TELSTRA INQUIRY

Submission No. 24

197 Chandler's Hill Rd
Happy Valley SA 5159.
17 Jan 03

The Secretary
House of Representatives Communications, Info, Tech. & the Arts Cttee.
Rl, Suite 16
Parliament House
Canberra Act 2600.

Dear Sir/Madam,

INQUIRY INTO THE STRUCTURE OF TELSTRA CORPORATION

Thank you for inviting comment re some aspects of a possible future structure for Telstra Corporation.
I will not attempt to respond to all of the items included in your terms of reference. Although my comments will be confined mainly to financial aspects, I have a very small vested interest. My only Telstra associations have been as:-

- a customer
- a small shareholder, and
- an ex-financial supporter of the organisation via Telecom debentures.

The following is submitted for consideration by your Committee:-

(1) PROPOSAL TO REDUCE THE C'WLTH S/HOLDING IN TELSTRA'S NON NETWORK BUSINESSES
Such a proposal should generate economic benefits for the people of Australia and Telstra s/hldrs. The C'Wlth's 50.1% stake is inimical to Telstra's cash flow position. It restricts access to equity markets, limits opportunity to re-invest dividends paid to s/hldrs, and negatively affects profitability. Overall Telstra's financial flexibility is reduced by the C'Wlth's 50.1% requirement. However, there would also be some disadvantages likely to accrue.

In Nov'02 a key ratings agency, (Moody's Investors Service) in commenting on Telstra's financial performance for the first quarter for this financial year, warned that its usually dependable earnings would not be sufficient to cover Telstra debt & expenditure, with a retained cash flow/to debt ratio of 33%. The agency was reported to have said that meaningful improvement in the latter ratio would require Telstra to boost its operating performance, and cut its debt, or lower its dividend pay-outs. S/hldrs who have seen their Telstra capital seriously eroded, would re-act against lower dividends, and past performances suggest that Telstra Board & Management seem not to have the ability or the desire to control expenditure at an acceptable level. To substantiate the latter assessment, the following examples are quoted from Telstra's past year expenditure:-

(a) In June'02 Telstra purchased naming rights for a sport stadium in Melbourne, plus another in Sydney, for $100 million. One would expect decisions re expenditure to that magnitude, would be taken at Board level. But when challenged, (at Board level) regarding such unproductive extravagance, Telstra replied that this expenditure had been "a Management decision". It is difficult to imagine what feasibility study considerations might have been contemplated by management, prior to spending that $100,000,000. How were the intangible benefits valued? In the event of unforeseen circumstances, would security of tenure be assured? Was the aspect of "ticketing/corporate box perks" for favoured spectators, a prime consideration? What credit could Telstra earn from such a PR exercise? (In Australia, credit belongs to those who earn it, (eg. the "ROD LAVER ARENA" has earned respect, as it honours one who remains an ornament to sport, but Australians give no credit to an impostor who "pushes-in" with no more than an undisguised cheque book). Or was a feasibility study ever conducted at all?

(b) In Sep'02, it was announced that Telstra had made arrangements for a radio announcer (John Laws) to publicise Telstra, (good or bad publicity would be the choice of Mr Laws). Media speculation re the fee for that "service" varied from $300,000 to $780,000 for a three year term. In response to questioning, Telstra advised, (their letter 16/10/02) that the Laws arrangement was also a "Management decision". The letter went on to say (quote): "Of course, Mr Laws continues to have the right to comment upon or criticise Telstra in whatever way

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he considers appropriate".(END QUOTE) The publicity content, and value for the advertising dollar do not appear to have been considered.
The above comments re expenditure, have been confined to advertising & P.R., only because that is a transparent area. Regardless of the area of expenditure, it is clear that the Telstra Board has over-delegated (eg. $100,000,000 for a P.R. exercise) and the above examples reflect a soft attitude to control of expenditure, at both Board and Management levels.
It is my opinion that any inquiry, involving Telstra's financial structure, convened by the controlling shareholder, would be incomplete without:-

- an idependent review of the Board, its Chairman & Directors.
- Board members being questioned regarding abnormal delegations of authority to management, particularly financial delegations.
- Directors being encouraged, by the controlling shareholder, to serve on fewer Boards, (the current eleven non-executive directors hold sixty three other directorships, including twelve other Chairmanships).

(2) POSSIBLE SEPARATION OF TELSTRA'S CORE NETWORK FROM ITS OTHER BUSINESSES.

Among Telstra's "other businesses", the division which might be separated with least disruption, would seem to be the retail outlets, ie. Telstra operated shops as distinct from those privately operated under license/franchise arrangements. The following advantages would accrue from selling the many Telstra operated retail outlets to franchisees:-

(a) proceeds from sale could be more profitably employed in the core network business, or by investing it in new network infrastructure.
(b) by reducing debt
(c) redundant staff could likely be absorbed by the incoming franchisees
(d) by the increased sales of franchise products
(e) by better service to customers.

The above items marked (d) and (e) may appear unkind to existing Telstra shop staff. Never-the-less it has been widely recognised that other privately operated franchise businesses, (eg. Australia Post (post shops & post offices) and Aust Gas Light Company Ltd (Energy shops)) more vigorously pursue increased sales & improved customer service, than do most semi-Govt employees.
The latter claim can be illustrated by examples of Telstra operated shop staff refering customers to competitors, (Dick Smith Electronics and Tandy Eelectronics) when unstocked by an essential accessory for a Telstra-brand product. At the same time a Telstra franchise shop (only a few kms distant) held adequate stock for the required item. A multi million dollar advertising budget is worthless if staff refer customers to competitors, and therein lies a problem which Telstra can partly solve by selling all its retail shops to franchise operators. The overall Telstra advertising policy problems are more deeply rooted. An impetus for expensive methods of advertising surprisingly developed in Telecom. prior to 1989. Surprisingly, because in 1989, Telecom still operated in a competitive "vacuum", in a telecommunications industry with no competition whatsoever, and therefore no need for advertising of the expensive type. Its advertising escalated around 1992, and again in 1997, culminating in a costly year in 2002. Costly, not only in economic terms, but also via bad press and lost goodwill. During the second half of 2002, one Telstra advertisement was described by the media as "deceptive", another advertising campaign as "misleading", and another as a "public scandal".
It would therefore, seem necessary to make it abundantly clear to the Directors, (whose role would normally include that of policy innovators) that the Australian public has become over-saturated with meaningless Telstra advertising. "Familiarity breeds contempt", and those frequent, one word (Telstra) ads are too familiar. It is not helpful for that one word (Telstra) to be displayed at every sporting arena, nor should it be superimposed on unrelated television programmes, nor should it be displayed with the "curriculum-vitae" for every racehorse presented via television coverage prior to every race, at every race meeting, during the Victoria Racing Club's spring carnival. Meaningless advertising still has to be paid for.

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SUMMARY.
About a month ago I received a letter from a Federal Govt. representative, regarding this subject of Telstra, and I was concerned by one sentence in particular, (QUOTE): "The Govt. does not believe it should advise Telstra how to run its business". (END QUOTE). Telstra is not owned by "its" Directors, it is owned by the people of Aust. and its s/hldrs. In my opinion, the controlling s/hldr. must not adopt the attitude of -"We must not tell them how to run their business". That was exactly the Sth. Australian Govt's attitude to the State Bank of SA, a decade ago. That State Govt. had special rights (as a guarantor) to intervene, but did not, and that bank went on to lose billions of dollars, it brought down the Govt. and brought the State of SA to the brink of bankruptcy. Now we have a Federal Govt, as a controlling shareholder, with special rights under the Telstra Corporation Act 1991. If that Federal Govt. intends to sell its controlling interest, and "desert the sinking ship", my recommendation would be "Don't Sell". If however, the Govt is prepared to induce the Telstra Board to "turn the ship around", then a strong controlling s/hldr would be most welcome to retain its 50.1% stake.

Yours sincerely,

D Connell

Denis Connell.