

Box 2

Liberalisation and price developments: the example of the telecommunications sector

The liberalisation of markets is normally associated with increased competition and downward pressures on margins and prices. Increased competitive pressure is generally considered to generate welfare gains in the form of more optimal resource allocation. In addition, increased competition might also result in stronger incentives for rationalisation and renewal, which could benefit productivity.

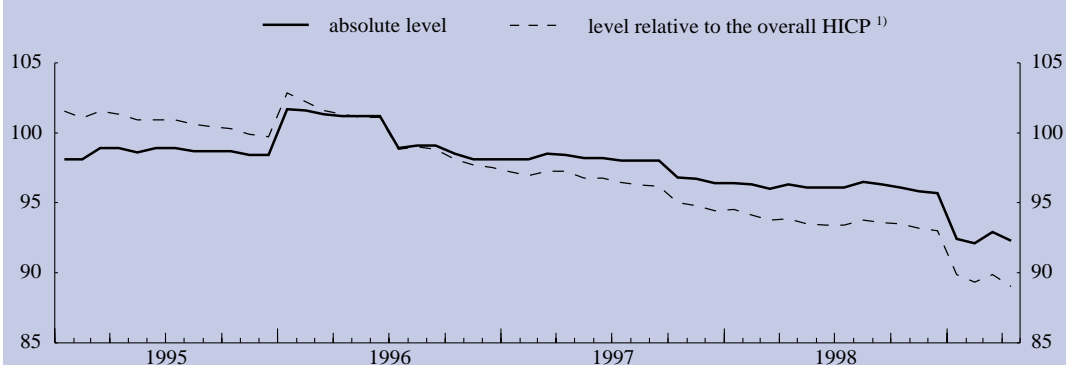
The process of liberalisation of the European telecommunications sector dates back to the 1980s and has largely been driven by a political will to open up markets, e.g. the Single Market Programme, and substantial technological and productivity improvements. Political agreements and legislation within the European Union laid down 1 January 1998 as the date for the introduction of free competition in the provision of voice telephony and telecommunications infrastructure. The harmonisation framework has been aimed at creating a single European market based on common principles for access to networks and services, and a common regulatory environment and harmonised standards for services and technologies. In addition, the obligation on EU Member States to liberalise their markets was reinforced by the discipline imposed under the World Trade Organisation agreement on basic telecommunications, which was finalised in 1997.

The timing of the opening-up of markets has so far varied across Member States. While some countries opened up their markets well ahead of the deadline stipulated by the harmonisation framework, others have had a derogation regarding the implementation date.¹ Furthermore, although the bulk of the Community regulatory package has been transposed, other barriers, such as long delays in granting licences as well as prohibitive licence fees and interconnection charges, have hampered competitive price reductions in some countries.

The experience of those countries which were first to liberalise their markets is that prices have fallen over a number of years following the increase in competition. In the United Kingdom, for example, prices for household telephone services have on average fallen by almost 3% per year since 1992, reflecting both increased competition and advances in technology. Furthermore, the traditionally open and competitive framework in the field of communications in Finland has had sizable positive effects, contributing both to the low price level of telecommunications services (which is among the lowest in the EU) and to the rapid spread of information technology. For the euro area, the liberalisation of the telecommunications sector has been accompanied by a downward trend in both the absolute level of telecommunication prices (telephone and telefax equipment and services) and the level of telecommunication prices relative to the overall HICP. This downward trend, which has been visible since the beginning of 1996, is, however, due not only to increased competition, but also to technological advances. The large fall in January this year is largely explained by the decline in prices for telephone services in Germany.

Price indices of telephone and telefax equipment and services

(index: 1996=100; monthly data)



Sources: Eurostat and ECB calculations.

1) Calculated as the ratio between the HICP sub-index telephone and telefax equipment and services and the overall HICP index.

Overall, the liberalisation of the telecommunications sector has resulted in increased competition which, in turn, has led to a greater supply and lower prices. In most cases increased competition forces firms to trim profit margins and, over time, to become more cost-conscious in order to gain (or avoid losing) their market share.

¹ Only Greece and Portugal still have a derogation, while Ireland opened up its market on 1 January 1999.