GOVERNMENTS IN THE TELCO BUSINESS: PRUDENTIAL INVESTORS OR BUREAUCRATIC INTRUDERS?

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“If it moves, tax it.
If it still moves, regulate it.
If it stops moving, subsidise it.”

Attributed to former United States President Ronald Reagan
GOVERNMENT BROADBAND INVESTMENT

Thirty years of telecommunications privatisation and market liberalisation
  – pursuing the competition ‘holy grail’
But more regulatory intervention than ever before

Unprecedented advances in technological innovation
  – falling costs – infrastructure and software
  – multiple platforms: fibre-optic cable, wireless, mobile, satellite
  – content convergence to a single common digital format

Yet governments back investing in the telco (FTTH) business
  – Australia and NZ
  – Korea and the Netherlands
WHY TURN BACK THE INVESTMENT CLOCK THIRTY YEARS?
No substantive justification in policy documents

Three plausible explanations:
1. The ‘conventional wisdom’ of ‘natural monopoly’
   • there will only be one FTTH network
   • inherent ‘market failure’: government must build and regulate
2. ‘Regulatory failure’
   • increasingly intrusive access regulation and separation directives have chilled private investment incentives
   • only governments prepared to undertake financial risks of building a truly open access network
3. Non-economic reasons
   • differentiated populist political positioning
   • ‘aspirational’ objectives
ARE ANY OF THESE JUSTIFICATIONS PLAUSIBLE?
1. ‘CONVENTIONAL WISDOM’

The (im)plausibility of ‘only one network’ (Hellwig, 2008; Levin, 2010)

Technological innovation in mobile, wireless
- growth engine is mobile data usage, despite widespread availability of fast copper-based networks

The end of application/network specificity
- application access, not network typology, will be paramount
- FTTH a complement, not substitute
- except for very high-definition digital entertainment apps
  - cost-effective close substitutes already available???

Flawed geographic thinking given decreasing real costs
- Australia and NZ amongst most urbanised OECD countries
- why is there no widespread fixed access duplication (i.e. cable tv) already in urban areas?
2. ‘REGULATORY FAILURE’

Theoretically and empirically substantiated (Roller & Grajek, 2009)

Why not change the regulatory regime to encourage private investment?

- ‘regulatory holiday’ – proposed for Germany (Gans & King, 2004)
- no broadband access regulation - USA
- regulatory technological neutrality – Finland
- precisely how most telephony networks were developed circa 1880
  - Government-owned networks lagged privately owned ones in deployment (both rural and urban) and pricing (Wallsten, 2001)

Few impediments to inter-platform competition from unregulated (e.g. cable, mobile, wireless) networks

Politically problematic

- ‘skew’ in existing investment patterns
- given long legacy of access regulation
3. NON-ECONOMIC CONSIDERATIONS

No credible empirical evidence yet that investment in faster broadband will generate positive returns

- BB and above average economic growth correlated in areas that were already growing above national averages (USA - Greenstein, 2009)
- firms using BB more productive than paired comparators without broadband, but no higher productivity levels observed in firms accessing faster (cable) BB (NZ - Grimes, Ren & Stevens, 2009)
- marginal vs average benefit given wide current BB use
- where will the benefits accrue? (Grimes & Howell, 2010)

Optimal risk management strategy is to wait for more information

But other countries’ governments are investing

- “we can’t afford to be left behind if it does ultimately prove to be an important differentiator”
THE (INEVITABLE) CHALLENGES

1. Competition implications
   • the new networks will not operate in a competitive vacuum
   • relationship to existing network provision
   • what form of competition will be supported?

2. Other policy implications
   • ubiquitous vs targeted deployment
   • open vs closed access regimes
   • vertically separate or integrated firms
   • what other regulation/intervention will be required?
COMPETITION IMPLICATIONS

Position of existing network providers
  – will NGBN network compete with them or supersede them?

Compete
  – hardly a ‘level playing field’
    • stranded assets (incumbent and unbundling entrants)
    • compensation?
  – distorted network investment incentives
    • mobile, wireless face significant disadvantages against subsidised fixed network

Supersede
  – again a compensation issue
  – strategic challenges – who (amongst existing providers) will lead the deployment?
  – ongoing regulatory involvement
UBIQUITY VS TARGETING

Where to deploy first?
- crowding out of private investment in urban areas
- overinvestment/technology skew in some rural areas?

Universal service obligations
- what is the objective
  - maximum deployment and uptake as soon as possible?
  - equalised prices, regardless of differentiated demand?
  - consumer or corporate universality?
  - geographic or market segment differentiation?
- how to fund?

Access to a technology or an access typology?
- application development crowded out by technology investment?
OPEN VS CLOSED ACCESS REGIMES

‘Open access’ ‘unnatural’ when private investor seeks to recover a return on investment

Limits ability to use bundling of applications and technology to

– induce uptake
– recover high fixed and sunk costs

Counterindicative to wide deployment and uptake objectives

Begs question of real target for universal pricing
– consumers or competitors?
VERTICAL INTEGRATION VS STRUCTURAL SEPARATION

Structural separation (network/retail) inimical to alignment of incentives to invest in cohesive infrastructure

- risk-free retail entry
  - short term investment horizon
  - few incentives for long-term contracts
  - real risk that NGBN will become stranded by retailers if new technology comes along

High regulatory costs

- as long as partial private investment exists
- few incentives for accurate forecasts

Risks overinvestment in retail innovation

- at expense of network, application innovation
REGULATORY INTERVENTION

Cost-based? Or other forms?

What primary objective?
  – welfare maximisation or promotion of competition ‘on the network’?

What types of tariffs?
  – connection or usage-based?

Will price discrimination be permitted?
  – on what bases?
AN ARTICLE OF FAITH?

http://www.trinitywallstreet.org/webcasts/videos/browse/worship
APPLICATIONS, RATHER THAN INFRASTRUCTURES, HOLD THE KEY

THANK YOU