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Telecommunications Statecraft

A Comparative Analysis of the Rise of the Industry in USA and China and their Implications for Consumers

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AIS5340 Infrastructure Development in China
Abstract

The free market is often held up as the gold standard for maximizing consumer benefits. This essay looks at the rise of the telecommunications industry in both the USA and China and notes why perhaps the Chinese model of doing things, despite not being that of the free market as espoused by the USA, was the best possible option given the situation.

Introduction

The rise of China is an undeniable fact since it’s opening up in 1978 (Bijian, 2011). It has been and continues to reshape not only its internal economy but also both its regional (Ash, 2005) and indeed the global economies (Sneader & Ngai, 2016). As such, the rise of China has begun to challenge the existing international order and the global hegemon, the USA (Allison, 2017). In such a scenario, it is important to note the core differences between the two systems to engage with how each country choose to shape their economies and, as such tangentially, affect the global economic system as a whole.

This essay shall look at the rise of the telecommunications industry in both countries and compare how the rise was managed and controlled in each country. The terms “manage” and “controlled” are used on purpose here as they are the working thesis of this paper, that while the USA manages the rise of industry by enacting laws and regulations after the fact, China chooses to control industry, by maintaining strict controls over who gets to be part of industry before the industry takes over. The question this essay aims to answer then is, in a rapidly developing economy, which method of allocation of property rights is best suited to maximize benefits to the consumer?

To answer the question, we shall first trace a brief history of the rise of the telecommunications sector in both countries respectively, then seek to answer the question by looking at several key factors. These key factors will be: accessibility, affordability and security. These have been chosen as each forms a key component of commercial property rights.

Access to consumers is important. If citizens are denied access to goods, then a state can be said to be failing its function (Chand, 2017). Furthermore, access should not be restricted unless in special
circumstances. Price of goods is another key factor as it can often determine whether or not a good is accessible. If a good is too expensive, even the availability of that good would not make it accessible and therefore price and access go hand in hand. That is not to say however, that any and all goods should be freely available at a cheap price in the market. Especially with a good like telecommunications, the state needs to be aware of the potential impact on state security (Coase, 1959) and therefore limit how easy it is to access that good by entities that may wish to use it for nefarious purposes.

Rise of the Telecommunications Industry in the United States of America

At the turn of the 20th century, and in particular in the aftermath of World War I, radio became an increasingly popular form of communication (Coase, 1959). Unfortunately, this brought with it issues of safety, particularly at sea where it was recognized that there may be concerns if a ship was using one wavelength to transmit calls of distress while rescue services were using another. In 1912, a bill was passed in both the Senate and the House of Representatives that required anyone operating a radio station to have a license issued by the Secretary of Commerce. In the wake of WWI however, the Navy controlled 111 of the 127 commercial shore stations but the House was unwilling to grant it a monopoly over the radio waves, which eventually opened up the market. In a landmark decision in 1923 (Hoover vs Intercity Radio Co, 1923), the courts decided that the Secretary of Commerce had no discretion to deny licenses. In a separate case, the courts rules that the level of restrictions the Secretary could place were also highly limited (United States vs Zenith Radio Corp, 1926) which resulted in a boom of commercial radio stations until 1927, when the Federal Radio Commission was brought into existence.

For the purposes of this paper, that much history shall suffice. There are three key takeaways from this short history of the rise of the telecommunications industry.

1) The government is reluctant to impose a government-led market monopoly on industry;

2) The government could not foresee the types of actions industry would take and was thus left chasing it; and

3) Industry had a very strong mechanism to challenge government decisions, namely the court system which also often ruled in favour of the market.

We shall return to these takeaways below in our comparison.
Rise of the Telecommunications Industry in the People’s Republic of China

China is the world’s largest telecommunications market (Higgins, 2015) Between 1953 and 1980, Chinese investment in the telecommunications industry fell short of a level required to grow, with a larger proportion of resources being diverted to heavy industry (Tjia, 2016). Once the open door policy was adopted, there was a boom in the telecommunications industry, with an annual growth of over 30%, which was significantly higher than the national GDP (Tjia, 2016).

How was the market growing so fast? Against the normalized methods of liberalizing and allowing the market to flourish, the Chinese government centralized the dispersed and fragmented assets into a few operators and allowed only some degree of competition, which was regulated.

In 1993, the government spun off China Telecom from the Ministry of Posts and Telecommunications, which itself had been formed way back in 1950, in order to utilize idle telecommunications assets. In the same year in December, a new telecommunications operator, China Unicom, was allowed to be formed to provide services. Thus creating the first two companies to provide these services to consumers. As stated above however, market competition was not really allowed, with the state ensuring competition in an “orderly fashion” and a “structured price war” leading to expensive fees and charges for customers, as well as a general disregard for customer complaints (Tjia, 2016). This, coupled with slow growth prospects due to guaranteed profits, eventually led to a re-centralization of the industry.

Once again, a detailed history of the events is not really the intention of this paper, but we can have three key insights from the stated history.

1) A lack of resources dedicated to the industry results in slow or minimal growth;
2) A lack of market competition can lead to inefficient and poor services; and
3) Industry is at the whims of the government, which has the ability to seize and control assets as it deems fit.

Analysis

There is a clear juxtaposition in the way the US and China began and continue to run the telecommunications industry. While the US has been a market led, industry driven market, China has
chosen to limit market exposure by having a centralized system with a top-down management of the industry. We shall now compare the two systems using the earlier metrics of access, price and security.

Accessibility

It is quite clear from the above histories that greater access is granted in the American system. However, I would like to bring a couple of caveats within this. First, unrestricted access to something as sensitive as radio waves may simply not be possible in China. As we are aware, the state keeps tight restrictions on the type of information that flows to the people (Shambaugh, 2016). In such a state, free and unrestricted access might not be in the states interest. Secondly, and perhaps more importantly, access to radio waves is a highly lucrative business, as was clearly seen above. The moment China opened up and began to explore this industry, profits started flowing in. Similarly, the profit incentive was the key driver in why the US telecommunications industry grew rapidly in the 1920, and why companies were willing to take matters to the courts to resolve any restrictions that the state attempted to put on them. Given then, China was a lucrative market, I would argue that even as China was attempting to grow, an allowance of sudden and increased access would have resulted in even poor management than that which was seen, in terms of poor customer service. Retaining control and restricting access then, was the only way for the Chinese state to manage “orderly” growth. The only other method to do this would have been to unrestrictedly open up to foreign companies, and I shall discuss why this would be a bad idea below. In summary, the free market allows for greater access, but greater access comes with its own set of conditions (freedom of information and media, corporate malaise and greed) which states need to be wary of.

Affordability

Once again, it is prima facie clear that the free market allows for more price competition and therefore seems to be to the benefit of the consumer. Once again however, two caveats. First is the fact that China did not just sit back and watch the telecommunications industry spiral out of control. It responded to the people by re-centralizing the sector and attempted to ensure that pricing remains low enough for consumers. This is in direct contrast to the US system, and this is the second caveat here. The unregulated system in the US has allowed corporations to continue to find ways to be profitable, leading to “more choices” for the consumer, but with a steep price (Robehmed, 2017). For example, while the increase in
streaming services in the US has led to more choices for the consumer than ever before, there are also more streaming services that the user needs to subscribe to, thus eventually paying more. This shows clearly that while monopolies can lead to poor pricing, the free market can lead to an excessive splintering of products, requiring consumers to end up paying a lot more for a multitude of services.

At the end of the day, consumers are faced with the decision of having one expensive service or several small cheap services that end up costing the same, and here I would argue that a state led system is actually better because while it may take a longer time for the price to normalize to a reasonable level, it is unlikely for it to spiral out of control.

Security

Finally, we must consider the security aspect of the telecommunications industry. As a core industry, the security aspect of allowing industry to dominate cannot be overlooked (Newsham, 2018). As a one-party state, China creates and manages several restrictions on the flow of information, as this is crucial to its continued survival (Shambaugh, 2013).

More importantly however, it is important to note the global position of the US and China at the time the industry was growing. In the 1920s, the US was already a global power, having just been on the victorious side of WWI. This would be amplified with the allied victory in WWII, meaning the US had little to fear by way of foreign countries coming in and dominating this core sector of industry. The market competition was thus predominantly domestic, allaying any security concerns the state might have of losing control of the radio waves which were previously in the hands of the navy.

China in the 1980s was very different. It was a nascent economy, with the USA and Japan economic superpowers that it felt the need to protect against. As such, consolidating the core asset was something that was vital to state interests to ensure its own continued power. Had China completely liberalized the industry, it would be my view that foreign companies could easily have come in and taken up this core asset, which may have resulted in regime collapse, similar to how it did in the Soviet Union, where excessive market liberalization led to the collapse of control of the Communist Party of the Soviet Union.

Conclusion

It is quite clear that in terms of the consumer, market driven policies tend to fare better in providing better services and competitive pricing. At the same time however, it is important to note that the
telecommunications industry is vital to state interests as well and these cannot be overlooked when trying to provide for the consumer. China can clearly aim to liberalize slightly more while retaining core control, and that might be the ideal win-win situation for both the consumer and the state.
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