



Policymaking in the Wireless Telephone Industry:

Let's Avoid the Rorschach Approach

John W. Mayo

August 2009

GEORGETOWN UNIVERSITY **McDonough**
SCHOOL *of* BUSINESS

37th & O Streets, NW □ Suite 558 □ Washington, DC 20057
PHONE: 202.687.3686 □ EMAIL: cbpp@msb.edu □ WEB: <http://cbpp.georgetown.edu/>

Policymaking in the Wireless Telephone industry:

Let's Avoid the Rorschach Approach*

The Rorschach test is a well known tool for psychological evaluation. In the standard Rorschach test a subject is asked what he or she sees in an ambiguous ink blot on a piece of paper. Unconstrained by context, the subject is free to interpret the ink blot as a giraffe, a tree, an airplane, the boogie man, or anything else. In recent weeks, some policymakers have, in Rorschach fashion, taken to seeing “market failures”, “price increases” and “barriers to competition” in the wireless telecommunications industry. Concerns include a nominal price increase on the *de minimus* portion of text messages that are not purchased with a bundled pricing plan and the exclusivity of certain handsets by wireless carriers. From these fragments of information, policymakers see the boogie man of competitive failure in the wireless industry. Unlike a Rorschach test, however, evaluation of the state of competition in the wireless industry is not, or should not be, an unconstrained exercise in which policymakers are free to imagine failures of competition from ink blots. Rather, an evaluation of the performance of this, or any, industry must be disciplined by both economic analysis and the empirical facts.

The application of an economic lens and the empirical facts drawn from the wireless industry project quite a different picture than the one some policymakers envision. In particular, the economic touchstone for competition is an analysis of pricing, output and innovation. In this regard, unlike policymakers’ interpretation of sinister behavior by wireless competitors, the economic picture of the industry is quite encouraging.

Consumers in the wireless industry have driven firms to offer flat-price bundles of services with blocks of usage over which consumers’ usage does not affect their total expenditures. Firms, in turn, must compete by offering consumers bundles that include more and more attractive handsets, with evermore features, and lower prices. The results have been dramatic. Consumers paid 55 cents per minute for wireless voice services in the mid 1990s. Today, the price in the U.S. has fallen to an average 6 cents per minute. By comparison, the prices the UK, Italy, Spain, Japan and Germany are all over 20 cents per minute. Similarly, the average price paid for text messages has fallen dramatically over time from 3 cents per text in 2006 to 1 cent per text today.

The decline in prices has surely contributed to the dramatic expansion of usage in the United States. Only 15 years ago, there were less than 20 million wireless subscribers. Today, there are over 270 million subscribers. Both voice and text usage have increased dramatically, with a typical wireless subscriber in the U.S. making and receiving over 700 minutes of calls every month. European counterparts, faced with higher prices, only typically consume between 100 and 300 minutes per month. Text messaging too has been a dramatic consumer success story in the United States, with usage growing from 81 billion texts sent in 2005 to over 1 trillion in 2008.

While price declines and rapid expansion of usage are strong indicators of a vigorously competitive wireless sector, the rapid innovation in the industry provides yet another indicator of the competitive health of the industry. Wireless firms have rapidly introduced sleeker, more powerful, more attractive handsets to lure customers to their service. And with over 20 million subscribers voluntarily disconnecting from their wireless service to subscribe to a different carrier in 2008, the competitive struggle between carriers to offer increasingly attractive handsets and prices will almost certainly continue.

Within the ink blot that is the wireless industry, it is possible to *imagine* a scenario of a competitive breakdown. When viewed through the discipline of an economic lens, however, the data we see point toward a significant consumer success story to this point.

*John W. Mayo is Professor of Economics, Business and Public Policy in Georgetown University's McDonough School of Business.