Your response

Question	Your response
Question 2.1: Do you agree with our overall approach to regulation in potentially competitive areas?	Confidential? – **N**
Question 2.2: What is your view of our access and charge control proposals for wholesale local access services in potentially competitive areas?	Confidential? – N
Question 2.3: What is your view of our access and charge control proposals for leased line services in potentially competitive areas?	Confidential? – N
Question 3.1: Do you agree with our overall proposed approach to regulation in non-competitive areas?	Confidential? – N
Question 3.2: Do you agree that a RAB charge control framework is appropriate for non-competitive areas? If not, please explain why you think an alternative is more appropriate.	Confidential? – N
Question 3.3: Do you have any comments on the design of a RAB charge control for non-competitive areas?	Confidential? – N
Question 3.4: Do you agree with our proposal to introduce dark fibre in non-competitive areas?	Confidential? – N
Question 4.1: Do you agree with our proposed overall approach to QoS?	Confidential? – N
Question 5.1: Do you agree with our overall approach to transitioning regulation as BT deploys its new fibre network?	Confidential? – N
Question 5.2: Do you agree with our proposal not to require BT to offer new forms of wholesale access to its copper network?	Confidential? – N

While we have discussed this consultation response with some other potential stakeholders within the company, it is always the case that a large global investment bank will have more than one opinion on any complex topic. As such, we should not be seen as speaking for the entire organisation with the answers to any of the questions in this consultation response.

Question 2.1

Yes, we agree with Ofcom's overall approach to regulation in potentially competitive areas.

We believe that Ofcom faces a difficult challenge to balance a dual mandate which requires Ofcom to create policies that inspire investment and create policies that inspire competition. We believe that the regulator has handled a difficult task well.

We believe the steps Ofcom has taken to increase predictability with respect to cutover, indexation of copper pricing with inflation, and the premium pricing of fibre relative to copper have gone a long way toward closing the gap between the level of return investors require to deploy risk based capital and the level of return Ofcom is comfortable allowing.

Furthermore, we believe that Ofcom has been extremely thorough in its efforts to create a fair playing field for competitor access to Openreach infrastructure through the DPA process. These steps have increased our willingness to invest in alternative network builds.

Additionally, we are extremely encouraged by the decision to create stability in regulation through the implementation of one five year UK policy.

Broadly, the proposal tells us that over the last four years Ofcom has gained an appreciation for the impact investor uncertainty has on UK telecoms pricing. Policy uncertainty and competition creates risk, and investors require risk to be priced appropriately. Thus higher risk forces up UK telecoms consumer prices or leads to an absence of network investment, while lower risk creates an environment where a higher quality fibre network can be deployed to consumers with moderate changes in pricing.

In sum, while we will highlight areas where we believe the policy risks lead to outcomes you do not desire, the efforts made in these initial proposals to reduce risk for all participants while creating room for competition tells us you're trying to strike a fair balance between risk and reward for capital providers. Given that obvious effort made by Ofcom, we agree with the overall approach to regulation in potentially competitive areas.

Question 2.2

We believe Ofcom's access and charge control proposals for WLA in competitive territories represent a strong step forward.

With respect to charge control pricing across competitive territories, we believe that Ofcom has done a good job of creating a framework which has the potential to balance the dual mandate.

Potentially competitive territories reflect 70% of the United Kingdom, and it is inevitable that build costs will vary over such a large area of land. As such, we are intrigued by the policy decision to enforce flat charge control pricing across all areas where the incumbent builds.

We believe this is a logical approach by Ofcom, as a flat charge control pricing policy eliminates the ability of the incumbent to crush alternative builders with predatory pricing. Furthermore, the application of flat incumbent pricing across a variable build cost base ensures that there will be some attractive niche investment opportunities for alternative builders.

This reduction of risk encourages investors to provide capital to alternative builds, inspiring competitive builds and lower consumer prices.

We highlight that the policy has the potential to balance your dual mandate, as this policy inspires us to provide capital to the alternative operators but does not currently inspire us to provide capital to the incumbent.

If there is a reasonable chance for the incumbent to lose, which is the stated intent of the policy, investors providing capital to the incumbent will want to know that we'll be rewarded if the incumbent competes more effectively despite the challenges the policy creates.

As things stand today, investors would have the risk of significant capital loss, investors would have no certainty on future policy changes, and investors would see returns capped if it all works out well. That strikes us as a bet which isn't fair, and we question whether members of Ofcom would like to see their own retirement money invested in such a risky scheme.

Since we believe the framework is sound, we would like to suggest some options for Ofcom to reduce investor uncertainty around the fair bet.

To reduce investor uncertainty, we believe that Ofcom could easily choose to set a specific future date for a review of the fair bet terms, perhaps guaranteeing investors that the terms set out for the fair bet in the 2021-2026 period will remain in place for the 2026-2031 period. This feels like an easy win which helps to inspire long term investment.

Additionally, to reduce investor uncertainty we believe that Ofcom could take steps to outline their view on the riskiness of the fair bet in advance. In prior years Ofcom has decided to judge the level of risk after the investment has been made, but we must stress that providers of capital do not have such a luxury. If it is your desire for investors to find out years later that we have judged the level of risk differently than the regulator, there is a cost to that uncertainty.

Beyond these steps to reduce risk, we question why the fair bet should carry an asymmetric payoff. If the incumbent fights a difficult battle and wins a larger share than expected, we believe there should be an uncapped reward until such time that the outcomes from a long series of regional investments demonstrate a sustained higher rate of successful risk taking.

With all of these comments we believe it is important for Ofcom to appreciate the price of the uncertainty they have created in the UK telecoms market through their prior handling of the fair bet.

As can be observed by the 60% share price decline in British Telecom, or by the relative difficulty alternative providers have faced raising capital, the decision by Ofcom to cap returns on the prior investment by the incumbent in a manner unexpected by investors has led all investors to be reluctant to deploy capital into any UK telecoms company. Investors always answer uncertainty by asking for higher returns, so any policy actions you can take to formally reassure investors will be met by a greater willingness to deploy capital.

Question 2.3

We believe Ofcom's access and charge control policies for leased line services in competitive territories are sound.

We commend Ofcom for the steps they have taken in DPA, not simply by forcing open access but also by pressuring Openreach to modernise their recordkeeping such that the DPA opportunities can actually be utilised by alternative builders.

As a provider of capital, we believe these steps have levelled the playing field considerably and thus the DPA changes inspire us to consider providing capital to alternative builders.

We would look to the responses of alternative builders to suggest whether enough has been done. Furthermore, we believe the market will begin to question the genuineness of their intent to build if successive policy changes do not eventually impact their utilisation of DPA.

Question 3.1

Yes, we agree with Ofcom's overall approach to regulation in non-competitive areas.

As investors, there is always a debate about the level of risk taken in telecoms investment, but the basic maths on risk and reward are relatively straightforward. If Ofcom is willing to reduce our risk through the regulatory process, we will ask for less in return when providing capital.

Within this answer we would stress that a fairly high level of detail about a RAB based model will be required by investors, such that we can reasonably calculate our expected return. Without the detail it will be impossible for us to calculate an expected return on our investment, which brings us back to the investment uncertainty that requires higher returns.

Question 3.2

Yes, we believe that a RAB based approach is appropriate for non-competitive areas. In fact we would encourage such an approach. These areas are specifically deemed non-competitive by Ofcom because the cost to build, the existing charge control process, and the risk of product acceptance make it impossible for a reasonable investor to deploy capital.

With access to fibre broadband being considered necessary for the public good, we believe calculating the cost to serve a regional area and creating charge controls specific to that regional area is a very logical approach.

A RAB based approach where the cost of a buildout is borne equally by the members in a rural community strikes us as highly sensible, and the lower risk of a RAB based model leads to a lower return requirement from providers of capital.

Question 3.3

Our comments on the design of a RAB based approach are relatively simple. We believe there should be a clearly stated path to cost recovery for the investor.

Specifically, we believe that Ofcom will need to clarify the timeframe of cost recovery through charge controls or forced cutover.

We believe that Ofcom will need to provide reasonable guarantees to investors that future policies will be stable despite the winds of political change.

We believe that Ofcom will need to clarify the calculation of the RAB in terms which an average professional investor could reasonably hope to understand.

We believe that Ofcom will need to clarify the process to create an allowed rate of return on the RAB such that an average professional investor can have a reasonable ability to create expected scenarios for allowed rates of return in future regulatory cycles.

We appreciate that these steps may be difficult to achieve for a regulator who has not historically used a formalised RAB based approach. With that said, without meeting these enablers the regulator will not have reduced the risk for investors, and reducing risk for investors is the only way to get the capital investment you desire in areas which would normally not offer a reasonable return on risk based capital investment.

Question 3.4

We do not agree with the proposal to introduce dark fibre in non-competitive areas.

We believe the goal of the regulatory policy in non-competitive areas should be to inspire investment in unattractive areas by reducing the level of risk for investors. Creating a limited risk RAB based approach will achieve the level of investment you desire while also achieving consumer prices at levels you will tolerate. Such a policy would solve a tremendously difficult challenge for the UK, as rural broadband is equally important to urban broadband but in rural areas it costs more to deliver their service.

The introduction of dark fibre increases the level of risk for investors. Such a policy would likely, in some small segments of the UK, result in lower consumer prices as alternative providers would inevitably find some small areas.

We see these small gains from competition outweighed by the needs of the majority. If dark fibre is introduced then Investors will not be able to clearly state, prior to providing capital, which of the non-competitive areas may see incremental dark fibre based competition. In response to higher levels of risk we will ask for higher rates of return on the RAB, driving up the prices for a majority of rural consumers to benefit a small minority.

Question 4.1

We do agree with Ofcom's overall approach to QoS.

We believe that in prior periods it was necessary for Ofcom to increase the level of pressure on Openreach, such that alternative operators and their customers were not disadvantaged.

We believe the existing policy approach has delivered tangible outcomes, with measurable improvements in QoS. An approach which delivers more of the same, while also encouraging investment in higher quality fibre networks which will inevitably increase the QoS for the UK, seems highly sensible to us.

Question 5.1

We believe Ofcom's overall approach to transitioning regulation as BT deploys its new fibre network raises a fair number of questions.

We believe the basic premise of the policy, to transition regulation from fibre to copper once the network is deployed, is sound. However, we would suggest that when put into practice the policy risk will lead to pricing requirements from investors that you do not desire.

We are encouraged by the introduction of rules for cutover which appear to be relatively clear, and we are encouraged by the concept that Openreach should have pricing flexibility in relation to its copper based products to encourage migration to the fibre network.

However, given the widely agreed benefits to the United Kingdom from the deployment of fibre, we would suggest that Ofcom consider striking a stronger policy balance between the needs of the many and the needs of the few.

A 100% coverage requirement to begin the cutover process and the shift of regulatory policy creates risk to investors. It will likely be the case that some landowners will fail to provide access for fibre, and it will inevitably be the case that some cities will be particularly slow to provide access.

As providers of capital considering the risk of investment, we can easily envision scenarios where our capital investment is largely stranded because a small minority of premises are difficult to connect.

Given that cutover to a faster and higher quality fibre broadband product is believed to be in the public's interest, and given that the cost of fibre investment is reduced by cutover which allows the maintenance of one network instead of two, we believe Ofcom may find it beneficial to consider setting the requirement at a level which can be achieved with a higher degree of predictability.

It may be the case that easing the cutover requirement slightly, perhaps to 90%, will provide the proper incentives to invest while also providing the proper incentives to external parties.

Providing a slight push to parties who stand in the way of societal advancement would not be new to Her Majesty's Government, as they have demonstrated a willingness to use eminent domain when weighing the needs of the many relative to the needs of a few. Thankfully Ofcom is not in a position where such an extreme policy stance would be necessary, but we do believe some policy flexibility could be argued as being in the national interest. After all, both the Ofcom fibre investment proposal and the statements by members of government have consistently indicated that enabling fibre broadband is a necessity for the development of the UK. Given such importance to the country, we question whether a small minority should result in a higher cost to all?

Question 5.2

We do agree with Ofcom's proposal not to require BT to offer new forms of wholesale access on its copper network.

To us this is very simple. The goal of the current policy should be to take the country forward with a single minded focus on generating as much fibre investment as possible with a risk profile that enables investment with a minimal increase in consumer prices. An increased focus on copper products sets the country backward, increasing the large fibre gap that already exists between the UK and Continental Europe.