



Speech

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Communications Alliance

The ever growing power of the telecommunications user

Good afternoon ladies and gentlemen.

Fifteen years ago there was no such thing as the Communications Alliance. There was no need to agree industry positions or to determine rules which applied to all carriers.

Fifteen years ago, like most other OECD countries, Australia had only one telecommunications operator. It decided everything, and customers could take it or leave it.

Our industry has changed enormously in the last fifteen years, but there is one change which stands out. The telecommunications customer has grown ever more powerful, year after year.

Many companies represented in this room today have played a big part in that, by offering real choices to customers.

And the Communications Alliance has also played a big part – for example, in developing Codes which protect the interests of consumers.

With our industry becoming ever more competitive, I believe the trend of growing customer power will only continue.

That is why I want to focus on this trend in my remarks today.

First, I want to give some evidence of growing customer power.

Next, I want to look at how our industry is responding.

Thirdly, I want to talk about the ongoing implications for our industry – and for public policy – particularly in the post T3 world.

The Steadily Growing Power of the Consumer

Let me begin, then, by pointing out how the power of customers has grown.

The first and most obvious change has been that as more vendors become available, customers have exercised their choice, and operators have needed to respond with sharp price reductions.

According to the ACCC, since the base year of 1997-98, the price of national long distance services fell by 27.1%; the price of

international long distance calls fell by 62.7%; and the price of local calls fell 44.3%.¹

And in 2004-05, the price of national long distance services fell by 1.7%; international calls fell by 3.6%; and local calls fell 11.1%.²

In the last two years, we have seen sharp price reductions in mobile services, with the arrival of capped plans.

For example, on a \$49 cap from Optus, you get up to \$230 of included value.³ Capped plans have grown to 24 percent of the Optus postpaid base.⁴

These price reductions have delivered substantial national economic benefits – worth \$12.4 billion to the Australian economy since telecommunications was deregulated in 1997, according to estimates published by the Australian Communications and Media Authority.⁵

The second change to highlight is that customers increasingly enjoy a choice of technologies.

¹ ACCC telecommunications reports 2004 – 05. Changes in prices paid for telecommunications services in Australia, 2004-05. April 2006

² As above.

³ www.optus.com.au/cap

⁴ Optus MD&A Q2 ended 30 September 2006. Page 41

⁵ Australian Communications and Media Authority Telecommunications Performance Report 2004-05. Chapter 2 – Benefits resulting from changes in telecommunications services. Page 21.

So if they are unhappy with their fixed line service, they can choose to use mobile. If they are unhappy with their fixed broadband, they can move to wireless broadband.

Indeed, the technology is also giving customers the opportunity to customise the service they want – what speed, what download limit.

For example, for a number of years, the incumbent limited its consumer DSL offering to a top speed of 1.5 megabits per second.

But competition is delivering a growing number of Australians the choice to take a significantly higher speed service, ADSL 2+, from Optus or perhaps another operator such as iiNet.

It is interesting that this competitive pressure has recently driven the incumbent to upgrade its broadband offering to ADSL2+ – but only in the geographic areas where Optus and others are providing competition.⁶

The good news for consumers is that the ‘competition zone’ is steadily expanding – Optus has now installed DSLAMs in over 175 exchanges, and we are on track towards our target of 340 exchanges by the end of 2007.

⁶ Media release “BigPond marks 10th anniversary with launch of national high speed broadband” 10 November 2006

Additionally, 1.4 million households served by the Optus HFC network can have cable broadband.

Added to that are wireless broadband offerings from Unwired in Sydney, from Optus satellite across rural and remote Australia, and other options besides.

In the US broadband market, choice is even more extensive. Most households are served by at least two physical networks, one from the local telephone company and one from the cable television company.

The result has been intense competition in the broadband market between DSL and cable modem services.

There are powerful forces underlying the expansion of choices and of customer power – a combination of more operators, digitisation, the growth of internet protocol and the rise of broadband.

Consumers are benefiting from a combination of changes in technology and changes in market structure. The result is that consumer preferences are much more readily satisfied today than fifteen years ago.

Every company represented in this room today has played a part in that transformation.

The ultimate demonstration of growing customer power is that technology is allowing for greater customisation.

Customers can choose what they want to do with their own content, where they want it to be viewed and shared with. We've seen this in the disintermediation of content through sites like You Tube.

Operator Strategies – What Works and What Does Not Work

Today, customers are well aware of their power.

Which means all of us in the industry face a strategic challenge in how we respond.

Let me offer some thoughts.

To start with, I'd like to share with you one of the biggest lessons I've had in my decade at Optus.

Customers are essentially technology agnostic. They buy benefits not specific technology.

You'll see that most of our advertising focuses on applications and benefits rather than pipes, and spectrums and bandwidth.

If you try to force technology down customers' throats, you will fail.

Wireless Application Protocol (WAP) and the early days of e-commerce are good examples of technologies that failed to inspire customers.

An earlier example is the attempt by AT&T to introduce video calling in the late eighties.

Customers were resistant, citing privacy concerns.

So AT&T fitted the devices with blinds – which the customer would only open once she knew who was calling and she was satisfied she wanted to be seen.

Sadly, the experiment was not a success – and we needed to wait until the new millennium before 3G made video calling a reality.

But the flip side of this lesson is that when the industry can deliver a technology which helps customers live their lives better, they will take it up in droves.

Two stand out examples are the take up of mobile phones and of SMS.

Mobile was expected to be a poor relation to landline long distance telephony when Optus paid for its license in the early 90s.

We originally planned no more than 200 base stations in Sydney and Melbourne – now we have more than 4,000 nationally.

Obviously, we are pleased that we moved on from that early thinking! We now have more than 6 million customers and Mobile is the most successful part of the Optus business.

Another excellent example of where customer usage has exceeded all expectation is SMS.

Last financial year, 2.837 billion messages were sent across the Optus network – with 34 million on New Year's Eve and day alone.

So far this financial year we have seen 2.464 billion text messages sent and we still have several months to go.⁷

Interestingly, one of the key reasons SMS took off was that carriers agreed to intercarrier SMS. The carriers stopped trying to own customers exclusively.

⁷ Optus Networks

This brings me to my second observation about how to succeed in a world where customers have the power.

Trying to force customers to deal with you exclusively does not work. Helping customers to exercise a choice does work.

We have seen this most clearly in the differing approaches to content in telecommunications.

At Optus we don't lock up content, we don't ring fence it and we don't do exclusive content deals.

Instead, we seek to aggregate leading content and services like Disney, MTV, ABC and Ninemsn for our customers to access if they choose to.

We also give our customers the tools they need to get the content they want - tools like Really Simple Syndication (RSS) feeds, personalised web sites and Google mobile search.

Indeed, Optus was the first to offer Google on mobile.

The alternative approach, preferred by some telcos, is to provide a fully programmed experience by being an originator, acquirer and distributor of online content.

We think the evidence shows that this approach is **not** going to work in a world where customers have the power.

The third way to respond to the power of the customer is to use a range of distribution channels, both retail and wholesale, to deliver your services.

Some customers will want to use your retail brand – but others will want to use other retailers.

Our approach at Optus is this: if customers want to buy from a different retail brand, we'll happily wholesale networks and products to allow that.

As an example, we now wholesale one of our newest products, ADSL2+.

We are presently providing services to operators such as Exetel, Westnet and isek communications and have recently signed up Dodo.⁸

So wholesale is a big part of what we do at Optus. We believe it is a win-win approach – creating opportunities for our wholesale customers, and letting us carry traffic on our networks which would otherwise go elsewhere.

⁸ Optus Wholesale and Satellite.

A fourth important principle is keeping pace with social trends and recognising what customers value, and what they do not, and adjusting your offers accordingly.

For example, Optus has removed “grudge payments” like line rental on some of our popular home phone plans.

Our research showed that line rental is a key reason why customers are increasingly choosing a mobile phone over a home telephone. Until recently there had been little opportunity to avoid paying line rental - with the incumbent dictating the price people pay for the majority of lines in the country.

But in May this year, Optus wiped the cost of line rental off customers’ bills with the introduction of our HomeOne plans.⁹

Using behavioural marketing, Optus has shaped new technologies to meet emerging customer preferences – for example by reducing the risk to customers.

For example, we pioneered speed throttling on our cable broadband product so customers wouldn’t get big bills if they exceeded their download limits and we introduced MyTime allowing, say a family of four, to all be on the same mobile

⁹ Media Release “No line rental on new Optus plans” 29 May 2006

account and call each other for free for the first five minutes of a call.

Implications for the Telecommunications Industry – and for Policy

I have talked today about the trend for power to pass to telecommunications consumers.

Let me turn now to talk about what this trend means for our industry – in both a commercial and a regulatory sense.

On the commercial front, I believe there are some key trends that will shape the industry over the coming years.

The first is that we are seeing rapid take up in fixed broadband services. (Indeed penetration today is more than 40% compared to being less than 5% just three years ago¹⁰.) Optus has responded by, for example, rolling out a new DSL network which offers ADSL2+ to our residential customers.

Secondly, broadband is an increasingly important part of mobile services.

¹⁰ ICCP Broadband Update by Sam Paltridge OECD 2-3 October 2003

More than 184,000 Optus 3G subscribers are enjoying services like video calling and fast data access and accessing content from the OptusZoo portal like ABC, CNN and MTV.

Optus was the first Australian mobile operator to launch always-on Instant Messaging (or IM) services giving customers the same experience on their mobile as on the PC.

We were the first to launch a data card that offers seamless roaming across GSM, 3G and Wi-Fi networks.

We offer robust location-based services like Find A, Friend FindA to help customers share each other's current location and are currently trialling Traffic Finder - which will allow customers to monitor traffic using their mobile phones.

The third trend is convergence across both fixed and mobile services. At Optus, for example, we changed the structure of our business last year to respond. In addition to our wholesale business, we created three customer facing divisions - each offering both fixed and mobile services - to ensure a clear, single-minded focus on delivering a superior customer experience.

Our Consumer division now offers a full range of fixed and mobile telephony and internet products and services to customers.

In our Small and Medium Business division we offer Smart Business plans which allow small businesses to aggregate account usage across their mobile, data and Blackberry services. The more customers integrate their services with us, the more they save.

In our Optus Business division, we are trialling the new concept of dual mode handsets - that is, handsets that can roam seamlessly between mobile, fixed and IP networks, offer the same functionality and still receive a single bill.

The fourth trend is that using new technology, operators will respond to customers' insistence on improved service and flexibility.

At Optus, we see that in the corporate market, where customers increasingly look to leverage the power of IP networks to reduce costs, to integrate their voice and data networks and to deliver improved functionality - for example, in their call centres. And we believe we lead the IP trend in Australia.

On the regulatory front, we have arrived at a significant inflection point in the history of our industry.

Much has been achieved. The 1997 Telecommunications Act sets the objective of advancing the long term interests of end users. As I have shown, end users have been significantly empowered over the last fifteen years.

But there remains much to do – particularly in areas where power has not yet shifted to the end user. Overwhelmingly, this is where the incumbent retains monopoly power – particularly in fixed line services.

There has been an assumption that somehow the privatisation of Telstra means that we have come to the end of regulation.

Much like the predictions that the fall of the Berlin Wall meant that we had reached the end of history, the view that we are at the end of regulation is premature.

With T3 now behind us, we can focus on the areas where strong policy direction from Government will continue to be necessary.

By far the most important area where this issue arises is the future of broadband in Australia.

Broadband should be a key element of increasing the power of the customer.

At Optus, we believe Australians need - and should be able to access in their homes and businesses – broadband speeds which match those in leading economies such as Britain, the US and South Korea.

But the incumbent has a very different idea – to act in its own interests, rather than in the interests of customers and the nation, by using a new broadband network as a bargaining chip to get the Government to restore its monopoly.

Telstra's intentions were made explicit in its 1 December 2005 press release, which set out the preconditions to Telstra proceeding with its new fibre to the node network. Telstra wanted specific legislative changes, including 'exempting new services from mandated 3rd party access.'¹¹

To the great credit of both the ACCC and the Government, Telstra's special pleading was given short thrift – and Telstra later announced that it would not be proceeding with a fibre to the node network.

Subsequently, the imperative of T3 led to 'peace in our time' between the Government and Telstra – and Telstra put aside all mention of restoring its monopoly.

But the ‘peace’ has lasted about as long as the one Neville Chamberlain secured in 1938.

With T3 now out of the way, we have seen Telstra come back to the old script.

Last week Sol Trujillo claimed that Telstra wanted to build its FTTN network, ‘but we could not ask our Australian shareholders to share the benefits of having risked their capital with our ... competitors.’¹²

Let me give you the full picture.

Telecommunications policy in Australia, for fifteen years, has been designed to break down Telstra’s monopoly.

That is why Telstra faces a statutory obligation – as does Optus incidentally – to provide its competitors with access to its network.

With Telstra having around 74% market share in residential fixed line¹³, the case for access regulation remains strong.

¹¹ Media release “Telstra seeks investment certainty for IP network” 1 December 2005

¹² Solomon Trujillo, address to AICC, 29 November 2006

¹³ JP Morgan Report – Telstra Corporation 7 October 2006

It is no surprise that Telstra's management team would want to overturn that, and have the law changed so Telstra does not have to give access.

It is no surprise that Sol Trujillo refers wistfully to different policy settings in the US and Germany.

But there are some facts that he neglected to mention.

As I pointed out earlier in my remarks, in the US there is fierce competition between pay TV operators and telephone companies, over their rival networks – so the policy case for an access regime is weaker.

In Germany, it is true that the incoming Government flirted with giving Deutsche Telekom an access holiday – but it has now been firmly overruled by the EU.

Incidentally, in Germany Deutsche Telekom was forced to divest its pay TV network some years ago¹⁴ – but I assume Sol is not suggesting that the Australian Government follow this regulatory precedent in Australia.

For Telstra to get an access holiday on broadband would be a fundamentally bad idea for Australia.

The Government has taken exactly the right approach in refusing to buckle to Telstra's threats.

Telstra's approach is based on the assumption that it is the only player that can build a FTTN network.

In the speech I cited earlier, Sol drew a contrast between Telstra, which was risking shareholder capital, and Telstra's competitors, 'who have shareholders who are not risking their capital.'¹⁵

This is obviously Telstra's message of the month, because in a separate speech last week, Phil Burgess claimed that Telstra was '...the only competitor in the country who wants to put money on the table to actually build high speed broadband.'¹⁶

Let me make it absolutely clear that Telstra is 100% dead wrong.

It is not the only player willing to risk its capital.

I have repeatedly stated Optus' readiness to invest capital in a broadband network.

Optus has gone further, working as part of a group of nine telcos and ISPs to develop an alternative, pro-competitive model.

¹⁴ Media Release "Deutsche Telekom sells its remaining cable TV business" January 28 2003

¹⁵ Solomon Trujillo, address to AICC, 29 November 2006

¹⁶ "ACCC a rogue regulator, says Telstra man" SMH, 2 December 2006

The G9 model, announced in July this year, sets out the way for Australia to get high speed broadband – and protect and stimulate competition.

We are continuing to work away behind the scenes on developing our model – indeed a combined team of G9 regulatory and technical specialists met with the ACCC just last week for a detailed working session on this very topic.

We are on track to lodging a special access undertaking in the first half of 2007, and we will have more to say in due course.

Conclusion

Let me conclude, then, by reminding you of the key themes in my remarks today.

Firstly, I have shown that over the last fifteen years we have seen a steady transfer of power from the telecommunications provider to the user.

Secondly, I have argued that this requires telcos to change their strategies – and I have given some examples of what we at Optus are doing.

Thirdly, I have argued that regulation in our industry needs to focus on the areas where the transfer of power has not yet occurred – which is overwhelming in fixed line services and particularly on the question of what Australia’s future broadband networks should be.

As the champion of competition, Optus has strong opinions on these subjects.

I thank you all for the opportunity to put those opinions to you today.

Check against delivery