



नेपाल दूरसञ्चार प्राधिकरण
Nepal Telecommunications Authority

Why regulation is all about economics

Strategic Planning Workshop

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AGENDA



1. Why does the telecommunications market needs to be regulated?
2. Why is economics important?
3. Outline of economic theory
4. What should the NTA be trying to achieve?
5. How can the NTA achieve this?
6. Conclusions



1. Why does the telecommunications market need to be regulated?



It is generally accepted that, wherever possible, the interests of consumers are maximised by having goods and services provided through competitive markets.

These competitive markets ensure resources are directed towards producing those things that consumers value most and at the lowest possible cost.

In the absence of any barriers to do so, markets will efficiently coordinate the actions of countless individuals for their mutual betterment.



1. Why does the telecommunications market need to be regulated?

However, in certain circumstances, markets may not effectively (or efficiently) maximise the interests of consumers.

- This is evident in the telecommunications sector.

Because of the industry cost structures in the telecommunications sector, there will be one, or at best only a very few, companies in the marketplace.

In order to maximise profits, these firms are likely to restrict supply in order to raise prices.

- Competition is unlikely to occur because the industry economics of scale and capital expenditure requirements create significant barriers to entry
- Market power in one market may be used to influence upstream or downstream markets
- Competitors need to compete and cooperate at the same time, meaning a high risks of anti-competitive behaviour.

This means that regulatory intervention is required.



2. Why is economics important?



The presence of such market failures in the telecommunications sector gives rise to the rationale for economic regulation.

Economic regulation can help to ensure that prices paid by consumers are reasonable, and reflect the efficient costs of providing on-going and reliable services.





3. Introduction to Economic theory



In general, regulators should try to maximise long run economic welfare (also sometimes called 'social welfare').

Economic welfare is the total benefit available to society from an economic transaction or situation.

To fully understand what economic welfare means from the perspective of economic theory, we need to understand the concept of 'consumer surplus'.

Consumer surplus is a measure of the welfare the people gain from consuming goods and services.

- Consumer surplus is defined as the difference between the total amount that consumers are willing and able to pay for a good or services, and the total amount that they actual do pay (i.e. the market price).

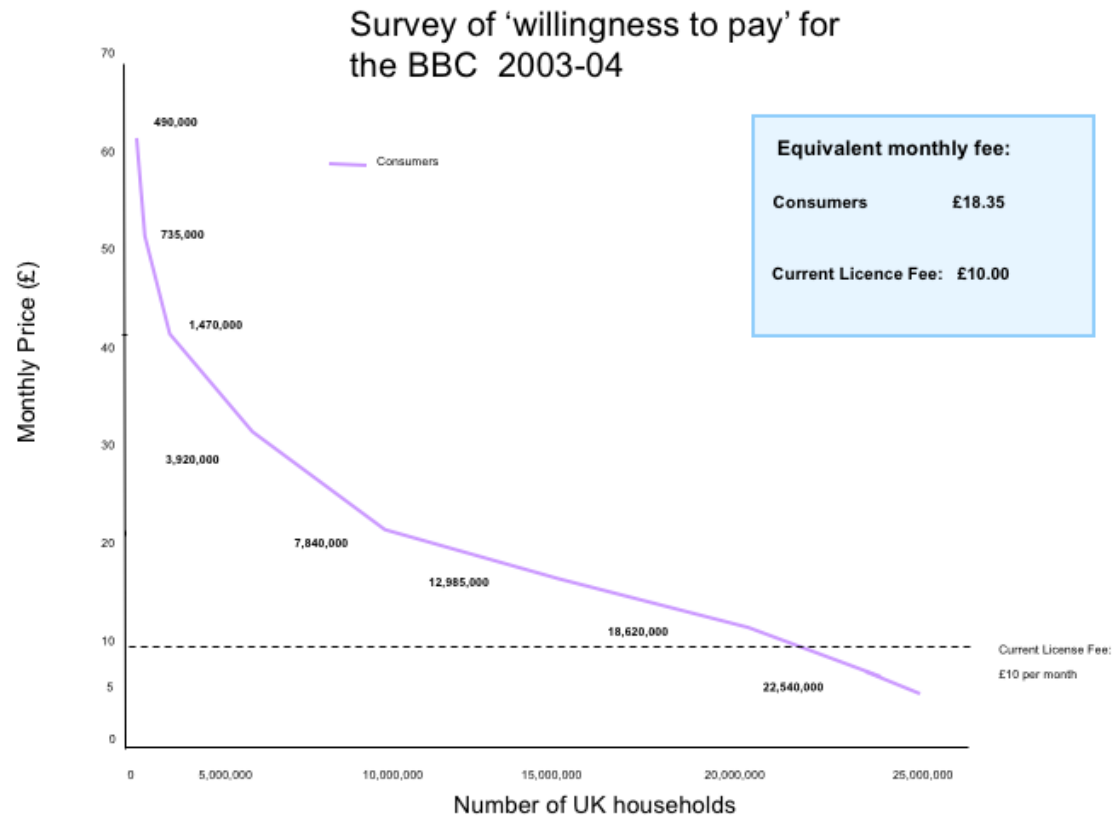


3. Introduction to Economic Theory



A demand curve indicates what price consumers are prepared to pay for a hypothetical quantity of a good, based on their expectation of private benefit.

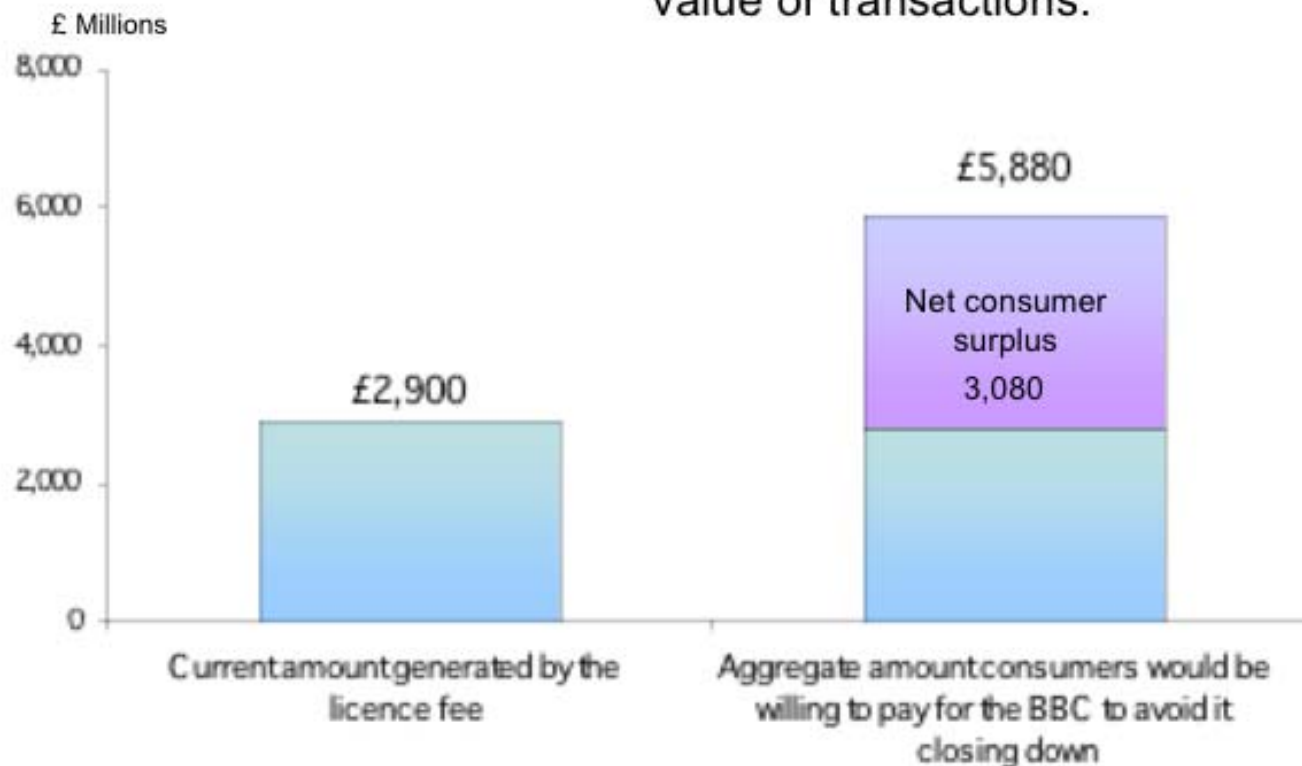
Example from broadcasting industry





3. Introduction to Economic Theory

Consumer surplus is greater than the value of transactions.

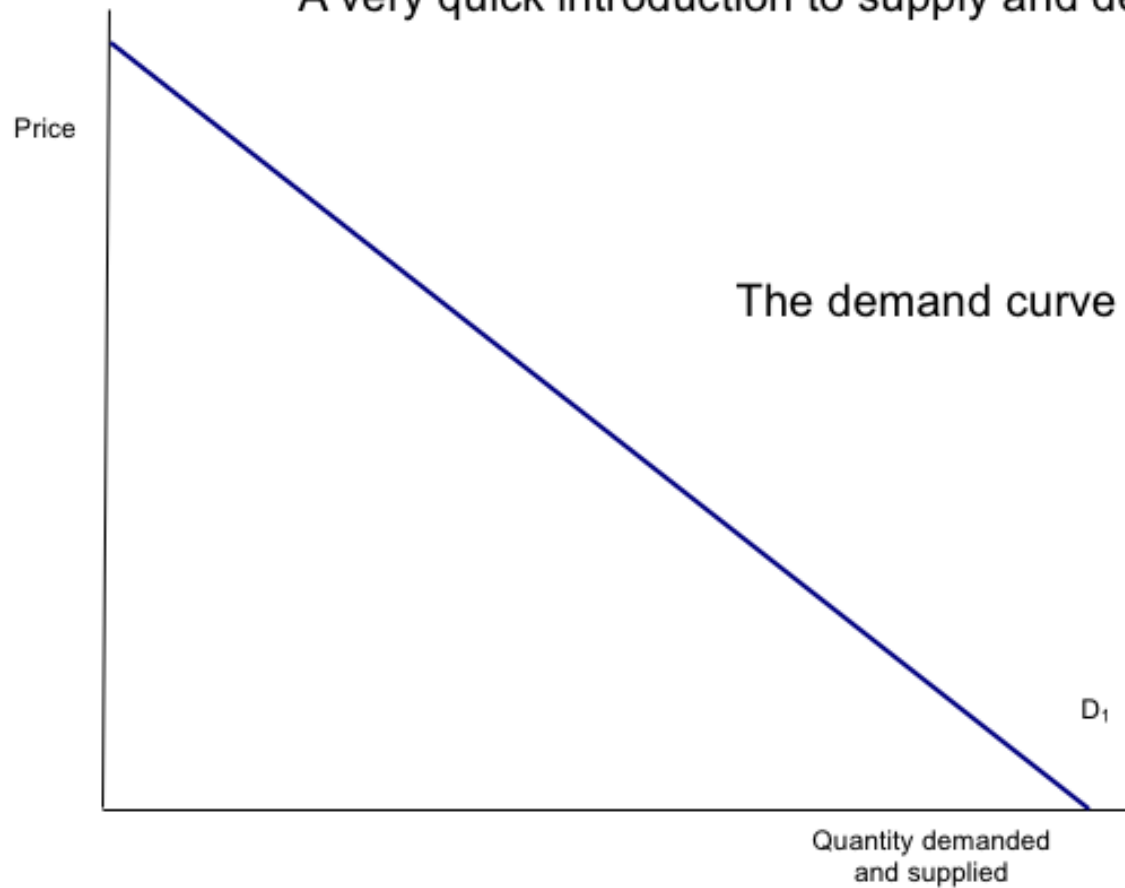




3. Introduction to Economic Theory

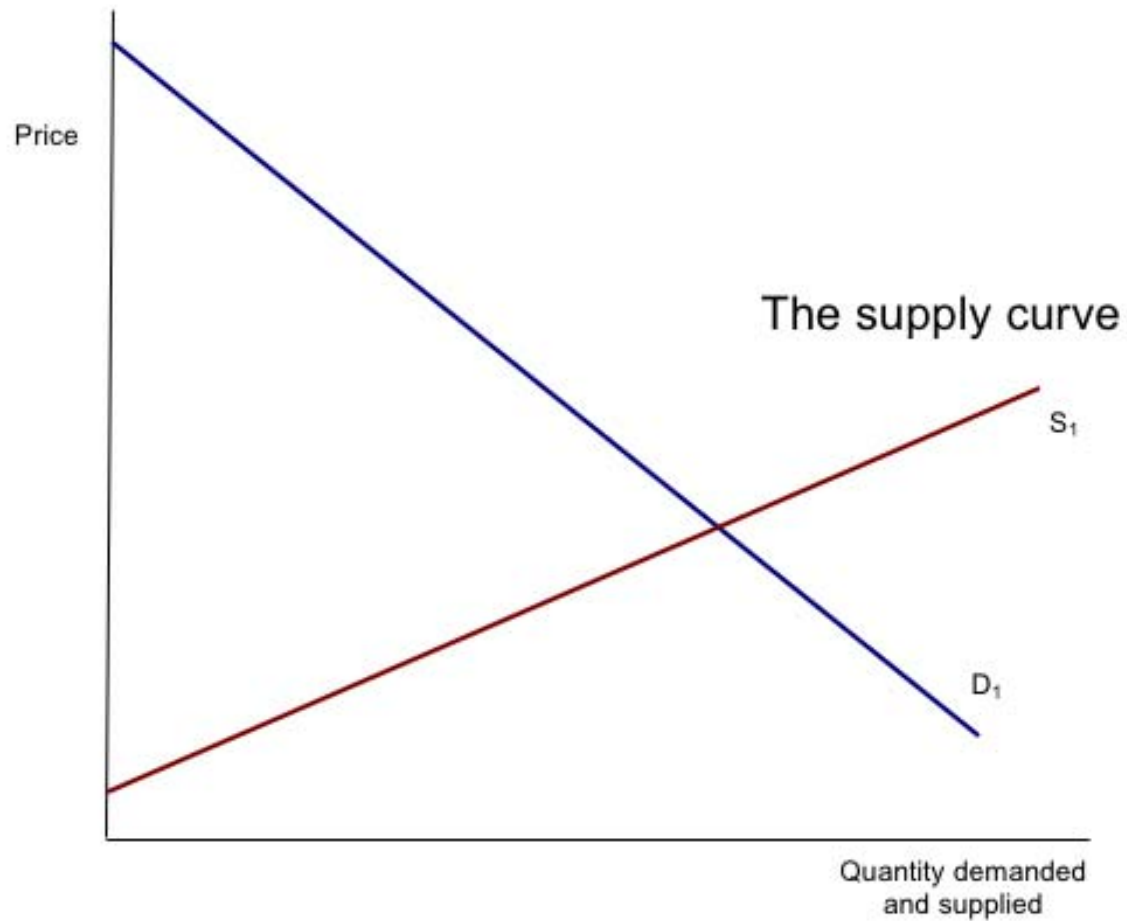


A very quick introduction to supply and demand



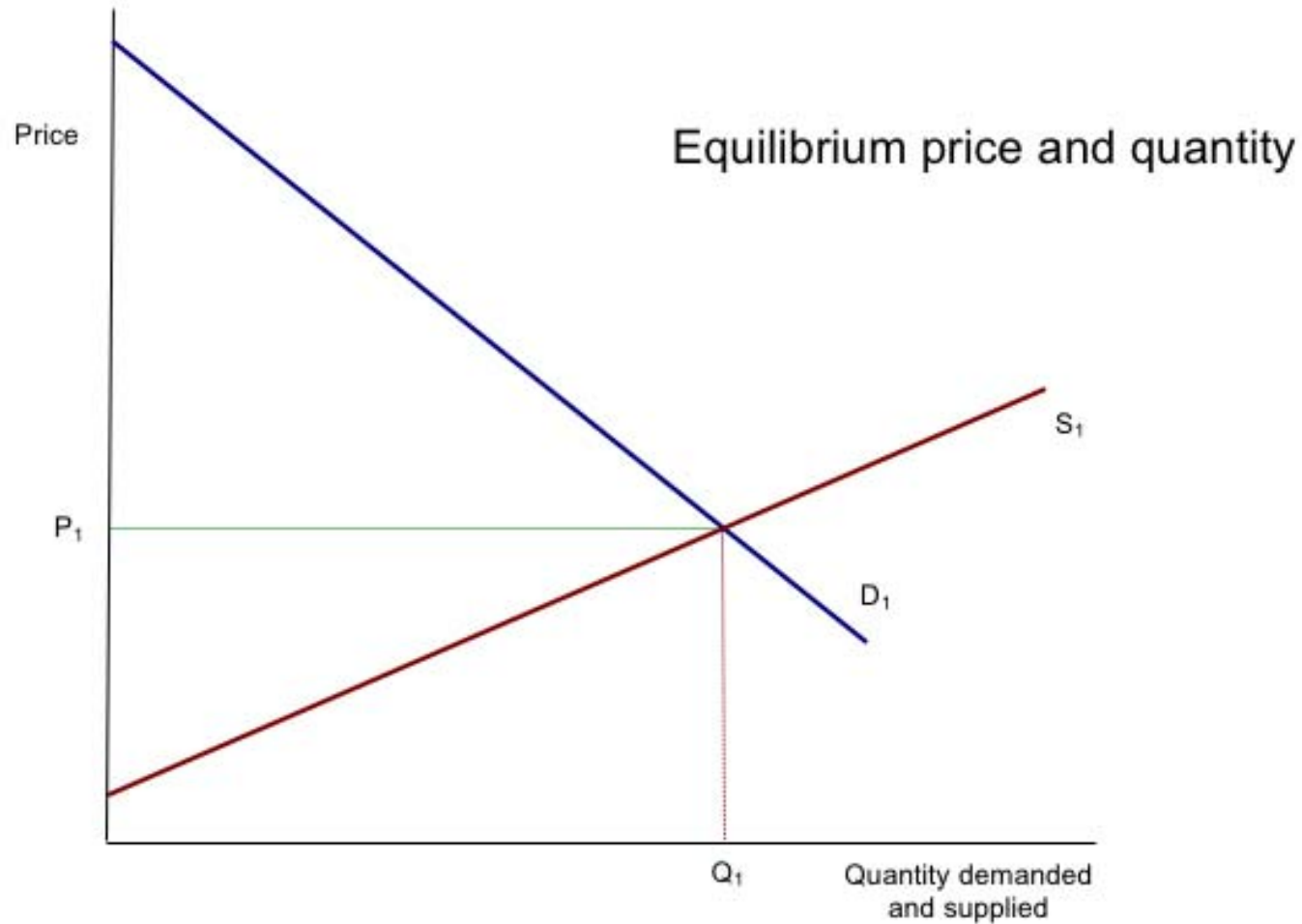


3. Introduction to Economic Theory



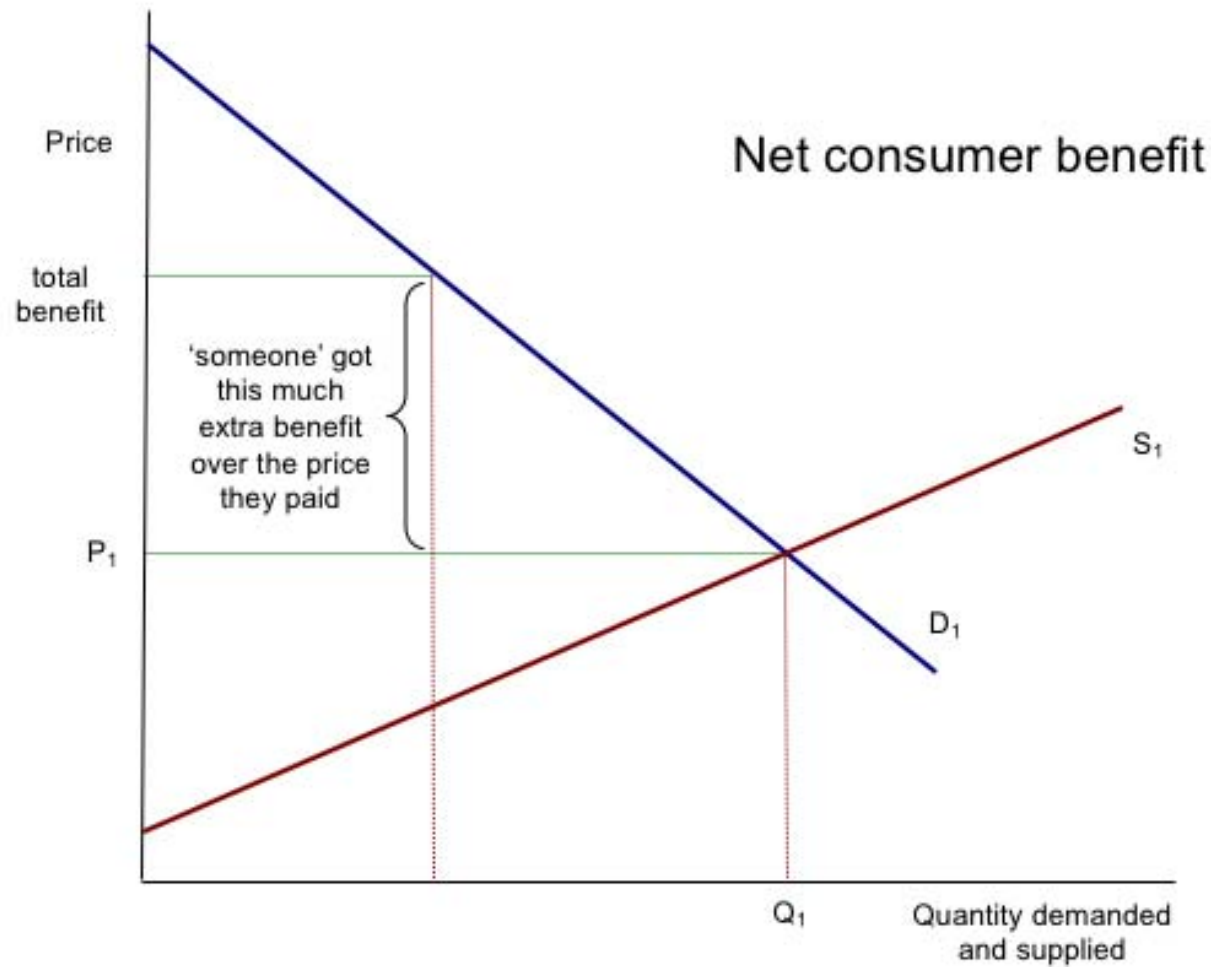


3. Introduction to Economic Theory



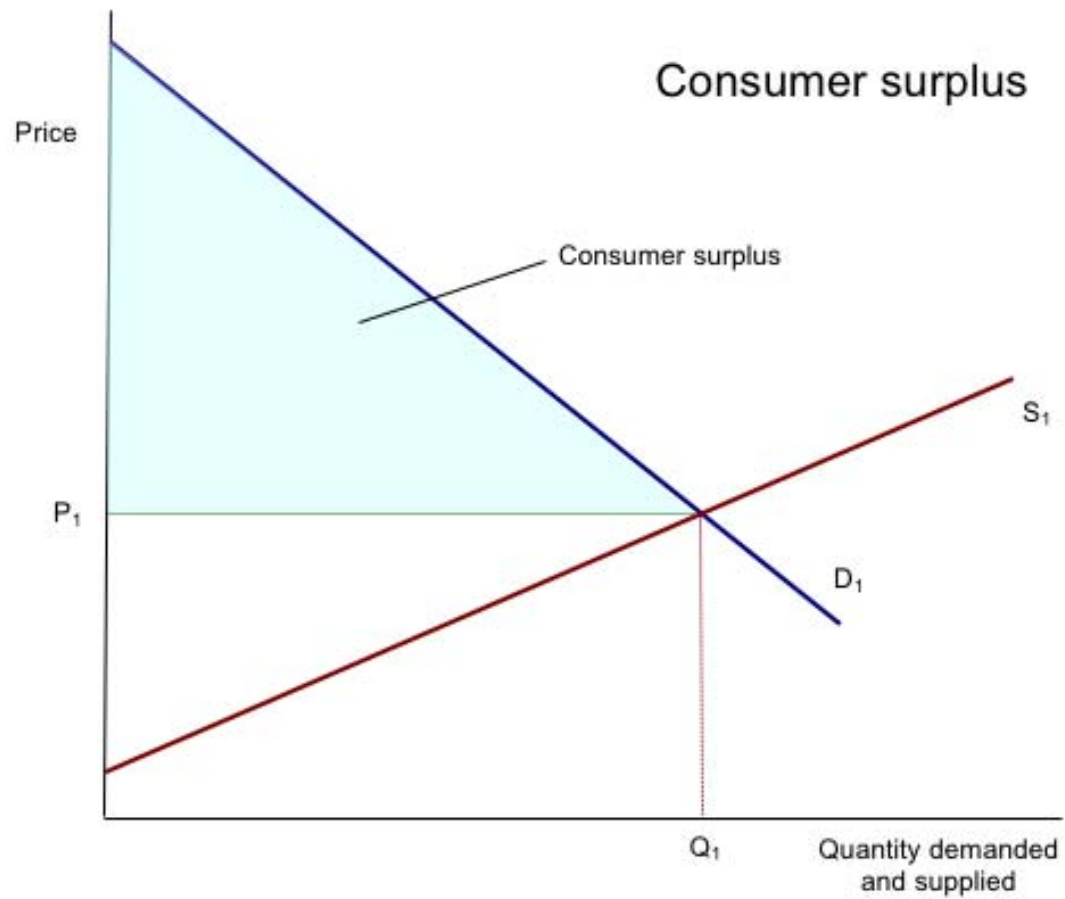


3. Introduction to Economic Theory



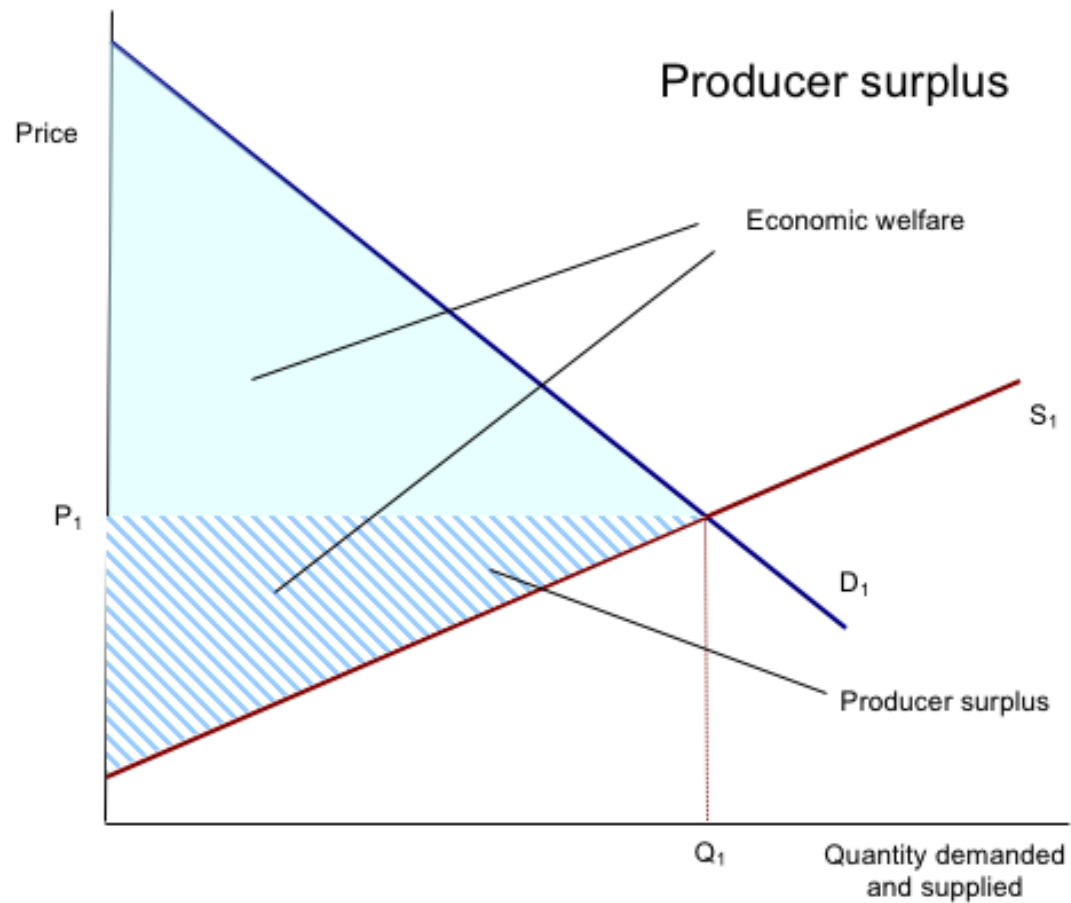


3. Introduction to Economic Theory



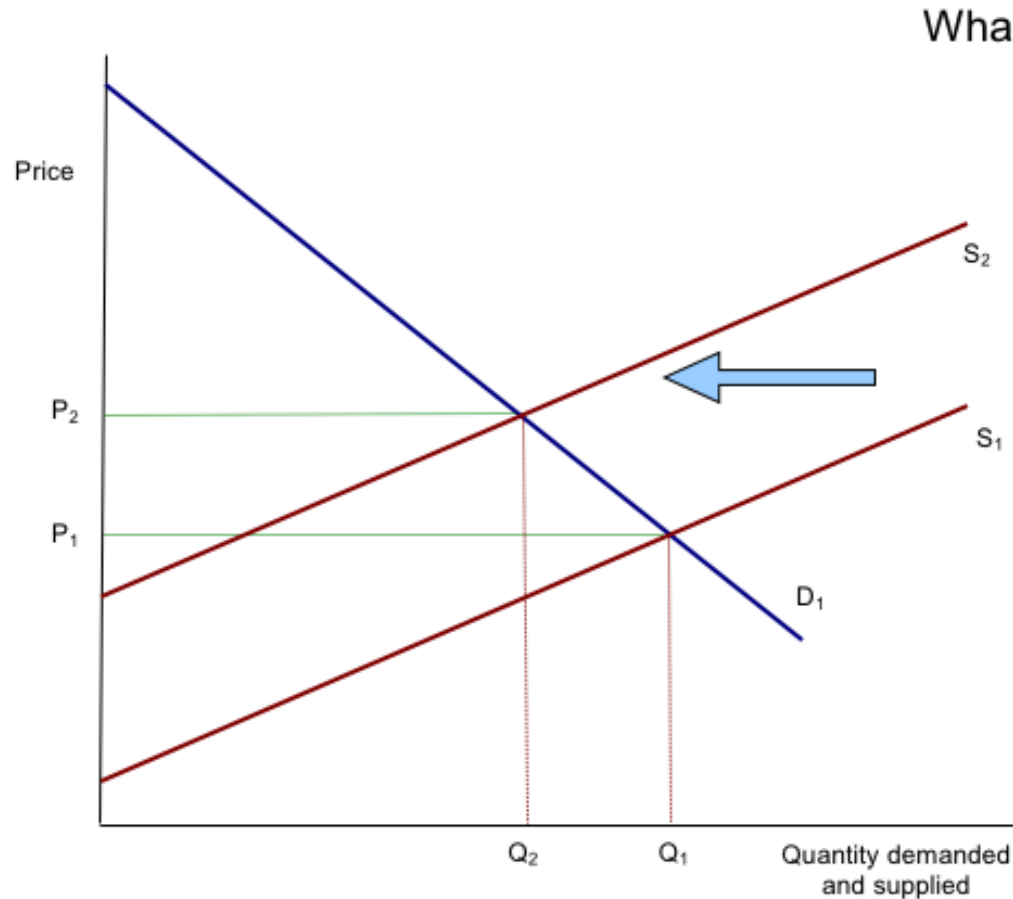


3. Introduction to Economic Theory





3. Introduction to Economic Theory

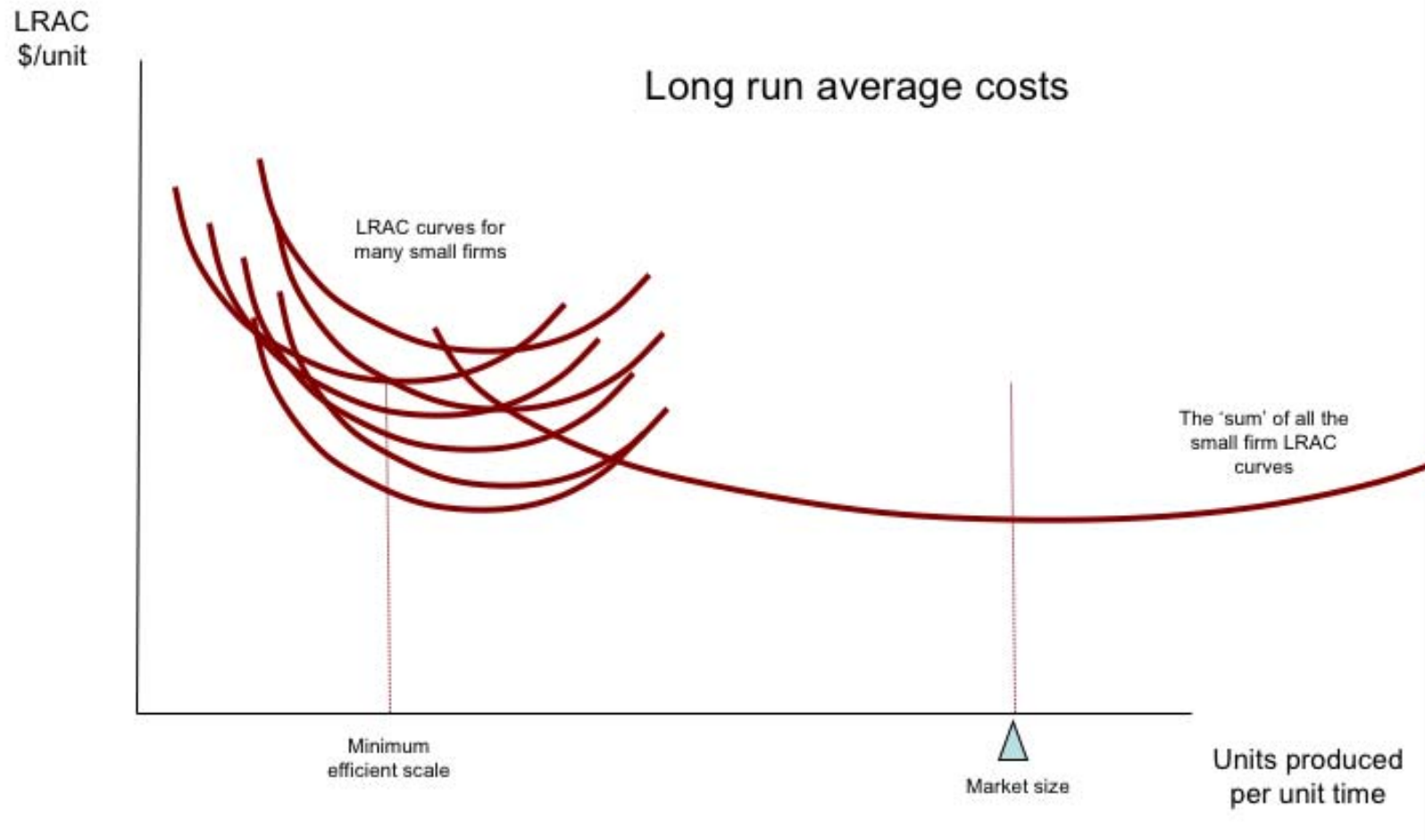


What do monopolists do?

- Restrict supply to rise prices and increase profits.
- A shift in supply
- What is the impact on economic welfare?



3. Introduction to Economic Theory

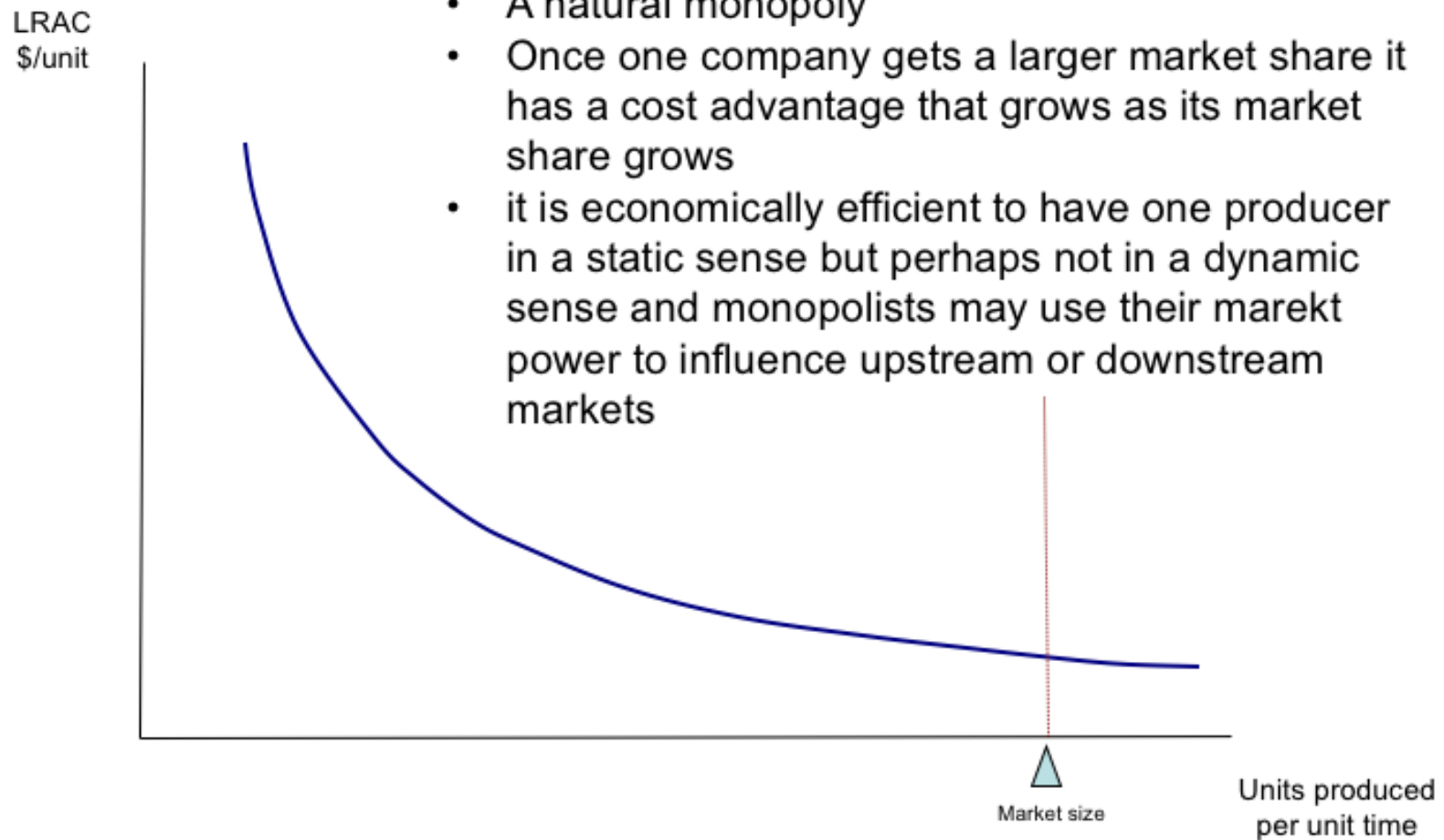




3. Introduction to Economic Theory

Decreasing LRAC and market size:

- There's only 'room' for one producer
- A natural monopoly
- Once one company gets a larger market share it has a cost advantage that grows as its market share grows
- it is economically efficient to have one producer in a static sense but perhaps not in a dynamic sense and monopolists may use their market power to influence upstream or downstream markets

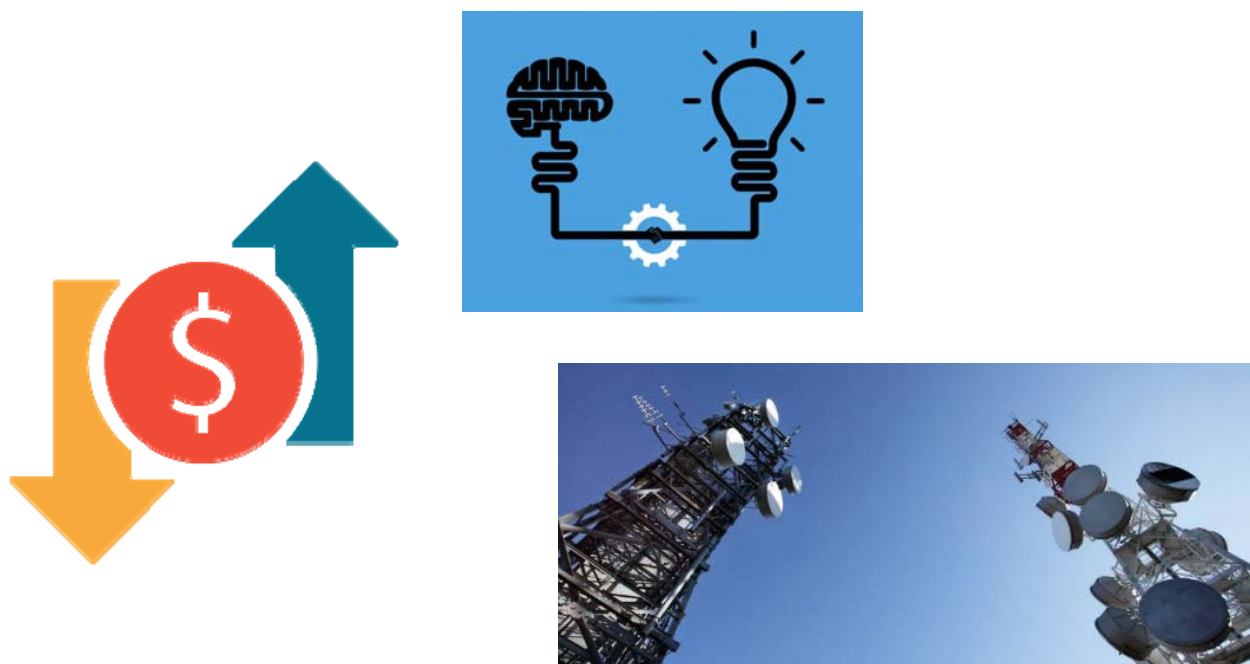




4. What should the NTA be trying to achieve?

The NTA, in the creation and implementation of its regulations, **should be aiming to maximise long run economic welfare.**

A concern with the long run means that not only pricing, but also innovation and investment in infrastructure is of focus.





4. What should the NTA be trying to achieve?



The NTA's regulation should focus on enabling the market to work more effectively, as opposed to correcting market failures.

That is, the NTA should seek to guide service providers towards outcomes (in terms of price, quality etc.) that would have occurred had the market been subject to adequate competitive restraints, in order to protect the interests of end users in the long term.

In this regard, it is important to note that regulation is only a second best solution to effectively functioning competitive markets – it is always preferable to let a competitive market emerge if possible.



4. What should the NTA be trying to achieve?

Notably, although competition is one significant objective - this need to be balanced against long-term goals.

For example:

- If competition is excessive, prices will fall to enable companies to earn a rate of return high enough to encourage investment.
- Companies will be unlikely to undertake risky innovation if returns are low (innovation typically requires significant capital investment).
- However, companies need to achieve economies of scale and scope where these are significant – this is likely to imply a certain level of market concentration.



5. How can the NTA achieve this?



Below are four regulatory approaches, all designed to increase competition and supply.

1. **Industry structure:** ensuring the right number of players, making industry more structurally competitive
2. **Access and access pricing:** enable new entrants to get access to incumbent's infrastructure (infrastructure sharing)
3. **Interconnect agreements:** inter-operability
4. **Promoting flexibility for consumers.**

Further, the NTA should follow the objectives of:

- **Focus;**
- **Adaptability;**
- **Efficient and proportionate regulation; and**
- **Cross-sector networking**

In order to ensure that regulation is in the long term interests of consumers.



5. How can the NTA achieve this?



Focus

The NTA should have clearly defined, articulated and prioritised statutory responsibilities focused on outcomes rather than specified inputs or tools.

In this regard, the NTA should have adequate discretion to choose the tools that best achieve these outcomes.

Adaptability

The framework of Nepal's telecommunications regulation needs capacity to evolve to respond to changing circumstances and continue to be relevant and effective over time.



5. How can the NTA achieve this?



Efficient and proportionate regulation

Regulation imposes costs on regulated companies, with these costs tending to be passed through to end consumers.

In this regard, it is important that such costs are proportionate and outweighed by the benefits achieved for consumers.

- Cost minimisation might, however, *not always* be efficient, as lowering costs can sometimes lead for foregoing bigger benefits to consumers.



5. How can the NTA achieve this?



Efficient and proportionate regulation (cont.)

As an organisation, the NTA should be efficient and well run, maximising the benefit that they can deliver with their available budget.

The NTA's interventions and tools should deliver desired outcomes in the least burdensome way, based on the established best practice for designing regulation.

- This means imposing requirements only where necessary, considering alternatives to regulation and minimising the risks of unintended consequences.

Regulatory decisions also need to be made in a timely manner.

- Delays to key decisions can cause uncertainty and raise the costs to industry or leave consumers unprotected.

Similarly, decisions must be based on robust evidence and judgement.



5. How can the NTA achieve this?



Cross-sector networking

It is important that institutional arrangements recognise interdependencies between sectors, and that the effectiveness of policies is not hindered by consideration of regulation in silos.



6. Conclusions



In conclusion, because of certain characteristics existent in the telecommunications sector, it is necessary for there to be regulatory intervention.

The presence of such market failures in the telecommunications sector gives rise to the rationale for economic regulation.

In this regard, the NTA, in the creation and implementation of its regulations, **should be aiming to maximise long run economic welfare.**

In order to achieve this goal, the NTA should follow the objectives of:

- **Focus;**
- **Adaptability;**
- **Efficient and proportionate regulation; and**
- **Cross-sector networking.**



Thank You