The Broadband Landscape in 2023

By Melissa Cogavin, Managing Editor, SCTE

Our grandchildren will ask us what it was like, living through this period. Astonishing innovation, rapid expansion, insatiable appetite for data, investment, collaboration and consolidation, all taking place in an environment defined by instability and chaos. And yet here we are, thriving, staying positive, looking to the future but living in the moment.

For the past few years the UK roll-out has been facilitated by private and public investment running into tens of millions of pounds, arguably very successfully. Rising stars have emerged, start-ups evolving into award-winning SMEs, larger companies establishing themselves as major players. The industry is maturing as households are connected, bit by bit.

Various Conservative governments have set targets, moved goalposts, crowed about achievements and, to the irritation of the altnets and ISPs doing the heavy lifting, at times taken credit for connecting homes and businesses all over the UK. Depending on what you're reading, superfast broadband is now available 97% to the UK (DCMS), but look closely. *Available* is rather different from *connected*. Ofcom's Connected Nations report in December advised that actually, only '42% of UK households, or around 12.4 million homes currently enjoy full fibre broadband. That is an increase of 4.3 million households over 12 months, the market's biggest annual growth rate to date," but it is still a long way off 97%. There is plenty still to do.

ISPs and altnets are now at the reinvention phase of their life-cycle, working out how to become a customer-facing service industry after the protracted period involved in raising awareness, getting communities on board, obtaining investment, securing the confidence of customers and finally connecting homes to fibre for the first time. It's been a long, at times frustrating, but ultimately gratifying process for consumers and providers alike, working through successive lockdowns, changing the way we relate to the world and each other over time, gobbling up data in ever-increasing amounts, our appetites for streaming, gaming, shopping and social media seemingly insatiable. The fibre roll-out has, for consumers anyway, silently enabled incredible progress and our lives have altered immeasurably.

As revolutions go, the Digital one eclipses all others for sheer pace of innovation and adoption. That this has occurred during a period of history defined by chronic instability is extraordinary, and if anything such a climate has accelerated much of the revolution's progress. Recently the Collins English Dictionary even declared the word 'permacrisis' to be 2022's 'word of the year'. Macroeconomic conditions including Brexit, a global pandemic, ensuing economic downturn and a cost of living crisis, widespread trade union disputes, a real threat of nuclear escalation, the first land war in Europe since the 1940s, hard-hitting sanctions and a dollop of climate change on top means looking into the future is a fun exercise, but only a fool would make firm predictions; few are willing to look further ahead than 2-3 years.

But what kind of publication would this be if we didn't at least press a few well-positioned experts in the pursuit of knowledge and learning? The fibre roll-out and its technical, legal and commercial imperatives contain multiple and interchangeable moving parts; it

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is worth examining these to gain a sense of where we have come from in order to work out where we are going.

Investment peaking

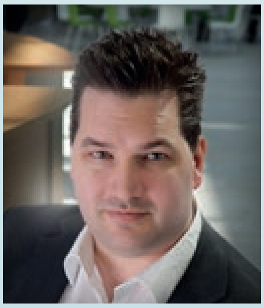
Shivani Saxena, Strategy Manager PMP Strategy

Shivani Saxena is a Strategy Manager at PMP Strategy, a consultancy working closely with investors, advising them on the telecoms sector. Her view is that investment in fibre is probably peaking, or has peaked, and that "we're seeing some shifts in the tailwinds already."

The mood, confident for a long time, is showing signs of unease. Openreach's jitters overwhelmed them in November last year, announcing that it is going to "tighten the timing of investment" in fibre as it seeks to control costs amid ongoing high inflation. In a blow to customers, the company decided it will focus on completing roll-outs at partially-covered locations and will postpone roll-outs altogether in new locations. This is probably not the only likely casualty over the next 12-18 months.

Such apprehension very much depends on how well financed you are and when you last inked a deal, Shivani says.

"Those who have very recently raised capital are not likely to slow down because they have deployment targets that they have to meet; at the same time, the cost of borrowing has gone up, the cost of capital has also gone up."



Clayton Nash, Strategy Director CityFibre

Clayton Nash, Strategy Director at CityFibre agrees. "I always like to say it's better to be lucky than smart. And we did our capital raise late last year and finished our five billion debt raise in March. Hopefully also a bit smart there. So we're fine at this point. Yes, the costs are going up. Yes, we need to get that under control and be sensible about what we're doing. There'll be a few adjustments along the way, but fundamentally, we're completely funded for what we want to do through 2025, '26. How does he feel about taking risks, knowing CityFibre is secure for the next few years?

"Our job is now to make sure that that runway stays sensible and not to get sucked into too much costly growth. We've been very good at keeping our costs flat even for a few years. Some of that stuff is going to bleed through, but we're just going to have to manage that really."

Shivani is similarly aligned. She says that "the outlook is optimistic but slightly cautious," adding that "Those that can draw down financing immediately, those that have capital available to them at this stage will continue to be a little bit more cautious about where they're going. While everyone was extremely optimistic post COVID, there was land grab, there was a general boom in the industry.

"Other developers are continuing to deploy fibre and they have the financial backing to do that right now. Those who have very recently raised capital are not likely to slow down because they have deployment targets that they have to meet." So, no need to panic. At the same time, she agreed the cost of borrowing and capital has risen. That is going to likely have an impact.

"With the change in the macroeconomic environment, there's a realism coming into the picture that's going to slow things down for a bit, but not enough to have an impact on the build and penetration," Shivani concluded.

Both Clayton and Shivani see the next 12-24 months as a period of consolidation in the market, a view echoed widely across the industry. The rising costs of borrowing will affect smaller companies who need to do another round of financing this year and next, and this will mean larger, well-financed companies will absorb the smaller ones feeling the pinch as time goes on.

The market matures

"There is a growing sense of skepticism from investors now," Shivani explained. "With HS2 being introduced, you'll see fewer and fewer funds available that may help that may slow down growth, and therefore I predict consolidation will start in earnest. Either firms will start going bankrupt or they will just start exiting their play, and then a bunch of smaller operators will become a little bit more widespread rather than previously. In the next five years you'll see fewer and fewer players – with larger and larger footprints." An opportunity for the bigger players like CityFibre, presumably.

Clayton smiled. "There is a sense out there that CityFibre is going to just buy up the whole industry. I'm not sure that that's necessarily an outcome that'll happen, but what I would say is we're keeping an eye on things. There are some nice footprints out there, some nice bits of business that we may want to pick up, and we'll do that on a case-by-case basis really. The other thing to note obviously, is we don't have to buy everybody to make this work.

"We announced a deal with broadband provider toob a few weeks ago to access their footprint on a virtual basis and I think we'll do a few more of those going forward. We're going to find a series of ways to make sure that our network's the biggest and most attractive place to access fibre to the home for the ISPs."

For the smaller companies in the shadow of CityFibre, "That's often the exit strategy, and that may have been the intention all along," Shivani says. "For a lot of them it might be a win-win. Not everyone sort of plays the game to come out on top. A lot of them just want to make some money and find an exit over a period of time."

Timing of course is crucial, since Shivani feels that as time goes on, "the fibre in the ground itself loses value and you've got significant overbuild," so this period of consolidation will likely occur when this value is at its lowest for the buyer.

Market challenges

In Europe, the risk of overbuild has had a recent dramatic outcome, resulting in the German arm of Liberty Global, helloFiber, appointing administrators and filing for insolvency. Attributing the decision to all of the above reasons - inflation and interest rates rising, a skills shortage, lack of access to capital again but as much as that, a lack of interest from communities - overbuild. It would seem this market is saturated and the bubble is starting to burst.

Shivani agrees there is more of that to come, that it is the outcome of standard consolidation that you see in industries when they've reached their peak.

Another element that is certain to impact the industry is the end of the 130% 'super-deduction' capital allowance for qualifying plant and machinery assets, and a 50% first year allowance for qualifying special rate assets. The scheme was introduced by the government in March 2021, at the height of the pandemic, allowing companies to "cut their tax bill by up to 25p for every £1 they invest, ensuring the UK capital allowances regime is amongst the world's most competitive", according to the government's website.

At a time of crisis, the scheme promoted vital growth and was welcomed, but it was never intended to be a permanent gesture. It comes to an end on March 31 this year. For

companies initiating a build after March 2021 and that completed in that two year time frame, the benefits were substantial, and have propped up the sector to some extent. According to Jeremy Chapman, Director of Capital Allowances at accountancy multinational Grant Thornton, “Without it, the UK is set to lag behind the Organisation for Economic Co-operation and Development (OECD) average for net present value for capital allowances for machinery. According to the 2022 Spring Statement, we will drop from first to 30th on its list of 38 countries.”

The fallout from this scheme ending is uncertain and is another reason for alarm; there is hopeful speculation the government may soften the blow by offering a combination of up to seven alternatives, so that the UK doesn’t fall behind any further and the sector isn’t overly affected. Combined with the ongoing skills shortage and an imminent global recession, this is more bad news the industry wishes it didn’t have to face. “Everyone thought the pandemic and associated lockdowns was the worst part,” Anthony Basham, CEO at DKT A/S, told Broadband Journal. “But there’s no such thing as a free lunch. Now we’re paying for all that downtime.”

‘We hold all the cards’

The pressure is on the government in other ways too as Brexit, which turned three years old in January, has not yet provided the ‘sunlit uplands’ promised by its champions. International trade deals have either been rolled over from existing deals, or disappointingly small - the Faroe Islands, for example (population 52,000), which does not come close to replacing trade with our nearest neighbour, a bloc of 500m people. GDP has shrunk, and the UK has fallen behind all its European neighbours economically post-COVID. Exports have fallen dramatically as exporters, mired in red tape, have either moved their operations overseas, reduced their output or ceased trading altogether. Government officials across the political spectrum are telling us we must make Brexit work, while the public appetite for it seems to have fallen off a cliff, according to recent polls. The most likely outcome is a renegotiated set of terms under a Labour government in the next 24 months, but rejoining is unlikely.

On the plus side, we have almost full employment, with thousands of vacancies in nursing, hospitality and transport remaining unfulfilled, but industries from logistics to the NHS are in serious trouble, in part because many Europeans left what they felt was an environment increasingly hostile to foreign workers, or were not allowed to remain. Others went home during the pandemic and did not return.

Skills shortage

In the telecoms sector the demand for fibre engineers is chronic, but it is proving difficult to source British talent, train the talent up and get newly trained workers out into the field. The British aptitude for problem solving has come up with some admirable ways to tackle the issue and larger altnets are providing their own training courses to speed the process up, but the problem remains, and is worthy of an updated piece in Broadband Journal on its own; there are other contributory factors, and the landscape is changing all the time.

In addition to alternatives to the super-deduction tax break, the government is also considering legislation that might provide a temporary working visa for fibre engineers, allowing them to bypass the usual immigration rules, but it remains to be seen if this is sufficiently enticing to plug the skills gap. During the ill-fated Truss administration, shortly before his resignation Chancellor Kwasi Kwarteng announced the ‘2022 Growth Plan’, alluding to special work visas of some kind, but it is still unclear at this point what form these will take.

Beyond the visa, it is obvious a temporary employment package would need to be pretty compelling for an experienced fibre engineer in mainland Europe to drop everything for a short period of time to work in an environment widely perceived to be hostile to foreigners. Offering competitive salaries for overseas engineers to plug that gap will surely only inflame tempers at home during a cost-of-living crisis and potentially cause industrial unrest. While the Communications Workers Union (CWU), have their hands full with striking postal workers, the telecoms sector, with starting salaries at £29k pa, seems fairly content with its lot at present. Hopefully it will stay that way.

Then again, there is a real possibility that the roll-out is completed by the time such legislation is ratified anyway, rendering the whole initiative rather pointless. An optimist would say this might just sort itself out on its own.

In other news

In any event, on these two matters the government needs to move quickly and provide clarity, but we have seldom seen the UK in such distress. At present, the government is under increasing pressure by countless public services threatening to strike or on strike, including the Civil Service, demoralised after 3 prime ministers in two years and engulfed by one scandal after another (three in the last week alone affecting two government ministers and ex-PM Boris Johnson. Wikipedia aren’t even updating their Tory scandals page anymore), with the press baying for resignations on a daily basis. Adding to this, the government is rushing through the Retained EU Law bill, which, as part of its Brexit pledge to 'take back control', aims to shred around 4000 laws ratified by the EU and replace them with British versions of its own, all by the end of 2023.

Lawmakers and pressure groups are condemning the incendiary action, which threatens to weaken workers' rights from holiday pay to maternity leave, stressing there is nowhere near the capacity within the Civil Service to make this a reality in a 12 month timeframe. At the time of writing however, the Retained EU Law bill appears a priority over most other issues; a government defined by Brexit has to be seen to be making it work.

Given the oxygen this initiative is taking up, the prospect of importing foreign fibre engineers looks slim, and the clock is ticking for the sweetener to replace the super-deduction scheme.

But Shivani was serene. "We're waiting for the inflationary pressures to ease up, which are partly due to the war in Ukraine. And if we get the right amount of fiscal benefits from the government, the cost of living crisis sort of eases up a little bit too." A small reduction in inflation, we are hearing, will have an incremental, positive impact on virtually every issue outlined above, bar Brexit. Plus it'll be spring soon; we can turn the heating off. 'And there's a Coronation to look forward to', a common refrain everywhere in these difficult times.

On a macro level, it all looks dire, but on a micro level business is brisk and the industry is thriving in the here and now; industrial action, war and recession seem a long way away when you're feeding cable into a hole in the ground or schmoozing people at trade shows, and there are still more vacancies than ever.

One BT Openreach engineer told Broadband recently, "37 years I've been with BT, 40 hours a week. I'm flat out, never had so much work on. I love what I do and I'm good at it."

ISPs and altnets are busy pivoting to customer facing businesses, and beyond obscure legislation outside anyone's control, staying relevant and at the top of your game is the priority. "There's a switch, yes, but we're making that switch now and we're making sure that everyone's pretty happy about what we're delivering," said Clayton. "And we're executing tens of thousands of these installations a month."

Clayton only had one more thing to add about predicting the future. "Every year I think we've brought forward a bunch of assumptions like three or four years. We thought that was going to be '26, that's happening now and it just gets faster and faster."

Competition is fierce; the race to complete the roll-out as consumers become ever more demanding will see winners and losers over the coming 23 months.

Such a demanding job is made all the more spicy by the unpredictable nature of external forces, but there is clear determination, passion and talent in this sector that will ensure the fibre roll-out continues in spite of, rather than because of the challenges it faces. 2023 won't be dull by any means.

We will return to this topic in a year's time and see how things have progressed.