an economic crisis, reaching these income levels will take us almost 60 more years," he continued. Calderon said Mexico's economic development depended on the country's ability to do a number of things, such as educating its workforce to boost productivity, expanding infrastructure, reducing poverty, providing housing, and managing water resources, among others. The conservative Calderon, who was elected after narrowly defeating left-leaning Andres Manuel Lopez Obrador in Mexico's July 2 election, takes office on December 1. In related news, the International Monetary Fund said Wednesday that the incoming government should implement structural reforms to ensure economic growth, according to Reuters. In its annual report on Mexico's economy, the IMF encouraged tax reform, stressed more targeted social and investment expenditure, and recommended that Mexico's state-owned oil company, **Pemex**, improve its governance and share risk with the private sector.

Argentine Supermarkets Agree to Extend Price Freeze Through 2007

Major supermarkets in Argentina agreed Monday to extend through the end of next year a price freeze for hundreds of goods to help the government contain inflation. Secretary of Commerce Guillermo Moreno said the biggest supermarket chains operating in the country, including **Carrefour**, **Jumbo**, **Coto**, **Wal-Mart**, and others had agreed to extend the 11 month-old price-freeze pact, which was set to expire at the end of this year, local daily *La Nacion* reported. The agreement came after a meeting of representatives of the supermarket chains with President Nestor Kirchner, Economy Minister Felisa Miceli, and Moreno. Striking price-freeze agreements with retailers has been a major component of the Kirchner government's efforts to combat inflation, which is hovering above an annualized rate of about 10 percent. In a research note published on Tuesday, **Credit Suisse** said the goods covered in the price-freeze accord with supermarkets number 300, "a small proportion of the 10,000-15,000 products that these establishments carry." Credit Suisse added that "the supermarkets' decreased profits due to these measures should be relatively limited, and maintaining a good working relationship with the government by complying with the controls could be important." Moreno said that "Kirchner is very satisfied with the conduct of our supermarkets, and the businessmen know the good of these types of policies that we are carrying forward."

POLITICAL & ECONOMIC BRIEFS

Two New Polls in Brazil Confirm Lula's Lead Over Alckmin

Two polls in Brazil released Thursday confirmed President Luiz Inacio Lula da Silva's strong lead over challenger Geraldo Alckmin ahead of an October 29 presidential run-off vote, Reuters reported. A survey by polling firm **Ibope** gave Lula a 14-point advantage over Alckmin, while a **Vox Populi** survey gave Lula a 10-point lead. A **Datafolha** poll published on Wednesday showed Lula with an 11-point lead.

Chilean Central Bank Holds Interest Rate at 5.25 Percent

Chile's Central Bank said Thursday it would hold its benchmark lending rate at 5.25 percent and that future rate hikes may not be needed for a "prolonged period" because of signs inflation is under control. In a press release, the bank said lower-than-expected fuel prices were contributing to inflation levels below projections. The Bank said it expects inflation to continue at around 3 percent in the medium and long term.

Mexican Authorities Investigating Possible Hezbollah Financing Cell

Authorities in Mexico are investigating the possible existence of a financing cell in the country linked to the Iranian-backed Hezbollah terrorist organization, Mexican daily *El Universal* reported on Thursday. The investigation is being undertaken at the request of the US government, which tipped Mexico off to a web of businesses that may be a source of financing for Hezbollah. The names of the individuals or companies under investigation were not made public.

Featured Q&A

Continued from page 1

ing fragmentation of the administrative procedures to provide convergent services and maintains crucial, open questions and technology-discriminating issues (*e.g.*, trunking services) that still require resolution."

A **Board Comment: Tim Perrott:** "Any environment that provides additional flexibility for incumbent companies to provide more services should be a positive for consumers and the markets alike. This flexibility can often be a catalyst for providers—both carriers and content providers—to bring more relevant products, services, and interesting content to those who demand these types of services. In the near term, however, demand for higher-speed broadband applications remains anemic at best, and stimulating demand for high-speed internet access—fixed or wireless—will be key over the long term to encourage companies to make the investments in broadband networks and become triple-play providers. In the very near term, I do not believe that the new plan to allow companies to offer the triple-play services will significantly impact competition in the telecom market. The market should not react very quickly to this added flexibility, although we could see some small level of consolidation during this period, as those who desire to play in this space bring the expertise 'in-house.' However, in the long run—several years in the future—I believe that the added flexibility will attract companies seeking to add additional high margin revenue streams to their businesses (*i.e.*, more opportunities for telecom providers) which could lead to more competition among the lucrative businesses that are today more or less monopolies. The level of attractiveness of triple-play operators will largely depend on the anticipated capital investment in the infrastructure, health of the economic environment, demand for higher-speed services, development of relevant content, and the expected returns anticipated by those companies wishing to play in this environment. Increasing the number and quality of content providers and capable infrastructure—along with an acceptable level of customer demand and willingness to pay for these services—will be a key factor in developing this market and increasing the opportunities for telecom providers and thus the level of competition."

A **Guest Comment: Jose Ignacio Crujeiras:** "First, it is likely that this agreement will permit technological progress in the country, which will be reflected in the quality and diversity of services. Moreover, this plan could contribute in the reduction of rates for services due to an intensified competitive environment in the market. This accord is likely to foster the entrance of new players, with new offers that could be more attractive to end users. Also, the agreement could work as a tool to allow higher penetration in diverse niches, as well as accessibility and the offer of new and sophisticated technologies. In addition, it could allow users in restricted or rural areas to obtain the benefit of these types of services for the first time. For current users, this is an opportunity to select the best operator and to acquire the three services from just one provider at a much lower price. Nevertheless, stronger regulation is required, and there are still issues, such as interconnection and spectrum distribution, that have to be considered as well. Surely this new alternative will place Mexico as a more prepared and competitive market in the region."

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