REVIEW OF ATLANTIC TELECOM (AT)[1]

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1/Origins and Development

In AT's 1998 Annual Report the "founder" of the group was identified as Graham Duncan, Executive Chairman since January 1995. According to James Ross, senior telecoms analyst at ABN Amro, Duncan is "one of the great unsung heroes of the Scottish corporate scene".[2]

Duncan started in business as a Chartered Accountant, working firstly for Thomson McLintock and then Arthur Andersen.[3] In 1983, when barely in his 30s, he branched out on his own and co-founded Aberdeen Cable Services Ltd, acting as its Finance Director and then Managing Director until 1988. A year later he founded Broadcast Satellite Television Ltd (BSTV) and in 1991 he set up the Devanha Group, to which he was Chairman.

Duncan is a member and past Chairman of the Board of the Cable Communications Association, the cable industry's trade association in the UK.[4] He also has an executive directorship with Duncan Ventures Limited.[5]

In 1994 AT's Non-Executive Director, Nicholas Berry arrived on the scene by taking a 33 percent stake in Devanha through his Stancroft Trust. His investment was welcomed by Duncan who commented that "the additional investment will allow us to develop the group in a way which we would not otherwise have been able to do".[6] Berry was appointed to the Board in January 1995 and is described by the company as "an investor and publisher".[7]

In early 1995 Devanha obtained a stock market listing via a reverse take-over of Worth Investment Trust. Dealings in the shares of the new company, to be known as Caledonian Media Communications, started on January 10, with initial interest being "subdued".[8] With the exception of £450,000 of unquoted investments, Worth's holdings were subsequently sold, raising £5.2 million which was in line with flotation expectations.[9] The new company was involved primarily in the cable TV industry.

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1 This paper has benefited from funding provided by the Targeted Socio-Economic Research (TSER) Programme of the European Commission (DGXII) under the Fourth Framework Programme, European Commission (Contract no.:SOE1-CT98-1114; Project no: 053).
2 Quoted in The Sunday Herald (28/9/99)
3 The Sunday Herald (28/9/99)
4 Annual Report 1998, p11
5 AT Prospectus, 1998, p49
6 Quoted in FT (27/7/94)
7 Annual Report, 1998, p11
8 FT (16/12/94, 11/1/95)
9 The Scotsman (6/7/95)

In July 1995 the company announced its expansion into fixed radio telecommunications in Scotland, by which time the FT was referring to Berry and Duncan as "partners".[10] This change of direction was facilitated by the company's purchase of Atlantic Telecommunications Ltd earlier that year. This Glasgow-based company had been formed by Robert Condon and Edward Hornsby, both of whom had previously worked for Cable and Wireless.[11] While Condon seems to have disappeared from the scene, Hornsby, was appointed to the Board of AT in August 1996 as Group Technical Director. In 1996 The FT reported that the company was changing its name to Atlantic Telecom to reflect its new direction.[12] It would, pointed out the FT, be the only quoted wireless telephone company in Britain.

The company underwent a complete "transformation" at the end of 1999 and the beginning of 2000.[13] Firstly it entered into a strategic agreement with Marconi (see below). It then acquired First Telecom in an all share transaction valued at £350 million (see below). By the time Duncan wrote his Chairman's Report for the 2000 Annual Report the company had moved on significantly from where it had stood the previous year.

The company's new look was reflected by the resignation of Berry from the Board in June 2000. His departure was preceded by the sale of the bulk of his share holding (involving four million shares) in February of that year. For this sale alone he collected £37 million, selling at a price of 930p. He timed the sale exceptionally well with the shares loosing around three quarters of their value over the following few months.

[10] FT (6/7/95)
[11] The Economist (4/3/95), The Sunday Herald (28/9/99)
[12] FT (12/7/96)
[13] 2000 Annual Report, p2

2/Investors

The transformation which took place within the company between 1999 and 2000 is reflected in the composition of its major shareholders. In mid 1999 (see table 1) the company was still dominated by its founders, with Duncan and Berry having almost a quarter of the equity between them. A year or so later (table 2) Berry was no longer a major shareholder, while Duncan held under four percent of the enlarged group. With the strategic agreement involving Marconi in December 1999, that company had emerged as AT's dominant shareholder. Meanwhile the acquisition of First Telecom in an all share deal in early 2000 had brought on board an entirely new group of major shareholders, including Morgan Stanley and Providence. Interestingly Mark Daeche and Marcus Citron, the founders of First Telecom (with 37 percent of the company between them), emerged from the deal as bigger shareholders in the new group than Duncan himself.

TABLE 1- AT'S MAJOR SHAREHOLDERS 1999	
(percent)	
UKAV Continuation Fund Inc	7.48
Guardian Royal Exchange	5.74
Shell Pension Trust Ltd	4.73
AXA SA	3.48
G J Duncan	15.83
N W Berry	8.43
Other Directors	0.95
Source - Hemmington Scott web site (3/7/99)	

TABLE 2 AT'S MAJOR SHAREHOLDERS 2000	
(percent)	
Marconi	18.7
Morgan Stanley	7.96
Providence	7.25
Marcus Citron	5.53
RBSTB Nominees	3.82
NY Nominees	3.61
M. W. Daeche	5.54
GJ Duncan	3.61
Other Directors	0.31
Source: Hemmington Scott Web site (8/11/2000)	

3/Disposals, Mergers, Acquisitions and Joint Ventures

Sales and Disposals

In April 1996, Caledonian Media Communications sold Coventry Cable for £23.7 million to KPN, the Dutch telecoms and postal group. Caledonian received approximately £9 million in cash for its 87.75 percent stake, with the balance representing the debts and contracted lease payments of the cable company. Duncan admitted that the performance of Coventry had been "disappointing". In the future, he indicated, the group would be concentrating on its fledgling wireless telecoms service in Scotland.[14]

In July 1997, AT's subsidiary, Devanha, sold Broadcast Satellite Television, its narrow band cable TV operating company to CDA Media for £400,000 cash. The sale did not include the operation in Hull.[15] In March 1998 the operations of Hull Cablevision Ltd, were closed down.[16] Duncan had made his views on this part of the operation clear in 1996 when he stated in a press interview that, “it’s a dying business and will be dead within two to three years”.[17]

Acquisitions

In August 1995, Glasgow based Atlantic Telecommunications Ltd was purchased by Caledonian Media Communications Plc which was at the time engaged in “the search for non-cable-linked telephony”.[18] In 1995 Duncan had “happened to bump into” Ted Hornsby and Robert Condon, the company’s founders who were in search of a backer.[19] As Duncan explained it:

> “they had the prospect of a licence in the west of Scotland, but no money and no financial backing. They were looking for a white knight”[20]

Caledonian made a £125,000 down payment in March of that year for a 51 percent stake in the company. At the time Atlantic had a draft licence to supply telecommunications to Strathclyde via a fixed link, non-mobile microwave-based system, which it had been testing during the previous year. A further consideration of £750,000 was to be paid in shares upon the granting of a full operating licence to Atlantic by the DTI.[21]

According to the Scotsman Caledonian Media Communication’s executives had come across the company while exploring ways of upgrading the company’s cable facilities

[14] FT (3/4/96)
[15] FT (31/7/97)
[16] Annual Report, 1998, p3
[17] Quoted in The Scotsman (5/10/96)
[18] The Scotsman (5/10/96)
[19] The Sunday Herald (28/9/99)
[20] Quoted in The Sunday Herald (28/9/99)
[21] The Scotsman (4/4/95)

in Aberdeen and Coventry.[22] Commenting upon the deal, Gordon Sleigh, Caledonian's Managing Director stated that:

> "This was a way of getting into telephony without digging up the streets again. We see it as the way forward"[23]

The company subsequently changed its own name to Atlantic Telecom to reflect the new focus of the group.

In the mid 1990s there were persistent rumours that the company itself was on the verge of being taken over. In 1995 the Scotsman in commenting upon mergers within the British cable industry stated that "the consolidation ...is certain to continue, with Caledonian Media looking as if it is next in line for a take-over".[24] Comments from Berry did little to stifle the rumours. In mid 1995 he stated that:

> "An independent company like Caledonian is eventually going to get involved with another company in some form or other. We are currently talking to several people but it would be invidious to mention names"[25]

In October 1996 Duncan denied that the Directors of the company, who then held 50.9 percent of its equity were intending to sell. "There are no 'for sale' signs up", he told the business press.[26] Rumours were rife during this year that an approach could be made for the company as part of the intense consolidation taking place within the cable industry in England. These reports were continually denied with Duncan claiming that "we have not had any approaches at all".[27]

As it turned out, then, rather than putting itself up for sale, Caledonian itself made an acquisition which was to change its strategic direction. This purchase allowed it to move towards telephony, something which the nature of its own cable network, leased from BT, inhibited it from doing. In turn it was reported that the limitations of its ageing cable system would have ultimately made it less attractive as a take-over target in its own right.[28]

In September 1996 the company acquired the whole of the share capital of Logicall Telecommunications Ltd for a consideration of £350,000, satisfied by the issue of £200,000 of loan notes and £150,000 in cash. This purchase took AT into the market for corporate telecommunications management and least-cost routing. [29] This company is discussed more fully in the Strategy section, below.

During its 2000 financial year the company also paid £231,000 for Collie

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[22] The Scotsman (4/4/95)
[23] Quoted in The Scotsman (4/4/95)
[24] The Scotsman (15/6/95)
[25] Quoted in The Herald (15/6/95)
[26] The Scotsman (5/10/96)
[27] The Scotsman (3/4/96)
[28] The Herald (15/6/95)
[29] AT Prospectus, 1998, pp7&30

Communication s Ltd.[30] Alongside AT's other major 2000 purchase (see below), however, this deal was of little significance and almost goes unnoticed in the company's accounts.

In late April 2000 the company announced its acquisition of First Telecom Group plc in an all share transaction eventually valued at £350 million. First Telecom provides telephone and Internet services to over 11,000 small and medium size businesses (SMEs) and over 290,000 residential customers in the UK, Germany and France. It also has expertise in DSL technology which it was rolling out in the German market. The company which was the UK's largest telecoms reseller had intended to float during the year but had been put off by the volatility of the market.

The purchase involved the issuing of 68 million new ordinary AT shares, representing almost 30 percent of the fully diluted share capital of the company. With a turnover of £59.9 million (and operating loss of £33.6 million) the company would transform AT's balance sheet. This transformation also extended to AT's new Board and management team. Mark Daeche, founder of First Telecom joined the main board while five of his colleagues joining AT's new Management Board consisting of 11 executives. [31] Soon after the deal AT announced that it would be investing £100 million in expanding First Telecom's DSL network throughout Germany.[32]

Joint Ventures

In mid 1996 Atlantic concluded an agreement with Internet access provider UUNET PIPEX, the UK arm of UUNET technologies of Washington, USA whereby it would launch and market the Atlantic PIPEX Dial service to its customers. The company also intended to offer a complete on-line business and information service to business and residential subscribers later that year. Through this alliance AT was also assessing openings within the Internet Service Provision (ISP) market, although by the end of 1998 it was not actively marketing the service and had only a "handful of customers".[33] Within another year or so, however, the company was to launch itself as a fully fledged ISP (see Strategy section, below).

In December 1999 AT announced a strategic partnership with Marconi involving the allocation of around 41 million shares in AT. In return the company got £50 million in cash and the exclusive use over a 20 year period of a dedicated pair of fibres on Marconi's broadband network spanning the UK. There was also a provision for £50 million in extended credit to allow AT to "light up" the fibre within its newly acquired network. The deal gave Marconi approximately 27 percent of AT's equity, making it by far the largest shareholder (later diluted with the acquisition of First Telecom). As such it was given the right to appoint a Board member, nominating Damian Reid, its Senior Vice-President of Corporate Finance, in June 2000. [34]

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[30] 2000 Annual Report, p31
[31] 2000 Annual Report, pp1-2
[32] FT (28/4/2000)
[33] BT Alex.Brown, Atlantic Telecom Research Note, 26/11/98
[34] 2000 Annual Report, pp3,44

On news of this “quantum leap deal” AT’s shares shot up by almost 70 percent with the company now poised to join the FTSE 350 index.[35] Duncan described the deal as “something of an adrenaline shot for Atlantic” and pointed out that the company’s association with Marconi would facilitate future fund raising attempts.[36] The view of analysts at Greig Middleton was that:

> “In a single stroke Atlantic has moved from being a small Scottish-based company to be a real UK national contender able to compete against even BT”[37]

Meanwhile the FT also seemed impressed, stating that:

> “Mr Duncan’s strategy of careful regional expansion has just received a spectacular shot in the arm”[38]

Interestingly, the contact with Marconi first came about when AT was in the process of testing high-speed transmission equipment made by Marconi’s Israeli-based RDC business (see Strategy section, below).[39]

In April 2000 AT announced that it had reached an agreement with Metromedia Fiber Network BV (MFN) and AboveNet UK for the provision of dark fibre throughout 16 European city networks being constructed by MFN. In return AT would provide its partners with two dedicated wavelengths on its new UK network. By gaining access to metropolitan fibre, particularly in Germany, AT would be able move ahead with the roll out of DSL facilities in that country.[40] In using its recently acquired network as a bargaining tool the company indicated that it fully intended exploiting the wider range of strategic options now available to it.

During its 2000 financial year AT took a 10 percent shareholding in Skyline S.A.. This deal involved £440,000 in cash and the provision to the company of consultancy services in relation to its application for a French telecommunication licence.[41] According to the FT the company intended using Skyline as a vehicle to apply for fixed radio access licences within France.[42]

In October 2000 AT announced a deal with Vodafone to provide its mobile customers with a fixed-line telephone service, undercutting the prices on offer from BT. The calls would be routed over AT’s new UK network with customers having to buy a separate dialler to plug into their phone socket. The service would be billed under the Vodafone brand with plans to offer one integrated bill for mobile and fixed calls within a year. It was pointed out that if only five percent of Vodafone’s 10 million or so customers took up the offer AT could increase its revenues by up to £100 million a

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[35] The Scotsman (13/11/99)
[36] Quoted in The Scotsman (13/11/99)
[37] Quoted in The Scotsman (13/11/99)
[38] FT (13/11/2000)
[39] The Scotsman (13/11/99)
[40] 2000 Annual Report, p3
[41] 2000 Annual Report, p31
[42] FT (21/6/2000)

year. The markets were impressed with AT's stock price jumping by 19 percent on the news.[43]

The deal represented the confluence of various parts of AT's recent strategy. Firstly the deal had originally been negotiated between Vodafone and First Telecom and represented one of the incentives for AT to takeover this company in early 2000. Secondly AT's part in the agreement was facilitated by its ability to route traffic over its own part of Marconi's UK network. Thirdly the logistics of dealing with mobile companies and issuing single bills was something which AT had already been exposed to through its involvement with Cellnet (see Strategy section, below).

IN SEPTEMBER 2000 AT ANNOUNCED THAT IT HAD PAID £9 MILLION FOR A 65 PERCENT EQUITY STAKE IN TELEPARTNER PLUS, A NETHERLANDS-BASED COMPANY PROVIDING DIGITAL SUBSCRIBER LINE (DSL) SERVICES. THE DEAL WAS SEEN AS PART OF AT'S EXPANSION INTO THE EUROPEAN SME MARKET.[44]

4/Network

Within much of its corporate publications AT uses the slogan "innovation is the key". The main innovation in question has been their ability to sidestep BT's monopolistic control of the local loop (or "last mile") by employing fixed-radio access (FRA) technologies developed by the Israeli company Tadiran. The system uses microwave transmission from Fixed Access Units (FAU's) attached to customer premises. These units send signals to the company's base stations which then interconnect with the national networks. To steer around the congestion on the 2.4GHz band used by the system, AT has utilised anti-jamming technology, incorporating "spread spectrum frequency hoping", developed by the Israeli army.[45]

With the collapse of the British company, Ionica, the FRA sector received a serious blow to its reputation, not least because part of the company's difficulties had been attributed to technical problems.[46] The successful development of AT's business has done much to repair this reputation and has helped to shed the "ghost of Ionica". As the FT put it, "although still loss making, Atlantic has shown that FRA systems work and provide a commercially viable service".[47]

Speaking of the technology in 1999, Duncan stated that "it is very robust and of course now we've been through three Scottish winters with it".[48] Prior to allowing AT to roll-out its FRA system the Radio Communications Agency had demanded extensive testing, which the Israeli system "passed with flying colours".[49] The company can also point to the successful operation of the Tadiran system within 40

[43] FT (20/10/2000)
[44] FT (25/9/2000)
[45] The Economist 94/3/95), BT Alex.Brown op cit
[46] FT (22/7/99)
[47] FT (21/7/99)
[48] Quoted in The Sunday Herald (28/9/99)
[49] BT Alex.Brown op cit

networks across the world.[50]

In December 1997, the DTI issued AT with a Public Telecommunications Operator (PTO) licence for the whole of the UK. This enabled it to locate switching facilities throughout the country and to provide its indirect service upon a national basis.[51]

In its 1998 Annual report the company reported a total of 42 operational base stations for its FRA system (up from 30 the previous year). Speaking in late 1997, Duncan indicated that this gave the company coverage of approximately 200,000 Glasgow homes .[52] The same Annual Report went on to state that its network was now "substantially completed" in the City of Glasgow and it was turning its attention to Aberdeen, Dundee and Edinburgh.

By September 1998 the company was claiming 46 base stations in the West of Scotland with 15 for the Aberdeen network which went live at the end of September 1998.[53] As of year end 1998 there were 77 base stations in existence.[54] By April 1999, the company clamed to have 101 base stations, with the increase due to the expansion to Edinburgh and Dundee. Within Scotland it was predicting an expansion to between 175 to 200 base stations, putting around 1 million customers within range.[55] By March 2000 it had reached a total of 133 active base stations.[56]
As can be seen from the table below the network supported just under 100,000 lines by the end of March 2000.

[50] Ibid
[51] AT Prospectus, 1998, p11
[52] FT (12/12/97)
[53] The Standard (30/10/98)
[54] FT (6/4/99)
[55] The Scotsman (8/4/99)
[56] Annual Report 2000

Table 3- **AT Network**					
	March 1997	December 1998	March 1999	June 1999	March 2000
Base stations	30	77	101	103	133
Direct Customers	2,476	10,202	12,478	15,152	24,394
Homes Passed (000's)	90	376	533	552	694
Businesses Passed	9,450	29,111	32,390	33,621	41,921
Penetration (percent)	2.49	2.52	2.2	2.59	3.2 (residential) 4.7 (business)
Indirect Customers	0	6,026	7,930	15,542	24,816
Total Lines	9,322	43,936	52,212	66,993	98,272
Source: Annual Reports 1998-2000					

Through its agreement with Marconi the company now has access to a nationwide fibre network, allowing it to route much of its own traffic. This network had originally been laid along the towpaths of the UK's canal network, with an agreement between Marconi and British Waterways stretching back to 1993. The network goes under the name Fibreway and stretches some 1,300km, with plans to expand it to 3,000km. In May 2000 it was reported that Marconi was considering a flotation of the network division in order to realise its full potential. In valuing the asset at around £600 million the AT deal (involving two of its 24 fibres) was used as a something of financial bench mark.[57]

Through its acquisition of First Telecom it gained access to that company's DSL technologies, with the first application of the service scheduled for Frankfurt in the summer of 2000. Through its agreement with MFN and AboveNet AT will also be given access to dark fibre throughout 16 European city networks.

Looking at the company's last cable network - that in Aberdeen - plans were announced for a digital upgrade of the cable system once the Directors are convinced of the general demand for digital services across the UK.[58] In the 2000 Annual Report, however, it was announced that the cost of such an upgrade could not be justified on economic grounds. By this stage the cable TV side of the business was becoming increasingly peripheral.

[57] FT (10/5/2000)
[58] AT Prospectus, 1998, p8

5/Addressable Market

Market Size: Scotland and England

The Scottish telecommunications market, that first targeted by AT, has been estimated at £2 billion a year.[59] Within this market AT started by focusing upon the Glasgow City area opening its operations on 30 October 1996. It then expanded to cover the following Scottish cities: Aberdeen (30 September 1998), Dundee (15 December 1998) and Edinburgh (29 March 1999).[60] By the end of its Scottish roll out AT was seeking to pass over 1 million premises.[61]

As part of its expansion into England it intends to focus initially upon the area around Manchester. This area alone will give it access to 1.9 million homes and 125,000 businesses - a greater coverage that its entire Scottish network. At present its five English licences give it access to a total of 8.6 million homes and 548,000 business.[62]

Market Size: The Rest of Europe

With its expansion into England and the rest of Europe (primarily through its takeover of First Telecom) AT is now increasingly addressing the whole European sector.

Credit Suisse First Boston suggested that the European telecoms market was growing at around 11 percent a year (comprising of volume growth of 17 to 18 percent and price deflation of 6 to 7 percent). It calculated that the market would grow from $194 billion in 1999 to $413 billion by 2005.[63] Virtually all of this growth was projected to come from data and mobile traffic with voice traffic growing just enough to offset predicted price declines.

According to Bear, Stearns and Co, the European market for voice, data and Internet services is worth more than $175 billion a year.[64] As the number of European connecting to the Internet increases this figure will grow substantially. Dataquest estimate that the number of European PCs going on line will rise from 13 million at the start of 1997 to 69 million by the end of 2002.[65] The European data market was expected to be worth $55 billion by the year 2000.[66]

Commerzbank has estimated that the telecoms sector in Europe is growing at eight percent a year. It predicts that the value of the top six territories: the UK, Germany, France , Italy, Spain and the Netherlands will grow from $129 billion in 1997 to $246

[59] The Scotsman (18/5/97)
[60] AT web site (27/7/99)
[61] AT web site (27/7/99)
[62] AT web site (27/7/99)
[63] Credit Suisse First Boston , Viatel Research Note (21/9/99)
[64] dowjones.com (13/5/99)
[65] Ibid
[66] FT (27/3/98)

billion in 2005.[67] Of these six territories AT now has a presence in all but Spain and Italy.

Target Customers

According to the FT Atlantic (or Caledonian as it was then) was intending to target small and medium business and heavy domestic telephone users.[68] More recently AT has given a description of its target market through its Operating Review within its Preliminary Report. Here it states that;

> "The Group is focused on providing advanced, reliable, high quality and attractively priced telecommunication services through its facilities based networks directly to small and medium-sized business and higher spending residential customers...In addition the Group provides indirect telecommunication services to larger businesses..."[69]

According to AT it is targeting residential customers who spend over £200 per annum. This emphasis upon heavy users is based upon research which shows that the top 20 percent of homes account for 51 percent of total telecom spending.[70]

The focus upon SMEs is supported by data showing that 76 percent of all business have less than 10 lines while 32 percent have between 1 to 3 lines. This makes the small to medium sector an extensive market segment.[71]

With the takeover of First Telecom the company has increasingly presented itself as focusing principally upon the SME niche market, although this has now been expanded to a European-wide level.

6/Share History

Fund Raising

In late 1996 AT raised £23.2 million through a public placing and open offer.[72] In February 1998 it was announced that AT was planning to raise a further £95 million through a sterling denominated eurobond, thereby "dwarfing" the amount raised in its previous fund raising exercise.[73] If it failed to secure the full funding, reported the FT, it would have to "scale back its expansion plans".[74] This hint at failure was to prove quite prophetic.

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[67] FT (18/3/99)
[68] FT (6/7/95)
[69] Preliminary Report (15/7/99)
[70] AT's web site (27/7/99)
[71] AT web site (27/7/99)
[72] The Times (5/10/96)
[73] FT (21/2/98)
[74] Ibid

In March 1998 the company announced the postponement of the £95 million bond issue due to unfavourable market conditions, particularly in the U.S. Some commentators saw the debt debacle as having more to do with Ionica's problems around that time, rather than wider market conditions. BT Alex.Brown, for example, suggested that "...high yield investors chose to focus on the similarities with Ionica and hence had no appetite for the deal."[75] Whatever the exact cause of the debt cancellation, Duncan admitted to feeling "annoyed and frustrated" about the affair, while the markets responded by marking the shares down by 9 percent.[76]

Commenting a few months later upon the aborted debt offering the FT claimed that AT "almost ran out of money earlier this year after postponing debt financing because of market conditions".[77] BT Alex.Brown stated that the cancellation was "almost a disaster" for the company.[78] This episode would have done little to enhance the company's reputation in the City, particularly among those already inclined to mention Ionica and AT in the same breath. In the end the company made a £430,000 exceptional charge for this aborted issue.[79]

Later in 1998 it chose an alternative fund raising route, securing £110 million through a share issue and underwritten senior debt facility - an amount described as "vast" given the company's value of barely £75 million and sales of less than £11 million.[80] Getting involved with a share issue for a company which "invites comparisons with Ionica" was, suggested The Times "highly speculative". The importance of the new funding was not concealed by the company which stated that "...if finance were not available, there would be significantly adverse consequences for Shareholders".[81]

Commenting upon the successful completion the new financial package, Duncan stated that Atlantic would now be "moving forward with an enhanced capital base and, importantly, a fully funded business plan.[82] Interestingly, the placing was effected on a non-pre-emptive basis, meaning that the new shares were offered initially to institutions rather than existing shareholders. This was explained via reference to the 31.9 percent of the shares which were then in the hands of the Directors who, at the time, had a "limited financial capacity".[83]

In September 1999 AT raised a further £7 million in new equity, through the sale of five million warrants with an exercise price of £1.60 a share. These warrants represented a legacy of AT joining the stock market through its reverse takeover of Worth Investment Trust in 1995.[84]

In December 1999 the company completed a £150 equity issue, at the same time that

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[75] BT Alex.Brown, op cit
[76] The Scotsman (14/3/98)
[77] FT (30/10/98)
[78] BT Alex.Brown, op cit
[79] 1999 Annual Report
[80] The Times (17/7/98)
[81] AT Prospectus, 1998, p10
[82] Quoted in FT (17/7/98)
[83] AT Prospectus, 1998, p9
[84] The Scotsman (21/8/99)

it announced its strategic alliance with Marconi. In February 2000 it raised £197 million through a high yield bond issue. [85] This was the first time it had used the capital markets since it withdrew its bond offering in 1998.

While acknowledging that the company would continue to access the capital markets to finance its development, Duncan stated that as of year-end 2000 the company was in the "enviable position" of having £250 million in cash at its disposal.[86]

Stock market performance

After the company was listed in 1995 its shares initially "traded sluggishly".[87] This led Nicholas Berry to comment that, "The shares are extremely cheap by the criteria used to value cable companies". The Directors dissatisfaction with the shares' performance encouraged the view that a take-over would not be unthinkable.

Over the last few years AT has figured quite frequently within the "share tips" section of the daily and financial press. Comment has a times been quite scathing. In 1997 The Sunday Express, for example, suggested that the company was "massively overvalued. It's much-hyped radio telephone technology is unproven". [88] This uncertainty concerning AT's technology was not helped by the collapse of Ionica.

On the whole, though, AT has received more positive than negative reviews. One of the early mentions for the company was in the Sunday Telegraph which suggested that AT's potential for under-cutting BT and the cable operators meant that its "shares could go far".[89] In late 1998 the broker BT Alex.Brown suggested that at 134p the price of Atlantic did "not reflect its proven ability to put in place an affective radio access network".[90] The same broker, in its initial coverage of the company, made a "strong buy" recommendation describing AT as a "compelling investment".[91]

In the spring of 1999 the changing focus of AT was recognised via its stock market reclassification from the media to the telecoms sector. This seemed to give the share an added impetus and it rose steadily in value throughout the year. The rapid growth of the company was shown by the fact that by September 1999 it was the 14th biggest company in Scotland, as measured by market capitalisation.[92]

With the announcement of the deal with Marconi in November 1999 the shares appreciated by a further 70 percent, standing at around £8.50. Over the next few months the enthusiasm for the stock continued with highs of around £13 being reached at the beginning of 2000. The dramatic rise of the stock was, however, followed by an even more dramatic decline. Throughout the rest of 2000 the share fell almost continually, standing at around £1.85 by November of the year. The news

[85] 2000 Annual Report, p2
[86] 2000 Annual Report, p2
[87] The Herald (15/6/95)
[88] The Sunday Express (6/7/97)
[89] The Sunday Telegraph (1/9/96)
[90] Quoted in The Daily Mail (28/11/98)
[91] BT Alex.Brown, op cit, p12
[92] The Sunday Herald (12/9/99)

emanating from the company during this period was far from negative, with the decline in its value reflecting a wider sell off within the telecoms sector.

In August 2000 the company called an EGM to approve the expansion of its share option schemes. The newly enlarged scheme was deemed necessary following the expansion of the group and the integration of new personnel following the acquisition of First Telecom. The new scheme was intended "…to align more closely the interests of key employees with shareholders interests"[93]

One silver lining in AT's falling share price during 2000 was that due to the all-paper nature of its acquisition of First Telecom it ended up paying around £350 million rather than the £520 million originally anticipated.[94] Neither this, nor the continuing decline of AT's share price is likely to have gone down well with First Telecom's investors who took 30 percent of the enlarged company.

Looking at the enlarged company's market valuation in 2000 the FT pointed out that it was trading at nine times 2001 earnings compared with a sector average for alternative network operators of 15. This implied that it was somewhat undervalued, especially given the stability of its management.[95]

7/Company Data

TABLE 4 - **AT EMPLOYEES**	
1997	156
1998	223
1999	324
2000	495
Source: Annual Reports 1998-2000	

According to the 1998 Annual Report AT employed an average of 223 people during 1998 up from 156 in 1997 (see table 4). The total workforce for 1999 was 324, increasing to 495 by 2000. With the integration of First Telecom this number will increase significantly.

TABLE 5- **AT TURNOVER**	
(£000's)	
2000	21,307

[93] Circular to Shareholders, 4/8/2000
[94] FT (14/6/2000)
[95] FT (14/6/2000)

1999	14,924
1998	11,390
1997	8,893
1996	10,510
1995	9,851
1994	9,661
Source: Annual Reports 1998-2000	

TABLE 6 - AT PROFIT (LOSS) BEFORE TAXATION	
(£000's)	
2000	(33,377)
1999	(16,263)
1998	(9,540)
1997	(2,848)
1996	(812)
1995	(678)
1994	392
Source: Annual Reports 1998-2000	

The above tables show a steady rise in AT's turnover as it rolled out its network during the late 1990s. In keeping with its level of investment during this period it losses increased year-on-year. The company is expected to break even in 2003.[96] With the acquisition of First Telecom AT's next set of results will bear little resemblance to what has gone before. Its pro forma consolidated historical revenues for the most recent year stood at £81 million.[97]

8/Strategy

In its 1999 Annual Report the company summed up its recent progress in the following terms:

> "Four years ago we set out our vision to provide telecommunications services on alternative access networks in the local loop, not by means of a wired network but by means of a fixed radio connection. Today that vision is a reality"[98]

[96] FT (14/6/2000)
[97] 2000 Annual Report, p4
[98] Annual Report ,1999, p4

The Move From Cable

In 1995 Caledonian Media Communications was still principally a cable operator and seemed content to stay with the sector, with Duncan stating in a press interview that,

> "we expect growth to be sustained in the cable television market and will continue to expand our broadband services in Aberdeen and Coventry".[99]

In that year, though, telephony began playing a more important role, with Aberdeen Cable (part of Caledonian) one of the first cable companies in the world to offer a combined service of telephone and TV.[100] By 1996, however, the company seemed to have decided to move away from a "combined" approach and towards a much greater focus upon FRA telecoms. This led to the disposal of its English cable assets (see Disposals section, above).

Following the company's change of direction and the disposal of its Coventry and Hull cable operations during 1996/7, its only remaining interest in the sector was through Atlantic Cable in Aberdeen (formally Aberdeen Cable Services Ltd). This division had a 'disappointing year' in 1998 with its customer base dropping from 17,392 in March 1997 to 15,420 in March 1998.[101] This fall was attributed, in part, to competitor activity, and in particular to the special offers initiated by BSkyB prior to the roll out of its digital services.

In 1998 the company started to respond to this threat by lowering its own cable charges. With the launch of its FRA service in Aberdeen in September 1998 it seemed determined to protect its customer base in the cable market because of the considerable potential which existed for selling telephony to its cable customers.[102] Evidence from the following Annual Report would suggest that the situation in Aberdeen was turned around with cable subscriptions up by 18 percent to 18,219 - the highest increase in the company's 14 years of operations in the city. This improvement was put down to its price reductions and its dual telephone/ television service package.[103]

This division then had a another disappointing year, however, with customer numbers down from over 18,000 in 1999 to just over 16,000 in 2000. In the 2000 Annual Report the company indicated that it would not after all be upgrading the cable network due to the potential cost involved.

Increasing Importance of Telephony

The broader shift within the company towards FRA telecoms was shown by the 34 percent contribution which this division made to total turnover in AT's 1998 interim results. In the previous year's figures, suggested Duncan, telecoms turnover "was

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99 Quoted in FT (6/7/95)
100 The Scotsman (9/6/95)
101 Annual Report 1998, p3
102 BT Alex.Brown, op cit
103 Annual Report (1999, p3)

insignificant".[104] By the Interim Report stage for 1999 the proportion of revenues coming from telecoms had risen to 59 percent .[105] By the time of the 2000 results this had risen to 71 percent.[106]

The change in the company's direction during 1997 was made clear by Duncan who, commenting upon the telecoms side of the company stated that:

> "a year ago we were not even in the telecommunications business. Now we have all these lines. We think its a great performance"[107]

By focusing on FRA for its expansion the company was clearly aware that the system offered considerable cost savings over cable. A level of penetration which would not represent break even for a cable system could prove profitable for one based upon FRA. Speaking of the company's early strategy Duncan stated that:

> "we could well see that building these networks using radio instead of wires was cheaper. That's something to do with me being a C.A.. It was obvious the economics would work, even at very low levels of penetration, because of the type of animal it was"[108]

The major costs savings involved in AT's system were recognised by the FT which stated that:

> "...fixed radio access systems provide profits much sooner than fixed line services. It is also reckoned that such networks can be profitable with a small share of the total market"[109]

FRA systems also have the advantage of freeing the operator from using BT's local network for the "last mile" component of a call - a factor which greatly enhances the system's competitiveness. Again this aspect was picked up by the FT which stated that this system "offers new operators a quick and efficient method of side-stepping British Telecommunications' stranglehold on the so-called 'local loop'".[110]

In AT's business Plan it is anticipating a penetration level of 10 percent within 10 years - an ambition described as "conservative" by broker BT Alex.Brown given the company's steady progress in Glasgow.[111] In Aberdeen, where the company holds the cable franchise, the target has been put at 20 percent. Much of this is forecast to come from cross-selling to existing cable clients. BT Alex.Brown have stated that "Early results suggest that this is achievable".[112] AT's existing cable clients are heavily skewed towards ABC1s, not least due to the company's credit control

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[104] FT (12/12/97)
[105] FT (12/12/98)
[106] 2000 Annual Report, p26
[107] Quoted in The Scotsman (23/10/97)
[108] Quoted in The Sunday Herald (28/9/99)
[109] FT (18/6/97)
[110] FT (22/7/99
[111] FT (6/4/99)
[112] BT Alex.Brown, op cit

practises and aggressive stance on non-payment. This gives the cable arm customer revenues which are 40 percent up on the national average. It also has the highest pay-to-basic ratio, at 261 percent, of any UK network.[113] This makes the cable customer-base a potentially lucrative market for value added FRA services, such as Internet connection. In the 2000 Annual Report it was indicated that the cable TV product would increasingly be bundled in with telephony offerings in order to retain more of its cable customers.

Network Construction

In rolling out its network, AT has followed a city-by-city approach so as not to over-stretch its resources and to risk poor customer service by spreading itself too thinly. This strategy was made explicit within the 1998 Annual Report which stated that, "The Group has developed a network architecture that has been designed in a modular way..." Such an approach was in keeping with Duncan's comment to when discussing the opening of the Glasgow service. "We're Scottish", he said, "and very cautious".[114] The same point is made on the company's web site which states that:

> "The company maintains a conservative, "building block" approach to expanding its networks and is currently fully funded for its Scottish building programme".

One can't help but wonder if the frequent references to the "cautious" nature of the company does not owe something to the experiences of Ionica. Whatever the case, by the end of 1997 the company was talking about expanding in the same incremental manner into England.[115]

Before the expansion into England had been put on the agenda, however, it was the raising of £110 million in 1998 for the funding of AT's network in Edinburgh, Dundee and Aberdeen, which was seen as "the great leap forward".[116] Once the company finally secured this substantial additional funding for an expansion of its Scottish network in 1998, it announced orders for £9.2 million worth of radio equipment from Innowave Tadiran of Israel and £1.5 million of switching equipment from Nortel. Commenting upon the expansion Duncan stated that:

> "the company is now fully funded for our entire build-out. We are battering ahead very quickly and expect to launch the Aberdeen service within the next month and Edinburgh and Dundee in the first half of next year"[117]

In early 1999 AT made good its promise to expand south by announcing that it had won licences from the Radio Communications Agency to set up networks in five areas of England: Manchester, Newcastle, Birmingham, London and Bristol [118] The move

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[113] AT Prospectus, 1998, p12
[114] Quoted in The Scotsman (3/4/96)
[115] FT (12/12/97)
[116] The Times (17/7/98)
[117] The Scotsman (2/9/98)
[118] The Herald (25/2/99).

prompted the somewhat cryptic headline "Aberdonian vaults Hadrian's Wall using Israeli technology" in the FT.[119] Duncan indicated that the company would have to raise between £100 million and £300 million to develop its first English licence. Commenting upon the granting of the licences, he offered the following comments:

> "The proposal to extend the licensing represents an enormous step forward and will allow Atlantic to achieve the scale it has been seeking. It puts the company on the map as a UK - rather than just Scottish - local access provider"[120]

The Sunday Herald agreed with this interpretation, arguing that, "Duncan and his team are well down the road towards transforming AT into a serious player in the UK telecoms market."[121] The success which AT has had in being awarded new licences for the English markets is partly attributable to the vacuum created in the FRA market after the collapse of Ionica. So for once AT has perhaps benefited from the removal of Ionica from the scene - a company whose collapse did so much to tarnish AT's own credibility.

Digital Technology

An increasingly important strand of AT's strategy in recent years has been the development of its digital capacity, most importantly to enable it to offer Internet services. AT's interest in the Internet was hinted at by The Economist back in 1995 which in the course of describing the company's radio technology stated that:

> "In time...it may be not just a competitor to cable, but a low-cost way to bring the interactive delights of the information superhighway to remote places such as the Scottish highlands and Glasgow's rough housing estates"[122]

On this occasion, The Economist was somewhat off the mark in suggesting that AT's technology was suitable for dispersed areas such as the Highlands. Duncan has recently commented that it is not commercially viable to build fixed radio access networks in urban areas of less than 100,000 people.[123] While misrepresenting the use of AT's technology within rural areas, however, The Economist did correctly forecast its increasing interest in the Internet and digital technology. In February 1999, the company announced an agreement with the Israeli telecommunications company RDC (which recently became a subsidiary of GEC Marconi) to apply its high speed data transmission technology to the AT network. This would enable AT to offer its residential customers high speed Internet access, video-conferencing and video-telephony with additional facilities for its business users. Commenting upon the agreement, Duncan indicated that the company had always intended to launch a high speed data service but that he had not expected it to be feasible until 2000 or 2001. Referring to the new high speed data service, Duncan claimed that, "This will make

[119] FT (6/4/99)
[120] Quoted in The Scotsman (25/2/99)
[121] The Sunday Herald (28/9/99)
[122] The Economist (4/3/95)
[123] The Herald (27/1/99)

ISDN seem like a tortoise".[124]

For his part, Pinhas Romik, founder and Chief Executive of RDC, gave his approval to AT's technical strategy, stating that:

> "Rapid deployment, combined with good economy, positions wireless technology to be one of the main answers to the increasing needs for high speed data access" [125]

This side of AT's operations is to go under the name AdvanceData which was launched in late 1998.[126] The national network facility accessed by AT through its agreement with Marconi in late 1999 gave this side a boost and in early 2000 the company brought its high-speed, two-way 2.4Mbs to market. Alongside this new service AT also launched its own ISP service under the name atlantic-e.com., aimed at both the residential and the SME market. This product offered customers always-on, unmetered high-speed Internet access. It was bundled together with unmetered UK voice calls, the first time such a deal had been offered within the UK telecoms industry.[127]

The increasing importance of the Internet over the last few years also lay behind this comment from the FT that:

> "Using radio links to deliver local traffic to fixed telephones has never really taken off in the UK and other western European countries but 1999 could be the year when it happens"[128]

Discussing the expanding digital market, it went on to suggest that there would be a "window of opportunity" for those companies which entered this market straight away, ahead of BT's own plans to offer asymmetric digital subscriber line (ADSL) - based services which will enable local lines to behave as if they were digital. In April 2000 AT announced that it would indeed be launching a symmetric digital subscriber line (SDSL) in parts of Glasgow, a system the company described as superior to the ADSL service due to the high capacity when sending (and not only receiving) data.

The potential of the Internet certainly seems to have been accepted by Duncan who has argued that the day is not far off when in telephony, as with the Internet, the whole world is treated as a local call area. Explaining his company's vision of the future, he has suggested that "it might take 20 years across the world, but we think distance is dead in telecoms".[129] This philosophy is already reflected in the company's service portfolio with the whole of Scotland (and eventually the UK) being treated as a local call area.

[124] Quoted in The Sunday Herald (28/9/99)
[125] Quoted in The Herald (16/2/99)
[126] BT Alex.Brown, op cit
[127] 2000 Annual Report, p2
[128] FT (18/3/99)
[129] Quoted in The Sunday Herald (28/9/99)

Marketing and Product Portfolio

In an article on AT, Paul Kavanagh suggested that "Atlantic devotes much of its energy to marketing", with an annual marketing budget of around £3 million (approximately 20 percent of sales).[130] This desire to get itself known is shown by diverse promotional activities which in recent years have included the sponsoring of Aberdeen Football Club, the Glasgow International Jazz Festival and the Glasgow Development Agency's Small Business awards.[131] The importance of this side of the business has been alluded to by Duncan, who, in 1998 stated that:

> "we completed our fund raising on August 10 and that has started to put a bit of a punch into our marketing spend" [132]

In March 1999, AT continued increasing its public profile via a £100,000 sponsorship deal with Dundee's Contemporary Arts Centre.[133] It has also been one of the official sponsors of Dynamic Earth, Scotland's millennium project. [134] In 2000 the company's diverse range of sponsors were brought together under the Atlantic "Live" umbrella. This was designed to make the various sponsorship arrangements more coherent prior to the Commonwealth Games in Manchester in 2002, to which the company is official sponsor. The initiative also incorporates a new web site, Atlantic-live.com, through which residential customers can access special offers from the company's sponsors.

In the process of marketing its products the company's emphasis has been upon enhanced service features such as two lines for the price of one, and local rate calls for the whole of Scotland. Duncan is fond of repeating that despite the highly technical nature of the company they are in the business of selling service, not technology.[135] As he puts it:

> "At end of day (sic), the customer is wanting service. He's not buying any technical bells and whistles."[136]

The same point was forced home with the company's 1998 Prospectus which stated that, "it is the service packages which create customer demand and not the technology that delivers them".[137] In delivering its services the company makes use of retail outlets in Aberdeen and Glasgow. Retail stores are also planned for Dundee and Edinburgh.[138]

The focus upon service as a key part of the company's strategy has meant that pricing matters have been moved down its list of priorities. AT has always avoided the

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[130] The Sunday Times (8/2/99)
[131] The Scotsman (4/4/97), BT Alex.Brown, op cit
[132] Quoted in The Herald (30/10/98)
[133] The Scotsman (3/3/99)
[134] The Sunday Herald (28/9/99)
[135] FT (6/4/99)
[136] Quoted in Sunday Herald (28/9/99)
[137] 1998 Prospectus (p13)
[138] BT Alex.Brown, op cit

simplistic message along the lines of, "switch to us: we're cheaper than BT". Rather, in the words of Duncan:

> "Our strategy at service launch in Glasgow in 1996 was to provide a high value added service and not position our services on a price-based message. Our aim was to capture customers who wanted to use our service, who wanted the convenience of our features, and who were not simply focused on price savings. This strategy has been the bedrock of our philosophy and will remain so..." [139]

On December 1, 1998, the company opened its own call centre in Glasgow, handling marketing activities which had previously been contracted out.[140] Additional services, such as billing, IT, finance and administration are centralised in Aberdeen. With this infrastructure in place the company can "...expand into other areas without having to re-invent these activities elsewhere".[141]

By including indirect services within its product portfolio, AT has also attempted to get its "foot in the door" in new areas. Duncan described the Crest indirect service as a "useful tool to bring customers onto the Atlantic brand and billing system ahead of the introduction of FRA to an area".[142]

In April 1999, AT announced that it was to launch a mobile telephone service, using the Cellnet network but operated, priced and packaged by itself under the name Atlantic Mobile. The service, initially to be introduced in Aberdeen, would allow residential customers to subscribe to a line rental package including both mobile and fixed lines, with both components on the one bill. Commenting upon this integrated approach, Duncan commented that it was another example of how the company was "breaking the mould of traditional telecommunications".[143] This initiative was followed up by an agreement with Vodafone whereby AT would offer that company's mobile customers fixed-line services (see Joint Ventures, above).

Logicall

Another side of AT's business is Logicall, based in Buckinghamshire, which supplies business lines to larger companies using BT's network. In the future the company will be able to utilise its own national network. This part of AT is a call management brokerage business which buys transmission capacity in the wholesale market, bundles calls from a variety of customers together and delivers them via the cheapest route. Its customers currently include Clarks Shoes and Prudential.[144] According to the 1998 Annual Report this side of the business "had an outstanding year and is now recognised as a leader in the provision of these types of services".[145]. In 1998 it was

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[139] Annual Report, 1999, p4
[140] FT (12/12/98)
[141] Annual Report 1999, p3
[142] Interim Report, 1998
[143] Quoted in The Herald (8/4/99)
[144] FT (6/4/99)
[145] 1998 Annual Report, p2

estimated that this unit accounted for 60 percent of telecoms turnover.[146] For the future, however, the margins for this side of the business could be put under pressure as the competition for corporate clients intensifies. On the positive side AT's increasing ability to route traffic via its own national network should help it remain competitive.

Future Prospects

Essentially AT's basic completive advantage lies in its ability to circumvent BT's strangle-hold over the local loop. This was the conclusion reached by BT Alex Brown which stated that:

> "A central theme of our research has been the shift in value from distance related services to local access services - Atlantic both confirms this hypothesis and capitalises upon it"[147]

While margins are expected to fall within the Logicall business, the reverse should be the case for AT's core telephony services. BT Alex.Brown estimate that for its FRA customers margins are likely to increase from 62 percent in 1999 to 70 percent in 2000 and stay at around that level.[148] It is margins such as these which have prompted it to suggest that "The FRA business is the key driver of value at Atlantic Telecom".[149]

Future Expansion

In 1999 Duncan suggested that the company might also turn its attention to the newly liberalised telecom markets of continental Europe. Summing up his medium-term view, he has stated that, "we'll be in most of our target cities within five years and we might have a foothold in western Europe".[150] This foothold came into being with the company's purchase of First Telecom. While broadening the company's geographical scope the acquisition prompted a narrowing of AT's market focus, with an increasing emphasis upon the SME market.

This "changed emphasis" was intended to capitalise upon the company's first mover advantage in this niche market and benefit from the increasing data requirements of this market sector.[151] The new focus was also a reflection of the strength of First Telecom's SME customer base. As Duncan said of his expanded management team:

> "These vastly experienced individuals have the capabilities to build the Group into a principal supplier of telecommunications services to the SME market across Europe"[152]

[146] BT Alex.Brown, op cit
[147] BT Alex.Brown op cit
[148] BT Alex.Brown op cit, p10
[149] BT Alex.Brown op cit, p9
[150] Quoted in The Sunday Herald (28/9/99)
[151] 2000 Annual Report, p3
[152] 2000 Annual Report, p4

In teaming up with First Telecom AT has also been able to supplement its FRA technology with DSL local access. Moreover the acquired company was well advanced in applying this technology in Germany, Europe's largest telecoms market. In valuing First Telecom ABM Amro put its residential business at around £300 million.[153] Upon this reasoning, and given the fall in AT's share price around the time of the deal, it effectively got the DSL business for £50 million (the final price being £350 million). First Telecom's closest German competition in the DSL market is QSC, which had a market value of about £900 million in early 2000. All in all AT seems to have got its European foothold at a very reasonable price.

9/Competition

Scotland

In Scotland, suggested Scotland on Sunday, AT is one of five main players, the others being BT, Scottish Telecom (now Thus), Telewest and CableTel. In addition, it also mentioned a number of niche providers such as ACC Telecom, First Telecom (now part of AT), Interphone and Jydecom.[154] AT itself, in addition to the main companies just mentioned, also identified Cable and Wireless, AT&T (UK), Racal Telecom and Energis as "potential competitors" which could elect to build or expand their local access networks within AT's operating area.[155]

Perhaps the company which is most frequently compared to AT is Thus, not least since both have use fixed radio access technology (supplemented by "indirect" services - Crest in the case of AT and Liberate for Thus). Thus, which was formally known as Scottish Telecom, emerged from within the corporate structure of Scotland's national power company. In describing AT's early development the Scotsman suggested that its activities put "the tiny company in direct head-to-head competition with the giant multi-utility Scottish Power".[156]

The fact that Thus began its life as part of such a large organisation helped it in times of trouble, such as the problems associated with its licensing deal with the ill-fated Ionica.[157] In 1999 Thus announced that it was abandoning its fixed wireless telephone service claiming that the collapse of Ionica had made its own position within the sector untenable. A spokesman for the company stated that "after Ionica went bust we soldiered on for a bit, but eventually decided that it wasn't worth it".[158] The withdrawal from this niche market affected a customer base of 6,000, with the company aiming to offer an alternative fixed wire service.

Interestingly, just a few days before the Thus announcement, RadioTel , a Cambridge operator, said that it would be moving into the Scottish market. Despite coming from the same part of the country as Ionica, the FT stated that:

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[153] FT (28/4/2000)
[154] Scotland on Sunday (19/4/98)
[155] AT Prospectus, 1998, p38
[156] The Scotsman (10/6/97)
[157] Scotland on Sunday (19/4/98)
[158] Quoted in The Guardian (25/7/99)

> "The move underlines the growing popularity of radio as an alternative to copper wire connections to home and office, as the spectre of Ionica's collapse recedes"[159]

The arrival of the new company on the Scottish scene was not interpreted as an immediate threat to AT, however, since its radio licence confined its activities to mainly rural areas.

Looking in more detail at the FRA market it seems unlikely that any competitor is about to replicate AT's services on the 2.4GHz band, not least since the Radio Communications Agency has stated that it intends only to issue one licence per frequency range. Those parts of the spectrum which have been allocated to other companies are more suitable for rural transmission, as indicated above. In short, the barriers for entry into AT's market seem high - a point made by BT Alex.Brown which stated that "Atlantic should experience no new FRA-based competitors in its existing market."[160]

Both AT and Thus project a strong Scottish identity, something which BT seemed to try and respond to via its setting up of BT Scotland, with a separate Scottish board in 1998. The new entity inherited a market share of 90 percent for residential, and 80 percent for corporate customers.[161] In a press interview the Director of BT Scotland, Doug Riley, indicated that the move was in response to the new mood engendered by the establishment of the Scottish Parliament. When questioned specifically about the two main Scottish rivals (AT and Thus) he responded that:

> "I don't mention competitors by name, but obviously I recognise that there is competition here. Am I frightened of it? Well, I sleep OK at night."[162]

In 1996 two of Scotland's cable companies, Telewest (Edinburgh) and Cabletel (Glasgow) announced that they were in negotiations to link their networks for telephony purposes. The competitive threat to AT was clear and was further forced home by Bart Bonsall, Telewest's Managing Director in Scotland who stated that, "What we have to do as an industry is make sure that we create the most effective competition for BT and the wireless telephone operators".[163]

UK Competition

An idea of the extent of the potential number of competitors in the UK market was given by BT which indicated that it exists alongside over 200 such competitors.[164] As AT expands into England it is naturally going to have to deal with many of these competitors. When asked by a journalist if the move into the crowded English market could prove the company's undoing (with a side reference to Ionica), Duncan

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[159] FT (21/7/99)
[160] BT Alex.Brown (26/11/98)
[161] The Scotsman (22/8/98)
[162] The Scotsman (22/8/98)
[163] The Scotsman (3/9/96)
[164] Scotland on Sunday (19/4/98)

responded by claiming that:

> "...the numbers of players in the first mile, tackling the customers we are targeting - and we're focused on the SME market and the higher spending residential market - is very limited."[165]

As of 1999 the company had no plans to focus on the City of London, due largely to the strong position of competitors such as Colt.[166] With its agreement to buy dark fibre from MFN within 16 European city networks (including London), however, the company seemed to be moving towards this market segment.

European Competitors

With its expansion to Europe AT will encounter an entirely different competitive environment. Its initial focus is upon the German DSL market where the other main operator is QSC. The market for local access in Germany is highly competitive with Deutsche Telekom losing a large part of its local business to a swathe a new competitors over the last few years.

10/Other Threats

Greater Price Comparability

There is currently a large amount of ambiguity surrounding the pricing structure of the telecommunications industry, with the Sunday Times commenting that getting the best deal is "fiendishly difficult".[167] It is frequently noted that this is to the benefit of all the operators in that it undermines basic market forces and prevents customers from spotting an over priced service. This view was taken by Scotland on Sunday, which stated that:

> "The trouble is that each company is trying very hard to make its price structures different from the competition to prevent the very thing you are trying to do - compare one company with another"[168]

Oftel, however, has been working on a model to make comparisons more straightforward. This has involved taking opinions from a forum of industry delegates, who in turn decided to appoint a firm of consultants to investigate the issue.[169] Such a development could pose some degree of threat to all the operators, especially if a particular service category looks comparatively over-priced. Much of, course, will depend upon the nature of the model since most of the companies can look either over priced or competitive depending upon the selectivity of the approach. AT would perhaps argue that as a competitive new arrival on the scene it has much

[165] The Sunday Herald (28/9/99)
[166] The Sunday Herald (28/9/99)
[167] The Sunday Times (12/12/98)
[168] Scotland on Sunday (19/4/98)
[169] Scotland on Sunday, 19/4/98)

less to fear than the traditional operators. This approach is implicit in the comments of AT's Managing Director, Gordon Sleigh, who, commenting on the progress of the forum stated that "not all the operators were keen to get into this comparison situation".[170] AT could also argue that its services are not purely price driven, as already discussed.

A Declining Share Price

With AT's share price soaring during 1999 it was occasionally commented that the company, together with the telecoms sector as a whole, was looking increasingly over-valued. In early 1999 the Scotsman pointed out that the telecoms sector had enjoyed an incredible bull run with valuations standing at around 50 times annual earnings.[171] Colt Telecom went down in history as the first constituent of the FTSE 100 never to have made a profit. The Scotsman went on to reveal research indicating that every person in Britain would have to spend 10 weeks continuously on the phone to produce enough profits to justify existing share ratings.[172] Later in the year there was a definite correction with the whole sector falling out of favour with investors. AT has suffered more than most of the larger operators, with its market capitalisation down by over 80 percent in a year. This has serious implication both for accessing funds on the capital markets and for the moral of management (with a new performance-related share scheme recently initiated). The severe decline in the company's valuation also makes it a much more affordable takeover target.

Customer Churn

As with all new comers to the market, AT has to keep on top of customer churn. As the FT put it, "Churn is the curse of liberalised communications", and pointed to research by Gemini Consulting showing that the cost of acquiring a new customer is between $300 - $400 while retaining an existing customer is only $45 - $50.[173]

For 1998 AT indicated that churn rates were satisfactory and below the levels originally anticipated. For the year ended 31 March 1998, it stated, residential churn averaged 17 percent with the business level at 10 percent.[174] By June 1999 the residential figure had improved to around 14 percent, while the business figure had gone up to 15 percent.[175] For 2000 the figure stood at 17 percent for both markets. This increased rate of churn in the key business market must be a cause for concern and a reflection of the increasingly completive operating environment.

In view of the company's resistance to a price driven strategy it is arguable that it should be in a better position to manage its churn levels. In referring to its "solid customer relationships" it has pointed out that over 30 percent of existing customers

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[170] Scotland on Sunday (19/4/98)
[171] The Scotsman (23/3/99)
[172] The Scotsman (23/3/99
[173] FT (9/6/99)
[174] 1998 Annual Report, p6
[175] AT press release, 7/7/99

have been referred to the company through recommendation.[176] It has also stated that, "Atlantic has the goal of eliminating voluntary churn".[177] So far, though, far from being eliminated, the company's churn rate seems to be on the increase.

All this hints at one of the main reasons for churning, that of poor customer service. During 1997 complaints to Oftel increased by 17 percent, an increase largely attributable to the increasing number of people moving from BT to new operators.[178] This could have the affect of reducing public confidence in the new operators such as AT. Whatever AT's own record it could be tarred with the same brush should defectors from BT to alternative suppliers meet with inferior service.

Health Concerns

Given that AT uses micro-wave based telephony it could be vulnerable should there be any increase in public discomfort at the proliferation of the commercial use of this type of technology. In addition, of course, there is always likely to be local objections to new constructions, such as radio masts, on aesthetic grounds. Duncan has alluded to these risk factors, claiming that with base-station power levels of only 100 milliwatts, it is "the Greenest radio network in Europe"

Not everyone has been convinced, however, and the company faced various neighbourhood protests during the construction of its infrastructure in Aberdeen, with plans for one 80 foot mast being abandoned.[179] Also in Aberdeen, local authority permission to locate cells on roof tops took 12 months to secure. As BT Alex.Brown put it:

> "As with all cell based networks the acquisition of cell sites can prove to be an arduous process" [180]

Such difficulties could escalate as the company rolls out its network in the densely populated English licence areas.

The potential for disruption which safety fears could have was also shown by West of Scotland Water's decision to suspend work on 11 transmission masts due to public health concerns in 1999. On this occasion AT was one of the phone companies directly affected, although the focus was not upon micro-wave systems in particular. Speaking on the matter, Ernie Chambers, Chief Executive of West of Scotland Water, stated that:

> "While existing research shows that exposures due to emissions from base station installations are very many times below official guidelines, we want to make doubly sure the public is protected"[181]

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[176] Annual Report, 1999, p23
[177] Annual Report, 1999, p23
[178] The Sunday Times (12/12/98)
[179] The Sunday Herald (28/9/99)
[180] BT Alex.Brown, op cit
[181] Quoted in The Scotsman (22/7/99)

In general AT is perhaps rather less prone to health scares than the mobile operators who are regularly the focus of safety studies. Should the public start to associate AT's system with the health risks of mobiles, however, then the company could find itself compromised.

Supplier Dependence

Another threat to AT could be an over-reliance upon Tadiran for its FRA network access equipment. The company has admitted that it is "critically dependent" upon its Israeli suppliers since it has no proprietary rights to the FRA technology.[182] This threat is made all the more significant given "the risks inherent in operating a business in the Middle East".[183] At first site the company would seem to be replicating this type of risk by using another Israeli company, RDC Communications, for its high speed transmissions. In the 1999 Annual Report, however, Duncan points out that they are also working with Breezecom (yet another Israeli outfit), together with their "existing suppliers" (Tadiran), to develop this technology. That Duncan is aware of the dangers associated with restricting the company to one source of equipment is implied by his comments that:

> "For the first time since we launched commercial services in 1996, we will have a choice of technologies in this increasingly important area"[184]

He failed to add the caveat, however, that all three potential suppliers are still Israeli-based.

Technological Obsolescence and Spectrum Interference

Finally, in its 1998 Prospectus AT alluded to two additional threats under the heading "Risk of technological obsolescence and spectrum interference".[185] In terms of the former risk, the company acknowledged that like its competitors it was vulnerable to future technical innovations which might make its own system less attractive.
This danger has also been recognised by the FT which in a discussion of Colt, indicated that:

> "what is becoming rapidly apparent... is that even sophisticated new operators are being caught out by the speed of technological progress" [186]

Its lack of an ageing and inappropriate "legacy network", however, does make AT less prone to technical obsolescence than the likes of BT.   The amount of investment which AT has "sunk" into its technology is also proportionately smaller than those operators who have chosen to lay their own cable.

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[182] 1998 Prospectus (p38)
[183] AT Prospectus, 1998, p38
[184] Annual Report: 1999 , p2
[185] 1998 Prospectus (p39)
[186] FT (18/3/99)

The latter risk of spectrum interference is more specific to AT's particular technology, operating as it does at 2.40 GHz, a shared and largely unregulated radio band. Should usage of this part of the spectrum increase then this could have a detrimental effect upon the quality of the company's telephony services. AT's system is also vulnerable to slight interference from mobile phones. As mobile usage increases this threat will also become more pronounced.