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Teaching Note

Mexican Telecom Industry: (Un)wanted Monopoly?

Prerequisite Conceptual Understanding

- To understand monopoly and other imperfectly competitive markets – Samuelson Paul A. and Nordhaus William D., "Imperfect Competition and the Monopoly Problem", *Economics*, 15th International Edition (ISBN 0-07-113914-1), McGraw-Hill, Inc., 1995, pages 144–162

Synopsis of the Case Study

Software guru Bill Gates and the Mexican telecommunications baron Carlos Slim Helu, have one thing in common – both of them made their fortunes by the near monopoly control of their markets. The major difference being that US regulated Gate's company Microsoft and created conditions for fair competition, whereas Mexico has done little to dismantle Slim's monopoly. The Mexican telecommunications industry is largely dominated by Slim's fixed-line operator – Telefonos de Mexico or Telmex, and Telcel a unit of wireless giant America Movil. Telmex has 90% market share and Telcel holds 72.5% in mobile telephony. The company is appreciated for developing the country's telecommunications industry single-handedly and expanding the foot-print to nook and corners. However, it is also accused of charging irrationally higher charges and thereby denying a vast majority of Mexicans a telephone connection – either fixed line or wireless. The company was privatised in 1990 and was granted seven competition free years of operations. Even after this time elapsed, the company enjoys same status due to various reasons, most prominent among them are weak regulations and the affinity of the company's management with political power corners. The company is accused of thwarting competition in any form and in effect ensuring its dominance. Mexico has been a paradise for practising unhealthy monopoly practices as the antitrust legislation is very weak, which has resulted in concentration of power and wealth in few hands making Mexico a vastly unequal place and slowing its economic growth.

This teaching note was written by Hepsi Swarna under the direction of Saradhi Kumar Gonela, IBSCDC. It is only an illustrative orchestration of the case study 'Mexican Telecom Industry: (Un)wanted Monopoly?'. It is never meant to limit the learning outcomes.

Pedagogical Objectives:

The case study can be used to analyse and understand

- Market structure of a monopoly and determination of market concentration and monopoly power of a company
- Price determination and social costs of monopoly
- How a weak regulatory authority and absence of enforcement of antitrust laws can help a company to maintain its dominance
- How a dominant firm thwarts competition and the importance of competition for an economy.

Assignment Questions

I Explain the market structure of monopoly and determine the monopoly power of Telmex and Telcel using Herfindahl-Hirschman Index (HHI).

II Explain price and output determination under a monopoly market. What are the social costs of monopoly, explain in context of Telmex and Telcel?

III Analyse the impact of Mexican antitrust laws. Examine why the Mexican regulatory authorities are failing to arrest the monopolistic practices of Telmex and Telcel and in a way helping them to maintain their dominance on the telecommunications market.

IV How are Telmex and Telcel thwarting competiton? How is lack of competition in the Mexican telecommunication industry affecting its economy?

Teaching Plan

The Teaching Note and Structured Assignment of the case study follow a specific Teaching Plan **[Annexure (TN)-I]**.

Case Analysis

I began my class by asking the students to describe Telmex before privatisation and after privatisation. They came up with the following observations:

Telmex before privatisation

1. Waiting period of 3 years for a telephone connection
2. Low efficiency
3. High operating costs
4. Less production
5. Under investment
6. Less penetration
7. No competition
8. Technological backwardness
9. High call rates

10. Corruption
11. Public monopoly

Telmex after privatisation

1. Lower waiting period for a telephone connection
2. Improvement in efficiency
3. Foreign Investment
4. Upgradation of network
5. High prices
6. Less penetration
7. 7 competition free years
8. Vertical integration, no segmentation
9. Corruption
10. Private monopoly
11. Low profit margins for businesses

Then I asked my students to come up with the problems faced by Telmex before privatisation and after privatisation. They came up with the following observations:

Problems of Telmex before privatisation

1. Long waiting period
2. Corruption
3. Inefficiency

Problems of Telmex after privatisation

1. High prices for consumers and competitors (interconnection fee)
2. Entry barriers
3. Weak regulatory body

If we analyse carefully, we notice that most of the issues which Telmex was facing before privatisation remained even after the privatisation. The most significant improvement was improvement in services after privatisation of Telmex. But the fact cannot be denied that a public monopoly was replaced by a private monopoly through privatisation and it did not bring the desired economic benefits.

I Explain the market structure of monopoly and determine the monopoly power of Telmex and Telcel using HHI.

When the production of good or service with no close substitutes is carried out by a single firm with the market power to decide the price of its output then it is described as monopoly. Monopoly is derived from the Latin word *monoplium* – Greek language *monos*, one + *polein*, to sell. Mostly monopolies are considered bad for any economy because they hamper free trade, which lets the market itself to set prices.

Features of Monopoly

1. Single control
2. The commodity produced has no close substitute
3. No freedom to other entrepreneurs to enter and compete with existing seller dominating the market
4. As there is only one firm, the demand curve of the monopoly firm is identical to the market demand curve. A monopoly firm therefore faces a downward-sloping demand curve (AR). The downward-sloping demand curve means that if the monopoly firm wants to sell more, it must lower its price. Since the monopoly firm must lower the price to sell more, the Marginal Revenue (MR) it gets from selling another unit is less than the price it charges. Thus, its MR curve lies below its demand curve.
5. A monopoly firm sets its output at a point where its marginal revenue equals the marginal cost. After fixing the output the company sets a price, which will allow it to sell precisely that amount of output
6. The monopolist may use monopolistic power in any manner, in order to realise maximum revenue.

According to books, monopoly is defined as only one firm producing a good with no close substitutes but in a real world, monopoly can be defined as one firm that provides the majority of sales, with the minority of small firms having little or no impact on the dominant firm. In practice it is difficult to find a firm, which is a total monopoly.

Under the monopoly policy of UK competition policy framework (1998 Competition Act), Office of Fair Trading (OFT) states, "Although it will vary from case to case, as a general rule an undertaking is unlikely to be considered dominant if it has a market share of less than 40%."[1] That means a firm, which has more than 40% market share is considered to be dominant. Article 4 of the European Commission's Interconnection Directive states that "an organisation shall be presumed to have significant market power when it has a share of more than 25% of a particular telecommunications market."[2] In US, court has found 90% market share enough to constitute monopoly but it is doubtful whether 60% or 64% would be enough and certainly not 33%. Under Mexican law, LFCE defines monopoly in terms of a company able to unilaterally set prices or restrict the supply in the market, without the competitive agents able to act or to potentially counteract that power **(page 8, para 2 of the case study)**. In Mexican telecom industry in (1st quarter) 2008, 90% of the local fixed-landline market was dominated by Telmex and 72.5% of the mobile market by Telcel. Telmex and Telcel sales amount to the majority of sales in Mexico, thus making them monopoly in the telecom industry. HHI can be used to decide if a company wields monopoly power over the respective market.

HHI can be used to determine the concentration and monopoly power of Telmex and Telcel. HHI is calculated by squaring the market share of each firm competing in a market and then summing the resulting numbers. The sum, or the HHI number, can range from close to zero to 10,000. The closer HHI to 10,000, the more monopolistic is the corresponding market (and the lower is competition). The US Department of Justice considers a market with a result of less than 1,000 to be a competitive marketplace; a result of 1,000–1,800 to be a moderately concentrated marketplace; and a result of 1,800 or greater to be a highly concentrated marketplace. The HHI is expressed as: $HHI = s1^2 + s2^2 + s3^2 + ... + sn^2$ (where sn stands for the market shares of the n number of firms). The greater the value of the HHI index, the greater is the degree of monopoly power. Greater concentration also indicates less competition in the market. "The closer a market is to being a monopoly, the higher the market's concentration (and the lower its competition)".[3]

1 "Competition Policy", http://www.edexcel.org.uk/VirtualContent/70280.pdf
2 "Market Power and Dominance", http://cbdd.wsu.edu/kewlcontent/cdoutput/tr503/page11.htm
3 Investopedia, http://www.investopedia.com/terms/h/hhi.asp

Concentration of Mexican Fixed-line Industry

When measured using the HHI, the market concentration of Mexican fixed-line sector comes to 8,125.

As we know, that Telmex holds 90% of market and there is no concrete data available over the share of other players, let us assume that the remaining 10% market share is equally divided among Axtel, Alestra Maxcom and Megacable Holdings. Thus, their market share holdings come to 2.5%, 2.5%, 2.5% and 2.5% respectively.

HHI= $90^2+2.5^2+2.5^2+2.5^2$

8,100+6.25+6.25+6.25+6.25=8,125

Any market with a result of more than 1,800 is considered to be highly concentrated market place. And as the industry's HHI value is 8,125 it is obvious that the market is highly concentrated. Thus, Telmex is a monopoly facing very little competition.

Calculations for Mobile Market

When measured using the HHI the market concentration of Mexican mobile sector comes to 5,647.54.

The major mobile players of Mexican telecom industry – Telcel, Movistar, Lusacell and Nextel has 72.5%, 18.7%, 5.6% and 3.2% market share respectively, **(page 7, para 3 of the case study)**.

HHI=$72.5^2+18.7^2+5.6^2+3.2^2$

5256.25+349.69+31.36+10.24=5647.54

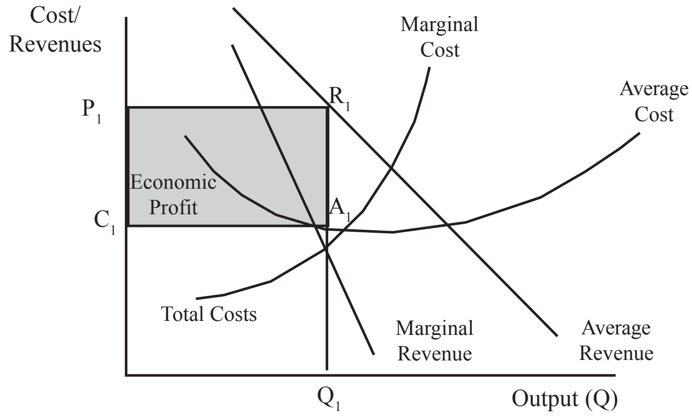
This value indicates that Mexican mobile Industry is highly concentrated.

Telmex is regulated through the price cap in five areas namely installation; monthly rental fee; local measured services, national or domestic long distance and international long distance, **(page 9, para 3 of the case study)**. Leased lines are not regulated by Cofetel, providing liberty for Telmex to set the tariffs for leased lines. As leased lines are exclusive between two certain locations and therefore are convenient for business requirements, they are mostly rented by businesses to connect various offices. This provides Telmex an opportunity to levy high tariffs, making Mexico one of the countries with highest tariffs, especially for business use. **Exhibit I of the case study** shows Mexico having one of the highest tariffs for business use; its tariffs are much higher than the OECD average. Even the tariffs for residential use are also very high compared to OECD and other countries.

Even though Telmex prices are regulated by Cofetel, the former repeatedly delayed signing interconnection agreement with competitors. Telmex, because of its dominant position does not respect the interconnection fees fixed by Cofetel, and it continues to charge high tariffs per minute **(page 12, para 1 of the case study)**. Competitors complain that Telcel too charges high interconnection fees. Both Telmex and Telcel wield too much power in their respective markets and the regulatory authorities haven't been able to counteract that power. For the competitors, they do not have any option but to obey the companies and hope that someday the authorities would live up to expectations and strip the two telecom monopolies of their monopoly powers – both theoretically and practically.

The price and output determination under monopoly **[Exhibit (TN)-I]** is achieved when MR=MC and MC is cutting MR from below. The cost structure may be so that there can be loss, no profit - no loss or profit. Here the profit is to the tune of $P_1R_1A_1C_1$.

Exhibit (TN)-I
Price and Output Determination under Monopoly



Prepared by the author

II Explain price and output determination under a monopoly market. What are the social costs of monopoly, explain in context of Telmex and Telcel?

Price and Output Determination under Monopoly

As discussed earlier a monopoly firm decides its output at which its marginal revenue would equal its marginal cost and then sets whatever price would enable it to sell exactly that quantity. As there is only one firm, the demand curve of the monopoly firm is identical to the market demand curve. A monopolist faces a downward sloping AR curve with a MR curve with twice the gradient of AR. The firm is the price maker and has some power to set the price of output.

A monopolist always produces half of perfect competitors output.

Perfect competitors output is derived as follows:

P=a-bq

P=MR=MC=AC

a-bq = c + dq

q= a-c/b+d

Monopolist's output is derived as follows:

MR=MC

TR= Pq=aq-bq²

MR= a-2bq

TC= Ac*q=cq+d²

MC= C+2dq

a-2bq=c+2dq

q=1/2[a-c/b+d]

Thus it is proved that monopolist produces half of perfect competitors output. Out of Mexico's population of 109 million for the first quarter of 2008, Telcel had 51.4 million subscribers. Telcel is reaching around half of Mexico's population. Telmex's reach is even more less. It indicates that majority of population do not have access to telephone, as the monopolist produces less and charges more for his output.

In the diagram **[Exhibit (TN)-I]**, the firm maximises profit where MR=MC. The output level under monopoly is fixed at Q1 where MR=MC, then the firm sells the profit-maximising output Q1 at the price P1. The firm does not fix higher prices always as demand may fall with increase in price.

This hold's true for the Mexican telecommunications market. Owing to high wire-line and wireless tariffs, the teledensity and the mobile density remains low in Mexico. In **Exhibits II (a) and II (b) of the case study**, it is clearly understood, that in 2006 out of every 100 people only around 18 had telephones and 54 had mobile phones, which is less compared to other countries. Only 3 people out of 100 were broadband subscribers **(Exihibit III of the case study)** much below the OECD average of 16.9%. Due to high mobile tariffs people use mobile phones only for emergencies or just for receiving calls. The high calling charges of Mexico has resulted in abnormally low usage rates[4]. In diagram **[Exhibit (TN)-I]**, the monopoly firm is making supernormal profits (or economic profits), shown by the shaded area. The area beneath AC1 represents the total cost of producing output Q1.

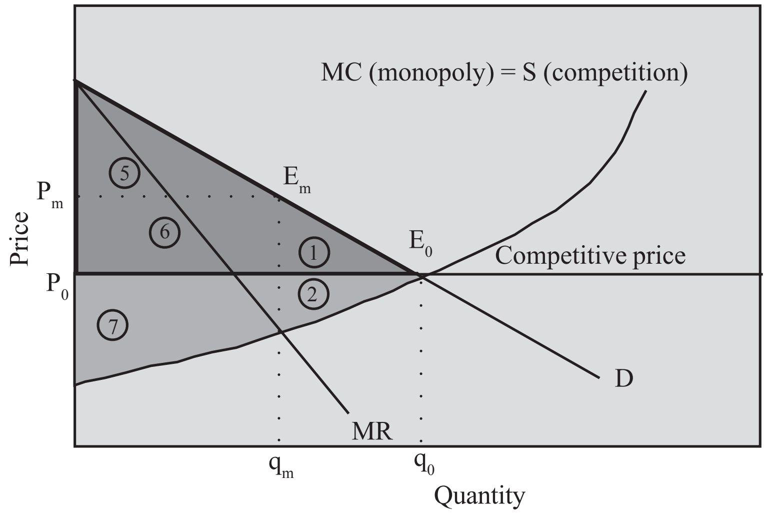
Telmex and Telcel have been earning considerable amount of profits by charging customer's high telephone tariffs and competitor's high interconnection fees. According to OECD reports, Mexico has very high telephone tariffs. Apart from high tariffs, Telmex and Telcel are also known for charging high interconnection fees. Generally, in the telecom industry an incumbent monopolist has an advantage over the competitors, as the competitors will have to buy services from the monopolist in order to offer their own services. For example, for a competitor to reach its customers, it should be able to interconnect with the already established monopolist's telecommunication company, by paying a fee for using monopolist's infrastructure. Since Telmex controls all of the local telephone lines in Mexico, every new competitor who wishes to compete in wireless services or international long distance has to pay a fee to Telmex in order to originate or terminate a call. In 2000, Avantel's 60% of the revenue directly went to Telmex in the form of interconnectivity fees **(page 8, para 1 of the case study)**.

The social costs of a monopoly can be explained with a diagrammatic representation of deadweight loss **[Exhibit (TN)-II]**, in the context of Telmex and Telcel.

Owing to high charges, the usage rate is very less in Mexico, thus resulting in deadweight loss. There are also other social costs resulting from monopoly. Firstly, a monopoly firm does not have incentive to keep its costs low. Secondly, monopoly firms squander lot of resources and money lobbying and engaging in legal battles to avoid getting regulated and also advertising in an attempt to retain its monopoly. Telmex and Telcel have spent considerable amount of money on filing case after case in courts against the rulings of antitrust agencies to avoid regulation. In late 1990s, when competition entered in Mexican long-distance market, Telmex fought back with patriotic marketing and advertising **(page 10, para 1 of the case study)**, thus spent a lot of money on advertising. Thirdly, a monopoly firm always tries its best to discourage entry of new players in its market, Telmex and Telcel are alleged to have always discouraged competitors by

[4] Minutes of use per subscriber per month.

Exhibit (TN)-II
Socials Costs of Monopoly



Monopoly is inefficient because it does not maximise the sum of consumers' and producers' surpluses. At the perfectly competitive equilibrium E_c consumers surplus is the sum of the 1, 5 and 6. When the firm is monopolised, price rises to p_m and consumers' surplus falls to area 5. Consumers lose area 1 because that output is not produced; they lose area 6 because the price rise has transferred it to the monopolist. Producers' surplus in perfectly competitive equilibrium is the sum of the areas 7 and 2. When the market is monopolised and price rises to p_m the surplus area 2 is lost because the output is not produced. However, the monopolist gains area 6 from consumers. Area 6 is known to be greater than 2 because p_m maximises profits. Thus, areas 1 and 2 are lost to society. They represent the deadweight loss resulting from monopoly and account for its allocative inefficiency.

Source: Keen Steve, et al., "A 75th Anniversary Present for Sraffa", http://www.debunking-economics.com/Maths/Present_for_Sraffa.htm

various means. According to some economists these social costs of monopoly are larger than those measurable by deadweight loss. In 2004, when US won the WTO telecommunications case against Mexico, "it was estimated that Mexico's artificially high interconnection charges resulted in excess payments by US companies and consumers well over $1 billion since 2000" **(page 11, para 2 of the case study)**.

Telmex has remained a monopoly for past 18 years and Telcel has been enjoying dominance for past 8 years in the mobile market. Indeed the most important question, remains, how a government could allow a company to be dominant for so long?

III Analyse the impact of Mexican antitrust laws. Examine why the Mexican regulatory authorities are failing to arrest monopolistic practices of Telmex and Telcel and in a way helping them to maintain their dominance on the telecommunications market.

In 1993, to ban anti-competitive behaviour, Mexico adopted Federal Law of Economic Competition (LFCE). Federal Competition Commission (CFC) was created to enforce LFCE. The competition policy goals of LFCE read: "To protect the competitive process and free market access by preventing monopolies, monopolistic practices, and other restraints of the efficient functioning of markets for goods and services." **(page 8, para 3 of the case study)**. CFC is responsible for investigating abusive practices of monopoly companies; it also determines the companies, which have dominant position in any sector.

Under LFCE, monopolistic practices are classified as absolute or relative monopolistic practices. Absolute monopolistic practices prohibited by LFCE include four types of horizontal agreements between competitors – price fixing, output restriction, market division and bid rigging. Horizontal agreement is an agreement between competing firms in the same industry, which may result in reduced competition – like agreements between competitors that fix price, allocate markets or restrict the quantities of goods or services to be produced or bought. Relative monopolistic practices are not termed illegal unless a company is found to have substantial power in the respective market. Vertical agreements like – vertical market division, resale price maintenance, tied sales, exclusive dealing and refusal to deal are considered to be relative monopolistic practices. Vertical agreement is an agreement between two or more companies operating at different levels of production, distribution or supply chain. These arrangements can, potentially violate antitrust laws. An example of a potentially illegal vertical agreement would be when a retail store has an agreement to buy from one manufacturer and is restricted to buy from other manufacturers. Mexico prohibits refusal to deal, as it potentially threatens competition. Other horizontal practices are also termed as relative practices – collectively treated under catch-all provision – that will unduly damage or impair the process of competition and free access to production, processing, distribution and marketing of goods and services **(page 8, para 4 of the case study)**.

In competition laws around the world there are two types of monopolistic behaviours, which are prohibited under abuse of dominance provisions. They are exploitative conduct and exclusionary conduct. A dominant firm when it uses its monopoly power to exploit the customers or the suppliers, it is known as exploitative conduct. Charging monopoly prices to customers and paying low prices to suppliers are examples of exploitative conduct. A conduct, which aims at excluding competition to maintain market power, is termed as exclusionary conduct. Refusal to deal, filing lawsuits in order to suppress competitors and increasing rival costs are some of the examples of exclusionary abuse. Mexican competition law does not prosecute exploitative practices like charging monopolistic prices but encourages actions against exclusionary abuses.

Exploitative prices are not prosecuted as monopoly profits are the driving force behind innovation and further it is assumed that exploitation of market power by charging customers high prices is self-correcting, as markets are flexible and new entrants will enter the market. Moreover, this type of prosecution is considered impractical because calculating whether price is excessive or not, involves complicated comparisons of prices with costs of production and amount invested. Since the Mexican competition law does not have any provision to fight abusive prices; this constitutes a major flaw in the law. There should be a provision under the law against abusive prices. According to OECD Mexico have some of the highest telephone tariffs. If there was a provision to prosecute high abusive prices in the Mexican law, the customers of Mexico would not have been burdened under such high prices and it would have had better usage rates. "Unlawful conduct is defined solely in terms of exclusionary practices at the expense of competitors or other firms in the chain of distribution, and not in terms of exploitative practices at the expense of consumers." **(page 9, para 1 of the case study)**. There is no provision for fair competition under the law; neither does it talk about protecting the interest of small enterprises and restricting business concentration. Even though both Mexican constitution and LFCE ban monopoly, no section of law deals with monopoly as such or with abuse of dominance.

Regulatory authorities of Mexican telecom industry have been unable to curb the monopolistic practices of Telmex and Telcel. Until 1995, the national telephone industry was regulated by SCT (Secretariat of Communications and Transport, Mexico). In 1996, a Presidential decree created Cofetel (Federal Telecommunications Commission) as an autonomous entity from SCT to regulate and develop the Mexican Telecom Industry. Cofetel is responsible for implementing regulations and technical standards and even for resolving the conflicts between competitors regarding interconnection fees. It has operational and technical autonomy but lacks political autonomy. Cofetel limits to suggesting on major issues to SCT. And SCT– the final deciding authority – retains the power to grant all concessions. Once a decision is made, Cofetel implements it. This set up was established to introduce competition and to regulate telecommunications sector. Cofetel has been termed as a weak regulatory authority. The liberal use of *amparos* by Telmex and Telcel has helped them to challenge against the rulings of Cofetel and CFC. An action for *amparo* can be filed whenever a fundamental human right provided under the Mexican Federal Constitution is allegedly infringed by any government agency. Parties can attack the government agency decisions by filing an *amparo*. A citizen can ask a judge to delay the implementation of a government decision, which he thinks is unconstitutional; often this delay is not less than couple of years. Any company can misuse *amparo* – if the regulatory authority finds a company guilty of anti-competitive practice, then the company can file an *amparo* against the ruling by saying it is unconstitutional, and thus protecting itself from getting regulated for years together. Thus *amparo* could be used by any company to escape regulation and that is what Slim's companies have been doing. Telmex and Telcel have taken advantage of this weakness of the Mexican law to a large extent by filing *amparos* after *amparos.*

In 1997, CFC found Telmex dominant in five telephony markets namely local telephony service; national long-distance service; international long-distance service; access or interconnection to local networks and interurban transport. In 1998, Telmex filed an *amparo* against the ruling and the case to declare Telmex dominant is still pending in the Mexican courts for 10 years. Till now Slim has filed 60 *amparos* to thwart the decisions of CFC and Cofetel.

The regulatory authority of Mexico even after knowing that Slim's companies are abusing their dominant position is tolerant towards his monopolistic practices. The reason being, Mexico is a country which is known for its corruption, around 62% of the companies have admitted to the fact that they keep a part of their revenues to bribe government officials to get favours done by them. Denise Dresser aptly says "Mexico has a dense, intricate web of connections and personal ties between the government and the business class, this ends up creating a government that doesn't defend the public interest, that isn't willing to go out and regulate in the name of the consumer, it is rather willing to help its friends, its allies and, in some cases, its business partners thrive at the expense of the Mexican people." **(page 12, para 1 of the case study)**. Slim's power and influence in the Mexican economy further protects him.

The Carlos Salinas, Ernesto Zedillo and Vicente Fox administrations were not able to arrest the monopolistic practices of Telmex and Telcel to a great extent. It is a known fact that all the above mentioned three Presidents were close to Slim. There are rumours that President Carlos Salinas who sold Telmex to Slim, secretly benefitted from the sale. In 2000, President Vincent Fox appointed Pedro Cerisola a former employee of Telmex as SCT. During his tenure that is till 2006, he was alleged for protecting Telmex's interests. Mexican government has often been accused for protecting the interests of wealthy businessmen and keeping the welfare of general public last in the priority list. Slim due to his influence and political connections with an added advantage of a weak regulatory authority like Cofetel is able to defend his companies against the accusations of monopolistic practices. The recent Telecom investigations initiated by CFC is looking into dominance and monopoly practices of Telmex in broadband internet and there are other eight probes also against Telmex and Telcel, six of which are investigating Telmex dominance related issues, out of the rest two, one is looking into the interconnection fees of Telcel and another is to determine whether Telcel wields substantial power in Mexican mobile market. The results of these investigations will be a huge test for Felipe Calderón's government and CFC – whether they are serious enough to regulate Slim's companies or not. Slim has just done what any other business magnate would do, the real blame lies with the Mexican government, which has allowed Telmex and Telcel to remain dominant for so long. Mexico needs a more focused and specific set of rules and regulations, without the legal loopholes that Slim's companies have been using plus a strong Cofetel.

IV How are Telmex and Telcel thwarting competition? How is lack of competition in the Mexican telecommunication industry affecting the economy?

Slim has always maintained that he likes competition but there have been absolutely no signs suggesting that his companies have welcomed competition or competitors in any ways possible. In 1997, Avantel and

Alestra entered the long-distance market but soon they discovered they faced very stiff competition from Telmex, which just would not let anyone snatch its market share, even if it had to indulge in monopolistic practices to maintain its market share. Cofetel was too weak to regulate Telmex. All the competitors complain of the high interconnection fees, which Telmex and Telcel charge them, these high interconnection fees has a crippling effect on their services, most of the companies that entered the Mexican telecom market in late 1990s, went bankrupt at least once.

The case provides an excellent example of how Telmex and Telcel have been denying other companies the very right for existence. In 1998, Avantel intended to introduce long-distance calls from public phones using prepaid cards. As majority of the public phones were operated by Telmex, Avantel was denied a free number and it faced a setback. When Avantel took Telmex court for monopolistic practices, Telmex kept them at bay, by getting a judge to issue an arrest warrant against the top lawyer of Avantel. The case did not proceed further. Finally in 2001, Avantel defaulted on its debt.

Similarly, in 2000, Telmex was found guilty of refusal to deal. A customer who called a toll free number (an 800 number) operated by other long-distant operator using Telmex payphone, had to buy Telmex prepaid cards. But the toll free numbers operated by Telmex were free. Competitors were losing on business, as they were unable to market their toll free numbers to businesses because businesses were not in favour of customers paying for a toll free number. Telmex refused to deal with the competitors regarding this issue. Because of this, a case was filed against Telmex and it was ordered to enter into an agreement with its competitors. As a result, Telmex provided a free toll free number to competitors who had an agreement with it.

Both Telmex and Telcel have been accused again and again for charging high interconnection fees. In 2002, US requested WTO to look into the matter of high interconnection fees, which Telmex charged US carriers. In 2004, US won the WTO telecommunications case against Mexico, in particular against Telmex. It was estimated that Mexico's artificially high interconnection charges resulted in excess payments by US companies and consumers well over $1 billion since 2000. It has been hard to compete even in the Mexican mobile market. In 2004 Movistar, the second largest mobile operator in Mexico, to increase market share, started selling mobile handsets at a cheaper price. But many of its sold phones were never used. Movistar discovered that Telcel purchased its handsets, replaced the chip and resold them. Movistar filed a case against Telcel. In 2006, CFC announced Telcel guilty of monopolistic practices as it refused to allow SMS exchange with Nextel. In November 2007 Movistar, filed many complaints against Telcel and Telmex with CFC. It appealed to CFC to compel both Telmex and Telcel to connect competitors to their network on fair terms. OECD referring to Telcel in its report ('Economic survey of Mexico 2007: Improving infrastructure in Mexico') declares, "In the mobile telephone market, in particular, the dominant firm is using its market power to squeeze out other players." **(page 11, para 3 of the case study)**.

The ongoing investigations are a ray of hope for the competitors that both the companies will be regulated to such an extent that they stop abusing their dominant position by connecting competitors to their network on fair terms.

Lack of competition in telecom industry is adversely affecting the Mexican economy. Mexico happens to be a country, which is known for its obsession with monopolies and duopolies. The widespread monopolies and duopolies in a country like Mexico, where 40% are poor, have resulted in concentration of wealth in few hands and unequal distribution of income and wealth. Industries – like telecom, cement, television, beer, tortillas and energy are dominated by monopolies or by very few dominant players, which are holding the country back. It is a sad tale when it comes to competition in Mexico, especially in telecom industry, where there is very little competition. In a bid to sell Telmex, government increased telephone tariffs. In 1990, it eliminated indirect taxes on telephone services and allowed Telmex to absorb the remaining taxes into the prices. As a result the local call rates increased from 16 pesos/minute to 115 pesos/minute. According to the World Bank report on the Telmex sale, the consumers were biggest losers from the privatisation deal; they were worse off by 92 trillion pesos **(page 13, para 1 of the case study)**. The report predicted that in the long run consumers will benefit from low prices. But that has not happened; Mexican consumers still pay very high telephone tariffs, especially for business use. Business firms need to lower their costs in order to compete in global markets, so if these high telephone tariffs are reduced, business firms of Mexico will become more competitive. Eduardo Garcia, a business journalist in Mexico, observes, “If not for those rates, Mexican businesses would have generated better profits and could have paid their workers better. Mexico would have been a more efficient economy.” **(page 3, para 1 of the case study)**. Economists say high costs of telephone and internet services that resulted from lack of competition are hindering economy’s growth. The high telephone charges for business use are driving away factories to countries like China. The consumers feel they are pouring lot of money into Slims companies by paying the excessive telephone bills. The usage rate is very low in Mexico, creating deadweight loss. Noll opines, “There is enormous loss of efficiency arising from the dominance of Telmex, especially with respect to the underutilisation of the network (low minutes of use) and the low penetration of the internet.” **(page 13, para 2 of the case study)**.

For affordable prices and better infrastructure, competition should thrive in an economy like Mexico. According to some studies the major improvements in telecommunications have emerged as a result of competition, as competition – leads to innovation. Consumers benefit from competition as it leads to lowering of prices and they can choose from great range of products as well. So, in an industry like telecommunications – on which major sectors of an economy like banking and insurance, healthcare, education, transportation and information technology heavily depend upon – competition should thrive.

Final Thoughts

> “Indeed, I think in most of the conversations I had with members of the private sector, entrepreneurs, women leaders and state Governors, and with intellectuals, they almost uniformly expressed the importance of improving Mexico’s competitiveness and increasing Mexico’s growth rate.”[5]

– Paul Wolfowitz, World Bank President, Monterrey, Mexico, April 26th 2006

It is high time that Mexican government start taking stern action against the monopolies and duopolies. Competition is the key to Mexico’s growth. Slim has just done what any other business magnate would do. Noll comments, “Telmex is regulated by Cofetel, which bears some responsibility of its prices.”[6] Hence the real blame lies with the Mexican government and the regulatory authorities. Cofetel needs to be empowered with more authority and freedom to act. CFC should be provided with ample resources and the cooperation between the government, Cofetel and CFC should be strengthened to work with a common goal of making Mexico globally competitive. *Amparo* rights should be reviewed, so that its misuse is minimised and courts with economic expertise should evolve. Analysts recommend that politically connected and protected businessmen who hamper innovation and competition, should be severely dealt with. Series of regulations should be imposed on Telmex and Telcel to such an extent that they stop abusing their dominant position, thus minimising the deadweight loss created by their monopoly pricing.

Additonal Readings

- To understand antitrust laws, “Competition law and Policy in Mexico”, http://www.oecd.org/dataoecd/57/9/31430869.pdf
- To understand Privatisation of a national company (Telmex) – Mariscal Judith, “Telecommunication Reform in Mexico: and Institutional Perspective”, http://www.telecomcide.org/documentos/008DTDAP-JMariscal-Telecommunication_Reform_Institucional-03.pdf, 2003.

5 “Press Conference with Paul Wolfowitz in Monterrey,Mexico, http://web.worldbank.org/WBSITE/EXTERNAL/COUNTRIES/LACEXT/MEXICOEXTN/0,,contentMDK:20903722~menuPK:50003484~pagePK:2865066~piPK:2865079~theSitePK:338397,00.html, April 26th 2006

6 Excerpt from an exclusive interview of Prof. Roger Noll conducted by the author. Please refer Annexure I of the case study for the full interview .

Annexure (TN)-I
Teaching Plan

Prerequisite Conceptual Understanding

- To understand monopoly and other imperfectly competitive markets – Samuelson Paul A. and Nordhaus William D., "Imperfect Competition and the Monopoly Problem", *Economics*, 15th International Edition (ISBN 0-07-113914-1), McGraw-Hill, Inc., 1995, pages 144–162

Big Picture
A monopoly is always scorned at, in economics. A monopolist, after all, is supposed to make supernormal profits at the cost of consumers. The consumers' cost is high price and there are other social costs. However, what happens if a monopoly is born out of competition – A competitive monopoly?

Teaching Plan Flow

Sl. No.	Analysis Section	Expected Learning Objectives	Forward Linkage	Ideal Duration (mins)
1.	Market Structure of Monopoly	• Market structure of monopoly and features of monopoly • Methods of measuring monopoly power, finding the concentration of Telmex and Telcel (using HHI).	Price Determination Under Monopoly	30
2.	Price Determination Under Monopoly	• Price and output determination • Deadweight loss • Supernormal profits.	Antitrust Policies of Mexico	30
3.	Antitrust Policies of Mexico	• LFCE & CFC • Absolute and relative monopolistic practices • Exploitative conduct and exclusionary conduct • *Amparo* • SCT and Cofetel • Corruption an aid to monopolistic practices in Mexico • Cofetel – a weak regulator	Competition	30
4.	Competition	• Telmex and Telcel playing fair or thwarting competition? • How is lack of competition in telecom industry affecting Mexican economy?		30

Prepared by the author