

Incentives for Investment in Telecommunications Services in the EU and Eastern European Markets outside the EU



Think forward

New perspectives in a networked world.

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1. Introduction

There is global competition for foreign direct investment

Investment only takes place when the potential benefits outweigh the costs

Foreign direct investment is very flexible and a typical investor will consider the following questions before investing:

Is the political environment stable ?

What is the market size ?

What is the market potential ?

What is my strategic fit ?

Return on investment ?

What are my risks ?

What are the national rules and ownership rights?

How is the economic and regulatory environment ?

1. Introduction

There are investment risks that can be influenced by regulators and some that can not be changed

...regulatory authorities will influence the regulatory environment and sector specific regulation risks for investors

Investors`questions	Responsibilities / Influence	Interest for regulators
Is the political environment stable ?	National Governments	National policy
What is the market size ?	Population and Market Size	Country specific
What is the market potential ?	Expected growth	Industry and country
What is my strategic fit ?	Investor`s strategy	Investor`s strategy
Return on investment ?	Financials	Financials
What are my risks ?	Specific risks	Investors
National rules and ownership rights?	National Governments	National policy
Economic and regulatory environment ?	Regulation	Regulatory authority



1. Introduction

The role of the regulator

... the presentation will build upon presentation on Role of Regulators

▶ **Topic of presentation will focus on regulatory framework
= investment factors that can be influenced by regulators**

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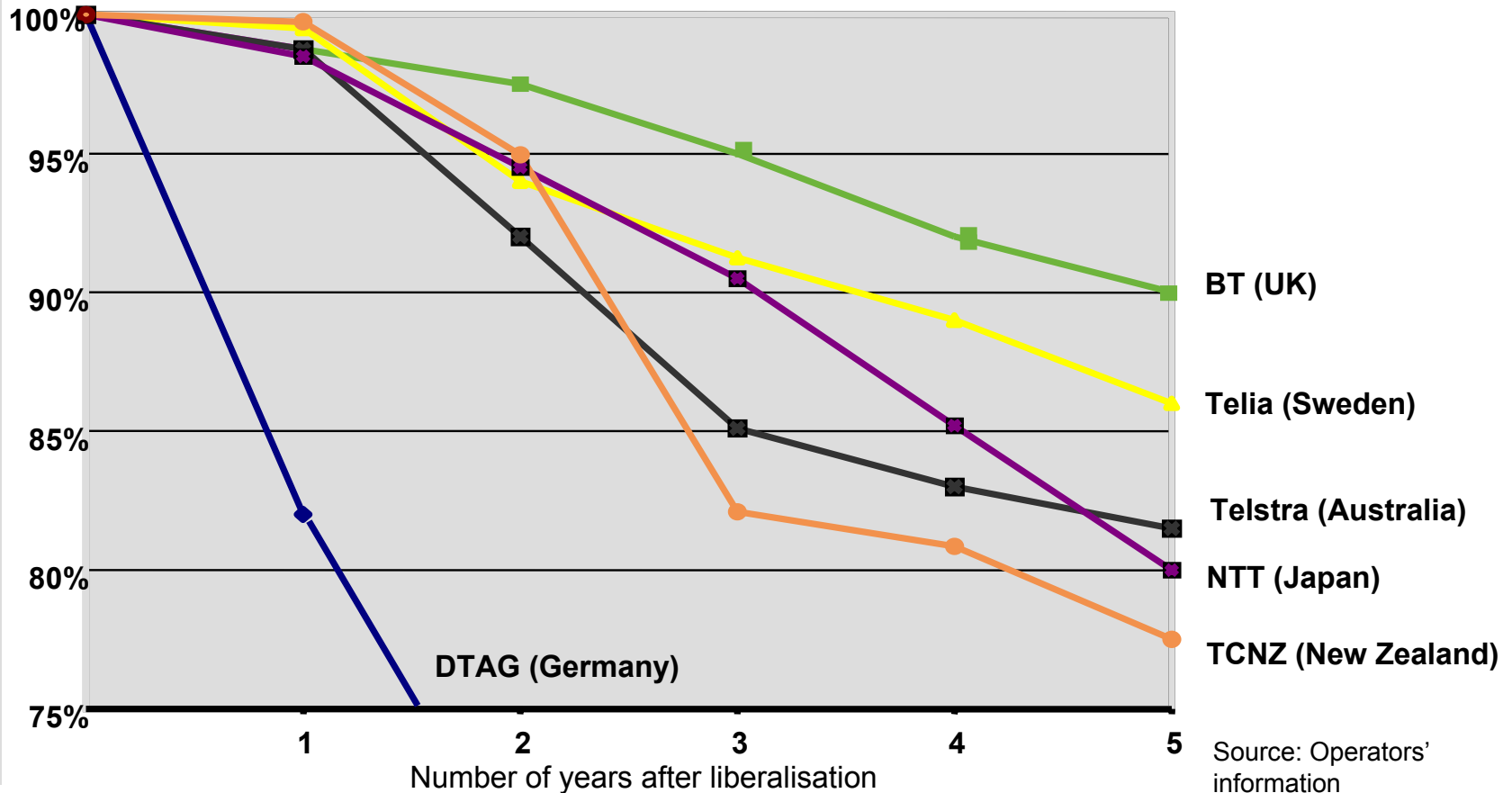
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2. Setting investment incentives in regulatory regime

The importance of the regulatory regime for investors

The Regulatory Regime has significant impact on the degree and speed of the incumbent's market share loss after liberalisation

Incumbents loss of market share (%) in the long distance market after liberalisation



Source: Operators' information

2. Setting investment incentives in regulatory regime

The importance of the regulatory regime for investors

Successful positioning in liberalized telecommunication markets and future revenues are highly dependent upon the regulatory framework

In order to determine an optimal strategy in line with regulation, it is important to understand the regulatory framework and to interpret possible consequences of the various regulatory parameters from an investor's point of view

More real competition and fully independent regulator will become reality in CEE and Baltic Countries

Operators will have similar experiences as in Western Europe

Incumbents will continue to have to do what other incumbents had to do



2. Operators need stable regulatory frameworks

Investment is threatened without a stable, reliable and predictable regulatory environment

Operators need to know that, if they make new investments those investments will not be challenged by inappropriate regulations

New entrants need certainty in the regulatory environment they will be working in when drawing up their businesses cases

Incumbents need certainty regarding their regulatory obligations

2. Setting investment incentives in regulatory regime

Investing in telecommunications market

Investing in telecommunications infrastructure is a long term investment

Return on investment for telecommunications infrastructure takes time

The regulatory regime may also attract different types of investments which do not require long-term investment. Example: Service based based competition re-selling etc.

It is basically a political and economic consideration of the regulatory and the ministries concerned which type of competition (or what kind of investment) is likely to occur

The EU approach favours Service based competition through regulation (Carrier Preselection, Carrier Selection, Local Loop Unbundling etc.)

2. Setting investment incentives in regulatory regime

What can regulators do in order to attract direct foreign investment?

Regulators should provide a fair level playing field for all licensed operators

Regulators should act truly independent

Regulators should conduct public consultations with operators

Regulators should regulate in open and transparent manner

The legislative framework should be kept to necessary minimum

▶ Regulators' role is to protect competition and not competitors

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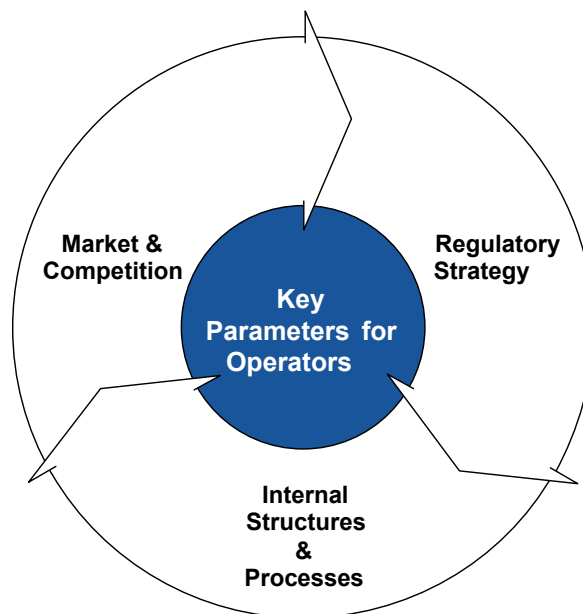
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3. The Operators' perspective

Critical Issues for Operators in Liberalisation Process

Strategy to become fit in the pre-deregulation power struggle

- How will the market develop in all parts of the value chain (Access Regulation) ?
- What kind of competitors will occur and where will they attack (Licensing/ Authorisation) ?
- What market strategy and marketing mix fits best to the specific circumstances?



- What is the most adequate regulatory position towards the regulator or competitors?
- Which regulatory issues are most crucial for corporate strategy?
- What is the most suitable wholesale strategy?

- How can financials be optimized?
- What kind of organizational change is necessary?
- What regulatory expertise needs to be developed?



3. Regulatory Framework: The Operators' perspective

Critical Issues for implementing the regulatory framework

With the liberalization of the telecommunications markets the National Regulatory Authority (NRA) develops a framework to promote fair competition and to ensure quality of service.

Such a framework is likely to address the following key issues with impact on investment plans:

General Framework

- Regulatory Objective and Scope
- Independence of NRA
- Procedures and transparency
- Numbering and number portability
- Standardization

Authorization

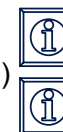
- Licensing
- Authorization and Registration
- Frequency Allocation, Assignment and Monitoring

Competition

- Discriminatory Behavior
- Significant Market Power
- Joint Ventures

Rights and Obligations

- Interconnection
- Unbundling of the Local Loop (ULL)
- Price Regulation
- Universal Service Obligation
- Quality of Service

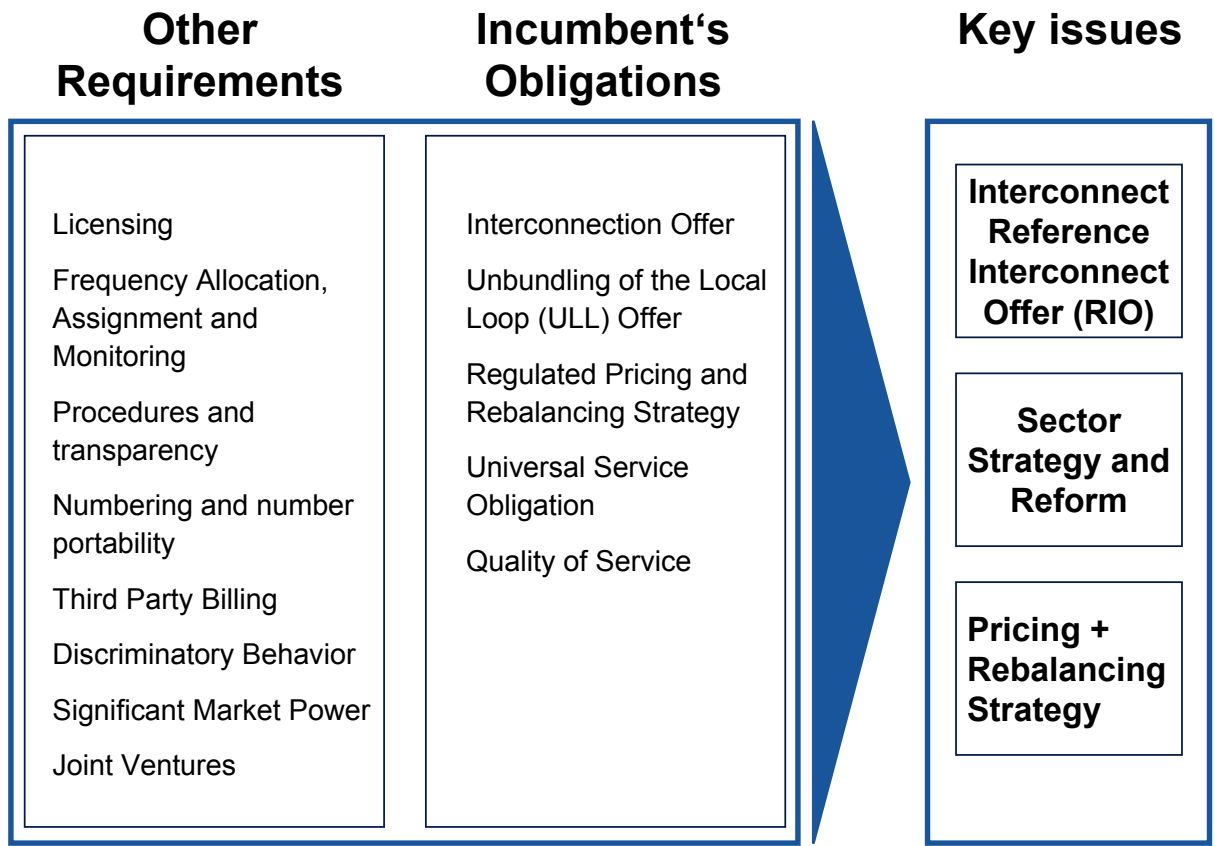


Implications for Incumbent's and new entrants Strategy



3. Regulatory Framework: The Operators' perspective

Implications for Incumbents' strategy



3. The Operators' perspective on interconnection and Reference Interconnection Offer (RIO)

Implications of interconnection policy for Incumbents' strategy



Interconnection Services will determine the core of the incumbent's wholesale portfolio at the beginning of market liberalization

The interconnection strategy will strongly influence the development of competition, and consequently the incumbent's future revenues

The Incumbent will be obliged to develop a Reference Interconnection Offer (RIO) dealing with the commercial, technical and operational conditions of the specific service

Prior to the development of the RIO, the incumbent will need to determine its strategy on interconnection services which is most advantageous compared to the applicable regulatory regime and which guarantees profitability



3. The Operators' perspective on pricing

Implications of Pricing and Rebalancing Strategy for Incumbents' strategy

With the introduction of liberalization, the incumbent has to develop a pricing strategy which complies with the regulatory framework.

The aim of price regulation is to mimic efficient competition with obligation for incumbent to set prices which are:

- cost-oriented (Tariff Rebalancing) and transparent,
- non-discriminatory,
- fair and objective

Price regulation limits pricing flexibility of Incumbents and can be implemented in the following ways:

- Ex ante regulation (proof of cost-orientation, price cap regulation)
- Ex post regulation (non-discriminatory behavior, prevent predatory pricing)

To reduce risk that prices are not accepted by the regulator, the incumbent should:

- develop a consistent pricing strategy
- use benchmarks to verify whether the derived cost-oriented prices are appropriate and likely to be accepted by the regulator.



3. The Operators' perspective: Failed investments.....

What should regulators do if operator fail/ go bankrupt?

The policy of the regulatory authorities in Western Europe and the USA can be described as “stand back” policy whereby the regulatory authority monitors the development of the market but does not try to protect a single competitor from the danger of bankruptcy

It is recommendable that the regulator should take the role of a referee monitoring and ensuring a fair level playing field for competition telecommunications and internet market without unduly interfering if a single competitor appears to have made a wrong investment

The analysis of regulatory authorities in the USA, the UK and Germany shows that regulatory authorities did not intervene to protect telecommunications companies from going into administration or bankruptcy

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The importance of the regulatory regime for investors

Regulators have an active role in shaping the regulatory framework in order to attract direct investment

Regulators should learn from the experiences of Western European regulation

The most important role for the regulator is to provide a fair level playing field for all telecommunications operators

Strong regulators are needed to ensure competition and investment

Regulators should be open, transparent and reliable to encourage investment

Regulators should regulate the market not protect single operators

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