



Office of the Director of
**Telecommunications
Regulation**

ODTR Conference – 19 September 2002

“New Market Perspectives”

Etain Doyle

Director
Office of the Director of
Telecommunications Regulation

Document No: 02/81

Date: 19/09/2002

Welcome

I am pleased to welcome you all to this ODTR conference on new market perspectives for the communications sector, in particular in relation to internet and the information society. I am particularly pleased to welcome our distinguished guest speakers who will inform and stimulate some debate on these issues.

The communications and related internet sectors have gone over a roller-coaster in the five years since the ODTR was established. We now find ourselves facing fundamental issues that will be difficult to resolve. This is hardly made easier by the fact that they need to be tackled at a time of greater constraints and less optimism than a few years ago. We have no realistic option but to press forward, keeping and developing what we have and opening new horizons on the future.

From where I stand there are two key challenges I would like to discuss with you today:

- ✚ First, the development of the use of internet and of information technology by business and consumers which has key implications for the communications markets and
- ✚ Second, the related issues of maintaining and developing sustainable competition in the communications markets.

As you will all be aware, the new EU Communications Directives provide the overall framework within which the communications aspects of these challenges must be met, and I am very pleased that Peter Scott has been here today to outline the Commission's approach and key elements involved. The ODTR has been working on implementation for some time and may I encourage you to review our papers and respond to our consultations on the subject. We are also issuing a paper on broadband delivery in conjunction with this conference, asking for your views and I very much look forward to your comments.

Oifig an Stiúirthóra Rialála Teileachumarsáide
Office of the Director of Telecommunications Regulation

Abbey Court, Irish Life Centre

Lower Abbey Street, Dublin 1, Ireland

Tel. +353 1 804 9600 Fax. +353 1 804 9680 E-mail info@odtr.ie

The last 5 years

For just a few minutes, let's take a little stock of where we now are and how we got there.

The biggest single change is that telecommunications is now 'consumer driven' not 'producer driven'. It seems like another world away when all government action was built around the needs of the incumbent. Yet it is as recent as 1996 that we had the decision to defer liberalisation; this was Telecom Eireann centred. The liberalisation agenda from 1998 has been user centred. The user has benefited from the competitive liberalised market through price and diversity of service.

We have little interest I suspect at this conference in hearing the list of regulatory measures introduced. You want to see *that* the thing works more than the detail of *how* it works. What matters is the outcome, what has actually happened in the market.

Ireland still operates, as most other countries do, in a fixed market which has a dominant player, but while there are serious limitations to which I will return the market is a very different place to what it was a few years ago.

There are 39 active operators in the Irish fixed line market, offering choice to users, providing a wide range of networks and services. The value of the total communications market (telecoms/mobile/and broadcasting transmission) has increased from EUR2.11bn in 1999 to EUR3.37bn in 2002 with the fixed line accounting for €521ml for 2nd quarter of 2002. There is a range of choices for many major businesses in terms of leased line communications, and 10% of retail leased lines are now supplied by OLOs: leased line delivery times have been transformed, from among the poorest in Western Europe to among the best. For SMEs and consumers, Carrier Pre-selection (CPS) is the key tool used by competitors to offer services. Awareness of CPS is high among SMEs 78% of SMEs are aware of CPS, 18% of SMEs switched their supplier of landlines in the past twelve months to a competitor. In the residential sector, 32% are aware of CPS and 43% have been approached about switching their fixed operator in the past twelve months.

The number of lines subject to CPS peaked at 160,000 [March 2001], just over a year after its introduction in January 2000, and I am glad to note that the most recent report shows a small upturn again.

All end users have seen reductions in retail prices of telecommunications in the past 5 years. 86% of those who switched in the residential market, switched to cheaper calls.

Since mid 1997, OLOs have been entitled to build their own fixed networks and a range of alternatives have been built mainly around the major cities. Ireland had a very short window before capital became scarce as the slow down started in the second half of 2000. It is clear from a recent ODTR survey that business is aware of and making use of alternatives technologies – with 14% of users of broadband surveyed saying they use wireless lan technologies.

I will return to the questions of internet and information technology usage and of course we have further presentations on these issues later this morning.

In every area in a dynamic market, it is important to maintain the pressure to keep looking outward anticipating as well as responding to the challenges of the market. Ireland has been operating in difficult market conditions, that have impacted the global telecoms sector. This environment tend to favour incumbents and it is particularly important to be vigilant in maintaining competition – not any particular competitor – at such times. The question of developing sustainable competition is the second key theme to which I will return.

In the mobile market now, Ireland has 76% penetration and you will see in the MRBI slides how much this is a familiar technology here. It is hard to credit that little over 5 years ago there was only one operator (to March 1997) and penetration stood at 10%. Nationwide networks have been built in a few short years and consumers have services readily available to them. Users in Ireland have particularly taken up prepaid services and SMS texting. It would appear the Irish reputation as communicators has been translated

to our high levels of usage of mobile telephony. While mobile has become the biggest wireless service, of course there are many others which have expanded rapidly in recent years, from radio links to business radio and most recently W-Lans..

Likewise, when we look at broadcasting transmission, in mid 1997, all TV was analogue only and there was no plan as to how digitalisation might be introduced. The plan was developed over 1997/8 by the ODTR and implemented in the following years for cable and MMDS. Sky has also developed a digital service. We are now at the stage where 22% of TV households currently subscribe to digital services. DTT has yet to launch and the new Department of Communications is reviewing how to move it forward, with input from ourselves. The increased capacity made available by digitalisation of the transmission mechanisms is to date, being taken up with imported content only.

Turning to the implications of internet and information technologies for the communications sector, I should first note that Internet services involve a range of services beyond the communications sector and are not (and rightly so) regulated by the ODTR. However, access to internet is via communications networks and telecoms regulators do what they can to facilitate the necessary competitive services.

We have also witnessed in the past 5 years the growing importance of internet to both residential and business users. We have - depending on the survey – around 4 in 10 residential internet users and we have almost 9 in 10 users of the internet in the SME sector.

For big business, leased capacity is key and smaller business need a range of capacities from dial-up and ISDN upwards. Business internet connection is high at over 80% of all businesses, but it is mainly still at e-mail stage. E-mail is an enormous benefit for industry, but much more needs to be done by Irish business to reap the benefits of fully integrated information technological solutions. At the residential level, internet penetration is not rising as quickly as in some other countries and it is important not only for the ODTR, but for industry and other public agencies to consider why and what more

might be done, while not losing sight of current initiatives including forcing the pace on flat rate internet and products like DSL. You will be aware that we have already introduced internet access codes to enable operators offer differently structured pricing packages, and more recently have been working hard on flat rate internet access which I would hope to see develop in the coming months. I am pleased to note the new services offered by UTV and Esat BT which I believe will be useful in stimulating increased use of the internet at the consumer end of the market.

Some two years ago this month the ODTR was made responsible for regulating postal services. Postal services are very different from telecommunications in that the barriers to market entry are low and there are very many forms of indirect competition.

History shows that Postal Services are very resilient and adaptable. Despite the growing use of email and the internet, mail volumes continue to grow. Over the 10 years 1991 to 2001 the number of Letter Post items delivered by An Post increased from 140.2 to 203.1 per capita per annum – compound growth of around 4% pa.

Market Research conducted for the ODTR shows that 59% of large and medium businesses say the number of letters they post has increased over the last twelve months, and only 6% report a decrease. The figures for residential customers are 25% increase and 38% decrease over a five year period.

So, now in Autumn 2002, we have more than price reductions, improved quality and greater choice. There is now greater understanding of the primary force that brings about such benefits... competition. While the incumbent still dominates the market we have significant competitive development in the fixed line business, particularly in Dublin. There is a strong second player in mobile with a third in market and 3G is on the way and Ireland has made substantial progress on the digitalisation of TV transmission, providing the capacity for substantially increased content, which is however, currently all imported.

Opening the market to competition has been critical to these developments. There are particular reasons why this fragile creature needs vigorous protection at this time. Along with most of the world, Ireland has been operating in difficult market conditions in recent

times. These conditions tend to favour incumbents. The key issue is how do we develop sustainable competition?

We have seen major price reductions and some elements of better service with competitors now in all communications sectors. There is considerable, widespread understanding as to the importance of competition for delivery of innovation and choice at best price. While the incumbent is still dominates the market we have significant competitive development in the fixed line business in particular in Dublin, a strong second player in mobile with third in market and 3G on the way. Ireland has made substantial progress on the digitalisation of TV transmission, providing the capacity for substantially increased content, which is however, currently all imported. The rate of progress has slowed considerably however and we need to consider how we can move forward again.

Issues of concern nationally

Ireland has made progress, but we are not as far advanced as we need or would wish to be in terms of internet usage and adoption of information technologies. There are a number of initiatives underway and we need to consider what the appropriate priorities are at this time. Increased communications capacity will be needed to what degree and where? It is clear that communications services will remain key to many aspects of economic development. Given the fragility of the market, we need to put special emphasis on strengthening the competitive roots of the market sufficiently so that it acquires its own dynamic and that users benefit more quickly and effectively than by forced regulatory change.

Moving from the headlines, to review in position in greater detail, for SMEs, it is not just a matter of e-mail or a web-site, but range of business process engineering issues that transform the business. Travel and tourism business is increasingly conducted over the web, with the most successful companies having adopted a completely integrated model linking their sales, distribution, accounting and management information systems. While

the up-front costs tend to be significant, operating costs should be substantially reduced, benefiting the company with increased margins and/or ability to compete on price/service delivery. In the light of the information from the MRBI survey, it is clear that simpler, easier to access sites are important for consumers.

Companies need to develop appropriate interfaces, whether for business or consumer use. If something cannot be purchased significantly quicker and/or cheaper on-line than over the phone, if the service offered does not markedly enhance choice, if it takes more than a few minutes, it is unlikely that users will persist. Consider the travel business which has transformed its business model with sharply discounted ticket sales over the web, or the range of tourism sites that offer greater and, if desired, more tailored choice than is available to consumers at any travel agent.

The most successful companies all meet one or more of the criteria and differ for example from most bank sites, which tend to be cumbersome, offer little by way of discount and no more choice than you would have if you visited your branch. Many banks are still in a situation where they have sunk substantial costs into internet banking sites, but have not gained sufficient internet customers to pay back the initial investments. It is easy to find examples which have not worked well and these should be used to identify what are the problems to be avoided. But the most successful adopters are doing phenomenally well even in difficult market circumstances.

As they develop their usage, Irish SMEs are increasing their bandwidth mainly on ISDN at lower speeds. I would expect DSL to address this segment's growing bandwidth needs but the cost of DSL is still a constraining factor. On the residential side, we will have the benefit of some interesting research by MRBI to consider later in the morning - the issues around content and cost remain. The launch of some flat rate products in recent weeks is encouraging and it would be hoped that these products will succeed. There are also opportunities for mobile and cable/satellite companies to offer content here. Although WAP has had its difficulties, we are now seeing the onset of GPRS. It is

encouraging to see the number of people in the MRBI survey who were familiar with mobile data services.

We also have gathered some survey material on consumer issues regarding internet usage. Substantial progress has been made, but given the national objective of ensuring inclusion in the Information Society and indeed the economic benefits that can flow if B2C is well provided, I will concentrate a few remarks on what problems have been identified as hindering further growth in residential usage. Further training would be helpful for those interested but not fully comfortable with the technology: there is a disparity in those not yet on-line between the costs of PCs and internet use and the benefits they would get if they went on-line. Slow connections are an issue for almost 40% of users.

On broadband, the ODTR is constantly reviewing and developing licensing frameworks, pressing for progress on pricing and access options and now wishes to help inform the debate with some practical modelling. The Ovum data to be presented later today represents what we hope will be an interesting benchmark, a case study on the network cost of rolling out a broadband network. I believe it will provide a reasonable focus and reference point for public debate and help shape practical considerations for the future. It may also be the case that some may want to put forward alternatives – for example the mobile and/or wireless operators – which could be reviewed against this benchmark.

New market perspectives - Moving to the future

As we move into new regulatory frameworks, both EU and national, it is important that we take the time to deal with them properly, but also that we keep as much focus on the market as possible. The market is more fragile now, and it is important to have a clear perspective on the potential future scenarios and what we can do to promote the benign aspects while minimising the effects of the less attractive ones.

The attitude in the market is more careful than in the 'boom' years, and in many ways this is a good thing. The real issues are clearer without the hype, and so too the nature and scale of the problems to be resolved, while the room for manoeuvre in dealing with them is limited. Now we need to make choices; the right choices.

Debt is a major problem in particular for some incumbents internationally, and this is being dealt with in a tough market way. While the Irish incumbent is relatively less encumbered, there are issues for *eircom* to which I will return. More broadly, Ireland is now very dependent on external investment in the telecoms sector. It is remarked and rightly, that Irish telcos have to compete with international companies' home operations and other subsidiaries for investment, and sometimes it is suggested that the simple solution is that Irish telecoms retail prices need to be relatively higher here.

The problem with this is that communications costs are a key input into many other sectors of the economy, including some on which we are critically dependent for growth and the highest quality employment. Communications costs are a significant business input generally, particularly in terms of developing e-commerce. If we move up the international league of communications prices, it does affect our competitiveness generally and will create problems in related sectors to telecoms, with potentially damaging effects on jobs and prosperity here. These will affect the telecoms sector also, in that communications revenues will expand less quickly and could even decline. As the largest company in the market, *eircom* needs overall growth in national telecoms revenues – it needs an active competitive telecoms market for its own development. Major companies require efficient, competitive communications suppliers offering state

of the art services. The arguments in favour of competitive suppliers that underlay the decision to open the Irish market in 1998 are no less valid now.

There are no simple answers to the issue of costs, but the elements of the solution are very clear. Firstly the base cost structure – in particular *eircom*'s – needs to be as efficient as possible. This is primarily a matter for *eircom*, although as regulator we play a role in reinforcing the signals on costs through decisions not to allow inefficient costs to be passed on to other operators and with the price cap.

Since liberalisation, the ODTR has worked to ensure where it can that the inefficiencies in *eircom* are not passed on to OLOs via regulated prices which do include a return on investment: it has also via the price cap put pressure on large margins on the less competitive parts of *eircom*'s business. The price cap covers about 1/3 of *eircom* revenues and between the pressure of the cap and competitive or regulatory pressures elsewhere, prices have fallen significantly in real terms. Consumers have benefited as a result and Irish telecoms prices have been more competitive than they otherwise would have been.

The price signals involved in these regulatory measures are intended to encourage major efforts to reduce costs so that there is a permanent gain in competitiveness, that benefits the company and also the economy generally. I do not underestimate the difficulties in dealing rapidly and effectively with inefficiencies, but the consequences of not progressing them quickly are most significant for the individual operators, the sector and nationally. This is not just a matter of numbers, but also of operating structures, service culture, response times etc. It is clear from international experience that competitive pressures are also very important in delivering change and, for my part I will do all I can to ensure that they continue to be applied.

Operators also need to know that they can get the access and services they are entitled to simply and cheaply from the incumbent. I should note what has been achieved in a short time by *eircom*, and in particular by the setting up of a new wholesale operation, but

there is more to be done and as regulator we are turning increasing attention to this issue. We are competing with other countries which may have started much earlier, but in a world of continuous change this is the challenge that has to be met.

There are other significant issues that affect all telecom companies operations here – for example, planning permissions and way leaves, which need to be further addressed. I have noted that local authorities are increasingly aware of and anxious to have better telecommunications infrastructure in their areas, and I believe that this, together with initiatives at national level, can bring improvements in these matters. It is also important that operators do explain what they wish to do locally, for at times local resentment has to do with lack of information and ungrounded fears. Spatial strategy is also very important – telecoms is a network service and as you will see in the Ovum presentation later this morning, costs are higher in areas of lower density populations. It is important that we recognise and quantify the costs of approaches for spatial strategic development and work out how they will be met.

We all need to be clear – costs incurred by telecoms companies are no different to costs incurred by other businesses – they have to be met by someone somewhere, whether they are way-leave costs, or construction costs, excess costs due to inefficiencies or delays in planning permission. We can see the difficulties if they fall on the retail and business consumer: we can also see the difficulties if they significantly reduce profitability as this can discourage investment and a presence in the Irish market.

There is a balance here, but it is my view that progress in achieving the range of cost efficiencies has not been as quick as is needed over the years and we do not now have much room for manoeuvre. There are inflationary pressures which need to be taken into account also. We need to keep our telecom input costs as low as possible and doing this requires action on all of these fronts.

New Market Scenarios

So let us now turn to the perspectives for a competitive communications market. The ODTR's vision is of a market of open sustainable competition in all sectors, competition across the value chain with diversity of networks and innovation benefiting the end user. This is a **choice** scenario where end users have a complement of competitive competing services and products to choose from. This scenario increases the focus on users and on sustainable development in the sector.

This is clear if we take two key tests for competition – barriers to entry and strength of competitive forces. It is important that the players in the market operate with the expectation that others may realistically enter, indeed given the time it takes to develop communications networks, you actually need a level of operating competitive networks, not just the juridical right to enter a market for players to feel the impact of the absence of a barrier to entry. This is particularly true in a market of the size and geographical location of Ireland, where externalities may affect a decision to enter to a very considerable extent. A fortiori, the strength of competition – and the vigilance and strength of the regulator – is particularly important in a small market to maintain and deepen the range of services on offer to users.

Let us look at where the market is now.

We have some new entrants coming into the market, some mergers and closures, small increases in overall revenues, some new services coming on-stream and expansion of others – not unlike developments in the economy generally. We are perhaps **grinding** along: This is reflected in market sentiment and a comparison of the Irish stock market trend to the competitive levels in fixed market.

What are the likely scenarios open to us now?:

Depending on what happens to the economy and in particular the ICT sector, we could **stagnate** in this position. However, the Irish growth rate, while modest compared with previous years is still high internationally: the expectation is that the international

markets will recover even if it is taking longer than was thought some time back. So if the external circumstances are strong enough to avoid slipping into stagnation, what are the alternatives? We may end up in what I call **platform**. **Platform** arises where there is effectively only services competition, completely dependent on a single network (or network per main line of service), which gives the owners of that network substantially increased leveraged market power. The costs of the platform operator are embedded in all services, it can to a significant degree determine what services are offered and it has no competitive spur to innovation. This is important even in relation to broadband development, where the technologies are not that new. While it is the case that in some countries the proportion of DSL lines issued by the incumbent is very high relative to new entrants, if you look more closely you will see that there has been competitive pressure – from cable operators in particular – which has promoted the roll-out by the incumbent, including action on pricing. In Ireland, that competitive pressure has been very muted in this respect and we can see the difference.

Accordingly, I am very anxious to see greater diversity of networks and services, with sufficient fluidity in the market so that no operator can feel it can sit back, let alone cut back on service or innovation. I believe that the new ntl should be in a position to compete more effectively in future and also in this context, the forthcoming roll-out of 3G and, I hope the development of DTT will play a role in offering choice.

As regulator, we have also taken action to respond to the investment issue, taking account of the small scale of the market here. From the start, our LLU offering has been based on what is known as ‘co-mingling’ which involves a smaller scale (although more complex to regulate) operation than the more usual separate room co-location. *eircom* has agreed to introduce arrangements to enable OLOs to purchase single bitstream lines, in addition to the existing 24 line arrangement which would involve higher levels of up front expenditures. I should note that, while the necessary minimum scale of purchases by OLOs are lower as a result, the prices do take account of *eircom*’s costs on an efficient operator basis or fully allocated as appropriate in regulatory terms. The involvement of

OLOs should help promote sales of DSL which have tended to be slow in all markets as services begin. There are issues on pricing that *eircom* needs to address to achieve commercial success, but we should note that *eircom* has committed €120million to the roll-out of bitstream services.

Strategic Responses – the ODTR strategy 2002

The first ODTR strategy, articulated in the months following establishment was to sort out key market threatening problems in the telecoms and broadcasting transmission markets and prepare for liberalisation. As the date for that moved forward, the whole panoply of regulatory measures necessary for a competitive market had to be set in train, and this was followed with our first strategy statement in 1999. For 2002, following internal discussions, we presented our proposed objectives to a meeting of industry representatives who were generally supportive.

The ODTR's strategic objectives for 2002 are clearly stated and were published in our December Quarterly report last year.

They were: -

1. Market competition and quality – tackling bottlenecks, and quality issues for users, seeking to intensify competition in existing services and best practice in delivery and range of services
2. Implementation of the new EU Framework for telecommunications liberalisation
3. Competitive infrastructure development and network sharing for broadband and narrowband, including LLU
4. Complete/ streamline costing/accounting modelling and frameworks for all sub-sectors, underpinning efficient pricing and stimulus to competition.
5. Complete postal regulation framework to encourage competition and quality for users
6. Maintain and develop ODTR 'centre of excellence' programme
7. Maintain and develop ODTR stakeholder relationships

I am pleased that, despite market difficulties we have made substantial progress on all elements this year. For 2003, the new Commission will be in operation and I am sure it would be helpful to develop the debate as to the priority to be given to tackling the key issues of maintaining and developing competition in networks and services in current market conditions as outlined above: seeking to reinforce the signals for better service quality and efficiency: ensuring that the regulatory framework works more smoothly for all parties: while at the same time completing the mammoth task of revising the whole framework to take account of the new Directives and bedding down the new Commission. This year we have won a couple of major training awards - an IITD (Irish Institute for Training and Development) National Training Award and the "Excellence Through People" Award". These Awards recognise organisations which have demonstrated best practice and an ongoing commitment to human resource development. This has enhanced the capability of the 120 staff of the ODTR who have a reputation for hard work which will be needed to meet the new challenges. I want to acknowledge and thank the staff for their contribution to the liberalised market we already enjoy and to encourage ever more efforts to move it forward further and faster.

Conclusions

There are no easy options for Ireland in terms of communications, nor – but are there ever – for the regulator. We have come a substantial distance over the last number of years, and we need to focus our efforts ever more clearly on the elements that will respond to the remaining current barriers that will deliver the best and most effective results. Developing internet and information technology usage generally is critically important for economic development in terms of business costs, and even more generally for we cannot afford to get to a situation where some Irish business is excluded from working with other companies because of inadequate ICT development. It is also important for Irish residents who should have access to an information society that benefits them. To the extent that Irish residents increasingly look to the net for tickets/insurance or other services, is it critical that Irish agencies in these sectors have

the capacity to respond. Increased broadband capacity is one element in the picture and I hope that today's seminar will help stimulate the debate and focus on the measures needed to move us forward.

Life is be more difficult for us in a more fragile market. The most energising development though is that there is vastly increased awareness amongst businesses and the wider public of the importance of competition. They have seen what it can do, and they want more.

Thank you