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Competition Policy Review Panel
Research Paper Summary

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Title: Eliminating Foreign Investment Restrictions in Canada's Telecommunications/Broadcast Sector

Subjects Addressed:

- Foreign investment restrictions in telecommunications
- Evolution of telecommunications and technological developments
- Overview of companies active in the sector
- Capital requirements and cost
- Asymmetric regulations (for new vs. incumbent enterprises)
- Convergence of telecommunications and broadcasting

Evolution of the telecommunications sector:

Telecommunications and broadcasting used to be separate, but now they overlap. All major telecommunications carriers – wireless or fixed-wire – are now actively investing in technologies to deliver video services, and all large cable television companies are now offering traditional voice services and examining options for delivery of data, voice, and video services over new wireless technologies.

Canada has two major fixed-wire telecommunications carriers (TELUS and Bell Canada), and a number of smaller carriers; two major national cable companies (Rogers and Shaw) and two regional cable companies (Cogeco and Quebecor); three national cellular wireless carriers (owned by Rogers, TELUS and Bell Canada); off-the-air television service by a government-owned network and a number of privately-owned stations; and two satellite broadcast services.

Implications of technological developments for investments:

The development of modern digital communications and their embodiment in the Internet has created a revolutionary change. Investments are now driven by the need to offer the full range of voice, data, and video services. The risk involved in such investments has risen substantially because of the inherent uncertainty in predicting which platforms will succeed and what new services will emerge that appeal to consumers. Traditional motion-picture and television production and distribution companies, and new start-ups providing Internet-based services, represent a large pool of capital that is seeking new outlets in a very risky age. Google and Yahoo! have been aggressively investing in acquisitions and joint ventures.

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The case for lifting foreign ownership restrictions in telecommunications:

Canada has one of the most restrictive policies towards foreign ownership of telecommunications carriers among the world's developed (OECD) countries; only 9 of the 30 OECD countries have any foreign ownership restrictions on telecommunications at all.

Traditionally, the case for lifting foreign investment restrictions on telecommunications was based on the projected effects of foreign entry and greater investment on the price of telephone services. Today, Canada has among the lowest rates for fixed telephone service in the OECD and among the highest rates of mobile telephone usage. Canada lags somewhat behind other OECD countries in the number of cellular subscriptions per 100 persons, but this difference is artificially inflated by the fact that many European subscribers have multiple subscriptions (SIM cards) to reduce roaming charges when they move across state borders.

Another traditional argument for lifting the ownership restrictions was that the restrictions limit the access Canadian companies have to capital and/or increase the cost of capital. However, Canadian telecommunications companies have been able to meet their capital needs domestically, and there is little evidence that their cost of capital has been increased due to the ownership restrictions.

The case for lifting the ownership restrictions now rests mostly on the ability to attract innovation and new technology. If innovative foreign firms at the cutting edge of technological change are dissuaded from investing in Canadian communications infrastructure or carriers, Canada runs a risk of falling behind. Canada's major carriers represent only a very small share of the world's communications sector, and very few large high-tech companies are domiciled in Canada. Opening the doors to foreign investment would offer Canadians a greater opportunity to share in the benefits of the rapid technological change occurring in communications.

Caveats to consider if foreign ownership restrictions are liberalized:

Liberalizing the foreign ownership restrictions on an asymmetric basis (i.e. for new and/or small companies only) would create an artificial bias in favor of investments in new carriers at the expense of established carriers, even when the established carriers could more economically deploy a new service or facility.

If the sectoral restrictions are liberalized, investment limitations under the Investment Canada Act (ICA) would also need to be reviewed. In addition, the Competition Bureau would have to account for the new reality in its merger reviews by re-examining the definition of the relevant market and allowing Canadian firms to grow to an internationally competitive size.

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It is not possible to establish separate policies for telecommunications carriers and broadcasters today. Liberalizing restrictions for telecommunications without addressing those in the Broadcasting Act might place telephone companies at a disadvantage. However, the more important reason for addressing the restrictions in both sectors at the same time is that reforms of both would have a much greater impact on the Canadian economy and send much clearer signals to the capital markets.

Conclusions:

The author concludes that foreign investment restrictions in telecommunications should be liberalized and eventually eliminated, not because of any historical difficulty accessing capital at competitive costs but because capital needs, especially for risk capital, are very likely to increase in the near future. In addition, allowing foreign investments in telecommunications will open Canada to new technologies and new ways of organizing the communications sector. If foreign ownership restrictions are liberalized, the ICA provisions related to the cultural sector should also be reviewed. In addition, the Competition Bureau should define the market as a global market in merger reviews to allow Canadian companies to grow to an internationally competitive scale.

The author cautions against liberalizing the foreign ownership restrictions on an asymmetric basis (i.e. for non-incumbents only) since this distorts the market. He also recommends addressing foreign-investment restrictions in both telecommunications and broadcasting at the same time due to the convergence in technologies and ownership.