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Celebrating Twenty Years of Competition and Looking Forward to the Next Twenty

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PREAMBLE

- Thankyous, acknowledgements.

WE DID IT!

One of the first things I'd like to do is celebrate the fact we've had a competitive telecoms industry in Australia for 20 years!

This is it – it was 20 years ago tomorrow that Optus was granted the second carrier licence and we got this party started.

It's kept all of us busy ever since, hasn't it? It's given me a job. It's given the policymakers rules to change. It's given the lawyers things to fight about – and to bill us for. It's given Telstra endless meetings about how to stop it!

You know, the reality of competition in this industry really hit me a few years ago when we formed the Terria consortium. Terria was created to fight for access to Australia's broadband infrastructure – or to build an alternative. It included Optus and pretty much everyone else except Telstra.

One day we all met up in Canberra to take our case to the Government. The joke is that we all fitted into one minibus. Imagine if we'd crashed – the whole of the competitive industry gone in one stroke!

Luckily we didn't. And I think we can all be proud of what we've achieved.

Australia has earned enormous benefits from competition. I'll look at those gains in some detail today as we review the past two decades and the impact competition has had.

But we've also got to keep fighting for these benefits every day. And the latest battleground is the National Broadband Network.

On that, I'd like to do three things:

- Talk about why we want an NBN and why it is a great nation-building exercise.
- Discuss why we believe it's not being set up right. We believe the NBN is on a knife edge – it could go either way as a success or failure.

- Call Telstra's bluff on the NBN and structural separation – these guys are saying one thing and doing another, again! It's time for it to stop.

20 YEARS OF COMPETITION

Let's start by casting our minds back 20 years to before competition.

Back then there was only one telco, Telecom, and it was fully owned by the Government. If you wanted a phone line you *wrote* a letter to Canberra, then you waited. And waited...!

OK, I exaggerate, but you get the point. You only had one choice.

Telecommunications was a vertically integrated monopoly and a sleepy one at that.

That all changed on 19 November 1991 when Optus won the licence to compete against Telecom in the fixed-line and mobile markets.

The deal involved us taking over the Government's struggling AUSSAT operation, which had debts of some \$800 million.

As a bit of fun, let me play you one of our early ads.

So, we were born out of the need for competition. We were the first challenger and we proudly remain the biggest challenger today.

There are a number of key points in our history.

The first was getting our licence and giving Australians a choice for their long distance calls. You might remember the pre-selection ballots and other steps of the early 1990s as people became familiar with this idea.

On 18 May 1993, we finished and launched our GSM network. Today, that network serves more than 9 million customers and reaches more than 97% of the population.

In 1994, we formed Optus Vision and started into the now infamous cable wars. We built dual infrastructure and competed aggressively for content rights. In the end, we wrote off a billion dollars and learned the hard way about competing on a playing field that isn't level.

It wasn't all bad though. In the 1990s, we also built our fibre customer access network throughout Australia's key centres. This gave business, government, ISPs and others a genuine choice of carrier.

We were also expanding fast. By the time of the Sydney Olympics, we had sales of \$4 billion and around 3 million customers.

But we were bleeding cash— as much as \$500 million a year.

I don't think people realise how close we came to failure a decade ago. My predecessor once told me a story of going to the bank one day to borrow the money he needed to meet payroll. It seems incredible today.

In 2001, we joined Singapore Telecommunications, or SingTel. This was an important turning point for Optus. It started our transformation from losing money to being a sustainable competitor today.

Since that time, we've continued to grow strongly. We now turn over more than \$9 billion. I'm pleased to say we've also just announced our 16th consecutive quarter of EBITDA growth in a very competitive market.

We are still the market leader in satellite as well, and we have continued to refresh our fleet. That's a huge turnaround since the days of AUSSAT.

Finally, we are making major strides in the digital media space. We've launched an array of digital products this year, which is making people rethink the notion of the telco or carriage provider.

BENEFITS OF COMPETITION

To recognise our anniversary, we commissioned a report into the impact competition has had over the past 20 years.

This report is called 'Unfinished Business' and was prepared by David Kennedy at Ovum.

The report tells the tale of two markets.

In the mobile market, the settings were right for vigorous, infrastructure-based competition. That market has exploded as a result, and consumers have enjoyed the benefits of choice, innovation and value.

But in the fixed market, we've had the legacy of a vertically integrated incumbent. This has stymied competition and limited consumer benefits.

The report notes that the decision that has had the most impact was the one to merge Telecom and OTC in 1992.

The Government's dream was that this combined entity would become an international powerhouse and a national flag carrier for Australia.

Unfortunately, Telecom and OTC never became a global telecommunications leader. Instead, it just created an oversized incumbent here in Australia – one that retained monopoly access to 90% of homes and reaped 60% margins.

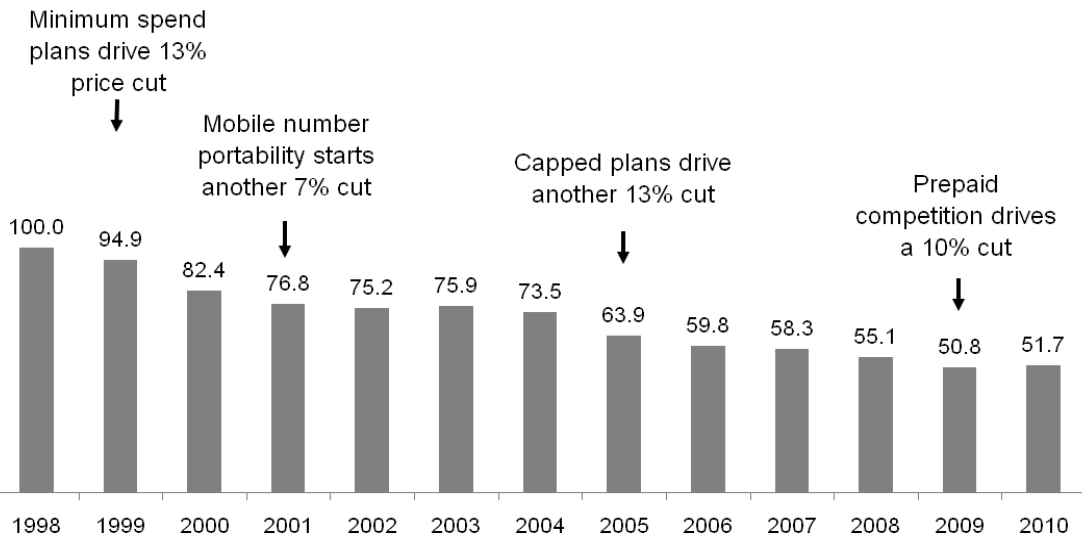
This gave it the profitability and market power to maintain its dominance, which it's done ever since.

Price, value and dirty tricks

This is why the report is called 'Unfinished Business'. We still don't have a truly competitive telecommunications environment in this country.

That said we have certainly seen benefits from the competition we do have.

Figure 1: Mobile price index and major competitive events



Source: ACCC, 2010

O V U M

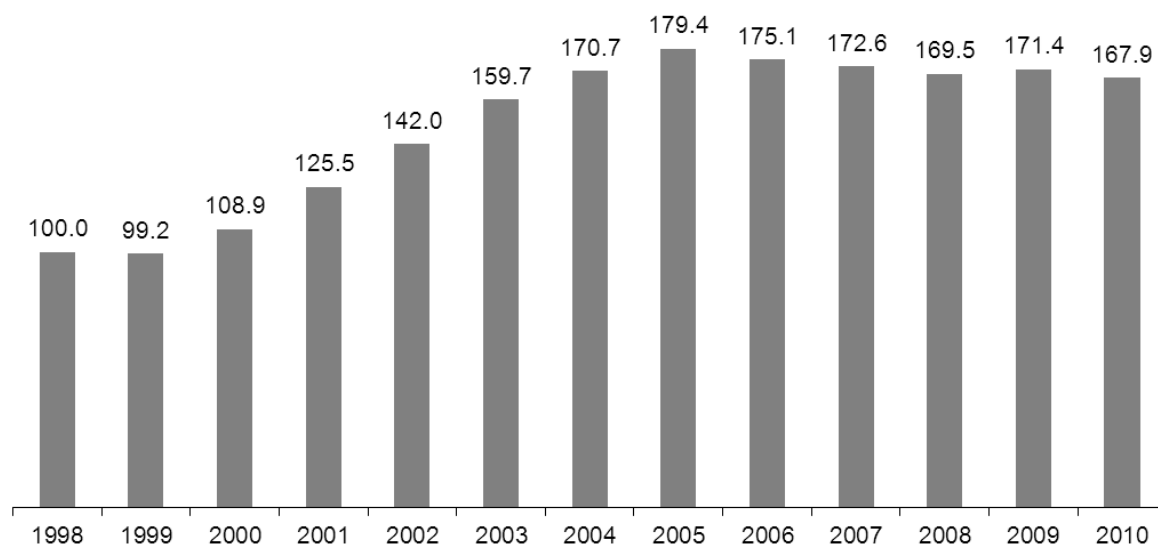
This shows how prices have fallen in the mobile sector, where there has been healthy competition since the mid-1990s.

You can see that prices have halved over the past ten years or so, and that these falls have followed some key events:

- In 1999, minimum spend plans drove prices down by 13%.
- In 2001, mobile number portability led to a 7% fall.
- In 2005, the arrival of capped plans drove prices down another 13%.

- In 2009, competition in prepaid saw prices fall another 10%.

Basic access price rises 1998 to 2010



Now, let's look at what's happened where Telstra has really held on to its monopoly – basic access charges for the national copper network.

Access prices rose 68% from 1998 to 2010. Wow.

Much of this follows Telstra jacking up its line rental charges to compensate for lost call revenue. The worst part about that is the government at the time let them get away with it! One reason they did, as we all know or at least suspect, is to maintain Telstra's value as they sold out of it.

So, you've got a monopoly with a complex relationship with government. This leads to poor regulatory outcomes and higher pricing for consumers.

Anyone feeling queasy about the NBN yet?

Haven't we seen this movie before? Do we want to see it again?

I'll come back to that...

Innovation

Another important benefit of competition is innovation.

Competition gives players a reason to introduce the latest technologies and possibilities for customers – and to do it first.

For example, Optus was first to offer data services over GSM. Today we continue to innovate with new products such as Optus TV Now, which allows you to record and watch free-to-air TV shows on your mobile.

Let me show you what I'm talking about.

Now, compare that sort of breakthrough to the snail's pace of innovation around the monopolised copper network. Just consider how we had to push to get ADSL going – that kept Australia in the slow lane for years.

Service

The third benefit of competition is better service.

I can tell you that this has been our main focus at Optus for a number of years now. As an industry, we're more focused on service than we've ever been. This is the new battleground and it's a race to the top.

Again, which future do you want for the NBN? How do we make sure NBN Co has an incentive to innovate and to provide great service to its customers?

A PROPHET IS NEVER RECOGNISED AT HOME

We have concerns about the governance of NBN Co but – and let me be very clear – we do support the creation of a high-speed, national broadband network. This is an important upgrade to Australia's infrastructure.

The policy idea is sound. An NBN will deliver real social and economic benefits. A new study shows that doubling the speed of broadband boosts an economy by 0.3%.¹

That might not sound like much, but in Australia 0.3% of GDP is \$3.9 billion a year. The NBN, as it's currently proposed, will increase our average broadband speed by at least 10 times.

The current debate about the NBN reminds me of the biblical phrase that a prophet is never recognised in their own land.

¹Study by Ericsson, Arthur D. Little and Chalmers University of Technology, released 27 September 2011. See <http://www.adlittle.com/press-press-releases.html?&view=346>

We can sometimes fail to recognise innovation when it's close to home. We focus on everything that can go wrong because we're in familiar territory.

Some great examples from the past are the Snowy Mountains Scheme, the Sydney Opera House and even the Australian Institute of Sport. They all had their detractors in their day but have since proven to be great successes.

When 'prophets' from overseas look at the NBN, they like what they see.

In January this year, Vint Cerf, the 'father' of the Internet, said:

“I continue to feel a great deal of envy because in the US our broadband infrastructure is nothing like what Australia has planned.”

Cerf has described the NBN investment as “stunning” and predicted it will have a “very long term benefit”.²

So, we think the NBN is a great idea. Top experts from overseas recognise that it is a visionary project. But let's do it right.

NBN ON A KNIFE EDGE

As I said at the outset, we believe the NBN is on a knife edge.

²Source: <http://www.theaustralian.com.au/australian-it/telecommunications/internet-visionary-and-google-web-evangelist-vint-cerf-praises-nbn/story-fn4iyzsr-1225992510039>

I'm being intentionally dramatic with that language because I want to make it clear that we believe this project could go either way.

It could be a major success. Or it could be a huge failure.

What is going to make the difference? The difference will be whether the network delivers in terms of quality, service and cost.

It will also be the impact the NBN has on our whole competitive ecosystem.

Optus has strongly supported the present Government's policy reforms. They are the most far sighted we have seen in telecoms since 1997.

We've also welcomed the Opposition's support for structural change. Though, as I'll highlight later, we are keen to see more detail on their position.

But it's important to recognise that we are embarking on a unique experiment. We are re-establishing a government-owned monopoly telecommunications provider.

Let's remember, the NBN will be a wholesale-only network. It won't have the incentives to discriminate that Telstra has. But it will still be a monopoly provider. In fact, the legislation has ensured it will face no competitive threats.

For this policy to work, we cannot rely on NBN Co to do the right thing. It must face the tightest form of regulatory oversight.

This isn't a new principle. Go back to the Hilmer Report in 1993, which is in many ways the cornerstone of national competition policy today.

Given Australia's size and small population, we were never going to build duplicate rail, electricity or phone networks. Hilmer recommended the creation of access regimes to stop natural monopolies in areas like rail, power and telecommunications from abusing their power.

Our concern today is that we've already seen NBN Co flexing its muscles on some issues. These include the location of interconnection points and its wholesale broadband access terms.

Some of the concessions NBN Co asked for in early versions of its Special Access Undertaking would also make Telstra blush.

Regulatory solutions

What do we need to put in place? How do we control this new monopoly called the NBN?

To help answer these questions, we recently commissioned a report from SPC Network, an independent consulting firm in the UK. The report states very clearly that the NBN must have clear rules and regulations if it's going to deliver the highest quality services at the lowest cost.

Based on the report and our own analysis, we believe the ACCC has a crucial role to play in policing the NBN. Let's look at some of the issues.

- **Spending.** NBN Co has asked for limits on the ACCC's ability to scrutinise its initial capital build. I'm sorry, but as an infrastructure monopoly, someone has to make sure this thing's spending is efficient or consumers will end up paying for it.
- **Pricing.** There should be no presumption that prices can rise over time. There should be a cap on the price changes NBN Co can make.
- **Efficiency.** If the ACCC finds NBN Co is operating inefficiently, it should have the power to order it to outsource some activities. In other words, if it can't do something well it should face competition.
- **Service and innovation.** NBN Co should have quality of service and innovation targets. Incredibly, its current wholesale terms provide little or no service performance guarantees.
- **Transparency.** When it comes to decision making, NBN Co should have the same transparency and bi-partisanship as the Reserve Bank. There should be a register of contact between the Government and NBN Co, to limit undue influence. The minutes of NBN Co board

meetings should be published, and there should be public consultation before major changes to NBN Co's Corporate Plan.

These steps would all help ensure the NBN Co has real incentives to perform – and that we know what it is doing.

This isn't about Optus seeking a better deal. It's about Australia getting the right settings in place for the next 20 years of competition.

The NBN will be a monopoly – probably one of the most powerful we have ever had in Australia. It's vital that it is subject to a forensic level of scrutiny and strong regulatory oversight. That way the interests of competition and consumers will be protected for the benefit of everyone.

CALLING TELSTRA'S BLUFF

Now, I'd like to call Telstra's bluff on the NBN and structural separation.

In a familiar game, Telstra is saying one thing in press releases and doing another in their regulatory submissions.

The key issue regarding Telstra right now is its Structural Separation Undertaking. This is the agreement to separate its last mile infrastructure from the rest of its network, and to ensure there is a more level playing field as we move toward the NBN.

There are two key reasons we need a level playing field.

The first is so that Telstra can't use its existing monopoly to lock down customers as it starts selling NBN services. Keep in mind that this process is going to go on for at least eight years.

Second, the NBN may never be completed in the form that is currently proposed. Let's say there was a change in government and the NBN is only half finished. In that scenario, we will need strong competitive safeguards.

Now, what has Telstra been saying and doing?

When Telstra released its undertaking, its current CEO said, "...the SSU delivers robust, effective and appropriate equivalence and transparency during the migration period."

What nonsense.

The first draft of Telstra's undertaking was woefully weak. I don't think I'd quite describe it as a middle finger to the industry – as one of my peers colourfully did recently – but it did represent breathtaking hypocrisy by Telstra.

But it gets worse. The changes Telstra has flagged since would wrap the SSU in more red tape. They would also further limit the ACCC's powers.

Here's an example. Telstra has finally accepted the need for an overarching equivalence obligation in its SSU. But guess what? There are at least 16 qualifications attached to this commitment. It is so limited, ambiguous and hard to enforce that it's not worth the paper it's written on.

The ACCC is reviewing the undertaking and working towards a resolution.

We call on the ACCC to reject Telstra's submission until it meets the test on all measures of equivalence. The ACCC should not compromise. It is too important to the future of the industry – and ultimately the success of the NBN – to concede at this stage.

Opposition stance on SSU

I'd also like to call on the Opposition to clarify its position on separation.

Successive governments have struggled to get Telstra to the negotiating table – and rightly so. As a private company, they've got an obligation to their shareholders to do everything in their power to protect their monopoly profits for as long as possible.

The Opposition says it supports the structural separation of Telstra. However, they have not said how they are going to force Telstra to co-operate. There is no proposed legislative instrument that would force Telstra to comply with its own undertaking.

We need to see that sort of legislative stick. This will be critical to forcing Telstra to the negotiating table if problems arise. We know they won't do it voluntarily (as this cartoon from *The Australian* in April 2009 sums up nicely).

We also know the longer the structural separation debate goes on, the longer Telstra gets to protect its monopoly profits.

TIME TO ACT

We're not at 11pm anymore on the NBN. We're at five minutes to midnight.

The decisions and measures we put in place now will have implications as long-lasting as the decision to merge Telecom and OTC.

It was a similar debate. Should we compromise on competitive principles and bring in light-touch regulation to chase an aspiration?

It wasn't a good idea 20 years ago. It's not a good idea now.

We're not looking for anything new here either. The cornerstones of competition that Optus has been promoting for many years are that we need:

- structural separation
- equivalence of access
- strong regulatory oversight, and

- fair access pricing.

If we can get these conditions in place, then I truly believe the NBN will be a fantastic asset and that it will play a key role in Australia's future prosperity.

CONCLUSION

Thank you for your time today.

We're excited to celebrate 20 years since winning our carrier licence, and thank you again to CEDA for the opportunity to speak.

I'd also like to acknowledge the enormous contribution that every member of the Optus team has made over the past two decades.

The introduction of competition in telecommunications has delivered vital benefits to Australia. We've seen better value, more innovation and improved service. We've also lived through three huge waves of innovation: mobile telephony, the Internet and the first generation of broadband.

Now we stand on the threshold of a whole new age: the era of fast and truly national broadband. We can't even imagine much of what's coming.

But there is one thing that has remained true throughout the history of commerce. This is that, over time, unregulated monopolies always behave badly.

Competition doesn't just happen. You can't take it for granted. You have to fight for it every day.

That's what we'll keep doing at Optus to ensure you – and all Australians – keep gaining the benefits.

Thank you and I believe we have some time for questions.