Ofcom Wholesale Fixed Telecoms Market Review 2021-26

Response by Swish Fibre Limited

1. Swish Company Description

This response to Ofcom's consultation on its Wholesale Fixed Telecoms Market Review comes from Swish Fibre Limited ('Swish').

Swish is a full-fibre broadband provider, bringing truly exceptional connectivity services to homes and businesses in the Home Counties. Our goal is clear and simple - to improve lifestyles and enhance the future of our communities by connecting people, businesses and services instantly through reliable broadband.

Swish is part of the Fern Trading group ("**Fern"**) which has an established track record in supporting renewable energy, healthcare, property, and now fibre broadband. Fern has provided a separate response to this consultation.

2. Key Points

- **Ofcom has drawn Area 2 too narrowly**. It has relied on incomplete operator data. Swish has annexed details of our audited plans to build fibre to more than ✂premises over the next five years (our "initial build plan"). Of these, approximately ✂premises currently lie in Area 3. These must instead be included in Area 2.
- **If Ofcom persists with its Area 2 definition, this should include <u>all</u> premises which are economically viable.** Ofcom identified 9.2m premises in Area 3. But DCMS identified 3.1m premises which require public subsidy, and a further 3.1m which are commercially viable but are at risk of receiving no investment. This suggests there are between 3.1m and 6.2m economically viable premises in Area 3. Our ✂extension build targets could lie anywhere in this area. **Swish will not build to any economically viable premises (whether in our initial build plan or our extension build target) if they are mis-classified as Area 3**.
- **This highlights that Ofcom's methodology for defining geographic markets is flawed**. Markets should distinguish between areas which are and aren't economically viable, and therefore have different competitive characteristics. This should be determined by modelling (or by dynamically reclassifying as economically viable, any location where an altnet builds).
- **If, however, Ofcom persists with its methodology for defining geographical markets**:
  - **A. Its Area 2 proposal to ban geographic price discounting should help support fibre build**, provided it redraws the Area 2 boundary to include credible committed and forecast build plans from operators;
  - **B. Its Area 3 proposal to allow geographic price discounting will disincentivise altnet build** if it does not redraw Area 2/3 boundaries; and
  - **C. Its Area 3 wholesale fibre price uplift remedy proposal is unlikely to incentivise BT**. It is unlikely to offset BT's additional deployment costs. BT will continue to deploy mostly in Area 2.
- **If altnets withdraw from Area 3, BT is unlikely to build there instead**. BT's plans cover only a tiny proportion of Area 3. Its track record of rural build is poor compared to altnets; the vast majority of its deployment is in Virgin areas. This is where it makes the greatest returns.
- **Ofcom's concerns about altnet build in Area 3 are unfounded:**
  - A. Recent history shows that **altnets are much more likely to go deep into the more rural parts of Area 3 than BT is**, given a fair playing field.
  - B. The current high levels of investment in fibre altnets demonstrates that **risks of insolvency are negligible**; cable industry history shows consumers did not experience service loss where providers suffered financial difficulties. Ofcom could seek powers to appoint a provider of last resort if it is concerned on this point.
  - C. **Consumers already have a choice of ISP in almost all potential fibre areas** - this comes from the wholesale obligations on BT's copper/FTTC network in the same area. Exactly the same applies in current Virgin Media areas.
- ***BT must be fully transparent about its fibre build programme. Without this, altnets will be cautious about where they deploy, in anticipation that BT can overbuild unannounced.***

3. Response

Introduction

1. It is vital that the UK secures nationwide ultrafast broadband infrastructure to enhance the lives of its citizens and consumers, and to drive productivity and competitiveness. Retail demand is booming, with new bandwidth-hungry applications driving willingness to pay for faster services.
2. We are at an inflexion point in national capacity to meet this demand. In the past year major investment has poured into the altnet sector. The engineering workforces of both BT and its commercial rivals have expanded and upskilled. The Government has committed £5bn to fund gigabit-capable[1] deployment in the hardest to reach areas.
3. If Ofcom gets the policy framework for this market review right, it can create conditions which incentivise telcos to connect a majority of the country's businesses and households with ultra-fast networks within the next five years. Decisions taken now will also determine what happens when BT's copper network is switched off, due in the next review period.

Ofcom has drawn Area 2 too narrowly. It has relied on incomplete operator data. Swish has annexed details of our audited plans to build fibre to more than ✄premises over the next five years (our "initial build plan"). Of these, we estimate that around ✄premises (c✄%) currently lie in Area 3[2]. These must instead be included in Area 2.

4. Ofcom proposes to define a geographic market, called "Area 2", based on whether "*there is already some material commercial deployment by rival networks to Openreach or where this could be economic*".
5. Ofcom proposes to include 21.3m premises in Area 2, based on the existing and forecast network coverage of "MSN"s. It defines MSNs as networks which cover business and residential customers, have wide geographic availability, and provide a wide range of services.
6. Ofcom has set the boundary for Area 2 incorrectly. It has not included data from Swish. Swish is an MSN, with £✄m of funding from Fern to enable it to supply broadband and leased line services anywhere in the UK to business and residential premises[3].

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[1] Ofcom notes that fibre networks will support the delivery of other ultra-fast broadband technologies, such as 5G and fixed wireless. It includes these networks within the term 'fibre'. We think Ofcom's thinking could be clearer if it focused on promoting positive consumer outcomes rather than the enabling technology. This could lead it to use either the generic term 'gigabit-capable' networks, which the UK government seeks to promote, or 'Very High Capacity Networks' ('VHCNs'), which Ofcom has a duty to promote under the forthcoming European Electronic Communications Code Directive.

[2] This estimate is derived by comparing all post code sectors in our initial build plan (more than ✄premises) against the Ofcom postcode sectors for Area 2 and Area 3. We have assumed all future network extensions in our initial build plan are Area 3, as such network extensions will take place in villages near the towns plan to build to. See Annex A of the board resolution which we have provided along with this response for a break down of initial build plan properties by geography and Area 2 and Area 3 classification. We have also provided full post code level data in our submission in an excel document (note that the post code data cannot, by definition, include the future extension data, which is why there is a slight variation in the data).

[3] I.e. Swish complies with Ofcom's definition for an MSN: "*These types of network tend to have a larger geographic availability and provide a wider range of services, i.e. leased lines and broadband ...* ". WFTMR Vol 2, 1.19.

7. Swish has fully funded credible and audited[4] plans to use these funds to build FTTP to more than ✂premises[5] in our initial build plan, between now and 2026, of which approximately ✂ (c✂%) lie outside of Ofcom's proposed Area 2. By definition, it is economically viable for us to deploy in these locations. To treat Swish consistently with other MSNs, Ofcom must reclassify all of the postcodes that contain our build premises as Area 2.

If Ofcom persists with its Area 2 definition, this should include <u>all</u> premises which are economically viable. Ofcom identified 9.2m premises in Area 3. But DCMS[6] identified 3.1m premises which require public subsidy, and a further 3.1m which are commercially viable but risk no investment[7]. This suggests there are between 3.1m and 6.2m economically viable premises in Area 3. Our extension build targets could lie anywhere in this area. Swish will not build to economically viable premises if they are classified as Area 3.

8. Ofcom identified 9.2m premises where *"there is unlikely to be material commercial deployment by rival networks to BT".* The Government's Future Telecoms Infrastructure Review identified 3.1m premises which required public subsidy, and a further 3.1m which were commercially viable but risked no investment. This suggests there are between 3.1m and 6.2m economically viable premises in Area 3.

9. In addition to the more than ✂premises in our initial build plan, we expect to build at least a further ✂premises (our "extension target") during the review period. We will fund this using a mixture of free cash flow, additional equity from Fern, and additional debt.

10. It is not possible for us at this stage to identify precisely where these ✂extension target premises will lie. Indeed, no operator's fibre plans are reliable beyond a couple of years ahead[8]. Our extension targets could lie anywhere in the UK that is economically viable[9], including the 3.1m-6.2m economically viable premises in Area 3.

11. We will not build to any premises in either our initial or extension target areas which Ofcom classifies as Area 3, if Ofcom carries through with its proposal to allow BT to abuse its dominant position by offering geographic price discounts in these locations. This simply makes our commercial business case too uncertain.

12. This means that Ofcom's proposals risk Swish axing plans for the ✂premises in Area 3 in its initial build plan **<u>and</u>** up to ✂premises from its extension plan. Based solely on Fern's initial investment of £✂m, this could mean a reduction in equity investment in fibre deployment from £✂m to just £✂m. However, this number would be substantially higher were Fern to invest

[4] Our plans were verified by an independent third-party auditor, Analysys Mason, between September and November 2019. Since the audit, our initial build plan has increased to the more than ✂properties identified in our response. We have provided a copy of a letter from Analysys Mason in which they confirm they undertook such audit

[5] As part of our response, we have provided a board resolution passed by Swish Trading Limited, which owns 100% of Swish Fibre. This sets out our proposed initial build plan plans and shows, in each case, whether the proposed area is Area 2 or Area 3.

[6] Future Telecoms Infrastructure Review.

[7] DCMS also identified 5m premises for intervention under its 'outside in' programme. Using this figure would imply that ✂% x (9.2m-5m) = ✂m commercially viable premises in our target market lie within Area 3.

[8] E.g. BT only publishes forecasts for its fibre programme up to two years ahead.

[9] The premises in our initial build plan lie in the South East of England and the Midlands. However, we operate a flexible business model which allows us to move beyond our initial target market to anywhere in the UK which is commercially viable.

more than £✂m in Swish, for example providing equity to allow Swish to pass more than the ✂fully equity funded properties to hit our extension target[10]. The outflow of investment from altnets as a whole affected by Ofcom's proposals will be multiples of this.

13. For this reason, it is vital that Ofcom includes all economically viable premises in its Area 2 classification.

This highlights that Ofcom's methodology for defining geographic markets is flawed. Markets should distinguish areas which are and aren't economically viable, and therefore have different competitive characteristics. This should be determined by modelling (or by dynamically reclassifying as economically viable, any location where an altnet builds).

14. As above, our primary concern is that Ofcom correctly classifies the more than ✂economically viable premises in our initial build plan, as Area 2. Our secondary concern is that all economically viable premises are classified as Area 2.

15. Notwithstanding this, we believe that the Area 2 and 3 classification is fundamentally flawed. Ofcom should not define Area 3 as "*where there is unlikely to be material commercial deployment by rival networks to BT*". This fails to identify a market with substantively different competitive conditions to Area 2. It merely shows the locations that operators don't **<u>currently</u>** plan to go to, even though they might be as viable as those in Area 2.

16. But operator plans change regularly and are unreliable beyond a couple of years (indeed this point means that it is quite possible that we will be forced to modify some of the target areas in our initial build plan, for example if a competitor builds there). Ofcom can only encourage altnet build by classifying *all potentially* economically viable locations as Area 2. Unlike Ofcom's current approach, distinguishing economic and uneconomic (without subsidy) areas in this way, draws a line between geographic markets with substantively different competitive conditions. This approach would allow Ofcom to target its interventions at unviable locations[11].

17. Ofcom can only assess potential economic viability by conducting a modelling exercise. This should consider commercial drivers (such as cost per property passed, property density, PIA availability, cost of money and likely adoption rates at current retail price), validated by actual and forecast operator build data. This would also enable Ofcom to assess the relative attractiveness of the viable areas, including identifying those which can support two or more retail fibre networks.

18. We are confident that such a model would show that fibre is an economically viable proposition in ***at least*** *6*.2m more properties nationwide than Ofcom has included in its proposed Area 2 (i.e. 9.2m minus the 3.1m that the Future Telecoms Infrastructure Review identified as requiring

[10] As part of our response, we have provided a board resolution passed by Swish Trading Limited, which owns 100% of Swish Fibre. This confirms that Fern has provided £✂m of equity funding, subject to certain milestones, for Swish to pass ✂properties. Additional funding from either Fern or third parties will help Swish complete its initial build plan (more than ✂properties) and its extension target .

[11] If Ofcom additionally wants to target interventions at the least attractive of the economically viable areas, then it should create an additional geographic market for this, in the same way that DCMS has done. Ofcom currently includes these areas in its Area 3 (because this includes areas which are economically viable but where deployment is unlikely based on current (unreliable) plans).

public subsidy[12]), although investment to some of these could be delayed (DCMS identified 3m commercially viable premises where this could happen).

19. Ofcom should also be fully aligned with DCMS on the issue of economic viability. They should work together to define an “intervention map”, and consult on it regularly, to ensure that public funds for fibre deployment in harder-to-reach areas are used appropriately and do not distort competition.

20. An alternative approach could be to reactively define as Area 2 any location where an operator other than BT lays fibre *after* Ofcom has concluded its review, as economically viable. Deployment in such areas is clearly considered by the provider to be "economic”.

If, however, Ofcom persists with its methodology for defining geographical markets:

A. Its Area 2 proposal to ban geographic price discounting should help support fibre build, provided it redraws the Area 2 boundary to include credible committed and forecast build plans from operators

21. Ofcom's proposed remedy to stop BT abusing its dominance by offering geographic price discounts in Area 2 will remove the disincentive which prevents altnets from building there. This will help support Ofcom's objective of maximising fibre coverage provided that it correctly defines Area 2 to include both actual and potential operator build areas.

22. We are agnostic on the Ofcom's wholesale charge control remedy.

B. Its Area 3 proposal to allow geographic price discounting will disincentivise altnets if it does not redraw Area 2/3 boundaries

23. However, if Ofcom applies its price remedy without redrawing the Area 2/3 boundary, this will disincentivise altnets from building in all economically viable locations within Area 3 *even if they currently have plans to build there.*

24. This will *reduce* - or at least slow down - the extent of UK fibre deployment. For example, on the basis of the proposed geographic market boundary, Fern may remove its funding for properties within Swish’s initial and extension build plans that lie in Area 3. The risk of BT overbuild and use of geographic discounting to undercut on price would simply be too great. As noted above, across altnets this would result in a massive outflow of investment.

25. Ofcom must realise that, if its Area 3 *really* captured all premises where "there is unlikely to be material commercial deployment by rival networks to BT", its proposal to allow BT to discount prices in these areas would serve no purpose. It does not encourage BT to build; and it has no impact on altnets (as they are unlikely to build anyway according to the definition).

[12] We believe that we could build, without subsidy, to a number of the 3.1m premises that the Future Telecoms Infrastructure Review identified as requiring public subsidy.

C. Its Area 3 wholesale fibre price uplift remedy proposal is unlikely to incentivise BT. It is unlikely to offset BT's additional deployment costs. BT will continue to deploy mostly in Area 2.

26. Given that it has limited funds, BT is unlikely to pick up any slack left if altnets pull out of Area 3. Instead, it is much more likely to continue to focus its fibre deployments, as it has done to date, on the areas which generate the greatest returns, and the area where it has a market share to protect from competition, which lie in Area 2.

    - BT's track record of building outside of major conurbations is poor. The vast majority of its deployment is in areas already covered by Virgin. Altnets deploy at least as much as BT does outside of cities and major towns. We see little prospect of this changing, based on its current proposals for Area 3.
    - Ofcom's proposed wholesale price uplift for fibre deployment appears to offer little incentive compared to the likely returns available from Area 2.

Ofcom's concerns about altnet build in Area 3 are unfounded:

27. If the objective of the WFTMR is to incentivise investment in full-fibre networks with competition where possible, it should make no difference to Ofcom whether it is BT or altnets which deploy. Yet, when it comes to Area 3, Ofcom openly favours Openreach investment over altnets and is distorting the market to encourage this.
28. We understand from INCA that Ofcom has given three concerns over Area 3 altnet investment which underpin this approach: A: lack of coverage; B: service continuity; C: lack of retail choice. We now address each of these points in turn.

A. Recent history shows that altnets are much likely to go deep into the more rural parts of Area 3 than BT is, given a fair playing field.

29. Ofcom is concerned that altnets would cherry-pick the most commercially attractive Area 3 locations, leaving other parts unserved. However, as described above, BT has the same financial incentives to do this as altnets.
30. In fact, as altnets are leaner and more nimble, they are more likely to build deeper into Area 3 than BT - a proper “Outside-In” approach that will help reduce the number of economically unviable properties. Furthermore, the investment to date and future build capacity of the altnet sector is as large as BT’s, and they have greater experience of building in rural and semi-rural locations.

B. The current high levels of investment in fibre altnets demonstrates that risks of insolvency are negligible; cable industry history shows consumers did not experience service loss where provider suffered financial difficulties. Ofcom could seek powers to appoint a provider of last resort if it is concerned on this point.

31. We believe that insolvency risks are negligible. Many altnets - even smaller players - are now backed by substantial investors (Swish itself is backed by Fern, a £2bn trading group). This

lessens the risk of insolvencies. Even where insolvency occurs (or a player enters financial difficulties), we believe a buyer is likely to be found (usually before an insolvency).

32. When smaller players in the highly fragmented cable industry of the 1990s entered financial difficulties, they were simply acquired by larger players, almost always without insolvency or loss of service to consumers.

33. The large premiums paid in recent transactions demonstrate that the market for full fibre providers now is as vibrant as it was previously for cable providers. Few predict this will change over the coming years, as the industry consolidates.

34. Nevertheless, to the extent that any problem does exist, Ofcom could seek powers - similar to those of Ofgem in energy - to intervene to appoint a provider of last resort in the event of an insolvency. We are also happy to explore the development of common standards and interfaces with other fibre providers, with the aim of facilitating takeovers if the need arises.

C. Consumers already have a choice of ISP in almost all potential fibre areas - this comes from the wholesale obligations on BT's copper/FTTC network in the same area. Exactly the same applies in current Virgin Media areas.

35. It is important that consumers have a choice of ISP. However, wherever altnets deploy, choice is *always* guaranteed through the regulated wholesale obligations on BT's copper/FTTC network in the same area. In exactly the same way, Virgin Media does not currently offer wholesale access to its network, but customers within its footprint always have a choice of ISP from the BT network in the same area.

36. We also have a natural incentive to ensure that, in any area where we deploy the only fibre network (alongside BT's copper network), we explore all options for commercially viable wholesale access. Without this, there will always be sections of our addressable customer base - those who want audio-visual services provided by Sky or BT for example - that we cannot attract.

37. This incentive is implicitly acknowledged by Ofcom when it discusses the scale of potential altnet deployments, and says that "these rely to differing extents on ... ability to wholesale access to retailers"[13].

38. Although many small providers exist across single-network areas, it is possible that an aggregation platform could consolidate these networks into a single large network for wholesale access purposes. We are confident that, with the support of Ofcom and retail ISPs, a solution can be developed that will address any concerns Ofcom may have in relation to wholesale access in locations where only altnet full-fibre networks are deployed.

BT must be fully transparent about its fibre build programme. Without this, altnets will always be cautious about where they deploy, in anticipation that BT can overbuild unannounced.

[13] WFTMR Vol 2, 1.28

39. Altnets will invest more in fibre if they know where Openreach is going to build. Openreach is generally transparent about its proposals, publishing plans of the exchanges it intends to upgrade up to 18 months in advance, for its Fibre First and 227 villages programmes.

40. However, it does not currently publish plans to deploy under its "*Retrofit Newsites Programme"*, nor does it publicise the existence of this programme. Openreach has told us that this accounts for around 10% of its current FTTP build, usually in small areas with newer housing stock.

41. In May this year, Openreach announced that it would publish a "rolling target, updated quarterly". This does not address the underlying issues. If Openreach does not identify which exchanges and specific locations are involved, altnets can start building in the belief that Openreach will not build within the next 18 months, only to find it arriving unannounced under the Retrofit Programme.

42. Furthermore, even after including the Retrofit programme, Openreach still says that it will not publish details for the further 10% of its fibre build that includes BDUK funded build, residential developments, Multi Dwelling Units, dig trials, and "other". This means that for 20% of its build in total, altnets do not know where Openreach will deploy.

43. Ofcom can encourage altnet investment by requiring Openreach to be transparent about its *entire* build programme. There is no logistical barrier to this; its 227 programme already includes build plans for tiny hamlets. There will always be operational reasons why Openreach, like altnets, makes late changes to its proposals. But Ofcom should require it to set out clearly when and why this is permissible, and should rigorously enforce adherence to these principles, requiring it to publish explanations whenever it deviates, so altnets can scrutinise them.