

Chapter 17

The future of the telecommunications marketplace

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What interests me is the international framework in which divestiture is taking place. The second stage in the game that began with the unraveling of telecommunications regulations in the United States has two components that relate to world markets. One is that United States domestic regulation and trade policy for telecommunications will have to be further internationalized in light of experiments and changes in the rest of the world. Inasmuch as Americans are sometimes proud to declare that deregulation has marched from the United States overseas, others' experiments with how to adapt that form of competition to their own circumstances are going to come marching back into the United States with important consequences.

The other component of this second stage is common to all countries: All the experiments with varying degrees of competition in communications and information services pose a fundamental problem of how to organize the world market. In organizing a broader framework for the world market, we will find ourselves subject to yet another round of experimentation with national regulation and changing national frameworks for communications and information policy.

Consider first the topic of bringing back home the regulatory experiment; this can be done by reviewing the process of adaptation and trying to come up with a list of what will happen to the United States in the future. Due to the nature of our political system and industrial structure, regulation happened here earlier than elsewhere. But the coalition for reform looks roughly the same in every country. International change represents a further stage of evolution of that coalition, but, aside from country by country peculiarities, a common denominator extends across the world.

The coalition is comprised of extremely large users of telecommunications systems, as Marvin Sirbu has indicated. A typical rule of thumb

is that about 5 percent of the users of national telecommunications systems constitute about half the long-distance demand in the country. Thus, a small, highly organizable set of players has the ability to act politically once the stakes are large enough.

The second group of players is the new electronics companies, especially firms that have moved to the forefront or the influential second tier of the industry since the days of the innovations in micro-electronics. Those firms have a less well-established relationship with traditional telephone companies and less privileged supply relations. In general, the firms have been an impetus for reform because they want to break the privileged access between the only telephone companies and their privileged old electronic firm suppliers.

A third set of players is the service firms, many of whom find it indistinguishable between their use of the system and the provision of new services. They now stand as halfway houses, both buyers and sellers, in the system.

The international coalition is evolving as all of them become more highly internationalized as firms, and as they themselves work out their policies in a world undergoing a shift at a broader level. That broader shift could be considered from many angles, but I will mention only a few of them.

Although the United States remains the preeminent economic and political nation on average in the world, there has been a significant redistribution of international strength. It is a rule of thumb in international political economy that the free trade system has greater problems as the dominant world economy declines. Yet, at the same time, a large percentage of world trade is receptive to new impetuses for liberalization, such as the efforts to open up telecommunications markets. Even though the United States' power is declining and there are rising problems for the management of the international trade system as a whole, the reform coalition and other elements in the globalization of the world economy are leading to new efforts to experiment with the regulatory framework that has guided our traditionally closed markets.

I believe that in the future we should not expect that the choices for the world will be between free trade and the collapse into a 1930s style protectionism. Instead there will be an effort to create new forms of selective liberalization tied to much more conscientious efforts to monitor and enforce international liberalization arrangements. In other words, trust will matter less and verification more in future international trade arrangements. That will have important implications for all of us.

The character of domestic political coalitions in regard to domestic regulatory bargains matters more in this game because domestic regulators will have a greater hand in trade politics. The implications for the United States are important. Yet a reform coalition and shifts in international power are not sufficient to explain the situation. Politicians, after all, do not respond only to interest groups: They respond to voters; they respond to a sense of the public interest; they respond to their own ambitions in Washington as significant leaders.

Politicians, not just in the United States but elsewhere in the industrial democracies, have strategic problems with communications systems. First, I know of no country, including the United States, experimenting with competition in communications that has abandoned in full the politics of cross-subsidies in the communications system. Every country, no matter how it is experimenting, remains committed in some way to cross-subsidies for household service; and they remain committed to major equipment suppliers for the communications network in its various forms. In addition, they are committed in many countries (much less in the United States than elsewhere but still even here) to some form of indirect subsidy for labor in those industries. This means that no matter what we say about the competition of markets, politicians will carefully weigh how cross-subsidies will be continued – perhaps at a diminished level, but nonetheless continued.

Congressman Edward Markey (D-Mass.), for example, opposes deregulation for deregulation's sake and wants a fully documented analysis of any change. This opposition establishes the legislative branch's rights to make certain claims about the payoffs from the deregulation process, in addition to asking sound questions about whether the policy proposals themselves are in order.

Moreover, a common theme across countries is that politicians are looking for ways of denying accountability as they introduce change. One of the lessons that politicians have drawn from our experience is that it is extremely dangerous to deal with the basic telephone system too outrightly. Potential complaints by consumers and other messy surprises might arise; and so we are discovering a variety of regulatory experiments that are difficult for the average household voter to decipher. Hide change, if you would, or put it at arm's length by various devices.

Almost every country continues to have a national champion, or champions, in the communications industry. The word 'champion' often brings to mind the image of a single, dominant, national firm that will

lead us into the world market. Yet the new champion may be a plurality of firms. In such a highly uncertain and changing industry, however, politicians will scrutinize prominent firms in world markets and ask how they are doing. The same will hold for national markets. The US Congress would hardly permit a complete collapse of competition in the long-distance communications market even if for some reason it would happen as a result of market forces. How many people would allow the theory of potentially contestable markets to carry the day as a form of discipline for AT&T? In some form or other the regulatory system would be tampered with to ensure that there are alternative long-distance carriers, and Congress will probably continue to watch certain bellwether firms (e.g., value-added industries like EDS or General Electric's information services) and see how they are doing. We will find continued constraints on competition in order to guarantee that at least some of our national champions are succeeding. Long-term constraints to the political concerns of working politicians will probably emerge as limitations on the marketplace.

A distinction between the United States and other countries is that the power of administrative bureaucracies in the United States is less on average than in other countries. When we deregulate, the assumption is that one should take away power from the administrative bureaucracy; if you want to change the rules of the game, institute new legislation or take it to the courts. In other countries, deregulation means making it possible for the executive bureaucracy to waive its powers temporarily. For example, many rules for the liberalization of value-added services and information services in other countries stipulate that competition is permissible but that extensive administrative oversight remains. Within that contingency for extensive administrative oversight lie potential trade barriers.

This situation creates difficulties for the United States that are not easily handled in the domestic marketplace. Few firms would accept the idea that the FCC will have unspecified powers of administrative discretion over deciding the fate of the information services market at home. But if the FCC cannot do so owing to our national administrative tradition, it means that the decision will get lodged someplace else in the international market. Where we lodge it and how we lodge it will be major questions for the United States.

Given a variety of national experiments with regulation and deregulation, how do we find a common international framework? One possibility is a continuation of the old international cartel for telecommunications services that is intergovernmentally sanctioned for the

International Telecommunications Union. I do not think that this is a viable possibility, however – even a slightly modified version of the cartel with minor liberalization.

What the United States prefers, of course, is the free trade system. We argue that services are like any manufactured good or raw material: They are potentially commodities, and as commodities they can be subject to the free trade rules instituted for the GATT, the world's trading organization. The United States has decided that for reasons of political expedience with respect to the GATT we will concentrate on enhanced services – value-added and information services only. But within that we are going to try to bring as much of the essence of free trade as possible. The United States, in bringing the free trade rubric to telecommunications and information services, is altering the meaning of the free trade rules themselves. Although we use the rhetoric of free trade rules, many substantive principles will change if we follow this route.

I will name just three principles that will change. First, the United States contends that free trade in communication services should operate as a guaranteed right of foreign investment, something that the GATT has never been able to do in any other group and service. Second, there will be organized rights for large users; that is, we vest large users in the international domain with minimum rights as users, a concept that lies totally outside the traditional domain of the GATT. Third, domestic regulations should be significantly internationalized; that is, that there is a presumption that the domestic regulatory system is subject to systematic oversight by the international community and will have to yield to minimum international obligations. In the long term this concept has important consequences for our federal system as well as for our conventional notions of regulation.

Even if we regard free trade as a beginning point, there is a serious concern that it may not be the end point. There are several alternatives. One follows from Marvin Sirbu's notion that large users seek end-to-end networks and yet current systems do not allow them to have that. To the extent that we have a large user community, it presents the prospect that we may eventually encounter a more massive restructuring of international communications systems than we have imagined thus far.

Consider, for example, a communications system that moves in the direction of the international airline industry, where the thrust is to establish about 15 to 20 major global carriers in the world. Imagine that in the communications system we change to a system dominated by a group of global communications companies, and those companies have

their rights organized quite differently from how we view trade. Besides enhanced services, for instance, they could trade voice services. But instead of allowing them to serve everywhere, they would be like the airline market which serves only international gateways picking up and landing traffic in the major business centers of their international users. Furthermore, imagine that the bargaining among governments constitutes a swapping of gateway rights for the rights of the number of carriers allowed to enter the market, much as it is in the airline industry. This kind of arrangement would allow for the combination of voice and data for large services in interesting and innovative ways and permit the sort of oversight of markets that politicians are looking for.

Another alternative is the possibility of new forms of international corporate alliances. For example, AT&T, KDD, and British Telecom are experimenting with the idea of an integrated global service where you can order from any one company services in all three countries with a uniform billing and pricing system. This arrangement constitutes a degree of consolidation and coordination of separate, quasi-dominant carriers that would be unheard of in the past, but may be possible in this market. Because governments are going to control entry, these firms have an incentive to stick together.

A final possibility is when governments say that we recognize the system is much more unstable than in the past, but we still want to retain controls over it. The way we will do that is to grant, on a preferential basis, entry to consortia representing all vested interests. Note, for example, that in Japan, many of the new common carriers represent a consortium of large service firms, large users, and firms in the new electronics equipment business. By an indirect process the new communication carriers in Japan have internalized much of the bargaining that we see in the coalition for reform in other countries. That, too, could be internationalized as the model. Although it is not clear which direction we will take, the United States will find that its regulatory and trade system will be significantly altered by the effort to find a common framework for the communication system of the world.