# Telecombat

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For almost the whole 20th century, governments around the world have enforced monopolies in telecommunications. In the early '70s the U.S. government was one of the first to change when it allowed some competition among long-distance carriers. The dismantling of AT&T (NYSE: T) in 1984 hastened the process. That same year, the British government privatized British Telecom and allowed more competition. Recently the German government sold off part of Deutsche Telekom (NYSE: DT). As large companies compete to become the dominant suppliers of telecom services globally, many people think that the most important issue is which country's telecom giant wins the race.

It isn't. Whether a country's government allows competition is much more important to its economy.

## DOLLAR'S BILL

Here's why. Define a unit of telecom services so that its price in a competitive market is $1. That dollar is not the telecom company's gain. The company's gain is its revenue minus its costs, which are more than most people imagine. According to one Gallup poll, many college graduates believe that corporate profits are about 45 percent of revenues -- probably because they observe markups of 50 to 100 percent on the cost of goods. But labor and capital costs are substantial. For U.S. telcos, net income between 1989 and 1996 was on average 10.8 percent of revenues. And much of this was simply a competitive return on capital.

Consider the loss to consumers if governments were to revert to their longtime policy of suppressing competition in telecom. Because protected monopolists don't need to compete for market share, they are slower to cut costs and improve technology. What sells for $1 in a competitive market could well be priced at $1.50 if governments blocked competition. So the loss to consumers for each unit of telecom services purchased from the monopolist could be more than five times the gain to a telecom company from winning in a competitive market.

The focus on which company will win the competition is natural because the competitors are so visible. Less visible in telecom, but even more important, are its millions of consumers.

This same mistaken focus on competitors rather than on competition also explains a common misunderstanding about international trade. Many people believe that allowing imports is a concession we must make so that other countries' governments will open their borders to our exports. Even the United States' chief trade representative, Charlene Barshefsky, thinks this way. Her focus is on persuading other countries' governments to reduce their barriers to our exports; she fails to acknowledge that the U.S. government's own import barriers destroy our well-being just as much.

Vice President Al Gore makes the same mistake. In his famous 1993 debate with Ross Perot about the North American Free Trade Agreement (NAFTA), Mr. Gore based his argument entirely on the benefits of free trade to U.S. exporters and said not one word about NAFTA's benefits to U.S. consumers. Mr. Gore's latest line on trade is that "the United States cannot be the importer of only resort." This is patent nonsense, for two reasons. First, as Mr. Gore knows, the United States is not the only country that imports goods. Second, and more important, what would be so bad about foreign producers' trying to sell their goods just to us?

## DUMPING FOR JOY

Even people who accept that free trade is good for us often think it's bad when foreign suppliers "dump" their goods -- that is, price their exports below the prices they charge in their own country, or below their cost. But if foreign firms charge us a lower price than in their own markets, it's typically because our market is more competitive than theirs. And the documented instances of foreign firms selling at prices below their true costs are very rare. What appears to be pricing below cost is often pricing to cover incremental costs but not sunk costs. Didn't Asian memory chip makers price their exports to the United States below cost in the '80s in order to bankrupt domestic competitors and then raise their prices? Actually, no. The economist Andrew Dick, in a 1991 issue of the Journal of Law and Economics, found that the Japanese firms were engaging in "learning curve" pricing, not predatory pricing. If additional volume will cut your future costs enough, it can make sense for you to price below current cost to generate that volume and then "learn" the most profitable price for your products at the most efficient volume. That is why, Mr. Dick notes, the Japanese firms also priced below unit costs in their domestic markets.

As Fred Smith, president of the Competitive Enterprise Institute, a public-interest lobby in Washington, D.C., once stated, "If our antidumping laws applied to U.S. companies, every after-Christmas sale in the country would be banned." Dumping is good for consumers. What matters is not which competitor wins, but whether consumers have cheap, good products. Without regulation, they do.