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***The growing importance of content for the telecommunications industry***

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For many telcos, content is a touchy subject.

Certainly Optus has its fair share of scars from our attempt in the mid nineties to build our very own content factory to supply our then fledgling pay TV business.

I believe that in Hollywood, even today, you need merely mention the phrase “Australian pay TV executive” and they double over in laughter – before telling some war stories of how much they took those suckers for.

Yet at the same time, a sober analysis of the threats and opportunities in telecoms suggests that content is becoming an ever more important part of the landscape – particularly as technologies converge and we move to broadband networks in both fixed and mobile.

So today I want to first remind us all briefly of how convergence is bringing the telecoms industry together with entertainment and information.

My next point is that a new value chain is emerging.

As I will show, different telcos have followed different models – in considering where in this value chain they want to play.

I want to discuss Optus' approach.

And finally I want to discuss the regulatory landscape in relation to content.

## **Convergence and telcos**

Five years ago, convergence was hype. Today it is a daily reality.

Let me give three brief pieces of evidence for this claim.

First, data is an increasingly important part of our mobile business.

This data usage explosion began with the rise and rise of SMS (Australians now send around 5 billion SMS annually<sup>1</sup>) – however it is increasingly moving to much richer content.

This reflects better network technology – both 2.5G and 3G – and handsets which are better suited to carry data – otherwise known as content.

Secondly, fixed broadband penetration is growing – and with that we are increasingly seeing fixed line operators delivering the triple play of voice, video and data.

Thirdly, we are increasingly seeing content businesses developing content for the networks operated by the telcos.

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<sup>1</sup> *Telecommunications Performance Report 2003 – 04*, The Australian Communications Authority, Chapter 6: Mobile Telecommunications Services.

Internet portals like Yahoo – which can already offer content to audiences of millions – are actively sourcing advanced video content for the Internet, a move which is likely to increasingly involve the giant Hollywood studios.<sup>2</sup>

### **A new value chain**

As these developments and many others suggest, a new value chain has emerged, extending across telecommunications networks and content businesses of all kinds.

The new value chain is underpinned by the dramatic impact of ubiquitous digital technology.

There are new opportunities for telcos in this new world. Can we, for example, now earn advertising revenue streams – as the broadcast television industry has done for decades?

But there are new threats as well. Just as convergence lets telcos compete with television and newspapers – it also exposes us to competition from these same sectors.

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<sup>2</sup> *Yahoo raises profile with Hollywood push*, 3 April 2005, [http://biz.yahoo.com/ap/050403/yahoo\\_goes\\_hollywood.html?.v+3&printer+1](http://biz.yahoo.com/ap/050403/yahoo_goes_hollywood.html?.v+3&printer+1)

And let's be honest – these players know a lot more about content than your average cardigan wearing telco engineer.

### **Telcos are following different models**

The biggest challenger for telcos in many ways is to decide where in the value chain it makes sense for us to compete.

Our traditional strength is in distribution. We operate the networks and will continue to do so.

More-over content is tending to move from single purpose networks, like television networks, to multipurpose digital networks, operated by telcos.

But should we move into other stages of the value chain?

There are several different models being tried.

One approach is for telcos to buy content companies and take on a content producer role.

We know that Telstra looked seriously at buying Nine and Fairfax in an attempt to lock up the content they provide. While these particular deals fell over, Telstra has spent big on several other content companies including the Trading Post.

In the mid nineties both Optus and Telstra set up vertically integrated pay TV operations incorporating substantial content operations.

The financial result has not been a particularly happy one for either company.

When we look at the track record in Australia and overseas (at companies like Bell Canada<sup>3</sup>), the record of telcos simply buying content companies does not seem a very inspiring one.

In my view, there are good reasons for that. Content operations require different skills to those required in the telecoms industry.

Telcos which seek to become content houses will likely only burn their fingers.

There is a second model which is often attempted by the telcos.

This is a walled garden or exclusive content model.

The logic usually runs as follows: “We own the relationship with the customer. We will control the content they can access.

Content providers will want to get on our platforms – they will have no choice. And customers will choose us because they will want to get content that they can only get through us”.

It is the model that broadband operators have tried, such as Excite@Home in the US.

In our view, this approach is not the right one either.

For one thing, trying to keep customers within your walled garden often doesn't work and frustrates – as the gradual erosion of AOL's market share in the US demonstrates.<sup>4</sup>

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<sup>3</sup> *It makes sense for BCE to sell Bell Globemedia: Fits strategic agenda*, 22 February 2005, Financial Post

<sup>4</sup> *Churn sours AOL*, 3 June 2003, *The Guardian*.

Similarly, forcing them to buy from you because you only have the content restricts competition on all the items that matter to customers – service, price, quality, speed and availability.

But more importantly, it is not the right way to maximise traffic – which is ultimately in the best interests of customers, network operators and content providers.

We telcos need to make sure that our mobile customers, our broadband customers, our pay TV customers, can access all of the content they want to see. Forcing them to choose one operator or another, because only one operator has the football for example, is not the right approach.

And the more content that a customer can access over any one telco's pipes and portal, the more money that telco will make.

### **Optus' content strategy in the broadband mobile world**

I now want to talk about Optus' strategy in content.

At Optus, we believe we have a critical role in delivering broadband and mobile content to our customers.

We see ourselves as enabling each and every user to have the richest possible content experience.

So we will seek out the best content providers and aim to make their content available to our customers.

We believe the mobile users of the future will want their handsets to be electronic passports to the world, not gateways to a limited, pre-chosen pool of exclusive content.

If I can draw an analogy, we think of ourselves as a bit like an operator of shopping malls. Westfield, for example, has built a hugely successful business through their skill in building shopping centres and drawing traffic to those centres.

They take care with the mix of stores in the centres, as well as the overall design and positioning and provide an attractive and secure environment for browsing and buying content.

What Westfield does not do is sell whitegoods, or clothes, or groceries. Westfield contracts with Harvey Norman, or David Jones, or Woolworths, to take space in their shopping centres.

And the totality of the customer experience depends on a combination of the skill with which Westfield does its job and the skill with which the retailers like Woolworths do their job.

The analogy is not perfect, but we think it is quite helpful in thinking about the appropriate role for telcos in content.

We think freedom is the name of the game for the modern consumer. Every customer will want a different mix of content.

Trying to predict what customers will want, and dictate to them, is in our view neither appropriate – nor likely to succeed.

As technology breaks down the old barriers between the telephone, the Internet, the radio, the TV and so on, the mobile and other broadband devices are well placed to become the integrated hub for people's connections to the information world.

Users want a consistent content experience regardless of the access method – fixed or mobile.

Let me talk specifically about what we plan to do for the ubiquitous user:

- We will give freedom of expression. From ring tones to music to video, each consumer can be an audience of one, building a truly personalised experience. Active personalisation is the key.
- We will manage content access. By providing clear categories, we will make it easy for the customer to navigate the cybermall.
- We will take the consumer quickly to where they want to be. We are investigating ways to simplify access to whatever content customers want. This includes search engines specifically designed for mobile usage.
- In broadband we'll offer video, voice and applications and all through one pipe.
- We are looking at leading edge location-based services, which are going to grow in importance.

- We are exploring advanced billing systems designed to give greater clarity and precision in billing.

Last month, I announced a business realignment that brings together our fixed and mobile consumer business.

An important part of that realignment is to take an integrated approach to content across all of our platforms.

Indeed, we have formed a company wide content group for the first time at Optus.

### **Policy issues relating to content**

Before I conclude, let me comment briefly on an important policy issue.

ACCC Chairman Graeme Samuel has been speaking about content exclusivity in recent months. He has highlighted concerns that some telcos may be using content exclusivity as a tool to reinforce their market dominance.<sup>5</sup>

Optus is pleased that the ACCC is investigating this issue.

We have noticed with some concern that our largest competitor has been building up a portfolio of exclusive content deals, covering AFL, V8 Supercars, NRL and other sporting codes.<sup>6</sup>

At Optus, we believe this kind of exclusive content model is bad for the industry and bad for customers.

Optus wishes to see a world where network operators with substantial power are not permitted to leverage and reinforce that power by acquiring exclusive rights to sporting and other content.

Optus has called for Government and ACCC action to investigate the Telstra-led push to rush to exclusivity.

The Italian regulator is actively trying to address this very issue and has been proactive in ensuring that all operators who invest in infrastructure are able to access quality content. FastWeb<sup>7</sup> – one of the most advanced triple play operators globally – is one of the telcos to benefit from this approach.

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<sup>5</sup> Speech by Graeme Samuel to the Australian Telecommunications Users Group, 10 March 2005.

<sup>6</sup>Telstra media releases:

*AFL multimedia content exclusive for BigPond broadband customers*, 16 March 2004.

*Bigpond provides only off-track live v8 supercar coverage to top end fans*, 14 May 2004.

*Bigpond is first pick for live 2004 National Bank's AFL Draft coverage*, 19 November 2004.

*NRL & Bigpond benefits*, Telstra website, [www.bigpond.net/nrl/](http://www.bigpond.net/nrl/)

Today Optus has no option but to operate in the second best world. But if regulatory action leads to a “first-best” world of non-exclusivity, we will be very happy to operate in that world and cease to acquire content on an exclusive basis.

## **Conclusion**

In conclusion, then, today I have discussed convergence and the growing importance of content in the telecommunications sector.

This is driven principally by market and technological changes, with broadband services becoming increasingly widespread in both fixed and mobile.

These changes clearly require telcos to respond – and to capture the opportunities which arise.

There are traps though, if you think the right approach is to become a content player yourself.

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<sup>7</sup> *Triple Play Case Study – Fastweb*, 9 March 2005, Telecommunications Sector Commentary, Goldman Sachs JBWere.

Rather, the best strategy is to work to deliver the widest possible range of content on your platforms.

That is the strategy Optus is following and we think it will deliver the best results for our customers – and our shareholders.