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## **Three's response to Ofcom's consultation on Promoting Network Competition in Superfast and Ultrafast Broadband**

1. This is Three's response to Ofcom's WLA consultation on promoting network competition in superfast and ultrafast broadband, published 1 December 2017.
2. Three supports Ofcom's proposals to protect nascent infrastructure competition by preventing BT from targeting reductions in wholesale FTTC and G.Fast charges in those areas where rivals are commencing fibre network roll-outs. Ofcom's proposal, however, do not go far enough and should also be extended to BT's FTTP wholesale pricing.
3. In the sections that follow we set out (i) the importance of infrastructure-based competition; (ii) the harm that would arise absent intervention from Ofcom; and (iii) the need for Ofcom to go further and extend its proposals to wholesale FTTP charges.

### **Ofcom has identified that network-based competition is the most effective driver of investment and innovation**

4. In its Strategic Review of Digital Communications (DCR), Ofcom set out its ten-year vision for ensuring the quality and availability of communications services in the UK. One of Ofcom's key strategic objectives, which Three strongly supports, is to reduce the country's dependence on Openreach. As part of its strategy for delivering this vision, Ofcom identified competition between fixed networks as the most effective spur for continued investment in high quality, fibre-based networks.
5. In setting out the three main elements of its strategy for delivering fixed competition and investment, Ofcom identified the pricing of regulated access to superfast and ultrafast services "to give everyone incentives to invest".<sup>1</sup> More specifically Ofcom

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<sup>1</sup> [Initial conclusions from the Strategic Review of Digital Communications](#), Ofcom, February 2016, pg 36.

committed not only to preserving the investment incentives faced by BT (by applying the 'fair bet' principle), but also to setting prices so as to ensure there are incentives for operators to build new networks, as opposed to relying overly on buying access from BT.

6. Ofcom must now stand firm on this commitment to prevent BT from exploiting its market power to undermine competing infrastructure deployments. Planned rollout by Cityfibre, Gigaclear, Hyperoptic, Vodafone and others is only expected to connect 6 million homes, or 20 per cent of the UK. We urge Ofcom to act decisively and protect these players in order to ensure the emergence of rival infrastructure to BT's.

### **BT has the ability and incentive to frustrate infrastructure-based competition**

7. In the absence of intervention from Ofcom, BT has both the ability and incentive to target reductions in wholesale access charges in those areas where rivals are commencing FTTP deployments. While this may benefit consumers in the short-term via lower retail prices, it will be to the ultimate detriment of consumers by damaging the emergence of infrastructure-based competition in the longer term.

#### *Impact on the emergence of infrastructure-based competition*

8. The investment case for competing full-fibre deployments relies on operators achieving a minimum efficient scale of subscribers. Investment in fibre networks is risky due to demand uncertainty, large sunk costs and long payback periods. It sometimes requires 'anchor tenants' that contract sufficient volumes upfront to make deployment economically viable.
9. Modelling by Analysys Mason shows that market share is a key determinant of the viability of FTTP deployment. In particular, Analysys Mason found that an operator would need an existing customer base with a market share of 20% to viably deploy an FTTP across 5% of UK premises.
10. Scale cannot be reached through retail subscriptions alone and requires that an operator also acquires a significant proportion of wholesale subscriptions. Indeed, [§<]).
11. Targeted wholesale price reductions by BT would have the dual effect of (i) reducing an infrastructure investor's ability to earn sufficient returns from retail customers (due to retail price reductions facilitated by the reduction in wholesale cost); and/or (ii) reducing its ability to acquire wholesale customers, which will be less likely to switch to the newly deployed FTTP network.
12. This will have the effect not only of undermining investment incentives in the specific locations in which BT engages in this pricing behaviour, but more broadly across the UK, by establishing a credible reputation for entry deterrence.
13. While there may be a short-term benefit to consumers in the form of lower retail prices (assuming pass-through of lower wholesale costs), in the longer-term customers will be worse off due to the foreclosure of infrastructure-based competition.

14. We therefore support Ofcom's proposal to amend the existing no undue-discrimination obligation to explicitly prohibit BT from geographically varying its wholesale charges for VULA and G.Fast.

### **Ofcom must go further to protect infrastructure competition**

15. Ofcom's current proposals would only prevent BT from engaging in targeted wholesale pricing in relation to its existing FTTC products and future G.Fast roll-out. BT would still retain the ability to limit infrastructure competition through local pricing of its FTTP roll-out.
16. This is highly problematic given BT's strong incentive, once committed to an FTTP investment in a specific location, to price to discourage further investment and maintain its local monopoly in physical infrastructure.
17. In fact, Ofcom's proposed half-way house of regulating only FTTC and G.Fast pricing, would actually increase this risk. This is because, absent an ability to lower FTTC prices by geography, BT has a strong incentive to use FTTP prices to reduce the differential between its FTTC and FTTP wholesale charges. This will ensure it acquires wholesale customers on its FTTP network at the expense of actual or potential FTTP network competitors.
18. This incentive is further exacerbated by BT's unique ability to subsidise targeted FTTP price reductions with the opex savings it can realise by switching off legacy copper network services in areas where it has made its FTTP investment.
19. Ofcom justifies its proposal not to extend the restriction to FTTP is on the basis that this "would do little to help" emerging network investment by rivals because:
- (i) BT is not as readily able to engage in regional FTTP pricing because it would first need to deploy an FTTP network; and
  - (ii) BT's FTTP roll-out is unlikely to overlap with competitors' given its current limited scope.
20. With regards to (ii) we disagree with Ofcom's assumption that there is a low probability of overlap in FTTP deployments. Both BT and its competitors will have undertaken geographic cost modelling analysis to inform the locations of their network roll-outs. For example, [3]. BT and its competitors will share a similar incentive to target their FTTP roll-outs in such areas to minimise the cost of deployment. This is also consistent with Analysys Mason's 2016 FTTP modelling which assumes that CPs deploying FTTP networks will target densely populated areas first.<sup>2</sup>

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<sup>2</sup> [Comparative analysis of the outcomes in the UK broadband market: coverage, connections and competition](#), Analysys Mason, October 2016.

21. As such, rather than being a justification for Ofcom not intervening, minimal geographic overlap in deployments is in fact the very outcome that BT will be seeking to achieve through targeted variations in its wholesale FTTP prices.
22. With regards to Ofcom's conclusion that BT is not readily able to engage in regional pricing of FTTP, we accept that it is less able to do so than with respect to its current FTTC products (or G.Fast which can be rolled out more quickly). However, given the strong incentives BT faces, there is a real risk that it may engage in this type of anticompetitive behaviour.
23. Given Ofcom has not identified any specific adverse effects or costs associated with extending its proposals to FTTP, it is therefore a proportionate and justifiable course of action for Ofcom to include FTTP in its proposals, in line with its duty to promote competition in communications markets.