Australian government caught in a bind over Telstra privatisation

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The Howard government's plan to privatise the remaining 51 percent of Telstra, Australia's major telecommunications carrier, ran into further problems last week with the release of a report from an inquiry examining the state of services in regional and rural areas.

Howard commissioned the inquiry in April, following an uproar in country electorates when Telstra announced plans to axe another 10,000 jobs—over 30 percent of them in rural and regional areas. The rural discontent sparked divisions in the ruling coalition, with National Party MPs threatening to vote against the full privatisation of Telstra unless rural telecommunications services were shown to be adequate.

The government had anticipated that the three-man inquiry panel, headed by Tim Besley, would return a favorable report, allowing National Party dissidents to change their stance while retaining some credibility with their rural constituencies.

However, the panel was unable to cover up the glaring deficiencies in rural communication services. It found that "a significant proportion of those who live and work in rural and remote areas have concerns regarding key aspects of services, which at this stage, are not adequate."

The report expressed "concerns" over every aspect of communications vital for private and business needs, including "the repair and reliability of basic telephone services, the level of mobile phone coverage and the adequacy of Internet services."

The release of the report has forced the government to again delay the full sale of Telstra until early next year, when it promises to unveil "a plan of action" to address the report's 17 recommendations. National Party Senate leader Ron Boswell immediately questioned this timetable, saying last week that "it would be difficult to get the sale through even before the next federal election," which is due by the end of next year.

In the last federal and Queensland state elections, the Nationals lost ground in rural areas to the extreme right-wing One Nation party, which exploited concerns over government cutbacks to rural services and the impact of a full Telstra privatisation. Boswell is clearly worried that the party would suffer further losses if it went to the next election in the midst of a debate over Telstra.

By delaying Telstra's sale, however, the Howard government faces further criticism from big business and financial markets for continually allowing electoral concerns to override the agenda of economic restructuring demanded by investors. The failure to fully privatise Telstra has been seized upon already as one of a number of indications that Australia is not part of the technologically-based "new economy" but is still an "old economy" reliant upon traditional resources and industries.

These sentiments have been reflected in the precipitous decline of the Australian dollar. Since the beginning of the year the value of the dollar has continued to hit new all-time lows and is now trading around 51 cents to the US dollar. Even a strong intervention in September by the Reserve Bank of Australia could not reverse the trend.

Investment in Australia is also falling. Statistics released by the United Nations Conference on Trade and Development showed that inward investment in Australia fell by 14 percent in 1999 to $5.4 billion, the lowest for four years, and lower than the annual average for the 10 years to 1995.

The sharp decline in the dollar and foreign investment is largely attributable to the flood of investment into the US and Wall Street which has led to the depreciation of the euro and other currencies. But markets are also critical of the Australian government's failure to encourage new technologies and industries, especially in the field of telecommunications and information technology.

As a result there is considerable pressure on the Howard government to press ahead with the Telstra privatisation as the present position—half-government, half-private ownership—prevents the corporation from raising the necessary capital for new initiatives, including global expansion, by issuing shares.

The company has been unable to engage in share exchange deals to forge alliances with other telecommunications firms and has to fund any plans by raising expensive loans. It is increasingly being left behind in a relentless global competition and also domestically, where it is losing income from traditional revenue areas such as STD and local phone call provisions to its rivals.

Telstra has recently suffered a string of failed business ventures, including a move to acquire a slice of the Internet search engine LookSmart, the fruitless purchase of a stake in the company Computershare and the collapse of its attempt to merge its own Solution 6 with Sausage Software.

Last week, the corporation only just managed to salvage a vital deal to buy into Pacific Century Cyber Works (PCCW} and Hong Kong Telecom's mobile-phone business, owned by Hong Kong millionaire businessman Richard Li.

When the US$3.5 billion agreement with PCCW was first negotiated in April, it was heralded by Telstra as a “defining moment of global importance”. But the moment was short lived. Almost immediately Telstra faced huge potential losses after PCCW shares plummeted, along with other technology stocks, on the US-based Nasdaq Index. Under a renegotiated deal, Telstra will now pay US$2.8 billion for a 60 percent controlling interest in Hong Kong Telecom and for the original share in PCCW.

The alliance with PCCW was designed to position Telstra to expand into the potentially vast communications market opening up on mainland China when that country enters the World Trade Organisation next year and allows 25 percent foreign ownership of its mobile-phone operators. Telstra will be up against some of the world's largest corporations, including Hutchison Whanpoa, NTT DoCoMo and Vodaphone and is already looking to forge a partnership with a major US carrier, possibly AT&T.

But as an editorial in the *Australian* newspaper pointed out: “Telstra's experience with PCCW has highlighted the limits of its ownership structure. While Telstra remains majority owned by the Federal government, the scope for negotiation with joint venture partners will be restricted.”

Market impatience over the privatisation issue has resulted in a plunge in Telstra's share values and the degrading of its credit rating. The price of the carrier's T2 shares, released in October 1999 in the second stage of its privatisation, plummeted to $6.77 at the beginning of September, well below the $7.20 issue price, and has hovered around that figure ever since.

At the end of September, Standard and Poor's downgraded Telstra's credit-worthiness by two notches from an AA rating to A+. The downgrade went ahead despite major changes to Telstra's management involving the appointment of three new “less politically sensitive” directors with experience in “turning around profit losing companies”.

The Howard government is caught in a bind. It has to press ahead with the full privatisation of Telstra in order to stem the erosion of market confidence not only in the corporation but in the Australian economy as a whole. At the same time, however, its moves in that direction threaten to further alienate rural voters and exacerbate tensions between the coalition parties.