

Incentivising infrastructure investment in a competitive market

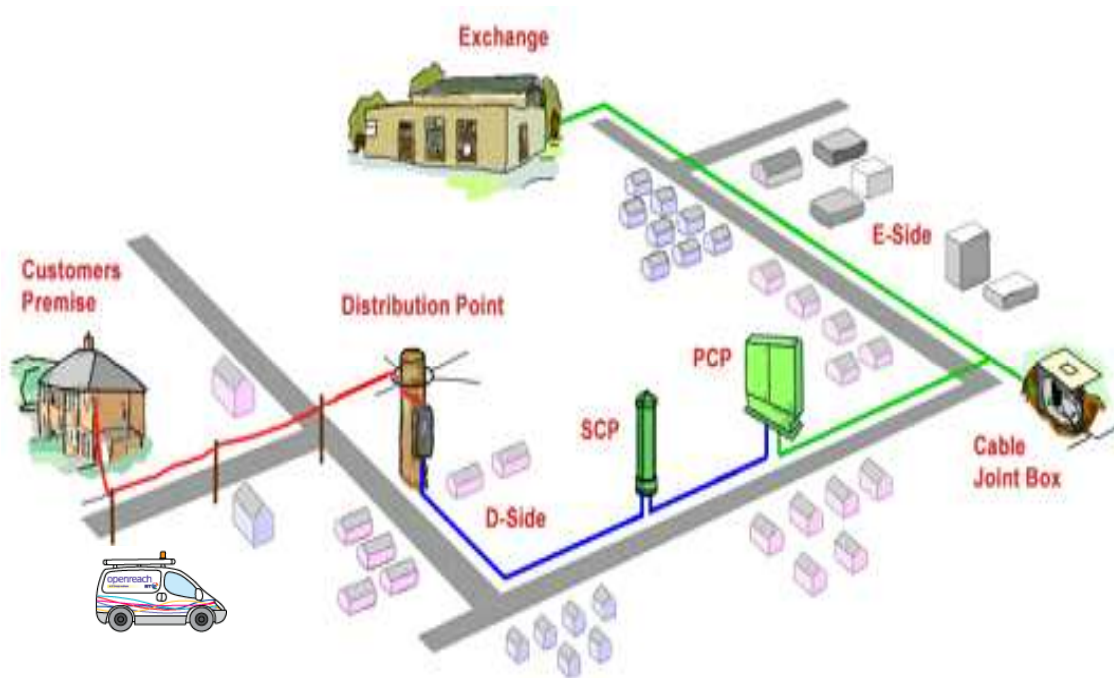
Alan Lazarus

RPI Conference

14th September 2010



Openreach: BT's access and backhaul business

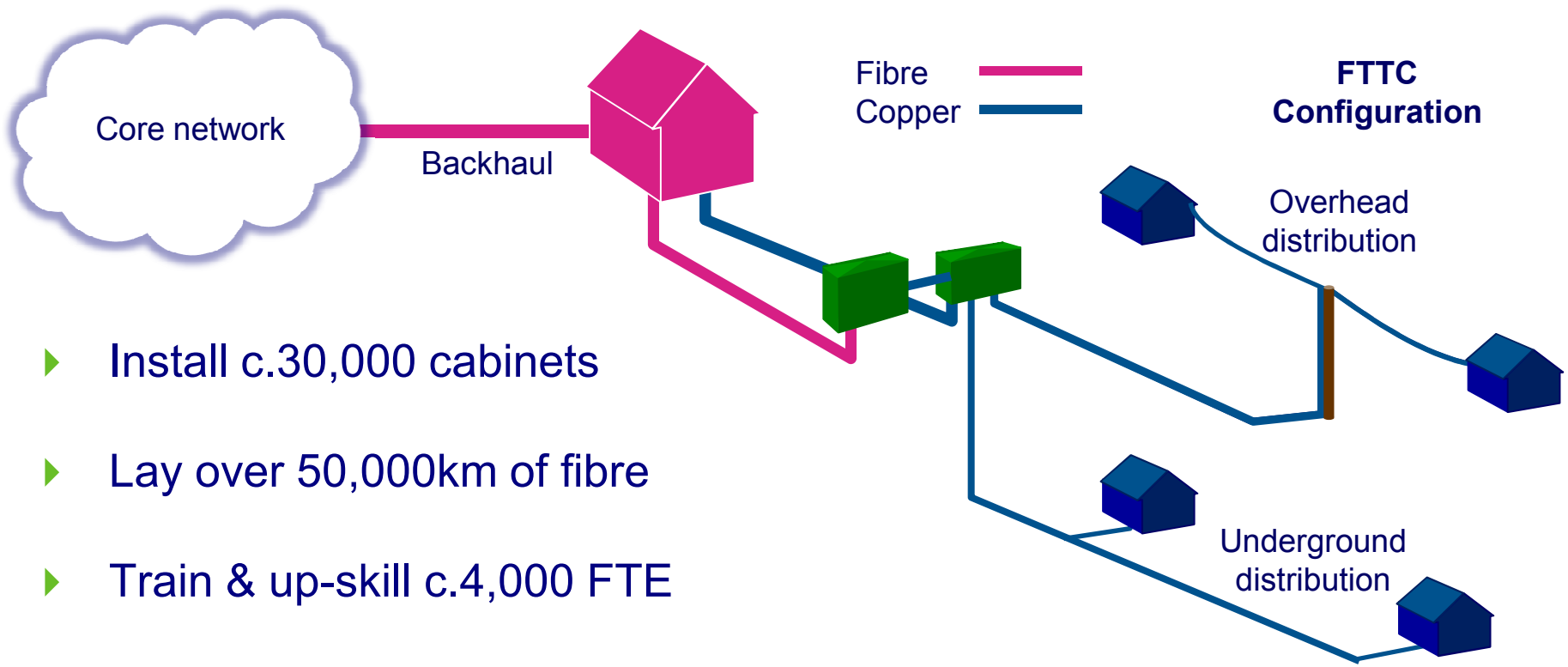


- ▶ £5bn revenue
- ▶ 32,000 employees
- ▶ 480+ industry customers
- ▶ 4.4m home visits a year
- ▶ c.£10bn assets (CCA)
- ▶ >24m end user connections

So is BT a utility?



Creating our super-fast fibre access network




- ▶ Install c.30,000 cabinets
- ▶ Lay over 50,000km of fibre
- ▶ Train & up-skill c.4,000 FTE
- ▶ Enable over 1,000 exchange areas

1.5m premises passed by early summer 2010



4m premises passed by end of 2010



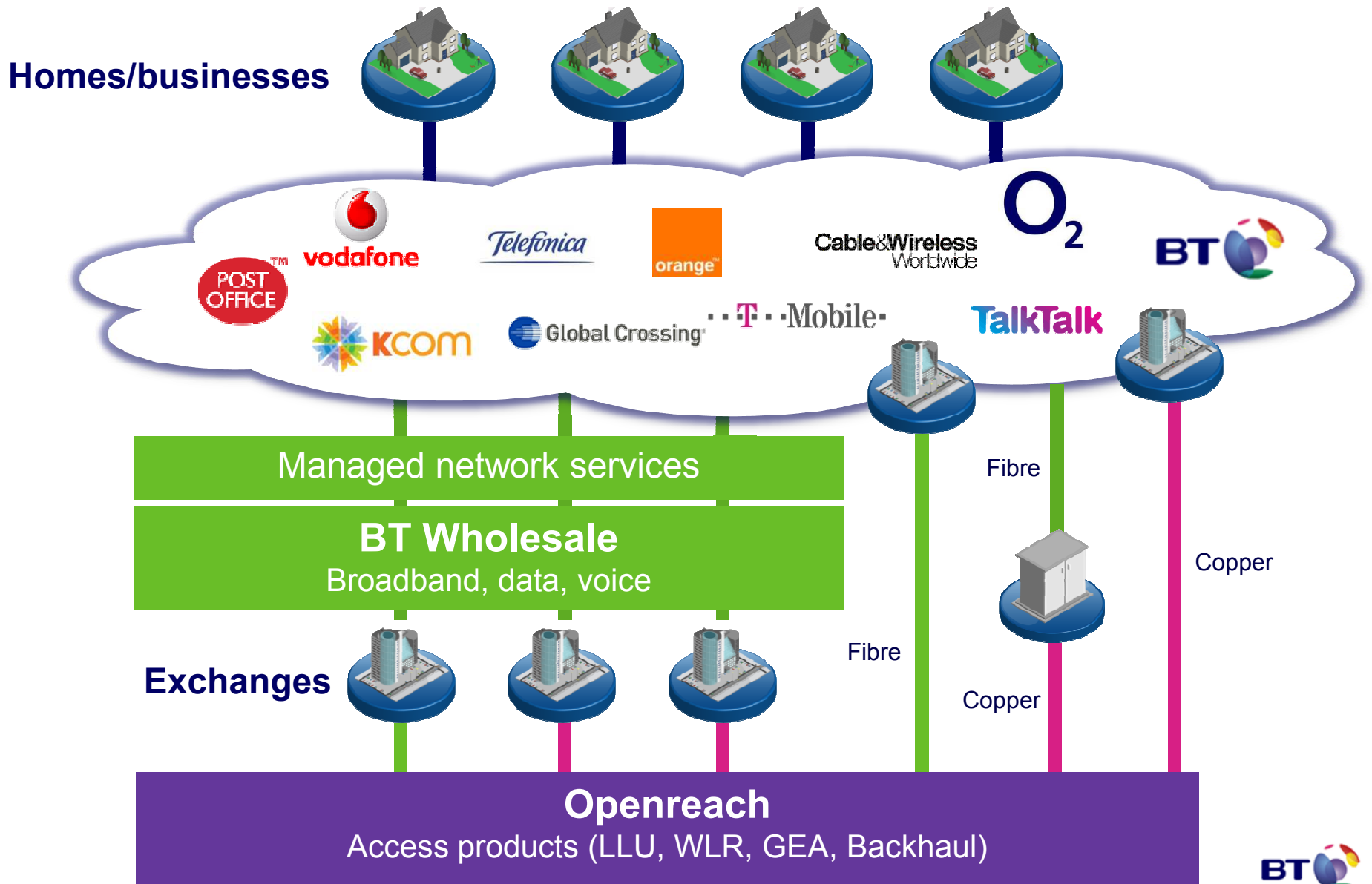
10m premises passed by 2012



2/3 of UK premises passed by 2015



Telecoms in the UK has a vibrant wholesale market



The most open market in the world

We provide many points of wholesale access to our infrastructure

NGA

- ▶ GEA
- ▶ SLU
- ▶ Duct
- ▶ Wholesale SFBB

Broadband

- ▶ MPF & SMPF
- ▶ WBC
- ▶ IPStream
- ▶ WiFi / Openzone

Voice

- ▶ CPS
- ▶ Indirect Access
- ▶ Wholesale Calls
- ▶ WLR



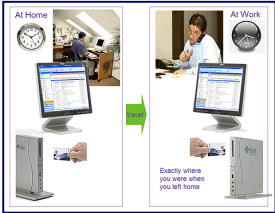
Leading to one of the most competitive marketplaces in the world



Our industry is converging on a multi-layer structure



The evolving role of regulation

<p>Ongoing challenge of investment and competition</p>	<p>Changing competitive market and difficult economy</p>
<ul style="list-style-type: none"> ▶ Equivalence ▶ Open Access ▶ Rewarding risk ▶ Climate for investment 	<ul style="list-style-type: none"> ▶ New incumbents ▶ Reduced new build ▶ Fewer connected lines
<p>Changing user requirements → converging industry</p>	<p>Changing portfolio mix as old products retire</p>
<div style="display: flex; justify-content: space-around; align-items: flex-start;"> <div style="text-align: center;"> <p>Mobile</p>  </div> <div style="text-align: center;"> <p>Content</p>  </div> <div style="text-align: center;"> <p>Fixed</p>  </div> </div>	<div style="display: flex; justify-content: space-around; align-items: center;"> <div style="text-align: center;"> <p>↓ WLR</p> <p>↓ ISDN</p> <p>↓ Private circuits</p> </div> <div style="text-align: center;"> <p>↑ LLU</p> <p>↑ Fibre</p> <p>↑ Ethernet</p> </div> </div>

All we can be sure of is that the future is largely unknown....

- ▶ *"This 'telephone' has too many shortcomings to be seriously considered as a means of communication. The device is inherently of no value to us."*

Western Union internal memo, 1876

- ▶ *"I think there is a world market for maybe five computers."*

Thomas Watson, chairman of IBM, 1943

- ▶ *"There is no reason anyone would want a computer in their home."*

Ken Olson, president, chairman and founder of Digital Equipment Corp., 1977

- ▶ *"640K ought to be enough for anybody."*

Bill Gates, 1981

- ▶ *"There will be a UK market of approximately 500k connections."*

BT Cellnet projections of the emerging mobile market, 1985



Fibre – the investment challenge

- ▶ BT has already announced plans to spend £2.5bn on reaching 66% of UK
- ▶ But demand is uncertain
 - No killer applications - IPTV less a driver in the UK
 - Consumers' willingness to pay a premium unclear
 - Public value but how do you monetise?
- ▶ Major supply-side challenges - network topology and state of ducts 'subject to survey'
- ▶ Copper wholesale products are underpriced
 - Weakens incentives to migrate to fibre
- ▶ Fibre cut-over an unknown quantity
- ▶ Regulatory uncertainty
 - Long pay-back s vs short market review periods



Would a different regulatory approach help?

- ▶ Utility price control models – RPI+k ? RIIO ?
 - Requires regulators' oversight (control?) of investment plans
 - Can these work with multiple layers of competition and without homogenous products?
- ▶ Can RPI-x be modified?
 - Treatment of common costs, risk and efficiency factors
 - Better regard of future transition/substitution issues
 - Proposed (previously) new Ofcom duty to 'promote investment'
 - Approach needs to be 'appeal-proof'
- ▶ Can/should competition be supported by regulation at every level?
- ▶ How can greater regulatory certainty be given?



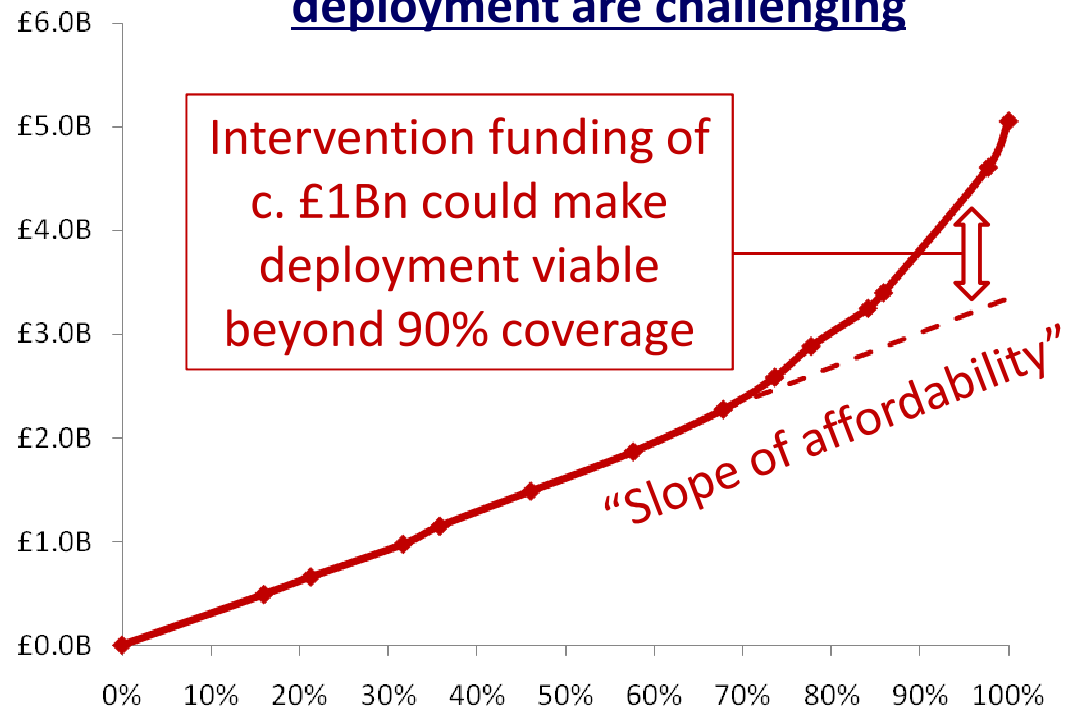
Will fibre go beyond 2/3 of the UK ? – raises even harder commercial and regulatory questions

- ▶ The single most important factor: *that customer take-up makes fibre a success*
 - Demand for speed
 - Importance of the TV triple-play
 - Assisted funding

We are open to innovative business and operational models

- ▶ Local partnerships....
- ▶ ...but avoiding micro-monopolies which will suppress customer choice

The economics of Final Third deployment are challenging



Source: Analysys Mason

