SHOUTING ABOUT OPENREACH

by DIETER HELM

BT's Chief Executive has written to his counterparts at Sky, TalkTalk and Vodafone complaining about their campaign to get Openreach out of his clutches. The squabble is all about the amount of fibre, the claimed and actual broadband speeds and the priorities for BT's investment as between sports rights and its higher risk new ventures, versus the spend on the basic core Openreach needs.

He doth protest too much. The very fact that these are the points at issue tells us a great deal about the core issues at stake. BT has conflicts of interest between itself and its competitors’ access to the networks, in its need to get as much revenue as possible out of its copper wires to underpin its dividends and provide retained earnings, the need to handle its awesome pension deficit (whilst at the same time paying out dividends), and the cross subsidy to its cost of capital.

The status quo is not good enough for an advanced industrial country, needing to build out its capabilities for a digital world of robots, 3D printing and Artificial Intelligence, electric cars, and a host of new and growing digital demands.

Britain not only deserves better, but in the post BREXIT world it desperately needs a faster broadband capability for a digital future. It needs it too as a matter of social justice and inclusion. A country that can contemplate spending over £20 billion on a twin nuclear power station at Hinkley and over £50 billion on HS2, can and should clearly give priority to spending on broadband and fibre.

Where BT does however have a point is in the convoluted and confused proposals from Ofcom. Sharon White understands the arguments for a separate Openreach, but cannot bring herself to actually make it happen. BT's lobbying all about an “investment hiatus” seems to have convinced her to instead go for one of the most muddled and confused forms of corporate governance yet witnessed across Britain’s utilities. It even makes Network Rail’s governance look sensible in comparison – which is no mean feat.

White would have Openreach's board deciding on investment matters and then simply telling BT’s main board to get on and provide the finance. The directors of Openreach would be independent of its owner, BT. This is a recipe for endless argument and interventions. Either the directors of Openreach will ignore BT, or they will fail to act independently. How could this be a stable and sustainable way forward?

My Paper - The new broadband utility and the openreach debate, Jan 2016 covers this topic in more detail...

What will happen is utterly predictable. The very people BT’s Chief Executive has now written to will adopt a clear strategy of complaining continuously to Ofcom about the lack of independence. There will from time to time be “reviews”, Select Committee inquiries, perhaps references to the CMA. A war of attrition will sap the energies of the players, and BT’s Chief Executive will have to get really good at writing letters. He will spend a lot of time trying to fend off Ofcom, DCMS, the Select Committees and his competitors...
and system users. MPs from rural areas will whinge about BT’s performance.

It does not need to be like this. Splitting off BT does not need to create an investment hiatus. This is just PR and lobbying. It did not happen when British Gas did the splits. What is more, like British Gas before it, having protected against break up (“the biggest smash and grab raid” as the Finance Director of British Gas called the then MMC’s report) Transco, BG plc and Centrica have thrived. As with BT, the low cost of capital for Openreach on its own will mirror the lower cost of capital for Transco and the risky stuff, like football rights, can be run by managers who are good at high-risk entrepreneurial activities. The recent acquisition price for BG paid by Shell should wet shareholders’ appetites.

BT shareholders would probably be better off with a split, but as with British Gas, shareholders’ interests are not necessarily the same as the managers. Ownership and control are different things. The Chief Executive would no longer have an integrated company to run. He might need to write a job application letter instead.

Very few mangers willingly downsize by splitting themselves up unless either forced by financial distress, or by regulators. White at Ofcom, and the new ministers at DCMS, should have the courage to grasp this nettle now in Britain’s interests, rather than play out a ghastly and drawn out regulatory battle, which will in any case probably result in the separation in Openreach – but not before the current performance has weakened Britain’s economic growth prospects and its record on social inclusion.

"The last prime Minister said that we should have, by right, access to fast broadband and it should be thought of like the services for electricity, water, transport and all the other utilities. He is absolutely right, but the implications of treating broadband as a new utility are quite profound. Broadband is now a core essential service, everybody needs it, the economy relies upon it, and the absence of fast broadband has become a serious detriment to businesses and lots of people, particularly in rural areas who cannot access even basic services."

The new broadband utility and openreach debate.
Dieter Helm.
Jan 2016.