

THE RECENT PRC TELCO REFORM AND ITS IMPLICATIONS TO THE PRC TELCO MARKET

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PRC's telecommunications industry has been through a number of major reforms in the past two decades, which included two main regulatory restructurings and three significant market reshuffles. As a result, the PRC Telco industry has developed by an astonishingly fast speed. In May this year, the PRC State Council initiated a biggest ever Telco reform in both regulatory framework and the market place. This reform has created a super power Telco regulator and three giant SOEs market players. Against this background, this paper discusses the recent reform in detail in line with the various reforms in the past and argues that - although the current reform is likely to bring in some positive impacts on both regulatory framework and market operation, these impacts would be limited. To achieve an aimed competitive market in Telco industry, PRC needs to continue its reforms a step further by creating a better regulatory independence and introducing private forces into its current SOEs dominated market place.

I INTRODUCTION

China, with its enormous population and arguably the biggest telecom market, has emerged to be the most admired nation among those new economies in recent years. By virtue of this fact, China has successfully developed its telecommunication infrastructure from one of the least developed into one of the largest and most sophisticated networks in the world. Within two decades, China had established its telecommunications network adopting advanced technologies. There are a wide range of services provided and extensive coverage.¹

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¹ L Wen, *The Glory of the Telecom in China's Recent 100 Years* (2004).

Along with rapid modernisation, the industry has received a lot of attention from international observers². There have been many studies in respect to the driving forces of this momentum development managed by the PRC government³: the finding was nothing like the regulatory theories by the Western developed economies such as complete deregulation, and competition. The real driving forces behind the industry growth have been mainly 'political'⁴. In addition, the PRC's legal and regulatory environment in the telecommunications sector has been weak and, in fact, far under regulated, which is putting negative contributions to the sustainability of this industry growth in the future⁵.

In May this year, the PRC State Council initiated a major Telco reform in both regulatory framework and the market place. This reform established a new industry regulator – the Ministry of Industry and Information Technology (MIIT), which replaced the previous industry regulator Ministry of Information Industry (MII). This reform also reshuffled the market place by merging previous six major market players into three and formed a ground to issue 3G licences in the near future. This paper discusses this reform in details and argues the following:

One, as to the regulatory restructuring, this regulatory reform is likely to bring some positive changes to the current PRC Telco regulation. It is however a good starting point only. More in-depth reforms should be considered in the future or even immediately at the completion of the current reform. More specifically, the newly established MIIT should consider setting up an independent telecommunications regulatory agency and the issue of converging broadcasting and telecommunications will need to be addressed promptly; and,

Two, as to the market reshuffle, there would be a couple of beneficial results. Firstly, this reform re-arranged the market into three major players (was six previously) and all these three are all-service providers. Therefore, the competition among them would be more comprehensive. Secondly, this 'six to three' arrangement created a sound ground for issuing 3G licence in the near future. However, these three players would still be SOEs and thus, the competition would still be limited. In addition, two of these three players are running different networks in mobile services, which is likely to contribute some negative factors to the future growth of either of these networks. Moreover, with the uncertainty of the

future 3G standard, all of these three players would be reluctant to further develop and upgrade their network and infrastructure in a timely manner.

II THE TRANSFORMATION OF THE PRC TELCO MARKET

A Fast Industry Development

Generally speaking, the industry growth during the period of 1949⁶ to 1978 was minimal⁷. The significance of telecommunications as a key strategic industry was not realised by the government at that junction in time⁸. This situation was changed by Deng Xiaoping's "open-door policy" in late 1970s⁹. In turn, the policy brought some tremendous changes to the country, as the results, the overall economy in China had developed at a high speed and living standards had improved considerably.

New strategies and policies were also formulated for the country's telecommunications industry along with a background of massive economic reforms. At that time, telecommunications was viewed as part of the resources, and the principal idea was to mobilize all resources to boost the development of the post and telecommunications industry¹⁰. A central regulator, Ministry of Post and Telecommunications (MPT), was consequently established by the PRC State Council responsible for overall planning in the industry and the international development. The industry legal framework during this period was very simple with the State Council on the top and MPT as a single Ministry deal with all the issues in its jurisdiction¹¹.

With the development of the overall economy, the crucial status of telecommunications as a foundation industry emerged gradually. In the mid to late 1980s, the Chinese government came to realise that the underdeveloped telecommunications infrastructure was an obstacle to overall economic growth. Thus, special consideration was consequently granted to the telecommunications sector, which then led to an effective sector growth in the following years.

Take a close look, an accelerated expansion period in China's telecom industry started from the 1990s with the average per annum expansion rate approximately 3.8% since then. The telecom industry has been particularly robust and well ahead

² Ibid.

³ For example: J Ure, 'Telecommunication in China - More than was Bargained For?' (1997) 2 *New Technology Quarterly* 34., L Press et al, 'The Internet in India and China' (2003) 1 *Information Technologies and International Development*. and G Li, 'Moving towards the Unsustainability - A Study of Chinese Telecommunications regulation' (2008) 1(1) *International Journal of Private Law* 47-64.

⁴ G Li, A Lau and A Young, 'Rethinking Telecommunications Corporate Governance and Law in China: The Theories, Rules and Practices ' (2007)(2) *Australian Compliance and Regulatory Journal* 60-70.

⁵ G Li, 'Moving towards the Un-sustainability - A Study of Chinese Telecommunications regulation' (2008) 1(1) *International Journal of Private Law* 47-64.

⁶ 1949 is the year when the Chinese Communist Party took the office.

⁷ Guan, S. Y. (2002). The Development of Telecommunications Competition in China Retrieved 7 May 2006, from www.innovationlaw.org/lawforum/pages/guan_development_telecommunication.DOC+MII+was+established+1998+state+council&hl=en

⁸ He Zhou, 'A History of Telecommunications in China: Development and Policy Implications' in Paul S N Lee (ed), *Telecommunications and Development in China* (1997).

⁹ Liu, G. (1998). *The Life of the Chinese: Real Life Stories*. Nan Chang: Jiangxi Publish.

¹⁰ Zhou, above, n 8.

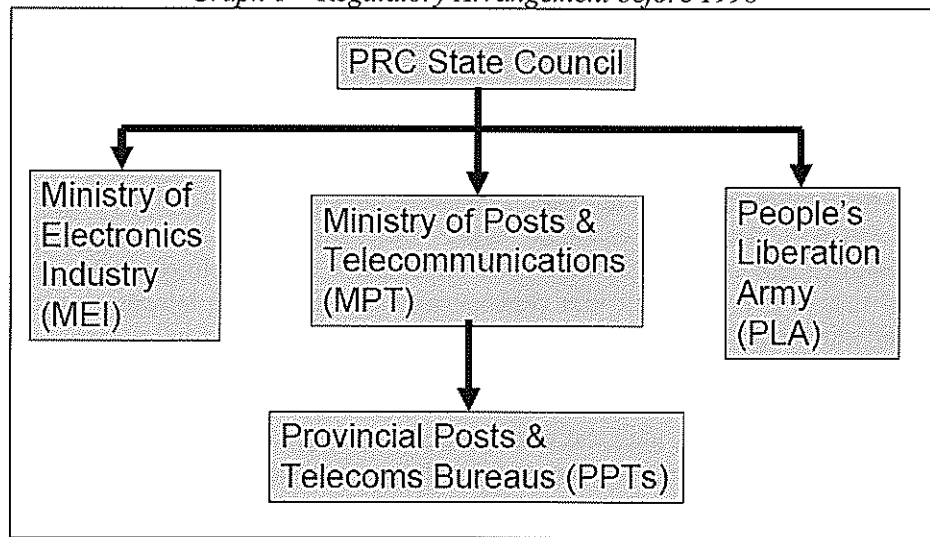
¹¹ Wang, S. (2001). Development of the Telecom Sector in Modern China. *Hubei Legal Review*, 2(3), 12.

of China's GDP growth in the past decade. From 1994 to 2000, the industry maintained a growth rate of about four times faster than GDP on an average yearly basis and the proportion of industrial added value increased gradually in GDP by being one of the fastest growing industries with the best economic result. There are external comments stating that the Chinese telecom sector has the strongest and fastest growth in the world in this line of industry¹².

B Regulatory Changes

Similar to many other countries in the world, the PRC Government used to have a government-owned and controlled telecommunications monopoly. At that time, telecom was considered to be a strategic element of the national economic infrastructure, which is vital to national security¹³. The sector was consolidated under a single authority MPT and its provincial branches Provincial Posts & Telecoms Bureaus (PPTs)¹⁴. Apart from certain telecommunications infrastructure operations delegated to the Ministry of Electronics Industry (MEI) for defense purposes and the Chinese People's Liberation Army (PLA), which had its own dedicated telecommunications infrastructure, MPT and PPTs enjoyed exclusive powers to plan, construct, operate and regulate the country's public networks¹⁵. The following graph demonstrates the regulatory arrangement before 1998.

Graph 1 – Regulatory Arrangement before 1998

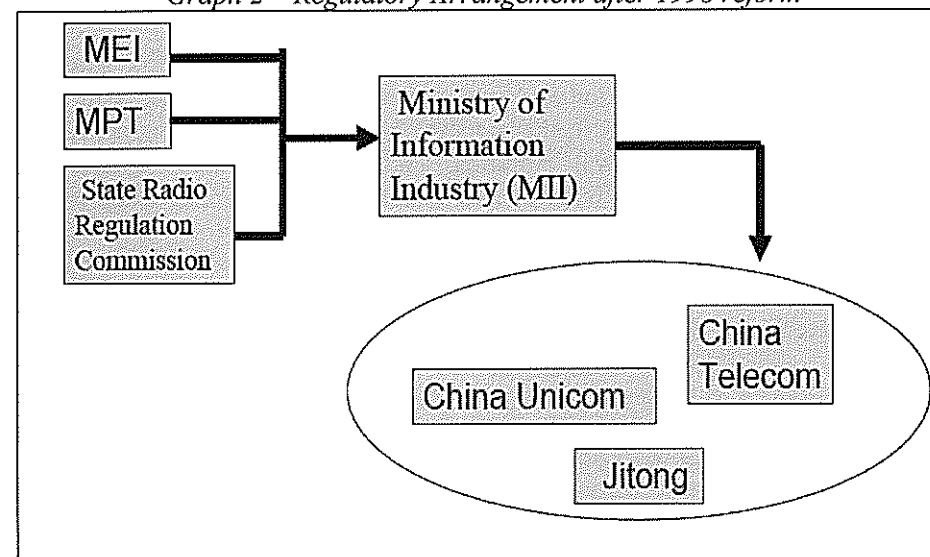


¹² E Sautedé, 'Telecoms in China: Towards a Post-WTO Shock Therapy' (2002) 45 *China Perspectives* 18.
¹³ L P Chavolla and R Samarajiva, 'Privatization, Market Liberalization and Regulatory Reform in the Mexican Telecommunications System' in D J Ryan (ed), *Privatization and Competition in Telecommunications* (1997) 150.
¹⁴ K Zita, 'Modernising China's Telecommunication' (1987) 23 *The Economist*.
¹⁵ Y Wu, 'China: Growth and reform in telecommunication' (2004) *Telecommunication reform in the Asia-pacific Region* 220-221.

With near absolute control there was a temptation to be complacent and gradually become torpid. By 1980s, MPT's substandard performance has undermined the industry for many years. Public complaints against MPT became more and more often. In addition, other Ministries also came to realise that telecommunication is a very lucrative business. Thus, the pressures to break up monopoly formed a strong force.¹⁶

The State Council, after years of hesitation and behind the scenes negotiation, acknowledged the importance of the information age and the need for the efficient flow of information to enable economic reforms to succeed.¹⁷ In March 1998, whilst reforming the Chinese bureaucracy, MEI and MPT, the former enemies in the telecom market, were merged with State Radio Regulation Commission and formed a new ministry – Ministry of Information Industry (MII), which became a principal regulator of the telecommunications and information industry. Government news release stated that the purpose of this reform is to set up an independent regulator and therefore a better competitive market.¹⁸ However, the result was turned to be a compromise of 'an uncompromised battle'.¹⁹ The regulatory arrangement after 1998 reform is demonstrated below.

Graph 2 – Regulatory Arrangement after 1998 reform



¹⁶ H Zhou, 'A History of Telecommunications in China: Development and Policy Implications' in P S N Lee (ed), *Telecommunications and Development in China* (1997).
¹⁷ J Ure, 'Telecommunication in China - More than was Bargained For' (1997) 2 *New Technology Quarterly* 34.
¹⁸ H Hong, 'Telecom Reforms to Enhance Competition', *China Daily* (Beijing), 8 January 2002.
¹⁹ W Hui, 'Who is a liar – the story behind the new reform in telecom sector' (2000) 12 *Wuhan University Law Review* 44-88; G Li, 'Moving towards the Unsustainability - A Study of Chinese Telecommunications regulation' (2008) 1(1) *International Journal of Private Law* 47-64.

C Market Reforms

Market Reform I – breakup of the monopoly

Like many telecommunications markets in the world, the PRC Telco market also started as a monopoly market. The Directorate-General of Telecommunications (DGT) used to serve as an administrative arm of the MPT was separated from the postal operations of the MPT's business and corporatised into a self-financing operator - China Telecom in mid 1990s, which signified a starting point of the PRC's Telco market reforms. The aim was to establish MPT as an independent regulator; and, at the same time, corporatise telecom business as part of the socialist market economy reform. The legal framework of the industry supposed to be the regulator and the policy maker, MPT, being an independent referee; and the market player and incumbent, China Telecom, operate as SOE.²⁰

This initiative was however failed. There were many reasons contributed to the overall failure. The most important one was that the new management in China Telecom had strong personal connections with MPT²¹, which enabled China Telecom to retain its dominance and enjoy vast policy privileges. In particular, China Telecom seemed immune from public dissatisfaction.²²

At the same time, other ministries started to look for ways to get a 'slice of the cake'. After years of negotiation and inter-ministries bargaining, the State Council finally approved new entrants in the market. As the result of this approval, China Telecom's legal monopoly was curtailed. Those early entrants included JiTong Communications Company (JiTong) and China Unicom, which were sponsored primarily by another ministry - MEI.²³

Unfortunately, new entrants did not bring in competition automatically. China Unicom was such an example. Since MPT embraced both regulatory and operational responsibility, Unicom as an entity outside the MPT seemed to encounter many problems with China Telecom. In fact, Unicom faced the same problems all new entrants face against the former monopoly - China Telecom. There were no agreed terms for revenue-share or universal service obligation. Unicom lacked vital resources to develop and was therefore more inclined to look

²⁰ Y Xu, N Levine and P Douglas, 'Competition Without Privatization: The Chinese Path' in S Macdonald and G Madden (eds), *Telecommunication and Socio-Economic Development* (1998) 375-392.

²¹ B P Y Loo, 'Telecommunication reforms in China: towards an analytical framework' (2004) 28(9-10) *Telecommunication Policy* 697-714.

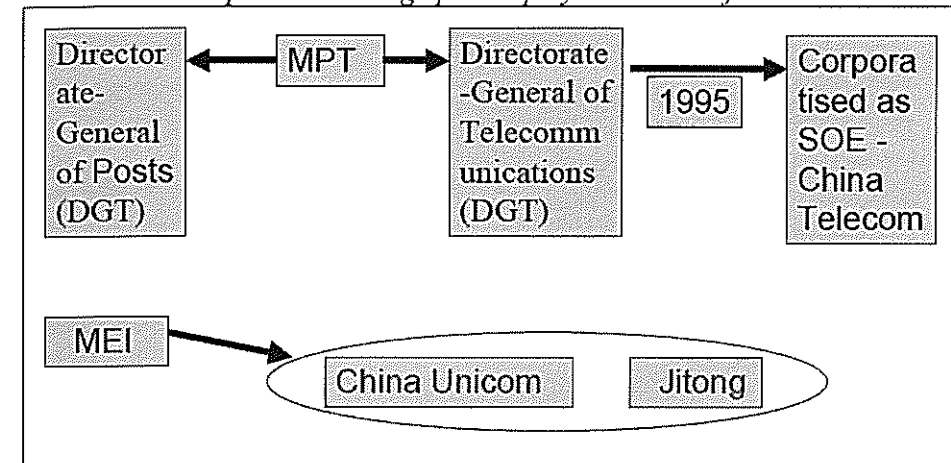
²² Y Wu, 'Growing through Deregulation: a Study of China's Telecommunication Industry' (Paper presented at the Telecommunication Reforms in the Asia-Pacific: can developing countries benefit from the experience of developed countries, Jakarta).

²³ Z Tan, 'China's Information Superhighway: What is it and who controls it' (1995) 19(8) *Telecommunications Policy* 721-731.

for overseas technical partners and finance, reason enough for the MPT to oppose foreign participation on any terms that might rival its position.²⁴

The breaking up monopoly process is demonstrated by the following graph.

Graph 3 – Breaking up monopoly in market reform I



Market Reform II – establishing six SOEs

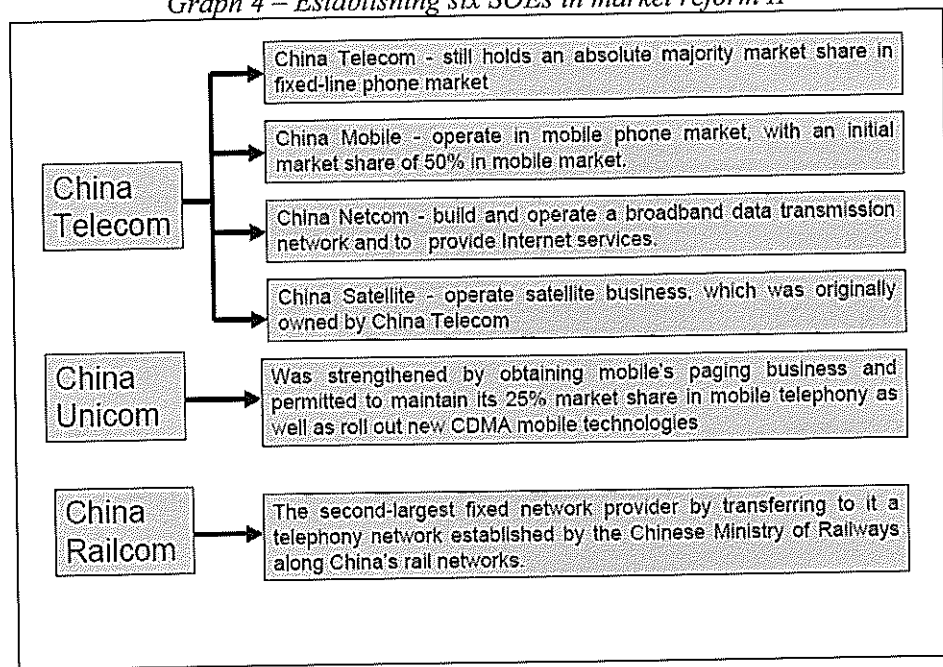
After the 1998 regulatory changes, the battle for domination in the telecommunications sector persisted. During 1999-2000, the newly established MII led the market through a complicated restructuring program to accommodate all other competing interest groups. As a result, ministries negotiated a new telecommunications configuration with a total of six SOEs in 2000, breaking up China Telecom's four divisions of services into separate entities. Consequently, four independent companies were formed. They are responsible for the fixed line, mobile, paging and satellite communication services, respectively. The fixed line services retained the name China Telecom. The new China Telecom was officially incorporated on 17 May 2000. The mobile service department of the old China Telecom became China Mobile, which was established on 16 May 2000. A new company, China Satellite, which provides satellite telecommunications services, was also approved by the State Council. The paging arm of the old China Telecom was merged with Unicom. In particular, after the restructuring the new China Telecom, China Mobile and Unicom were comparable with each other in size and hence more equal rivalries were established.²⁵

²⁴ J Ure, 'The Chinese Telecommunications Market' (Paper presented at the Business & Technology Exchange Forum on Telecommunications, Hong Kong Industrial Technology Centre Corporation Tech Centre, Kowloon).

²⁵ Y Wu, 'Growing through Deregulation: a Study of China's Telecommunication Industry' (Paper presented at the Telecommunication Reforms in the Asia-Pacific: can developing countries benefit from the experience of developed countries, Jakarta).

The following graph demonstrates this process.

Graph 4 – Establishing six SOEs in market reform II



Market Reform III – Re-arrange the service areas of the six SOEs

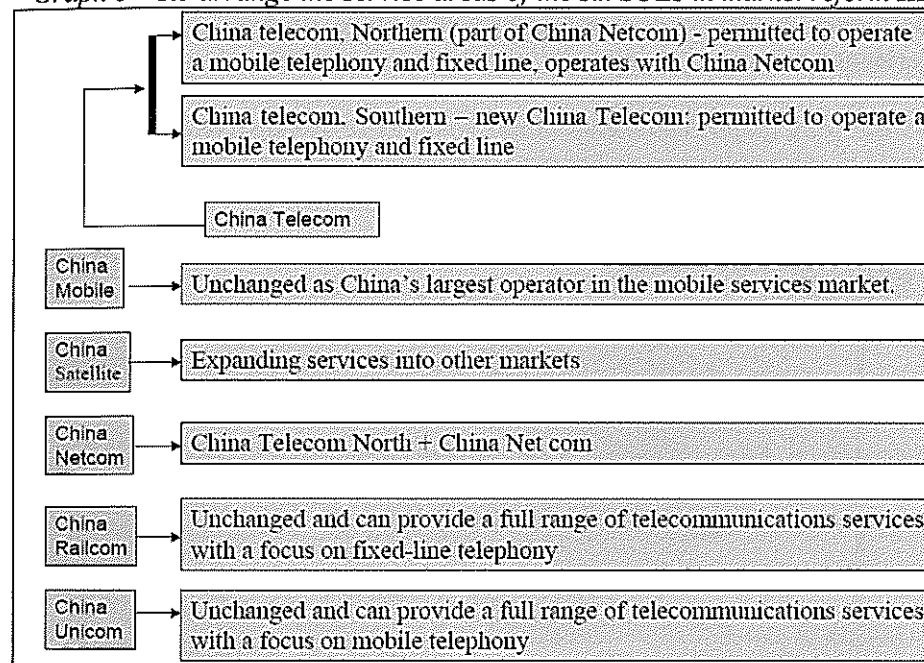
As always, the superficial compromise of conflict interests is never a permanent solution. Not surprisingly, after several years reallocating market share between the various providers the changes were still far from completed. In May 2002, the PRC State Council created six multi-functional state-owned enterprises with a high degree of functional overlap. The market configuration was reorganised again to reflect the socialist market economy policies or another compromise of conflict interests.

In simple, this reform inter-mixed the functions of the market players. Old China Telecom was separated into two parts – southern and northern. China telecom, Northern was permitted to operate mobile telephony and fixed line services and they operate with China Netcom. Southern China Telecom became a new China Telecom and they were permitted to operate a mobile telephony and fixed line services. China Mobile remained unchanged as China's largest operator in the mobile service market. The New China Netcom combined Northern China Telecom, old China Netcom and Jitong, which remained a strong presence in northern part of China's telecom market. China Unicom remained unchanged and can provide a full range of telecommunications services with a focus on mobile telephony. China Railcom also remained unchanged and can provide a full range of telecommunications services with a focus on fixed-line telephony.

Not surprisingly, industry observers commented that the current regulatory framework is more of the result from turf war rather than the result of a genuine better regulatory practice.²⁶ Although the MII claimed that the complicated reform was designed with a primary purpose of improving competition and efficiency²⁷, complaints from other Ministries to the State Council and the involvement and the decision made by the State Council showed that the real motivation of these reforms were to ease the inter-ministry tensions.²⁸

The following graph demonstrates this process.

Graph 5 – Re-arrange the service areas of the six SOEs in market reform III



III THE RECENT REFORM

A Regulatory Change – Establishing a Super Ministry

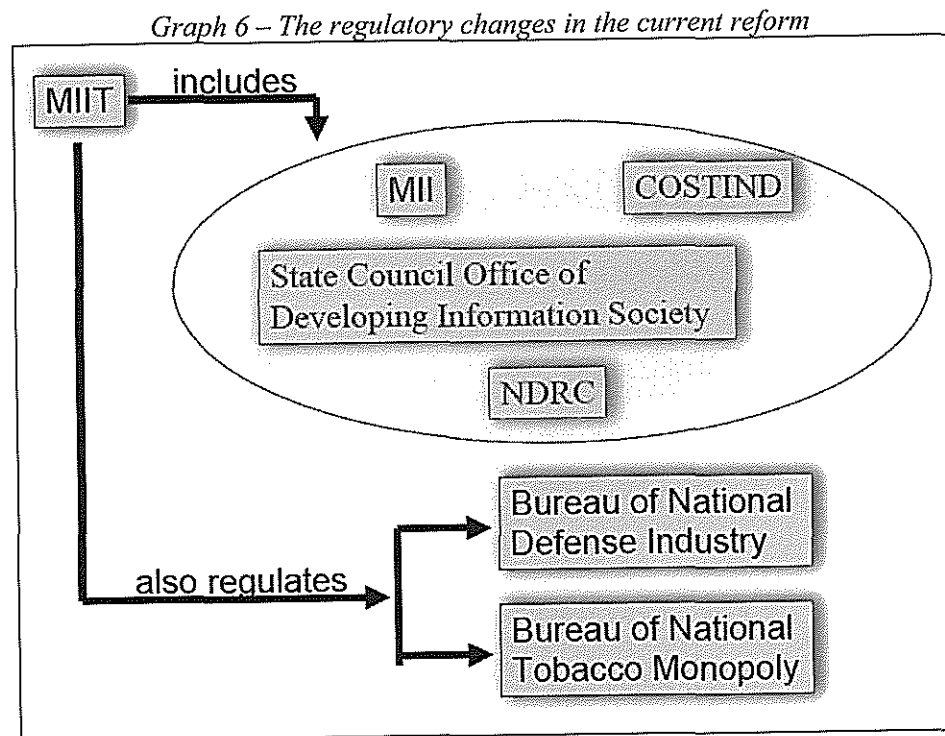
The PRC State Council announced its Ministerial Reform Plan on 11th March 2008. The plan includes establishing of five super Ministries including a Ministry of

²⁶ H Zhang, 'Vicious Domestic Competition Pushed the Industry', *People's Daily* (Beijing), 9 October.
²⁷ W Jichuan, 'Breaching the Monopoly and Separating Chinese Telecommunications Businesses from the Government Administration', *Hong Kong Financial Review* (Hong Kong), 25 Feb.
²⁸ X Wang, 'Reforms in the Key Sectors and the Impacts on the Current Legal Practice' (2003) 12(2) *Wuhan University Law Review* 68.

Industry and Information Technology of the People's Republic of China (MIIT). This newly established Ministry is to replace the previous Telco regulator MII.²⁹

MIIT is established by merging previous MII, The Commission of Science Technology and Industry for National Defense of the People's Republic of China (COSTIND), the State Council Office of Developing Information Society and some offices of PRC National Development and Reform Commission (NDRC). The primary responsibilities of MIIT include: setting strategic planning for industries, setting industry policies and standards, monitoring industry operations, promoting the development of major technological infrastructure and inventions, regulating telecommunications sector, supervising and promoting the establishing of the information society and coordinating with other agencies to protect national information security.³⁰

The following graph demonstrates this regulatory re-arrangement.



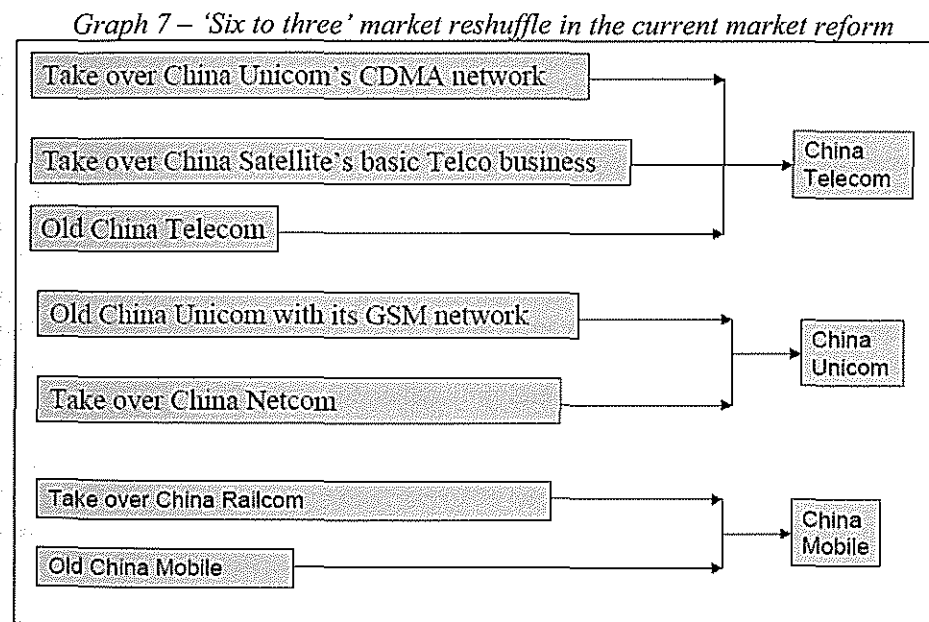
²⁹ The PRC State Council, *The PRC State Council Ministry Institutional Reform Planning* (2008) the State Council <http://www.gov.cn/2008lh/content_916855.htm> at 1 May 2008.
³⁰ Ibid.

B Market Reform – Merger 6 SOEs to 3 super SOEs

On 24th May 2008, A Notice of Deepening Reform in Telecommunications Sector was published by MII in conjunction with NDRC and National Treasury.³¹ The notice specified the new market reform planning, which includes a sale of China Unicom’s CDMA network to China Telecom, merge China Unicom with China Netcom, merge China Satellite basic telecommunication business with China Telecom, and merge China Railcom with China Mobile.³² In simple, this reform plan was to merge the existing six Telco SOEs into three super SOEs. It is therefore widely referred as the ‘six to three’ reform.

Also on the notice, it is specified that the objective of this reform aims to set a common competition platform for the major players on the telecommunications market by allowing all there players to operate all the telecommunications services including fixed line service, mobile service and Internet service. Commentators observed that this is to set a good ground in preparation of issuing three 3G licences to these SOEs in the very near future.³³

The market reform is demonstrated as below.



³¹ MII, NDRC and N Treasury, *A Notice of Deepening Reform in Telecommunications Sector* (2008) MII <www.mii.gov.cn/art/2008/05/24/art_2001_45730.html> at 25 May 2008.
³² Ibid.
³³ H Wang, 'the Right Reading of the New Reform in Telco Market' (2008) [22] 45(3) *Southern Telecommunications* 22-34.

IV EVALUATION OF THE RECENT REFORM

A Comment on the Regulatory Change

There have been controversies regards to this recent Telco regulatory change – more specifically, the establishment of the super power regulator, MIIT. The controversies started immediately after the State Council published its Ministerial Reform Plan in March this year and it was intensified after MIIT officially started its administration on 26 June.

On the one hand, people from industry viewed this regulatory change as a ‘big surprise’.³⁴ They argued that this regulatory change can only deliver an unsatisfactory industry regulation in the future due to the fact that it was not following the widely accepted regulatory theories such independent and impartial industry regulation and separate regulation in telecommunications.³⁵ Moreover, instead of establishing a super power Ministry, the State Council should have followed the experiences in many developed countries and set up an independent regulatory agency, which should be strictly separated from the government and independent to the industry.³⁶

On the other hand, commentator and industry observers have expressed positive views about this regulatory change. The Telco Industry Analyst Xinfeng Zhang believed that the super power Ministry would make some changes to the current multi-regulator situation. He explained that the PRC Telco regulation before this reform was in fact very messy with MII at one hand acting as the ‘regulator’ and, on the other hand, many other government departments were active in sharing the ‘slice of the cake’ in the regulatory business. This reform made the new MIIT became a real empowered regulator who will act as the monopoly figure in Telco regulation. Therefore, the regulatory environment in the future would be simpler and easier to understand, which in turn, will be beneficial to the market players when seeking permission or making complaints. The super power Ministry will reduce the overlapping administrative procedures as well.³⁷ The independent director of China Netcom, Mr. Zoning Hou also stated publicly that - “it is a good thing to see the merge of the Ministry of Industry and Ministry of Information. This will be very beneficial to the future of China Telecommunications industry. The supervision will be stronger after this regulatory change”.³⁸ In addition, Professor Jianqiu Zeng observed that there is no need to set up a separate regulator in China,

³⁴ J Wang, ‘Expect the Unexpected - a Study of the Current Regulatory Change in Telco Sector’ (2008) [45] 73(2) *Wuhan University Law Review* 45-44.

³⁵ L Xiang, *What Is the Effective Telecommunications Regulation* (2008) Sohu <<http://xiangligang.blog.sohu.com/>> at 27 June 2008.

³⁶ H Wang, ‘Where Is the Independence in the Telco Regulation?’ (2008) 78(1) *Wuhan University Law Review* 55-67.

³⁷ X Zhang, *the 3G Market and the Competition Behind It* (2008) Sohu <<http://digi.it.sohu.com/20080401/n256025661.shtml>> at 1 June 2008.

³⁸ Z Hou, *IPTV and Video2.0* (2008) Sina Technology <<http://tech.sina.com.cn/t/2008-04-11/20482133534.shtml>> at 12 June 2008.

regulation and supervision run by MIIT would be enough for the industry and the PRC Telco market in the foreseeable future.³⁹

Despite some reservation, it would appear this regulatory reform can bring some positive changes to the current poor Telco regulation in PRC. It is however a good starting point only. More in-depth reforms should be considered in the near future if it is not immediately. More specifically, MIIT should consider setting up an independent telecommunications regulatory agency and the issue of convergence broadcasting and telecommunications will need to be addressed in a timely manner. The following paragraph explains this view in more details.

Firstly, the regulatory reform can bring some positive changes to the current Telco regulation. MII, who used to be the major industry regulator has become one functional part of the newly established MIIT. Therefore, all the functions of old MII transferred to the new MIIT. MIIT is now responsible for the Telco market, industry operation as well as performing all other MII’s previous functions. In respect to the regulatory functions, it would be no doubts that MIIT can fully replace the old MII without concession. There will not be any diminishing in performing regulatory functions. What happened in the past would pretty much be what would happen in the near future. Moreover, the super power MIIT can even strengthens its regulatory power. For example, in the past, MII was responsible for planning and building of the base telecommunications towers. However, MII would have to apply for a written approval from NDRC to commence any building project. Under the old administrative process, the procedure of running such project could have been very lengthy. The situation could get changed after this reform. This regulatory reform has pooled both NDRC and MII under the big umbrella of MIIT. It is therefore fair to expect a quicker and administrative procedure under the new MIIT regime.

Secondly, this reform is of a starting point only. It does not solve many key issues in the industry regulation such as independent regulator, removal of market entry barriers, and convergence of broadcasting and telecommunications. For instance, with IPTV and mobile TV becoming more and more popular, the issue of converging broadcasting and telecommunications regulation is becoming pressing. Many countries have merged their broadcasting and telecommunications regulators to reflect the trend of convergence, such as Ofcom in the UK, ACMA in Australia, MCMC in Malaysia, Agcom in Italy and Ficora in Finland. In fact, the convergence of broadcasting and telecommunications is technically mature in China as many other places in the world. But PRC is not ready to move on to the convergence phase yet with its long standing battles between Ministry of Broadcasting and the old MII.⁴⁰ This regulatory uncertainty has lagged the development of these

³⁹ J Zeng, *Number Portability Can Not Change the Unbalanced Telecommunications Regulation In China* (2008) <<http://www.cnii.com.cn/20080308/ca473443.htm>> at 30 June 2008.

⁴⁰ Li and Rahaju, ‘Regulatory Multiplicities in Telecommunications Reforms in Indonesia and China’ (2005) 2 *Macquarie Journal of Business and Law* 135 –167.

technologies for years.⁴¹ Although PRC can just leave this issue aside for the meantime, they will need to address the trend of convergence and response to it in the very near future.

B Comment on the Market Reform

This recent 'six to three' Telco market reform has brought PRC a major market shake up. Six competing Telco SOEs was basically ordered by the State Council to merge or take over businesses from each other. There is much to discuss in this new set up.

First of all, this paper is to comment on the reform plan.

The reform plan was released through a Ministerial notice, the Notice of Deepening Reform in Telecommunications Sector, which was published by MII in conjunction with NDRC and National Treasury.⁴² This notice clearly stated the reasons for reform as below:

'[M]any new situations and new problems have merged in the PRC ICT industry in the recent years, especially in regards to the competition framework and the allocation of telecommunications resources. In particular, an extremely fast growth of the mobile service sector and a much slower development in fixed line service sector has shifted the competition platform to an unbalanced status, which has also created a big disparity in terms of competitiveness among the current market players. All these have presented an urgent need for a market reform – a reform to address the new issues and find solutions.

As regards to the objectives of this reform, this document stated that:

[T]he aim of this reform is to, by using the opportunity of adopting 3G technology, allocate the telecommunications resources logically, realise all services operations, create an appropriate and healthy competition environment, which will prevent the monopoly and avoid excessive building of infrastructures...

This document also made it very clear that:

[T]his market reform is to be conducted with the consideration of the 3G licensing arrangement in the near future. 3G licenses are to be issued after the completion of this reform.

These statements indicate a strong political will of developing telecommunications industry in China by the government forces rather than the actual market, although

⁴¹ G Li, A Lau and A Young, 'Rethinking Telecommunications Corporate Governance and Law in China: The Theories, Rules and Practices ' (2007)(2) *Australian Compliance and Regulatory Journal* 60-70.

⁴² MII, NDRC and N Treasury, *A Notice of Deepening Reform in Telecommunications Sector* (2008) MII <www.mii.gov.cn/art/2008/05/24/art_2001_45730.html> at 25 May 2008.

the latter is promoted by the government in many other occasions.⁴³ These statements also revealed a high hope on the reform to bring in positive changes in the current unbalanced market competition in the coming years with the issuing of three 3G licences in the very near future.

What is the real reason causing the unbalanced market competition? This paper believes that the answer could be indicated by the recent Telco reform history in PRC. Firstly of all, in the 2002 market reform, market players were restricted as to what services they could provide, which included granting China Mobile an exclusive power to run mobile service and granting China Telecom an exclusive power to run the fixed line service. This arrangement contributed positively in promoting the telecommunications development in those days. It however has started to date in the recent years with the global surge of the mobile service taking up. As expected by various studies, 'mobile phone will exceed fixed line phone in many jurisdictions'⁴⁴, what we are experiencing today is 'mobile phone has exceed fixed line phone in some parts of the world'.⁴⁵ Secondly, there has been little promotion of the more advanced deployment of digital technologies, which led to a slow development of ADSL broadband deployment and minimal development in FTTH or FTTN technology in PRC. In turn, this contributed to a slow development of the fixed line phone market, which eventually contributed to the unbalanced positions in market competition. In addition, in running its Telco businesses, China Unicom adopted multi-standard networks (GSM and CDMA) due to some historical reasons⁴⁶, which now lead to a situation where China Unicom is facing a lack of resources, low efficiency and a difficulty of pooling its customers to serve both of its networks. In simple, the leads of the current unbalanced competition situation in PRC Telco market is not caused by a single reason, but a number of contributory factors.

Then, how does one ease the existing unbalanced market competition and can this recent market reform make changes? The short answer is – it remain to be seen in the following years, the reform itself will not bring in competition automatically due to its political nature, which limited the reform and the market within an realm of SOEs. SOEs biggest interests are always the government. It is therefore hard to claim a real competitive market place. However, if the current three full service

⁴³ R Chen, 'The Challenges and Opportunities for 3G Development in China' (Paper presented at the The 4th Senior Forum on VA ICT Businesses and Exhibit Beijing, 26 September 2005); J Wang, *3G Development in PRC Sould Speed Up* (2008) Sina Technology <<http://tech.sina.com/t/2008-04-03/04352117105.shtml>> at 2 July 2008; G Xi, '3G in China' (Paper presented at the International ICT Summit Beijing, September 2005) <www.mii.gov.cn/art/2005/12/12/art_131_3100.html>.

⁴⁴ Analysys, *European mobile calls to exceed fixed line* (2008) Telecommunications <<http://www.gizmag.com/mobile-calls-to-exceed-fixed-line/8783/>>; M Jones, 'Watch This Mobile Advertising Space', *Financial Review* (Sydney), 12 Feb.

⁴⁵ M Castells et al, *Mobile communication and society: a global perspective* (2006).

⁴⁶ G Li, A Lau and A Young, 'Rethinking Telecommunications Corporate Governance and Law in China: The Theories, Rules and Practices ' (2007)(2) *Australian Compliance and Regulatory Journal* 60-70.

players can be creative in running their special businesses based on their advantages after the reform and further after receiving their 3G licence, a better competitive environment (not a real competitive market) could be achieved. The following analysis is to support this view by discussing the three players in details.

Firstly, China Mobile, it owns the best quality GSM network in PRC with the most number of subscribers. In fact, China Mobile's alleged its GSM network becoming the biggest network in the world in recent years.⁴⁷ Domestically, it is no doubt that China Mobile is the 'big brother'. Internationally, China Mobile is still a big company with the biggest number of subscribers, it is however not the strongest in terms of competitiveness with other international players – it is still sitting outside of the top 10 international Telco companies on the authoritative global ranking.⁴⁸ This reform made China Railcom merged with China Mobile. Is this a gain or a loss from China Mobile's perspective? The answer is definitely not straightforward. By the end of 2007, China Mobile had about 390 million subscribers.⁴⁹ The merge with China Railcom is comparatively insignificant both in the number of subscribers⁵⁰ and in the net assets⁵¹. This merge is therefore not vital to the development of China Mobile. This paper suspects that the real reason behind this merge is because of the long time unfavorable operation of China Railcom, which made it a big burden instead of an asset. When the PRC State Council considered the issuing of 3G licence and tried to balance the interests of all the Telco stakeholders as they always need to, they had no choice but to find a new home for China Railcom. China Mobile became the inevitable victim due to its superior leading position in the RPC market. There could be a couple of advantages in merging Railcom and Mobile: one is to remove China Railcom as an insignificant players with insignificant infrastructure and insignificant number of subscribers in the market; and, two is to give China Mobile some fixed line business and therefore it might want to build its future network based on it. Nevertheless, the merger of Mobile and Railcom did not change the battlefield in a great way, China Mobile is still the biggest operator in PRC market and it will probably continue its super power in the following years.

Secondly, China Telecom, the core business of China Telecom has been its fixed line service. Although it does have a Personal Hand Phone System (PHS) network,

⁴⁷ China Mobile Ltd, *Introduction of China Mobile Ltd.* (2007) China Mobile <<http://www.chinamobileltd.com/about.php>> at 12 July 2008.

⁴⁸ Total Telecom, *Top100 – Total Telecom Ranking* (2007).

⁴⁹ China Mobile Limited, *China Mobile Limited 2007 Financial Report* (2007) China Mobile Limited <http://www.chinamobileltd.com/images/pdf/2008/ar/CMHK_ar_2007_e_full.pdf> at 13 June 2008.

⁵⁰ The number of subscribers of China Railcom is about 1/10 of China Mobile. Re Ibid. and China Railcom Limited, *The Operation of China Railcom in 2007* (2007) China Railcom Limited <<http://www.chinatietong.com/news/index.php3>> at 13 June 2008.

⁵¹ the net asset of China Railcom is about 1/10 of China Mobile. Re China Mobile Limited, *China Mobile Limited 2007 Financial Report* (2007) China Mobile Limited <http://www.chinamobileltd.com/images/pdf/2008/ar/CMHK_ar_2007_e_full.pdf> at 13 June 2008. and China Railcom Limited, *The Operation of China Railcom in 2007* (2007) China Railcom Limited <<http://www.chinatietong.com/news/index.php3>> at 13 June 2008.

the technology that this support PHS network is far less advanced than the cellular mobile communications technology.⁵² After a sharp rise in the number of subscribers in 2003 and 2004 with a peak in 2006,⁵³ the take up rate of PHS phone showed a huge decrease in the past two years.⁵⁴ The direct reason behind this decrease was the price of using GSM and CDMA mobile was marked down heavily at the end of 2006 by China Mobile.⁵⁵ In fact, the number of PHS subscribers decreased around 6.08 million in 2007 and 5.05 million in first 4 months in 2008.⁵⁶ If this trend continues, which is highly likely given the fact that this is what happened in many other places in the world⁵⁷, cellular mobile will take up most of the market in the coming months. Thus, to effectively compete with other operators in the market, China Telecom has been in great need of a permit to provide real mobile services. After the reform, China Telecom would take over 410 million CDMA subscribers from China Unicom, plus its existing 2200 million fixed line subscribers and 60 million PHS subscribers, China Telecom would be able to compete with China Unicom and China Mobile in both fixed line and mobile services market.⁵⁸ However, the price that China Telecom paid is also high. China Telecom paid RMB110 billion (about AUD\$18 billion) to take over China Unicom's CDMA network.⁵⁹ Nevertheless, the challenge for China Telecom does not ease with the taking over of China Unicom's CDMA network. In fact, with the trend of losing subscribers in their fixed line services and PHS subscribers, the challenge for China Telecom still persists. Moreover, the China Unicom's CDMA's network has not been as reputable as to its GSM network. The future of China Telecom is thus very uncertain.

Thirdly, China Unicom, it owns two national wide mobile networks (GSM and CDMA) due to the historical reasons. In 1999, China Unicom publicly announced that its GSM resources could only adopt around 80 million subscribers and therefore they decided to build a CDMA network, which uses another band of spectrum, based on a more advanced technology and brings in 'green' mobile phone.⁶⁰ Although the introduction of a new CDMA network received many critics

⁵² N Muller, *Desktop encyclopedia of telecommunications* (2002).

⁵³ mainly because the policy did not allow fixed line service provider to provide mobile services in those days and PHS is a limited mobile service which was categorised into fixed line service category

⁵⁴ T Hu and J Sha, 'Suggestions to the PRC Mobile E-Commerce' (2007) 24(5) *China New Telco*.

⁵⁵ F Lu, 'Analysis of China Telecom's PHS Strategies' (2008) 18(1) *Information Network*.

⁵⁶ X Wang, 'Continue Decrease in Xiao Ling Tong Subscribers', *Market News* (Beijing), 27 Feb.

⁵⁷ T Hu and J Sha, 'Suggestions to the PRC Mobile E-Commerce' (2007) 24(5) *China New Telco*.

⁵⁸ B Lu and Y Xiao, 'China Telecom CEO Xiaochu Wang - High Price Taking Over CDMA Network for Future 3G Licence', *Financial Daily* (Beijing), 3 June

⁵⁹ Ibid.

⁶⁰ C Unicom, *Launch of the CDMA Network* (1999) China Unicom Pty. <www.chinaunicom.com.hk/en/tech/mobile/standard/mobileNetwork.html> at 4 Oct 2002.

in those days and MII also set up a face-to-face forum for it⁶¹, the final decision was still made in favor of introducing the new network. The consequence was not only a very slow CDMA taking up rate, it also separated the GSM subscribers and lead to a much slower development of GSM network. The CDMA network had been running in loss until about 2006. All these contributed to the decision of selling the CDMA network to China Telecom. Nevertheless, this paper argues that, separating GSM and CDMA networks could be a short term solution to a number of issues. One, this separation effectively granted China Telecom a permit to provide mobile service; two, it allows China Unicom to concentrate on developing its core GSM network; and, three, as indicated by the CEO of China Telecom, this separation creates a sound ground for issuing 3G licence in the near future.⁶² Another change that this reform has brought to China Unicom is the merger with China Netcom. The main business of China Unicom is PHS and fixed line services. It has 200 million PHS subscribers and 110 million fixed line subscriber.⁶³ Both of these services are however decreasing due to the same reason as seen in the China Telecom's situation. If China Unicom does not effectively retain the China Netcom's subscribers and transfer them to the Unicom's GSM network, China Unicom is to face a similar challenge that China Telecom is to face.

Thus, after this 'six to three' reform, all three major operators will be able to provide mobile service and fixed line service, which would presumably lead to a better but still limited competition. China Telecom would face the big challenge of retaining their user in its fixed line network and PHS network, and, at the same time, attracting more subscribers to its newly acquired CDMA network. China Unicom would be in the situation of trying to retain or transfer their fixed line and PHS subscribers (these subscribers are from the old China Netcom) to its GSM services. At the same time, as to the mobile service sector, China Unicom would expect some level of competition coming from China Telecom's CDMA sector. Comparatively, the situation of the PRC Telco 'big brother' China Mobile is less critical. Although the merger with China Railcom is not likely to bring many benefits to China Mobile, the insignificance of China Mobile would unlikely affect the general operation of China Mobile. In general, this reform significantly reshuffled the PRC Telco market place. As to the real result of the reform, it remains to be seen in the next few years.

V CONCLUSION

Despite the controversies of the current reform in both the regulatory structure and the market place, this paper further argues that, the significance of this reform lies in a real game in the near future – the 3G game. This current reform is a 'warming

⁶¹ T Hu and J Sha, 'Suggestions to the PRC Mobile E-Commerce ' (2007) 24(5) *China New Telco*.

⁶² B Lu and Y Xiao, 'China Telecom CEO Xiaochu Wang - High Price Taking Over CDMA Network for Future 3G Licence', *Financial Daily* (Beijing), 3 June.

⁶³ China Netcom Limited, *The Business of China Netcom in 2007* (2008) China Netcom Limited <<http://www.chinanetcom.com.cn/2j/dxsc/index.asp>> at 14 June 2008.

up' stage of the real 3G game. The PRC State Council is trying to set a fair starting point for all the three players. Unfortunately, the starting point is hard to be a real equal basis. In addition, the political will has been playing a vital driving force in the development of PRC's Telco industry for many years. It however could not solve all the problems such as the under-developed TD-SCDMA standard and the slow development of CDMA network.

In conclusion, this current reform is of a beginning of a new arrangement trialed by the PRC government. The real issue remains in the post-reform stage and in fact, the post-3G licensing stage. Who is to win and who is to loss in the coming 3G battle would be an interesting thing to see.