

The WTO Negotiations Domino Cause or Effect

Michael Reede, Gilbert & Tobin

Article

Abstract

The WTO telecommunications negotiations were proclaimed to be a great success. The 69 signatories represented over 90% of the world's basic telecommunications services and included a large number of Asia Pacific nations. However, the extent to which the negotiations altered pre-existing liberalisation plans is debatable. The impact of the agreement will prove to be significant but claims that it created a new dawn in telecommunications competition are perhaps excessive.

More than 12 months have now passed since the agreement became operative on 5th February 1998 and another round of telecommunications negotiations are expected to commence in 2000. Therefore, as the results of the last arduous round are being implemented, the process will begin anew. What then did the original round achieve and has there been a shift in policy attitudes in the region that will help promote further concessions in the next round?

Basic telecommunications remained an unresolved issue during the Uruguay Round and was therefore allocated a separate negotiating stream with its own timetable. In many ways this reflected the fact that, at that time, many governments were in the midst of a paradigm shift in their attitude towards the liberalisation of telecommunications markets. While competitive markets now appear so natural, regulatory and economic thinking on this topic have been developing rapidly since the closing phases of the Uruguay Round.

The negotiations were expected to conclude in early 1996 but the deadline was extended for 12 months. The offers were deemed insufficient by the United States, particularly those from Asia. On 15th February 1997, sixty nine members of the World Trade Organisation (WTO) finally entered into the Fourth Protocol to the General Agreement on Trade and Services (GATS) relating to basic

telecommunications services (Basic Telecommunications Agreement). The result did not simply represent trade policy "catch up" for basic telecommunications services. As a networked industry with high barriers to entry, telecommunications inevitably threw up many challenging trade issues.

The regional offers improved during the extension but the results were hardly startling. They extended from Australia and New Zealand (which had already planned to introduce fully open markets and which had implemented the agreed regulatory measures) to Brunei (which proposed to review international and mobile entry in 2010). In between were countries such as Japan, Hong Kong, Singapore, Korea, The Philippines, Malaysia, India, Sri Lanka, Thailand and Indonesia with a range of specific sectoral commitments and liberalisation dates.

The Rich Tapestry of Trade Pressure

Telecommunications market liberalisation occurs within a complex pattern of domestic policy, bilateral negotiations, regional multilateral negotiations and international multilateral negotiations (including the WTO). While the GATS has been one of the most important drivers of international economic growth one must not ignore its political dimension. The United States is the largest exporter of telecommunications equipment and services in the world and has significant net accounting rate out-payments. It is naturally in its national interest to see a range of telecommunications markets opened without restriction.

The national carriers of many nations that are yet to fully liberalise their telecommunication industry will inevitably find it very difficult to compete in the global market for either traffic or equipment supply. Within their domestic policy environment there are competing policy concerns to increase the quality and reduce the price of telecommunications services. One also looks to obtain the flow-on effects of price and quality improvement for other economic sectors, to increase the level of access to networks and services (universal access), protect net out-payments and foreign exchange reserves and to maintain the value of government-owned capital assets.

These countries must balance the fears of losing national control access against the benefits of stimulating economic growth. Where a government owned monopoly exists a narrow view may suggest that competition will erode public value. However, it also stimulates growth within and outside the telecommunications sector and the net cost or benefit to the economy is not always so obvious. Both Singapore and Hong Kong approached this issue analytically, modelled the benefits of early liberalisation and elected to pay compensation to exclusive licensees for the early surrender of rights. That is, liberalisation was so deemed beneficial for their economies that they were prepared to pay for it. However, other countries are upgrading their resources to resist competition.

Ultimately, no nation can afford to be left with a substandard communication infrastructure. World Bank and ITU studies have demonstrated the significant loss of GDP that can occur when telecommunications markets are not stimulated. However unconstrained and unregulated competition may be damaging to national objectives such as improved universal access. The issue is not whether liberalisation should occur but when and how a balanced and sophisticated regulatory environment may be deployed in order to ensure that complex national objectives are achieved.

Privatisation, Liberalisation and Regulation

Since 1994, 44 previously publicly owned incumbent carriers have been privatised raising a total of US\$159 billion and half of which has come from the Asia-Pacific region (although the privatisation of NTT raised US\$70.5 billion which exceeds all the other Asia-Pacific privatisation combined). Approximately one third of investment into privatisation comes from outside the domestic economy. However, this privatisation program has not fundamentally changed the pattern of service provision. The discipline of capital markets assists in improving operational efficiency of carriers but certainly not in the same manner as competition.

For example, the ITUs Regulatory Colloquium concluded in December 1997 that the accounting rate system was not the main problem in reforming international trade in telecommunications services. Rather, the fundamental problems revolved around the lack of telecommunications development in many countries due to inadequate investment, inefficient pricing policies, monopolistic industry structures and the lack of clear and effective regulation. In short, the policy focus should be on the entire fabric of regulation, not simply the licensing of new entrants. Accounting rates are an important part of the liberalisation process but they are not an end in themselves.

As many foreign carriers investing in the region have realised the grant of competitive telecommunications licenses without a supportive regulatory regime often presents an entirely illusory opportunity. Nevertheless there has been a history of investment by North American and European carriers that appear to be ready to accept deficient regulatory regimes in the short term in the hope that conditions will improve in the long term. One only needs to look to the fortunes of new mobile and fixed line entrants in India and KSO partners in Indonesia to see the dangers of this approach. Investors and banks in many countries in the region are now clambering for regulatory reform.

The WTO recognised the critical importance of pro-competitive regulatory regimes and, in addition to specific commitments to open up particular services, 57 of the signatories committed themselves to the Reference Paper on Regulatory Principles

which addressed:

- competitive safeguards · interconnection under non discriminatory terms and at cost oriented rates · transparent licensing processes · the independence of regulators

The Reference Paper is open to interpretation and many nations sought exemptions. Its implementation in legislation and subsequent application is often questionable. Nevertheless it reflects the four basic pillars on which a successful regulatory regime must be based and at least dispels the myth that different countries require fundamentally different regimes. It provides a benchmark blueprint for regulatory environments. As anyone who has experienced liberalisation first hand will know, in regulation the "devil is in the detail". There is a chasm between principles of the type found in the Reference Paper and its pro-competitive implementation. However, it is a necessary line in the sand. Many countries with liberalised countries have, or are in the process of, appointing semi-independent regulators to oversee the conduct of the telecommunications sector. Very often these regulators see their role as facilitators introducing competition to the domestic market as rapidly as possible. In this process they are heavily influenced by the role played by existing regulators which has had the advantage of normalising a lot of regulatory initiatives around the region. However the uncritical application of existing regulatory models carries its own risks. Fledgling regulators are currently testing new powers and developing policy models to address unique national objectives in the region.

No Market is an Island - Resistance to Commitment But Recognition of Need

Perhaps the most interesting phenomenon of liberalisation policy in the Asia Pacific region since the Basic Agreement on Telecommunications Services has been that a number of countries have moved faster than they had originally planned, in spite of having had reservations from the outset.. For example Thailand is moving ahead to develop its telecommunications masterplan which will involve liberalisation prior to its WTO commitment date of 2006. Hong Kong moved to liberalised ISR on 1st January 1999 and facilities will be liberalised on 1st January 2000. Both Korea and Malaysia have indicated that they will relax foreign ownership restrictions. Rumblings of further progress are also being heard from Indonesia, Vietnam and Brunei. Why has this occurred? While a number of regional WTO members were unwilling to yield in the face of WTO pressures, they have recognised the economic imperative of liberalisation and are driven by 2 factors: The implications of failing to obtain investment and technology transfer to build essential telecommunications infrastructure that will support economic growth during a critical period.

The difficulties of remaining outside the group of liberalised nations because of the domino effect of liberalisation. The Service Based Global Economy - Being Left

Behind During a Global Transition Although it is possible to overemphasise the contribution of services to GDP growth the explosion in trade in services has been one of the most significant economic developments of the last 2 decades. The growth of telecommunications networks as a medium for the dissemination of information and education has also been quite revolutionary. What will be the economic impact on those countries that have insufficient connectivity to participate fully in these developments? In an environment where foreign telecommunications investors are becoming increasingly scarce it is this question that will weigh most heavily upon the minds of policy makers. Can a country afford to lose comparative advantage to its regional neighbours or to fail to develop as part of the information society? The implications of being left behind will be significant. Amongst the faster growing Asian economies, Hong Kong has led most forms of telecommunications liberalisation. It is not surprising that Singapore would now want to move more quickly to ensure that it is not disadvantaged as a regional headquarters and hubbing centre. In a similar manner, Hong Kongs more recent desire to liberalise its broadcasting regime must be assessed in the context of the loss of a number of major broadcasting facilities to Singapore. Taiwan and Korea are also mindful of the competitive disadvantages of allowing Hong Kong and Singapore to more rapidly develop their telecommunications infrastructure. This is the competitive drag effect of asymmetric regional liberalisation. Put in another way, the domino effect caused by significantly shifting the competitive paradigm of a region through the introduction of a different economic model by one nation.

Indonesia, which has invested significantly in developing a sophisticated aerospace industry as part of a shift from its agrarian base, has remained one of the most restrictive telecommunications markets. While it has been pursuing a policy of developing advanced technology based manufacturing facilities it has failed to keep pace with the international transition to an information economy. Many countries in the region have now begun to recognise that the Internet is an important manifestation of the emerging global information infrastructure which will be critical to economic development. For many years development theory was dominated by strategies that sought to leapfrog stages of economic development. It is ironic that many nations may now have failed to grasp the adverse implications that a failure to stimulate telecommunications infrastructure investment may have on their ability to participate in the global information infrastructure.

A Return to Investment Conservatism?

A critical regional issue that is yet to be fully appreciated by many regional governments is that foreign investment in telecommunications infrastructure is no longer treated as a blue sky proposition. The first half of the 1990s represented a halcyon period for direct foreign investment in telecommunications carriers in liberalising countries. Many North American and European carriers found

themselves with highly profitable domestic businesses but static revenues. The almost universal strategic response was to expand into value-added services and new geographic markets for basic services. The second strategy led to a variety of carriers seeking to take strategic positions as second carriers in liberalising markets or to establish resale positions in preparation for the collapse of the accounting rate regime. In the Asia-Pacific region investment in new carriers in, for example, Australia, Hong Kong, Singapore and New Zealand has proven to be relatively predictable. This is partly due to the demographics of those countries but also because they have offered sophisticated regulatory regimes that facilitate entry. However, investment in other countries in the region has often been a marginally profitable scenario or a loss making venture that hopefully is positioned for return to profitability in the longer term. Many projects have not produced the returns that foreign carriers had hoped would offset market share loss in their domestic markets.

The pressures of rationalisation have forced these carriers to re-examine their offshore investments and decide whether their capital can be re-deployed more profitably elsewhere. A number have withdrawn from the region and others have stalled further investment, only a few remain aggressive investors. The regulatory regime has proven to be one of their most sensitive business case assumptions. Service based investments in resale operations and Internet service providers remain popular as they are not major infrastructure projects. However, major fixed line investment opportunities are now viewed as less viable. There are exceptions for network positions in the PRC appear to remain attractive and Taiwans fixed line licensing process may well be successful. However, stimulating telecommunications markets in India and Indonesia will be difficult and investors will review Malaysia, Thailand and Korea carefully.

Accounting Rates the FCC and Single Marketsv

The accounting rate debate has also echoed around the Asia Pacific region. Reform of the international settlements regime is conceptually little more than applying to international network connectivity the regulatory principles have been applied to local network interconnection. However, the policy dimension of interconnection is far more complex in the context of international traffic because it is no longer dealing with the relationship between a single incumbent and one or more new entrants in a particular market but between the interests of different countries and a large number of carriers. A significant debate took place within the WTO negotiations regarding the treatment of accounting rates and whether they were measures of a member subject to the basic GATS obligations. This argument was pursued on the basis that accounting rates were struck on a commercial basis between international administrations and were not in fact the result of Government intervention. Ultimately the negotiations produced no specific commitments on accounting rates. It is therefore not surprising that the FCC then pursued alternative

approaches.

The FCC Accounting Rate Report Order suggested that it proposed a means of restructuring the economics of international telecommunications services to promote technological innovative interconnectivity serving all the worlds consumers. However, this significantly overstated the sensitivity of the FCCs policy to the needs of developing telecommunications markets. While the FCC maintained that the margins on international termination fees required US consumers to pay artificially high prices, a significant proportion of the net out-payment of the United States is not caused by US originated traffic but by profitable US call-back operations and the significant market for the re-file traffic through the United States (often working in combination). The United States has sought to apply trade pressure and attach commercial costs to non-compliance with its views on accounting rates. Concepts such as the equivalent competitive opportunity or ECO test have frustrated foreign carriers in non-liberalised countries and their associates in entering the US market Under these circumstances there are also an attached a price to closed markets. This may be persuasive for international carriers that require access to the US market. But what of major regional carriers that are not themselves subsidiaries of international carriers requiring access to the massive US market? For example, do VSNL, the PLDT, PT Telkom, China Telecom really care about reciprocity? Settlement rates are simultaneously being addressed by the ITU through Study Group 3 and, significantly, will also be the subject of a review at the next round of WTO negotiations. On the one hand the FCC has increased the pressure on the ITU and countries resisting liberalisation. On the other hand, the initiatives of the ITU and the WTO have allowed the FCC an option to walk away from what appears to have been something of an international relations policy nightmare. Like the WTO the FCCs efforts may contribute to the liberalisation process but the real drivers remain economic.

The Inevitable Shift Towards Competitive Policies

To prevent competitive incursion a Government cannot be neutral, it must be committed to maintaining a closed market. As a first principle markets are open unless Governments restrict access through monopoly and oligopoly licensing regimes, spectrum restrictions and other measures. Therefore closed markets require Governments to take active steps to restrict a natural competitive market outcome. In the absence of this action there is a relatively rapid and permanent migration towards forms of liberalisation. However, the ability of Governments to resist these trends is declining and the economic cost is increasing.

When only one or two national markets are open to competition it is not difficult to resist the tide of competition. However, when the majority of national markets have been liberalised it becomes very difficult to manage traffic flows. This problem is exacerbated by relatively inexpensive technologies that allow fledgling competitive

operators to play the exclusivity gaps that may exist technically or legally. In other words, it requires a significant effort to treat particular national telecommunications market as a fortress that is economically resistant to external developments and new technologies. Ultimately Asia-Pacific regional economies will face a difficult task in stemming the tide of competition and they are no longer confident of their closed market policies. The next round of the WTO negotiations could well see far more significant development as nations in the region will progressively see their economic interests as being best served by open competition subject to reasonable measures to enhance universal access imperatives. However, timing remains critical as the window of opportunity to attract global capital for telecommunications infrastructure projects may be closing and sensible and comprehensive regulatory environments will be required to keep it open.

[Home](#)[Magazine](#) [Contact Us](#)[Careers](#) [Tell a Friend](#)[Site](#)[Map](#)

©Copyright World Info Comms Ltd.