

5. It might be possible to allow access to these processes under specified circumstances not only by Governments but also by other directly affected parties (for example, carriers).

#### IV Conclusions

IV.1 While termination charges are not a panacea, *integrating a consideration of foreign termination charges into the process of multilateral trade negotiation could help subject these charges to more effective international discipline.* By helping to eliminate the severe distortions which currently characterise this market, this would provide immediate and material gains to users of international telecommunications services; there would also be substantial benefits to economic growth more generally, as the reduction in charges for international telecommunications removed transactions costs barriers to international trade and investment.

IV.2 The distortions built into the current system involve a large number of countries and a dense matrix of bilateral relationships. Table 4 sets out data on the pattern of Australian traffic and payments for all the streams on which international service is provided. Partner countries are grouped in quintiles by traffic density. As can be seen from this data, while the "thinnest" 200 streams generate less than 15 per cent of two-way minutes, they currently account for close to 50 per cent of net out-payments<sup>9</sup>. Reducing the gaps between prices and costs would consequently involve many relatively small adjustments, creating complex scope for trade-offs and compensation.

Experience has shown that Multilateral Trade Rounds provide a setting in which these trade-offs can be made in a manner which is both effective and allows for overall equity in outcomes. For example, by subjecting the current price-cost gaps to "tariffication" -- that is, converted into tariff equivalents or, as with agricultural prices, producer subsidy equivalents -- changes from current levels could more readily be made in the context of Round offers and concessions. At the same time, agreed targets (for example, equal percentage cuts) could be set for outcomes, with the resulting levels being bound. The greater transparency of the process could only increase the chances of successful reform. The data set out above, on the extent of the current distortions and their likely impact on demand, suggests that the direct economic gains from progress in bringing inter-carrier charges towards costs would be large<sup>10</sup>. Less readily quantified, but perhaps even more important, dynamic changes -- such as the accelerated development and diffusion of new international telecommunications services -- would make these gains all the greater.

IV.3 Though this paper has not been able to model the gains from reform in a full multilateral (N-country) setting, there is reason to believe that they could be widespread:

- Countries with high current levels of out-payments would clearly benefit from reforms which brought termination charges down.

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<sup>9</sup> This pattern of course partly reflects real income differentials (one would expect Australians to consume more international telephony services than their counterparts in poorer countries); but it is also significantly affected by the widespread distortions in prices, with foreign-end charges (including in high-income countries) being substantially higher than those in Australia.

<sup>10</sup> For Australia alone, the consumer welfare gains from bringing foreign effective termination rates to cost would be in the order of \$60 million, assuming that this allowed a 20 per cent fall in outgoing IDD charges. The proportional gains would typically be even larger in other countries, since Australia has relatively low retail prices for IDD service.

- So too, however, might countries which have until now secured net in-payments. In particular, a multilateral reduction in termination charges would allow a general reduction in prices for international calls. Given that the elasticity of demand is well above one, the substantial additional traffic which price reductions gave rise to would almost certainly more than outweigh the revenue loss from the change in settlement payments<sup>11</sup>.

These gains might be especially substantial in the developing economies:

- Many developing countries have undergone far-reaching internal and external liberalisation in recent years, and attach increasing importance to achieving and maintaining dynamic, outward-oriented, economies.
- As this process unfolds, these countries have become increasingly reliant on international telecommunications -- more than doubling their share of international telephony over the last decade.
- The distortions arising from the current arrangements therefore increasingly affect these countries as they seek to bring call charges down to the levels expected -- and ever more vocally demanded -- by outward oriented firms and communities.
- Particularly in developing countries, a very large share of long haul traffic is business related. Bringing rates and charges down would eliminate a tax on business which currently limits international trade and investment and hence depresses domestic incomes.

IV.4 While the greatest gains from effective reform might be fairly long-term, more immediate benefits would also accrue. Thus, in addition to the benefits cited above, a termination charge system would accommodate resale and the provision of international value added services more readily than do the current arrangements:

- This is because such a system would “unbundle” international transport, which is increasingly competitive, from domestic termination, where change is likely to occur more slowly.
- Value Added Service providers and resellers of international service could then secure international transmission from an increasingly wide range of sources of supply, while accessing domestic termination on terms no less favourable than other market participants.
- The increased ease of entry -- which would also extend to new facilities-based providers -- would encourage innovation and help to more rapidly eliminate price anomalies.

IV.5 Given the potential benefits, the central issue is how to reduce the risks which the transition to a termination rate system might involve. The measures which could be taken to this end include constraining the level at which termination charges are set, requiring some degree of tariffication, and/or seeking agreement on an MFN basis to settlement principles.

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<sup>11</sup> Countries in which traffic was subject to binding capacity constraints would not secure an increase in revenue in this scenario. However, this is a relatively small and rapidly diminishing group.

IV. 6 As a practical matter, many countries are moving to shift responsibility for telecommunications out of the core public sector, with reforms in some cases aiming merely at commercialisation while others have gone as far as full privatisation. As a consequence of these changes, accentuated in numerous countries by some degree of liberalisation, many governments are reluctant to intervene directly in decision-making by telecommunications service providers, except in so far as is necessary to protect the public interest. Regulating and making transparent international inter-carrier charges may be viewed in some countries as being primarily a matter for these service providers themselves, rather than as a responsibility of governments. Nonetheless, the current arrangements do reflect a regulatory and policy environment established under an inter-governmental agreement. And given the gains which could be secured by reform in this area, governments should establish a *framework* within which the providers of telecommunications services can take commercial decisions, freer of the inherited distortions which now weigh so heavily on the international telecommunications system.

Table 1

Country (Quintiles)	F C Rs	Ratio of F C Rs to A C Rs (FCR/ACR)
1. Quintile	A\$ 2.49	1.617
2. Quintile	A\$ 2.81	1.412
3. Quintile	A\$ 3.59	1.639
4. Quintile	A\$ 4.71	2.141
5. Quintile	A\$3.18	1.465

F C R: Average Foreign Collection Rates  
A C R: Average Australian Collection Rates

Table 2

Average Accounting Rates and Mark-up by Traffic Volumes

	Accounting Rate Indexed to Average	(Settlement rate - Cost)/Cost
Lowest Quintile	1.18	4.93
2nd Lowest Quintile	1.17	4.59
Median Quintile	0.94	3.40
2nd Highest Quintile	0.98	3.99
Highest Quintile	0.73	3.14
2nd Highest Decile	0.73	3.35
Highest Decile	0.70	2.91
Average	1.00	4.01

Table 3Domestic Competition and International Rates

	Account. R. Indexed to Avg	(Settlement Rate - Cost)/Cost	Foreign Collection Rates	Foreign Collection/Aust. Coll.
Countries w. dom. competitn	0.69	1.67	\$A1.74	1.35
OECD w.o. dom. competitn	1.20	3.45	\$A2.59	1.70
Average	1.00	2.76	\$A2.32	1.59

Table 4Call and Outpayment Imbalances by Traffic Quintile

(Expressed as percentage of respective totals)

	Outgoing Calls	Imbalance	Total Calls	Out payments	Outp. w. SR as terminatn	Outp. w 1/2 SR as term.
Bottom quint.	0.3%	0.5%	0.3%	0.7%	0.6%	0.9%
2nd bottom quint	1.3%	3.5%	1.3%	4.9%	2.9%	4.0%
Median quintile	3.8%	8.8%	3.2%	10.0%	6.3%	8.4%
2nd top quintile	10.4%	31.5%	8.5%	31.9%	19.2%	26.3%
Top quintile	84.1%	55.7%	87.0%	52.5%	71.1%	60.5%

Chart 1

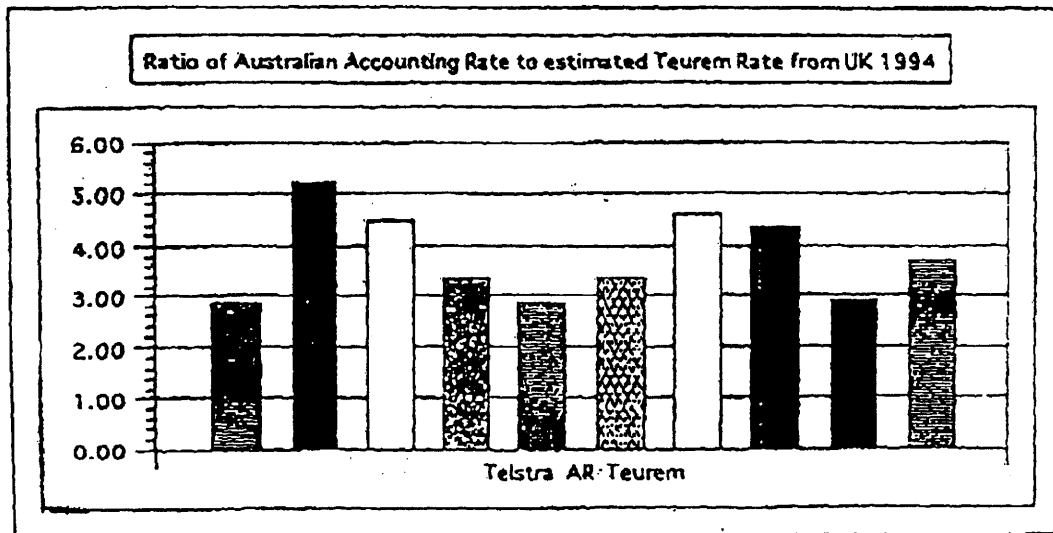


Chart 2

