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Regulatory Reform in China's Telecommunication Sector: A Case of Policy Transfer Failure or of Policy Divergence?

Dr Marc Laperrouza, Senior Research Associate
Swiss Federal Institute of Technology (EPFL)

Content

- Introduction
- Theoretical framework
- Case study: introduction of competition
- Key findings and conclusion
- Policy implications

Research question(s)

Is the regulatory reform in China's telecommunication sector a case of **policy transfer failure** or of **policy divergence**?

- How has China gone about liberalizing its telecommunication sector?
- Is there a “Chinese” telecommunication liberalization model? If so, how does the model differ from those across other sectors or across the world?
- What caused the transfer failure or the policy divergence?



Improve understanding of:

Telecommunication policy-making in China
Policy convergence phenomenon and its limits

Why does it matter?

- 15 years of telecommunication reforms
- Increased integration of China in international economy, via trade and politics
- Emergence/fostering of national champions with international strategies
- Emergence of Chinese IP and standards
- Largest telecommunication market in the world

China's market-oriented reforms, 1993-2008

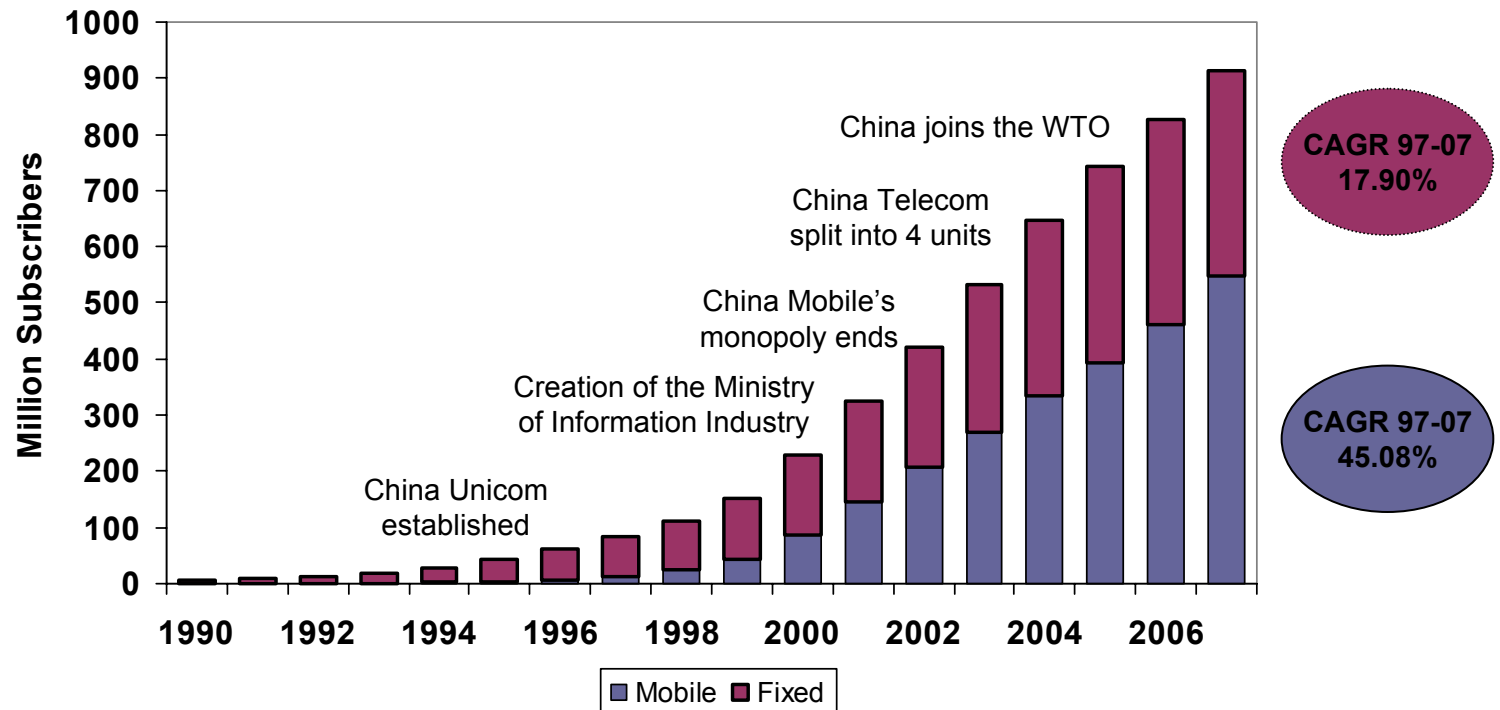
- **Deregulation**
 - Separation of PTO from Ministry
 - Creation of MII, acting as Ministry and regulator (but weak level of autonomy)
- **Competition**
 - Partial competition in fixed telephony (China Telecom and China Netcom)
 - Partial competition in mobile telephony (China Mobile and China Unicom)
- **Privatization**
 - Minority share privatization via Hong Kong
 - Limited opening to foreign/domestic investors



Growth took place in spite of failure to implement “orthodox” liberalization model

China's mobile vs. fixed Lines: Leapfrogging and managed competition

In 2008, still around 5 million new mobile subscribers per month



Source: ITU (2008), compiled by author

Priorities of the Chinese government in telecommunications sector

- **Very much inward looking...**
 - Build out infrastructure
 - Preserve state assets and generate revenues
 - Foster domestic competition to « keep barbarians at the gate »

- **But at the same time...**
 - More overall transparency in policy-making and regulation
 - Arbitrage by the State Council between numerous State agencies (SASAC, MII, SARFT)
 - Rise of consumer advocacy

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Historical Institutionalism

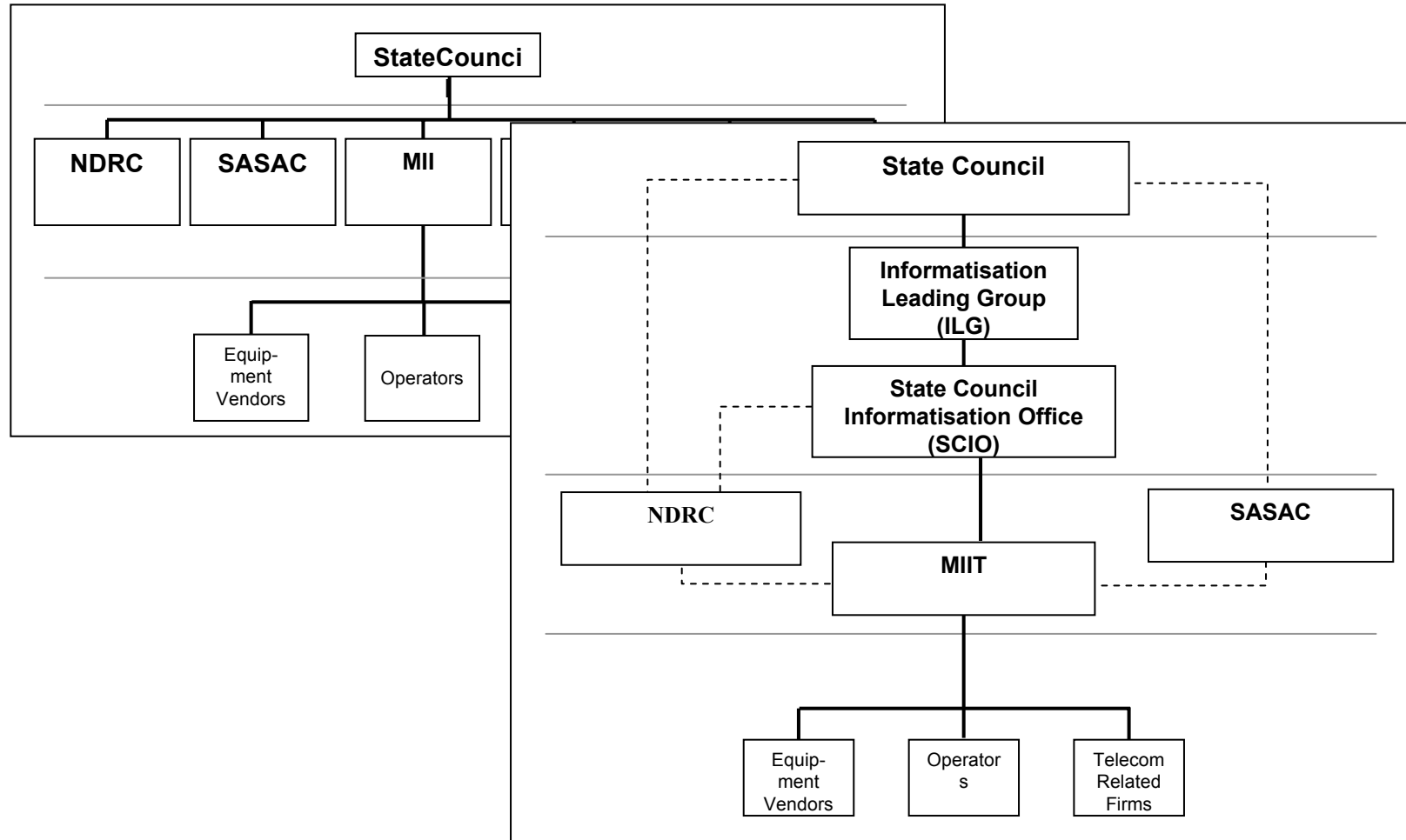
Test the axiom on China's telecommunication policy-making

- Used by a number of scholars in the field of telecommunication reform (Thatcher, Bartle)
- Components: primacy of institutions (and role in shaping values), path-dependency, uniqueness in space/time, structure vs. agency
- Cons: more descriptive than explanatory, overemphasis on institutions vs. ideas, difficulty to explain initial choices, actors circumvent institutions, used for comparison between nations
- Pros: explains well policy continuity.... less well policy change




To understand reforms, institutional factors need to be taken into account

Lines of influence in policy-making: the theory and the reality



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Case study: Introduction of competition

- Failure to introduce « significant » competition despite several rounds of reform → HHI:
 - Strategy of monopoly breaking politicized industry (bureaucratic rather than market competition)
 - State control over market structure (SASAC)
 - conflicting goals (revenue for State, consumer welfare)
 - Weak regulatory framework (no Law, no independent regulator)
 - Lack of *direct international pressure* (via FDI) and despite WTO accession (*red line not to be crossed*)
- Competition more a product of domestic political power games than of market economics

Herfindahl-Hirschman Index (HHI)

Table 3: HHI for Chinese mobile operators, 1994-2008e

	Market Share (%)														
	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008e
Operators															
China Mobile	100	94.50	92.70	92.45	93.70	87.95	77.84	71.70	67.00	65.70	64.80	66	67	69	71.9
China Unicom	0	5.50	7.30	7.55	6.30	12.15	22.16	28.30	33.00	34.30	35.20	34	33	31	20.8
China Telecom	0	0	0	0	0	0	0	0	0	0	0	0	0	0	7.3
HHI	10000	8961	8647	8604	8819	7883	6550	5942	5578	5493	5440	5512	5578	5722	5602

Source: Deutsche Bank (2003), various analysts reports (2008)

Not a fully competitive market but positive results

- Dramatic improvement in the rate of **network deployment** with arrival of additional operator (China Unicom) in mid 90s
- Prices in fixed and mobile services **dropped** significantly
- Quality and breadth of services improved
- Adoption of **more advanced** technologies (e.g. VoIP) but also sometimes of **less advanced** technologies (e.g. xiaolingtong)

Comparison with electricity sector

- Shared characteristics:
 - Restructuring and separation of government regulatory functions
 - State retained majority ownership
 - Central pricing
 - Ministry of Electric Power dominated the sector as owner, regulator and policy-maker (abolished now)
- Differences:
 - Decentralized generation system at the periphery, owned by government organizations at different levels and by **private enterprises**
 - Little concerns about **sovereignty and national security**

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Key findings I

- Comparison with electricity sector shows that **timing, pace and nature of reforms varies significantly**:
 - Much better defined regulatory framework (Law in 1995)
 - Foreign investment has been allowed in the electricity industry
 - Role of private investors complementary to that of public enterprise
 - Appropriate restructuring of bureaucracies and « frictionless » implementation



Restructuring telecommunication sector prior to the WTO accession has gone in the **exact opposite direction**

Key findings II

- Regulatory process can explain disappointing structural reforms → requires transparency, accountable institutions and a set of accountability mechanisms
- Domestic constraints played significant role on scope of reforms → institutional factors (Ministerial rivalry, weak regulatory framework)
 - Lack of law attests of Ministry's failure to be a credible regulator + lack of consensus → no finite boundaries around policy-making
 - Lack of institutional constraints proved a stumbling block for in-depth reforms
- International pressures had limited impact on extent of liberalization → compliance with Reference Paper (technological neutrality) to be seen

End of coordinated competition and rise of Regulatory State?

- Agencies are learning to *regulate* the market but
 - Competition is engineered
 - State-ownership remains cause of conflict
 - Missing independent and convergent regulator
 - Heavy-handed interventionism based on strong industrial policy imperatives

P.S.: Overview of China's telecommunication regulatory situation (2008)

- **2008 restructuring** → aims at creating 3 operators who will be allowed to compete against each other in **all market segments**:
 - Regulator → Ministry of Industry and Information Technology (MIIT) re-born
 - Legal framework → a piece of legislation and administrative rules but **no Telecommunication Law**
 - Regulatory responsibilities → except for price regulation, all other regulatory functions carried out by **MIIT**
 - Licensing regime → « **unclear** » and split between MIIT and NDRC, e.g. 3G
 - Ownership → grouped under SASAC and partially privatized
 - New entrants → still no private or foreign operator in the pipeline

Plus ça change, moins ça change

Conclusion

- Transition to a competitive market has proved much harder than what was initially hoped for → not uncommon in telecom world...
- Telecommunication liberalization conforms only partially to other models (origin and outcome) → driven first and foremost domestically
- **Failure** attributed to institutional features specific to the sector:
 - Absence of telecommunication law
 - Rivaling factions → bureaucratic in-fighting
 - Compete for preferential policies and not for market share
- **Divergence** attributed to:
 - Strong notion of sovereignty and national security
 - Little impact of external pressures (WTO or World Bank)

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Policy implications

- It is difficult to **engineer competition** in the telecommunication sector
- **Public ownership** makes it difficult for the government to balance consumer welfare with total welfare
- WTO commitments or the passing of an anti-monopoly law are no guarantee of **pro-competition policies**
- Asymmetric regulations (any regulation for that matter) are valuable tools to correct market failure but effectiveness rests on the regulator's **enforcement** capacity



More weight should be put on the creation of an institutional framework conducive to competition but that takes time and resources!

« Modest » policy implications

- **For China:** go beyond the competition rhetoric → if you believe in competition, open the market to private (foreign AND domestic) operators
- **For the rest of the world:** don't try to mimic the Chinese telecommunication liberalization model – it didn't work there (not yet...), it won't work elsewhere BUT learn from the case study:
 - Institutions matter
 - Good institutions matter even more
 - Technology and the market matter too but not as much as institutions

Appendix

China's changing telecommunication environment

1	1978	Creation of the telecommunication monopoly
	1984	Leading Group for Revitalisation of the Electronics Industry takes responsibility for planning telecommunications sector growth
	1985	7 th Five-Year Plan propels telecommunications as a national priority
	1987	First cellular mobile telephone system introduced in China
	1993	Registration of China Unicom , organised by then MEI, first competitor of China Telecom
2	1996	Launch of GSM network
	1998	China's 9 th NPC approves an ambitious reform of the information and telecommunications industry and merges all the information and telecommunications related regulatory institutions into one single regulator, the Ministry of Information Industry (MII)
3	1999-11	Sino-US agreement to open the telecommunication market to international competition (WTO Reference Paper and commitments)
	2000-09	PRC Telecom Regulations
	2001-11	China joins the WTO
	2002	Restructuring of China Telecom and China Netcom; Launch of CDMA and GPRS
	2003	PAS allowed in major cities and first WLAN hot spots; Launch of CDMA2000 1X
4	2009....	Telecommunication Law and 3G Mobile licenses

Regulatory policy-making

The study of regulatory policy-making is dominated by two perspectives:

- Regulatory agencies are vested with vast discretion and are the major force in regulatory policy (Wilson, Katzman)
- Regulatory agencies are dominated by their environment – Interest groups, legislative committees, economic forces and technological change are among the determinants of policy (Stigler, Lowi, Sabatier)