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**Dr Herbert UNGERER**

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**Infrastructure, Telephony, and Competition**

*Developing cable networks into  
full-scale multi-media networks -  
Deregulation Futures*

The deregulation of telecoms since 1<sup>st</sup> January 1998 sets a radically new framework for the operators of cable networks both in Europe and across the world.

My main message during this talk will be that cable can no longer be seen in isolation from other types of communication infrastructure.

Cable networks must now be seen as going far beyond their traditional role as distribution systems for television, but rather as one of the future multi-media networks in the local loop, in the interacting markets of television broadcasting, broadband Internet access, telephony via the Internet, and distribution of new types of video-products. With the introduction of digital television and of interactive services, and the revolutionary progress of the Internet and of e-commerce, the sector is passing through a decisive stage which will determine the conditions of competition in the marketplace for years to come.

The EU Cable Review carried out by the European Commission last year, identified cable networks in Europe as a key component of Europe's future communications infrastructure, and a vital factor in determining access to the local loop to the customer. We see cable as a critical factor in competition in the local loop and in breaking the bottleneck in the provision of high bandwidth capacity to homes.

Cable networks will become one of the most powerful ways to reach customers. At the time of the Review, there were more than 40 million households connected across the European Union - though this penetration is, as is well known, very unevenly spread across the EU's Member States, with a wide variation from nearly 0% to nearly 100% penetration . And, again, we have a big difference between the number of households passed by cable and those actually connected - a fundamental problem in a number of Member States.

Large as these figures for penetration are, cable is nevertheless competing with other access methods, for example connection via satellite, and, with the advent of the new generation of xDSL technologies, may one day soon have to compete with the most widespread, in terms of penetration, of them all - telephone networks, with more than 190 million subscribers in the European Union and a near 100% household penetration across all the Member States.

It is *deregulation*, which will determine how far new technological advances are used in the real world - and how far cable will be able to respond to this challenge.

Before turning to the issue of the Cable Review, I believe it would be useful to have a short look at the global situation, and at the main new paradigms of the communications scene :

- Digitalisation ,
- Liberalisation ;
- Privatisation ;
- Convergence.

## **Digitalisation**

Digitalisation basically means transforming our networks, both cable but also telephone, into multi-purpose /multi-use carrier systems. This brings new types of service. New services mean new market structures. Digitalisation has radically transformed telecoms networks since the beginning of the eighties and has been accompanied by a complete reform of telecommunications markets and their systems of governance.

It is unlikely that digitalisation of television will not do the same for broadcasting in the coming years - and, of course, the writing is on the wall, as everybody in this room knows.

## **Liberalisation**

Liberalisation of telecommunications in Europe has meant a fundamental change of the market place in a dramatically short period. 1<sup>st</sup> January 1998, in fact, constitutes two major milestones :

- Full liberalisation of European telecommunications markets, as stipulated in EU Liberalisation Directives ,
- World-wide commitments made by the European Union, the United States, Japan, and a number of other countries according to their commitments in the WTO framework.

Again, cable will not be able to stay outside this wave of change- and it must be able to respond to it.

## **Privatisation**

Privatisation completely transforms the operation of communications networks. In Europe, it is a necessary response to a liberalised market place. It brings a new dynamic but also a new market scrutiny. It brings forward the hour of truth when the true economic value of these networks is determined - and for some, this has meant waking up to some unpleasant facts.

And, of course,

## **Convergence**

We are seeing the convergence of markets : telecoms / media - ultimately the Internet which is testing the basis of our regulatory and pricing structures. As all of us here today know, the European Union has launched a wide-ranging debate on this issue.

The total potential markets worldwide are impressive. According to almost every estimate, total market turnover corresponded to some 3 trillion € in 1998 (roughly a third in telecoms, a third in computing, a third in the broadcast media, taken in the broadest sense). Out of the worldwide market, Europe constitutes about a third.

Finally, the Internet puts all conventional ideas about how the telecoms / broadcasting sectors work in question - not as it currently exists, although even now it is already revolutionising most of the current services and distribution sectors.

This revolution will accelerate in the near future. Imagine the Internet with a cost/performance ratio for the end user 100 times greater than at present. The telephone would become a fully integrated subservice of the Internet, there would be nearly un-limited distribution capability for television or other video products from distributed video servers via the Internet - not just for national but for world-wide distribution. Market players in both sectors would have to completely review their current strategies and renew their current revenue base, just as regulators will have to review regulatory systems. As I have already mentioned, the European Commission has launched an EU-wide debate on the future regulatory system which will result from convergence, through the Convergence Green Paper and subsequent consultation phases.

Such possibilities may seem remote at current Internet performance and use, but there are some indications already : cable access to the Internet, high performance video streaming techniques, distributed video servers.

In all of these issues, cable will be at centre stage in future - which will, without a doubt, present a more deregulated environment than at present. It will no longer be economic to operate cable networks on just one segment of communications networks - television broadcasting, even on an enlarged digitised and on a pay-per-view basis. All the cable operators will have to decide if they want to base their business on the larger market opened up through telecoms liberalisation - convergent Internet services, including Internet telephony, and so doubling or more of their potential revenue base - and their attractiveness not only to pass homes but also to connect them at a higher bandwidth.

Just shifting 10% of current telephony revenues from the telephone network to cable in Europe would transfer more than 10 billion € to the sector, out of a total of well over 120 billion €. This would be more than cable currently earns on its traditional core business in the whole of Europe.

Cable operators in Europe - and worldwide - are conscious of the potential of the new markets, and, of course, the agenda of this conference testifies to this. Awareness has further been raised by the business plans announced elsewhere, such as the AT&T acquisition of TCI, after its recent approval by the US authorities , and it's the agreement, announced two days ago, on its future co-operation with Time Warner.

The most critical impediment to such an expansion of cable in future in Europe is the cross-ownership between incumbent telephone operators and existing cable TV networks, a situation which persists in a number of EU Member States. It is this issue which was principally addressed by the EU Cable Review. But the Review was undertaken with a broader perspective and a broader framework : the need to create the conditions in Europe, for the “rebirth” of cable systems under the new conditions of Europe's communications markets.

One word here on the relationship between this Review, and the general debate on convergence of telecoms / audio-visual which was launched by the Commission's Green Paper on Convergence and on future regulation, for which the second phase of consultations has now drawn to a close, and where many here are also involved.

The convergence debate has addressed the general framework. The EU Cable Review was much more tightly focused.

The European Commission was obliged, on the basis of the First Cable Directive (Dir 95/15/EC) and the subsequent Full Competition Directive (Dir 96/19/EC) to examine, by 1<sup>st</sup> January 1998 two aspects :

- The competitive impact of the provision of both telephone and cable by the incumbent : the famous issue of "cross-ownership" ;
- It was also obliged to examine the impact of potential restrictions on the use of telephone networks for the provision of cable television capacity - the latter with a view to the introduction of xDSL.

In short, the latter point was found still to be premature at this time. Therefore, the conclusions concentrated on the issue of cross-ownership.

In examining potential impact, the investigation reviewed all future network possibilities against four basic criteria.

- The range of possible services ;
- The degree of innovation potential ;
- Potential limitations of new technological capabilities;
- Contribution to competition in the local loop.

Again, to briefly summarise, on all of these points only two network types fully qualified at this stage : telephone networks and cable.

All other options such as wireless and satellite are still unable to reach the same interactive multi-media capabilities.



This makes the future development of cable and telephone to achieve their full multi-media potential critical for the whole of Europe's multi-media future.

In its report on the Review of last year (OJ C 71, 7.3.1998), the Commission came to the conclusion that cross-ownership could ultimately prevent the development of both networks :

- For telephone networks, there is not enough incentive to fully develop its broadband capabilities ;

and

- For cable networks, there is not enough incentive for the full use of new multi-media potential, for fear of cannibalising the dominant owner's telephone business interests.

As a result of the Review, the European Commission published in March of last year a draft Directive for the structural separation of cable and telephone networks where they are both owned by the same incumbent, under EU Competition Rules. The Commission made it further clear at the time that it would apply EU Competition Rules in order to avoid further anti-competitive effects of continuing cross-ownership in this area. In the context of the proceedings concerning British Interactive Broadcasting (BiB) under EU Competition Rules, BT agreed to divest its remaining cable interests in the United Kingdom, in order to make this project acceptable and not to expand cable interest any further as set forth in the Commission's Notice on the venture published in October of last year. Subsequent to the Cable Review, Deutsche Telekom announced that it would proceed with partial divestiture and regionalisation of its cable networks. Other announcements seem to indicate a profound restructuring of the cable sector in France, as well as in other Member States.

The new Cable Directive has been subject to a substantial public consultation process. Nearly forty organisations, many of which are represented here in this room, forwarded comments. In October of last year, a public hearing was held in which representatives of industry and regulatory authorities participated.

The European Parliament is expected to vote on its resolution on the Directive on 9<sup>th</sup> February, and the Commission is expected to take a final decision soon after.

During the consultation, there was some criticism of the proposed directive on the grounds that a mere legal separation of telephone and cable interests does not go far enough and that cross-ownership should be abolished altogether.

Let me be clear on this. It is true that the Directive is a limited deregulation measure. In fact, in its Communication on the Review, the Commission concluded that legal separation is a minimum measure in order to be able to monitor markets effectively, in the of highly dominant market players in this instance, in order to establish abuse under EU Competition Rules where it may occur, and to enable the development of competitive structures.

In many instances, further measures will be required. And the recent announcement in Member States concerning plans for full or partial divestiture show that the message has been received and understood.

The Commission has made it clear that it will strictly apply Competition Rules to ensure competitive structures in the cable sector. This could include the opening of own initiative cases or action upon the receipt of a complaint. In addition, under Article 85, and more specifically Regulation 17/62/EEC and the Merger Regulation, it can be expected that an extension of an operator dominant in telecommunications and present in cable television networks into related fields can raise serious competition concerns, depending on the case given.

That line was followed by the Commission in its position on British Interactive Broadcasting (BiB), where BT's decision to divest its remaining cable interests in the UK and a commitment not to re-enter the cable sector was a central condition (OJ C322,21.10.1998). BiB may be the first of a line of cases where companies expand into the multi-media field and where the development of competitive structures in both the new markets and the local loop is at stake.

This leads to a more general remark on convergence and competition.

The immediate question underlying most competition cases in the cable / media sectors is how to allow integration - television / telecoms - in a situation where competition in these markets is still clearly insufficient. We have liberalised to allow innovation. Convergence must not now mean the creation of new super-monopolies - and this danger is very real.

The Commission has made it clear that it is favourable to convergence in order to allow emergence of new markets. This is the very essence of the debate on the Convergence Green Paper.

But it has also shown that a number of conditions will have to be fulfilled in order to safeguard competitive market developments. Where these conditions can be fulfilled, the Commission has indicated that it intends to give the green light. Examples are TPS in this country and ONDigital in the UK. Where the conditions are *not* fulfilled, a prohibition decision may be inevitable - as was the case in the Kirch / Bertelsmann Decision of last year.

The telecomms / media sector is undergoing dramatic change as everybody in this room knows . The introduction of digital television, the new role of cable in the deregulated telecomms environment, and the Internet requires re-positioning and new alliances in many cases. We have a number of the main players of the cable sector in this room and we will be getting first hand information from them.

I do not believe that it is necessary to emphasise to this audience the necessity to develop our cable networks into full-scale multi-media networks. But let me leave you with my take-home message: the development of the full multi-media potential of the networks can only happen through open markets - here in Europe as elsewhere. Sacrificing competition on the way towards multi-media would sacrifice the new dynamic, which we have just won through the newly liberalised telecoms markets. It would lead directly to market stagnation.

With current divestiture plans underway, we may see a fundamental restructuring of the European cable market this year. Development of the sector will be highly dependent on its future legal framework - particularly on access and must-carry obligations. The second phase of the Convergence Green Paper consultations have addressed this issue but further comments will have to wait until the publication by the Commission of its forthcoming report on this consultation phase. But whatever the future developments in this area, we need to keep in mind the substantial loss of investment incentives which any additional regulation may entail.

The development of Europe's existing cable infrastructure into true multi-media networks will require investment in the range of 10 to 20 billion €. Securing the right investment climate to attract this capital will have to be one of the primary goals in the immediate future.

