Policy Brief
Competition in China's telecommunication sector

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Despite several rounds of reforms conducted during the last 15 years the Chinese government is embarking once again on a vast restructuting of the telecommunication sector. The previous reforms saw the creation of a new entrant (China Unicom), the separation along segment (China Mobile for mobile services and China Telecom for fixed services) and the division along geography (China Telecom in the South of China and China Netcom in the North). This time, the restructuring aims at creating 3 operators who will be allowed to compete against each other in all market segments and all regions.

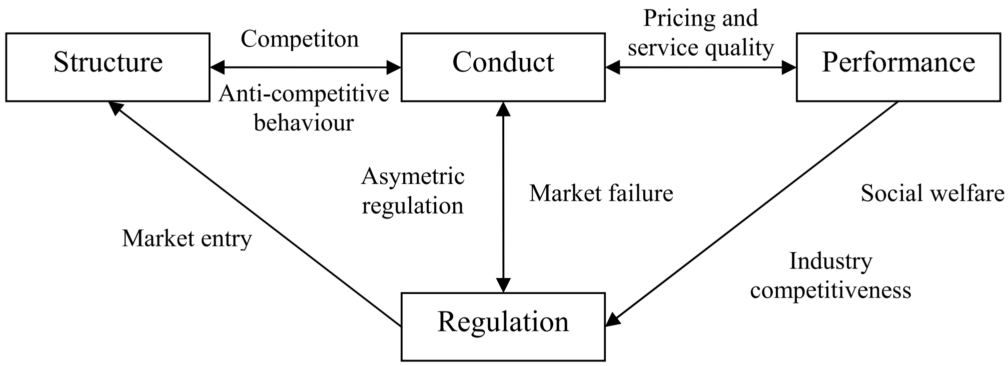
There is no doubt that the government is taking restructuring seriously. The discussions around network roaming, subscriber market share limit, asymmetrical pricing, co-location on existing and new networks, interconnection rates, one-way mobile number portability (MNP) or the adjustment of spectrum allocation bear witness that many alternatives have been studied. But these measures are in no way a guarantee for increased competition. For instance, MNP saw increased competition in countries such as Hong Kong and Korea but relatively little change in Australia and Taiwan. Re-balancing of interconnection terms amongst the operators may well re-equilibrate the finances of new entrants but they have relatively little impact on market share. Similarly, MIIT's announcement of an "active pursuit of network sharing amongst China's operators" will improve capital expenditure efficiency in the areas of tower construction and conduit-laying but hardly lead to a better distribution of market shares.

Instead, they highlight once again the government's heavy-handed intervention in the overall management of the telecommunication sector. This tendency can also be found in the technological solutions imposed on the mobile operators for 3G (i.e. TD-SCDMA, CDMA2000 and WCDMA). In fact whereas current policy aims in many countries include making spectrum licenses more flexible and transferable, the Chinese governments severely restricted use of licensed spectrum.

A number of other hurdles may render the creation of fair competition an elusive objective. First, as long as China's operators remain publicly-owned it will remain difficult to balance consumer welfare with total welfare as the government faces conflictual goals. Whereas incremental competition may rise, as long as all Chinese operators remain majority-owned by the SASAC, cut-throat competition will be ruled out. Second, the telecommunication sector still lacks pro-competition policies despite the country's WTO commitments and the passing of an anti-monopoly law. The widely held belief that market forces are important and that they should determine the development of the industry is countered by the government's active shaping of market structure, tariff adjustments and rationing of licences. At times, the government gives the impression that it doesn't feel comfortable with introducing more competition, seeking instead more and better control. Third, asymetric regulation are a valuable too to correct market failure in the telecommunication sector. However, their effectiveness rests on the regulator's capacity to enfore them. Unfortunately the re-branding of MII into a Ministry of Industry and Information Technology (MIIT) is not accompanied with heightened enforcement capabilities or the creation of a strong regulatory framework. While most telecommunication regulators have been moving from *ex post* to *ex ante* regulatory regimes, China still relies on a "delayed" *ex post* approach.

At the end of the day, the real question is how to tackle the market power of the (dominant) incumbent operator. Although competition will change post-restructuring, China Mobile has already reached a creditable scale with over 360 million mobile subscribers. Experience in other countries suggests that dominant players' market shares and margins are generally more resilient to rising competition than those of less established players within the market.

The creation of a level-playing field market depends on the alignment of numerous (and sometimes contradictory) policies. There is no magic formula to achieve fair competition since broader social objectives also need to be taken into accout.



Creating a level playing field in the telecommunication sector is by no means an easy task. While many governments have tried to reduce the incumbent's market power by sector-specific regulation or/and by general competition rules fair competition often remains a distant obective. The history of the Chinese government's "failed" attempts to introduce significant competition in the telecommunication market should not undermine its resolve to reform the sector. But it should make sure that the reforms undertaken have a chance to succeed and, for this to happen, more weight should be put on the creation of an institutional framework conducive to competition.