Comments

Miguel Urquiola: The main goal of this paper is to estimate the welfare effects of the Peruvian telecommunications privatization. The authors also use their findings to provide an explanation for why privatization is not popular in Peru (as in much of Latin America), despite the fact that it seems to have had a number of salutary effects. The paper improves on the previous literature insofar as the data it relies on offer advantages relative to those typically analyzed. The use of these data, unfortunately, is simultaneously a significant weakness, in that information collected during a single year is used to make inferences on a lengthy period that witnessed many changes in the sector, which introduces several potential biases. This comment closes with some thoughts on what we can learn from such results regarding the low approval rates accorded to privatization.

This issue of how privatization affects the level and distribution of welfare has been analyzed before for Latin America, notably in a series of papers summarized by McKenzie and Mookherjee in an earlier issue of this journal.[1] Such work generally relies on household survey data, which have a key limitation because they typically describe only households' expenditure on broad aggregates like telecommunication services. From these, it is sometimes impossible to identify the specific quantities of services consumed at specific prices. This is particularly problematic in the case of telecommunications, which involves a complex basket of available services (such as fixed-line local calls, national and international long-distance calls, and cellular telephony). Estimations thus have to rely on a series of assumptions and approximations.

In contrast, Torero, Schroth, and Pasco-Font use a survey specifically geared to telephone services, one that also entailed the transcription of billing information. The survey has a substantial sample size and follows a panel of households over a period with price variation, so that changes in quantities and prices are accurately observed. In this regard, this paper

1. McKenzie and Mookherjee (2003).

offers a solid starting point for its estimations. Collecting such data is never easy, and the authors should be commended for doing it.

Unfortunately, the use of this information also introduces a number of potential biases, which arise because the data were collected over a period of only ten months, mostly in 1997. One illustration of the type of problems this may cause is the correction for access to fixed-line phone services in the demand estimations, which is a key aspect of the estimation implemented. The postprivatization expansion of fixed-line connections in Peru essentially took place between 1994 and 1996. This means that the characteristics of households that did not have access in 1997 (at the time the survey was taken) are probably quite different from those that did not enjoy it in 1993 or 1994, and this can affect the validity of the correction substantially.

A related point concerns the introduction of cellular telephones. Given their relative lack of importance in 1997, the survey used did not collect information on cellular services. Cell phone coverage has expanded dramatically since then, however. This is very important because as the authors themselves explain, the main source of variation in welfare changes across socioeconomic groups originates in the relative importance of fixed costs. A driving force behind the increase in cellular coverage, however, is precisely the reduction in the fixed costs of access (certainly relative to fixed-line services), and it is likely that new subscribers have experienced large welfare gains from this service. This simply cannot be elicited using the 1997 data. The very low penetration rate that existed then may explain, for instance, why the authors find cell phones are complements to rather than substitutes for fixed-line services. This might be the case for high-income households, but it would be surprising among low-income customers that gained access more recently—and these are precisely the individuals that, in some sense, are the ultimate focus of this study.

The bottom line is that information from one year is being used to make inferences on six rather different years. This is a key source of concern over and above any other methodological issues one may worry about (like the use of weighted price averages), which would also arise with other types of information.

A more general point concerns whether we can attribute all these effects to privatization itself. Cellular expansion is a major part of the story of what happened to telephone services in Peru in the 1990s. Calling this a privatization effect implies that no such expansion would have occurred under the state-owned CPT-ENTEL, which seems a rather extreme assumption. A general obstacle in this type of analysis is the lack of clarity on what the appropriate counterfactual should be.

A final comment arises because the authors use their welfare findings to make inferences on why privatization is not popular in Peru, as elsewhere in Latin America. This discussion, while certainly interesting, seems to be too narrowly focused. To truly gauge the public's reaction to these reforms, at least two issues must be considered. First, other economic aspects, like the effect of privatization on workers, must be taken into account. As the debates over free trade illustrate, a few severely affected groups can do much to undermine support for policies that are welfare enhancing for the population at large. Second, understanding the public's perception of privatization is probably not possible relying solely on data on welfare effects. Rather, people's evaluation of specific reforms is probably related to broader factors like their assessment of the government(s) that implemented the reforms, their opinion of the government(s) that initiated the entire liberalization process, and their perception of their country's current economic condition. For instance, presidents can get credit or blame for booms or recessions that economists say they had little to do with. Similarly, in Latin America, neoliberal policies (many of which made privatization a flagship reform) are blamed for a regionwide recession that began in the late 1990s.

In short, the leverage one can get out of pure economic welfare calculations in this area seems rather limited. Nonetheless, the calculations and discussion presented in this interesting paper certainly are a useful contribution to evaluating the social consequences of privatization in Latin America.

Rolf J. Lüders: The topic of the paper by Torero, Schroth, and Pasco-Font—namely, the welfare impact of telecommunications privatizations in Peru on all consumers as well as by income groups—is clearly an important one. Most economists today would agree that the agency problem is more acute for firms in the public sector than in the private sector, and that governments should therefore leave the management of firms in the hands of the latter. Privatizations do not enjoy widespread popular support, however, either in Latin America in general or in Peru in particular. In the Peruvian case, Torero, Schroth, and Pasco-Font explain the apparent contradiction of significant aggregate net welfare benefits combined with low approval rates as the result of the differential welfare impact of telecommunications privatizations on the rich, which are relatively few and received most of the benefits, and the poor, which are many and benefited little if at all.

The authors' approach is interesting. The use of available survey information to estimate the differential welfare impact of telecommunications privatizations on different income groups is, as far as I know, novel and leads to an interesting analysis. Specifically, Torero, Schroth, and Pasco-Font use an available 1997 survey to estimate yearly consumer surplus changes—both total and by different income levels—following the Peruvian telecommunications privatizations. Demand functions are derived from a relatively standard consumer behavior model. The evolution of the estimates of the consumer surplus changes induced by telecommunications privatizations, by socioeconomic level, are then compared with the evolution of the approval rates of all privatizations in Peru. The conclusion, without any formal proof, is that the latter evolution is closely related to the consumer surplus changes of the lower income groups. Finally, a policy proposal is made.

The paper is not sufficiently explicit about the methodology used to obtain the consumer surplus estimates for different years based on a one-year survey. In particular, there is not a sufficient discussion about the implicit assumptions and their implications for the results of the study. It is not clear how quantitative restrictions affect the consumer surplus estimates, nor what the impact of changes in the quality of the telecommunications services might have been.

A major problem of the paper is that it offers no evidence that the effects of the telecommunications privatizations determined the approval rates of *all* Peruvian privatizations. In fact, there is not even a very close relationship between consumer surplus estimate changes of the two lower income groups, which constitute the "losers" in the process of telecommunications privatizations, and said approval rate changes. The link to approval rates certainly makes the paper more interesting, but given that this link is not proven, insisting on it detracts from the value of the very interesting consumer surplus estimates.

The policy proposal is in need of further analysis. Privatization was accompanied by a big shift in the tariff structure, in which the fixed charge was raised and the user rate lowered. Since lower income families use the telephone relatively little and the rich much more, this tariff structure shift increased the price of each call for the poor (which according to the authors explains the low approval rate) and reduced the price for the rich. The authors propose, therefore, to partially reverse the tariff structure change, so as to increase the consumer surplus for the poor and lower it for the rich. If—and this is a big if—the present tariffs are optimal, this will reduce the total efficiency gains of the telecommunications privatizations. The authors do not even ask by how much. Furthermore, the paper does not explore whether there are any other, more efficient ways to compensate the poor. If, for example, present tariffs are higher than optimum because the government wants to ensure a normal rate of return on assets that were bought at an excessively high price, then lowering present tariffs for everybody, compensated by a direct transfer from government to the telecommunications companies, might make a lot of sense. It would increase efficiency and also consumer surplus for all groups, including the poor.

In summary, Torero, Schroth, and Pasco-Font present a paper on an interesting subject, in which they use a novel approach to estimating welfare impacts of privatizations for different income groups. The paper would have gained significantly if the methodology had been made more explicit, perhaps in an appendix. The paper loses rigor when it tries to infer, without any proof, approval rates for *all* privatizations from consumer welfare changes of *telecommunications* privatizations. The policy proposal made in the paper is, in all likelihood, oversimplified and alternatives are not discussed.

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