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## Telecommunications Mergers: Impacts on US Customers and Markets

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Many people view the current wave of telecommunications mergers in the US as simple industry consolidation. This view is wrong and detracts from the economic and regulatory fundamentals that make mergers necessary and potentially good for consumers.

Here's why:

Everything about telecommunications today is vastly different from when companies were given franchise territories decades ago. Customers once only expected voice service, but now expect a constantly changing mix of communications and information management services. Technologies used to be specialized for voice, but now serve as platforms upon which innovators build new capabilities and applications. Markets were once stable, but are now in constant motion as companies look for new ways to match capabilities and applications to customer expectations.

Even though these economic fundamentals have been shifting for years, the companies have remained stuck in an antiquated structure. When I was a state regulator, I attended public hearings where telephone companies would open the meetings by talking about how they had been town X's telephone company since before the Great Depression. It was sobering to see how much the world had changed while the telephone company had stayed the same. The regulatory system, which had also come from the Depression era, imposed and reinforced a monopoly mindset that created this deceptive stability.

Now with Europe's 1998, the World Trade Organization agreement, and numerous country-specific initiatives such as the US Telecommunications Act of 1996, public policy fundamentals are starting to catch up with economic fundamentals. Consequently, the company structure that may have been exactly right for yesteryear's monopoly voice telephone service is exactly wrong for today's and the future's constantly changing mosaic of services and delivery systems. As a result, companies are changing.

But successfully moving a company from a nearly 100-year-old structure to a business architecture that no one yet understands is no simple task. It involves shedding assets, creating and invading markets, and combining with other businesses. AT&T's divestiture of Lucent Technologies and Cincinnati Bell's spinning off its data and billing services are examples of companies splitting off operations which, while perfectly good businesses, are better off separate from the network company. Sprint's creation of collaborative multimedia products, SBC's entry into New England through the purchase of SNET, and AT&T's alliance with British Telecom are examples of companies creating and invading markets.

The headline-grabbing mergers are simply another way that companies are recombining assets to manage costs, differentiate products, and provide end-to-end service. They can also increase the

intensity of competition by giving companies greater incentives and abilities to enter each other's markets.

Consider the following hypothetical. Suppose that regulators had not allowed SBC to merge outside its five-state region of Texas, Oklahoma, Kansas, Missouri, and Arkansas. The primary key to the company's success would have been to ensure that no competitor invaded its region, and SBC would have focused all of its resources on that cause. Few competitors would have wasted resources trying to invade SBC's markets. The end result would have been little change in the old status quo.

Fortunately, this is not what regulators did. They let SBC merge outside its area. As a result, SBC is developing into a global player with a potential for \$43 billion in annual revenues and 47 million local customers in the US. It is establishing footholds in Bell Atlantic's region, in Europe, and in Latin America, and will probably take steps to solidify footholds wherever SBC's global and national customers need connections.

Of course, Bell Atlantic realizes this and is trying to counter by establishing footholds in SBC's old region. A merger with GTE, which would give Bell Atlantic over \$53 billion in annual revenues and 61 million local customers in the US, would also give Bell Atlantic one such foothold. Companies with strong footholds in Europe also realize this and are looking for ways to bypass SBC's local infrastructure to secure global customers. For example, the Global One companies Sprint, France Telecom, and Deutsche Telekom, with combined annual revenues of \$78.5 billion, 77 million local customers in Europe, and 7.4 million local customers in the US, have local footprints in SBC's, Bell Atlantic's, Ameritech's, and BellSouth's regions.

The mergers trigger a cascading industry dynamic that carries into other markets, pushes other companies, and affects other customers. The result is a global rivalry that drives local infrastructure investments, which can be used to economically serve local customers. This means all customers benefit from greater choice and lower costs.

The obvious questions at this point are, "Don't companies have an incentive not to compete?" and "Isn't a dollar gained from not competing just as good to a company as a dollar gained from lower costs or from innovation?" And the obvious answers are, "Yes," and "Yes." But there are at least two more questions. The next question is, "Is the media industry becoming more or less concentrated?" Based on current research, it appears that the answer is, "Less concentrated, even with large mergers." The other question is, "What can regulators do to increase the incentive to compete relative to the incentive to not compete?" The answer to this question is to favor mergers that get competitive responses from rivals; i.e., mergers that get companies out of their traditional borders and into positions that pose a serious threat to others.

*This paper is one of two papers that I am distributing regarding telecommunications mergers. This paper addresses the domestic dimension. The companion paper addresses the international dimension. Please feel free to contact me with questions or comments or for other sources of information at 352.392.2929 or [mark.jamison@cba.ufl.edu](mailto:mark.jamison@cba.ufl.edu). This paper is based on research conducted in the Communications Competition Research Initiative.*