

by Brian Williamson

# News analysis

## *Laying the foundations for a new regulatory paradigm in Europe*

### The fibre investment problem

Europe has seen a protracted debate about the policy foundations for investment and competition during the transition from copper to fibre networks. This is best understood in the context of the existing approach which is focussed on entrant based competition via cost oriented access to copper.

Whilst the rhetoric of the "ladder of investment" may have sustained a belief amongst regulators that they could have their cake and eat it, investors did not in general concur. It has therefore become clear that the principles and practice of regulation conceived for a world in which copper access infrastructure already exists are not fit for purpose if one wishes to see a transition to fibre.

The concept of cost orientation is both difficult to apply in practice to a new technology with uncertain demand, and inimical to efficient investment. However, the success of the previous approach in motivating broadband take-up and upgrades (albeit in a different static context) and the interests of copper based entrants who had little appetite for climbing the "ladder of investment" have led to a drawn out and (at times) bizarre policy debate about what to do. In particular the idea that cheaper copper might actually

promote fibre investment has taken time to root out.<sup>1</sup>

### The proposed approach to copper and fibre regulation

The European Commission have now moved decisively in favour of a fresh approach emphasizing price flexibility for fibre and price stability for copper – firmly rejecting the notion that more of the same is appropriate under different circumstances.<sup>2</sup> Neelie Kroes' recent conclusion in relation to copper pricing and the proposed approach in relation to fibre were:

- » "The evidence shows that lowering those [copper] prices will not induce greater investment in very fast broadband."
- » "More flexibility [is required] on how 'next generation' wholesale products can be priced: subject to meeting strict conditions to ensure fair competition."

It was also made clear that next generation broadband was the objective, not fibre *per se*, and that copper-fibre hybrids including cable and fibre to the cabinet as well as wireless can be expected to play an important role in delivering high

speed broadband on a timely and cost effective basis.

It was further proposed that:

"These decisions will be put into legal form through formal Recommendations I'll make before the end of this year. And they will be durable, applying until at least 2020."

The detail of the legal form will be crucial, but the principle that the approach should be durable is a further departure from the status quo of national regulation which involves frequent (3-yearly) reviews of the market and regulation, and therefore no clear mechanism for commitment to support long-lived investment.

### The reaction

The reaction has been, to put it mildly, mixed. The investment community welcomed the decision with the HSBC headlining their note "The most important development in telecoms this decade".<sup>3</sup>

The European Competitive Telecommunications Association (ECTA), which had advocated lowering the price of copper, headlined their press release "Vice-President Kroes turns her back on competition".<sup>4</sup>

1 See previous article making the counter-argument in the March 2012 *Intermedia* "If you want fibre...should you lower the price of copper?"

2 Neelie Kroes blog. 12 July 2012. "Broadband for all: new regulatory certainty to allow investment in the next generation." <http://blogs.ec.europa.eu/neelie-kroes/broadband-investment/>

3 HSBC Global Research. 13 July 2012. <https://www.research.hsbc.com/midas/Res/RDV?ao=20&key=y8jHxePhJa&n=335848.PDF>

4 ECTA. 12 July 2012. <http://www.ectportal.com/en/PRESS/ECTA-Press-Releases/2012/Vice-President-Kroes-turns-her-back-on-competition/>

Figure 1

## An assessment

In terms of competition there are grounds for expecting it to intensify:

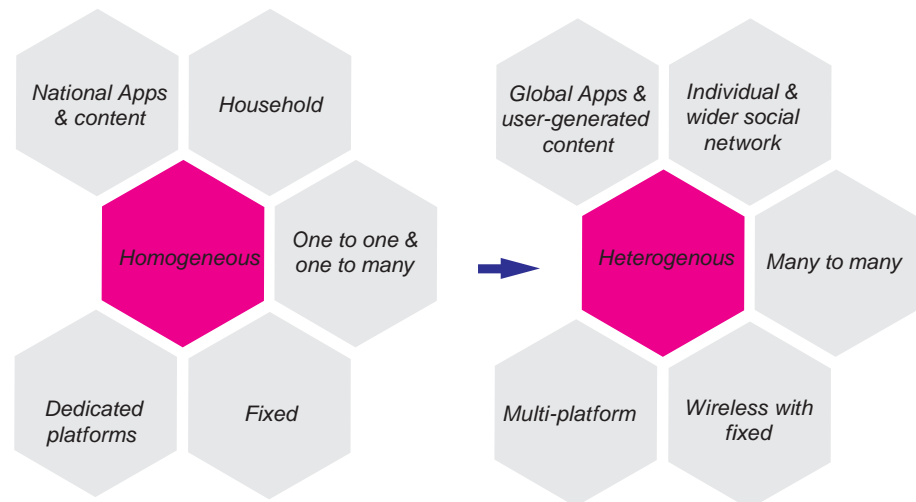
- » Platform based competition will intensify in the near term as fibre competes with price regulated ADSL during a period of transition, and as upgraded cable (DOCSIS 3.0) and wireless (LTE with more spectrum) compete with ADSL and fibre.
- » Services based competition will intensify as over-the-top applications including VoIP and messaging applications delivered on a global basis grow in importance.

In terms of investment, time will be required in order to assess the market reaction. However, there are grounds for believing that considerably more commercial investment will be forthcoming than would otherwise have been the case, provided detailed implementation remains true to the announced principles. Pricing flexibility and regulatory stability can be expected to promote investment since investment is supported by the opportunity to differentiate and adapt services and pricing over time, and commitment is required to assure investors that their investments will not be expropriated via regulatory changes.

## The challenges ahead

A clear challenge is to flesh out the detailed recommendation in a manner that is unambiguous, consistent with announced principles, but sufficiently flexible to allow implementation consistent with local, and changing, circumstances.

However a more fundamental challenge will be to continue to articulate and advocate a position that will inevitably come under intensive opposition by those who favour the status quo – both in terms of regula-



tion and a market characterized by access to unbundled copper loops.

The challenges will also be broader than those addressed to date. Convergence will continue to drive fundamental changes in the market including transitions to:<sup>5</sup>

- » Fibre (and ultimately away from copper where fibre to the premise is deployed)
- » Wireless and smart personal devices
- » Heterogeneous access and applications, moving away from one-size-fits-all
- » Towards heterogeneous and therefore local access market competition
- » Towards heterogeneous and global applications market competition

The main transitions, driven by convergence, are illustrated in Figure 1.

## Impact of convergence

Thus, in addition to the underlying assumption that networks pre-exist, the assumptions that services are (or should be) homogenous and that the

default relevant market is national rather than local or global are no longer valid. The changes, which are well underway, will require:

- » A more sophisticated assessment of what constitutes good outcomes as price reduction does not necessarily indicate improvement in a world of heterogeneous services.
- » Greater focus on transition and retirement of legacy networks and applications including revisiting concepts such as universality and providing a clear option, but not an obligation, for timely copper retirement.
- » Reassessment of whether services (beyond broadband access) should be within the scope of sector specific regulation or subject solely to generic consumer and market governance.

In short, the decisions by the European Commission in relation to next generation broadband regulation are an important first step in a fresh appraisal of what is fit for purpose in an altered and more dynamic technological and market environment. As John Maynard Keynes once put it "When the facts change, I change my mind. What do you do, sir?"

5 Williamson and Punton. June 2012. "Connectivity metrics for a converged era." [http://www.plumconsulting.co.uk/pdfs/Plum\\_June2012\\_Connectivity\\_metrics\\_for\\_a\\_converged\\_era.pdf](http://www.plumconsulting.co.uk/pdfs/Plum_June2012_Connectivity_metrics_for_a_converged_era.pdf)

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