

**TESTIMONY OF THE TELECOMMUNICATIONS INDUSTRY ASSOCIATION
(TIA) REGARDING INVESTIGATION 332-491: CHINA, GOVERNMENT
POLICIES AFFECTING U.S. TRADE IN SELECTED SECTORS**

**Before the
U.S. International Trade Commission**

October 30, 2007

Good morning. My name is Mike Nunes, and I am Director of International and Government Affairs for the Telecommunications Industry Association (TIA). TIA is a leading trade association for the information and communications technology (ICT) industry, with approximately 600 member companies that manufacture or supply the products and services used in global communications. TIA represents its members on the full range of public policy issues affecting the industry, forges consensus on industry standards, and helps its members develop new business in foreign markets. Together, our industry generates revenues exceeding \$923 billion in the United States and over \$3 trillion worldwide.

TIA thanks this distinguished Commission for the opportunity to provide its views on the U.S. telecommunications equipment trade with China.

Trade and investment trends

The Chinese market holds the promise of opportunities and continued growth for TIA member companies. China is the 6th largest export market for U.S. telecommunications equipment (Appendix, table 1). In 2006, U.S. exports to China of such products reached \$826 million¹, representing an increase of 17 percent from \$703 million in 2005. During the period 2003 to 2006, U.S. telecommunications exports to China increased by a total of 37 percent. With respect to the product mix, in 2006 the U.S. exported mainly component parts, with telegraphic apparatus leading the top 10 export product list at \$259 million. Also included on the top 10 list were coaxial (\$27 million) and fiber optic (\$21 million) cables, and part thereof. The U.S. only exported \$3 million worth of finished cellular telephones to China during 2006.

In contrast, the U.S. imported nearly \$11 billion worth of cell phones, topping the list of telecom equipment imports from China in 2006. In all, U.S. telecom equipments imports from China totaled \$18 billion² in 2006, making China the leading U.S. source market. Such imports rose 27 percent in 2006, up from \$14 billion in 2005 (Appendix, table 2). During the period 2003 to 2006, U.S. imports of telecom equipment from China increased by over 200 percent.

The whopping U.S. telecom equipment trade imbalance with China, approximately \$17.3 billion in 2006, is indicative of the overall U.S.-China trade relationship, where the total deficit in U.S. trade with China approached \$164 billion in the first eight months of 2007.

¹ USITC, dataweb.

² Ibid.

However, the U.S. telecom equipment trade relationship with China is complex and should be examined with a view to the overall technology market in China, much of which is comprised of U.S. and other foreign technology companies that are directly invested in the market. Indeed, China has become the world's largest recipient of foreign direct investment (FDI). In the first four months of 2006, China saw FDI of \$18.48 billion, up 5.76 percent over the same period in 2005.³ In the first four months of 2006, 12,639 foreign firms were authorized to be established in China.⁴ According to China's Commerce Minister, the value of foreign direct investment in China has surpassed \$700 billion since opening its market to foreign companies.

An increasing share of such investment is derived from the ICT sector. In 2006, the high technology sector contributed approximately 4.75 percent to China's Gross Domestic Product (GDP), up from 2.35 percent in 2000. A large share of the sector's output is attributable to foreign companies.⁵ Approximately 50 percent of high tech's GDP contribution comes from the manufacture of communications and electronic equipment (ICT). For comparison purposes, the remaining balance came from computer manufacturing (30 percent), medical equipment (6 percent), and other (14 percent). In 2006, China's total exports of ICT products reached \$214 billion, up from only \$37 billion in 2000. China's 2006 high tech exports represented approximately 29 percent of China's total export volume, as compared to 5 percent in 1993.

According to a Chinese official, much of the Chinese surplus in high-tech trade is created by U.S. and other foreign-based companies, with foreign enterprises accounting for over 75 percent of high-tech export value in 2007.⁶ Reportedly, U.S. companies top the list of China's high-tech companies, together accounting for approximately \$30 billion worth of exports in 2005. Recently, many of these companies have experienced increased sales in the Chinese domestic market as demand for U.S. technology products, including ICT, increases, effectively reversing the propensity of foreign invested firms in China to re-export finished products back to the U.S.⁷ Such interesting trends are worthy of further study.

Market trends and opportunities

Increasing demand for ICT products in China is creating opportunities for U.S. firms. With respect to China's overall telecom market, the country has the largest wireless and fixed line markets in the world, both of which have recorded huge increases during the past five years. Those gains were the result of a substantial investment in the fixed line and wireless infrastructure, a total of \$183 billion since 2000, including \$25 billion in 2006. These investments had a dramatic impact on the market. During the past five years, the total number of telephone connections (landlines plus wireless) more than doubled to 835 million from 323.8 million in 2001 (Appendix, figure 1). Even though penetration

³ Xinhua News Agency and China Ministry of Commerce, 2006.

⁴ Ibid.

⁵ China trade official, Shenzhen, China, 2007.

⁶ Ibid.

⁷ Ibid.

remains lower than in many other countries, China now has the largest and one of the best developed landline and wireless networks in the world.

In addition to these investments, China plans to spend \$1.8 billion through 2010 to expand its Internet protocol (IP) infrastructure. Substantial investment in third generation (3G) wireless infrastructure is also anticipated during the next four years. Licenses originally scheduled to be awarded in 2006 are now scheduled for 2007. TD-SCDMA, China's home-grown 3G standard, was named the national standard by the Ministry of Information Industry. A national TD-SCDMA license will be the first to be awarded, although the exact timeframe remains unclear. China will also issue national licenses for the CDMA2000® and WCDMA technologies. To expand their subscriber base and position themselves for the 3G rollout, carriers cut their wireless rates in 2006. China Mobile and Shanghai Unicom each slashed their wireless fees by more than 60 percent. Those steep reductions contributed to the increase in wireless subscribers (Appendix, table 3).

TIA estimates the total number of connections in China will increase to 1.3 billion in 2010, a 425 million increase over 2006 (Appendix, figure 1). To accommodate the increase in traffic that these new connections will generate, China Telecom and China Netcom are building an optical cable network that will initially connect China with Taiwan, South Korea and the United States. The optical cable network, scheduled to be completed in 2008, will have a bandwidth of 960 Gbps.

Finally, we see significant growth opportunities in China's broadband market, where the number of subscribers is expected to accelerate significantly, approaching 130 million by the year 2010 (Appendix, figure 2).

Market impediments

Despite such promising market trends and opportunities, a number of significant impediments exist in the market, many which directly affect TIA members. Despite some improvement in the U.S.-China trade relationship, which is apparent in the growth of U.S. exports to the market, we remain concerned about lack of progress in the several key areas, which are discussed in detail below.

Indigenous Innovation

China's "indigenous innovation" policy was articulated in China's Five Year Program issued last year. The policy is inherently protectionist, and anecdotal evidence suggests that some U.S. companies have lost bids in China's government procurement process as a result of this policy. TIA is actively involved in this issue, supporting the U.S. Information Technology Office (USITO) in its efforts, which include developing position papers and letters, holding seminars and panel discussion throughout China, and meeting with government representatives. USITO's Indigenous Innovation white paper is being used as a platform for developing the agenda for an upcoming "Innovation Seminar," which will be held on the margins of the Strategic Economic Dialogue (SED) in Beijing in December.

Telecommunications Services

While a number of value-added telecommunications services are technically open to foreign competition through joint ventures, to date MII has effectively blocked the foreign provision of value added services by maintaining high-entry barriers, both through its licensing authority and its ability to define narrowly the scope of services included in each value-added category. In addition, the process for reviewing and approving applications is opaque, discretionary and conducted with a conservative view that the listed services represent a ceiling, rather than a floor, for what MII is inclined to approve. Those foreign-invested ventures in telecom services that do receive approval are subject to onerous restrictions, such as geographic restrictions, which keep ventures from selling their services outside one city or even a single district of one city, and strict joint venture requirements, in which foreign joint venture participants may not bill customers directly for telecom services, control the billing process, or collect payment. They cannot provide assurances of service quality, and their ability to manage network security is severely constrained by a confusing legal regime around encryption technologies.

In addition to the market access barriers discussed above, a high capitalization requirement is a significant restriction for most companies. Other impediments to the provision of telecom services in China include regulatory ambiguity; inconsistent interconnection rights; restrictive personnel requirements, such as lack of representation by foreign boards of directors; and licensing restrictions for basic services.

With these impediments in mind, TIA urges the Chinese government to (1) lower the capital requirement for investment in basic services; (2) eliminate or change the MII "Catalogue of Telecommunication Service Categories" such that every new service offering by foreign providers is not subject to review and approval by MII; (3) permit joint ventures to be established as "inter-provincial" value-added service enterprises; (4) permit joint ventures to manage the end-to-end customer experience, including billing; (5) permit joint ventures to hire qualified staff using clear qualification criteria, as opposed to using quotas from the two principals; (6) permit joint ventures to partner with Chinese investors other than the existing state-owned enterprise carriers; and (7) to comply with its Reference Paper commitments to establish an independent regulator.

Technology Neutrality

We urge the Chinese government to subscribe to the principle of technology neutrality on the part of the regulator. Technology neutrality is a key principle for regulated sectors like telecommunications. Markets and innovation benefit most when ICT manufacturers and suppliers engage in demand-driven competition, standards are openly and competitively developed, and governments do not interfere to choose technology winners and losers.

With respect to technology neutrality, we note that Chinese Vice Premier Wu Yi stated on April 11, 2006, that China would adopt a technology neutral approach in its 3G policy, and that in May 2007, MII approved the use of global wireless standards WCDMA and CDMA2000®, in addition to China's home-grown 3G standard, TD-SCDMA. However,

the Chinese government has not yet signaled when licenses will be issued or how many will be awarded. Accordingly, TIA reiterates its position that the decision to provide 3G services should be a commercial one, that the regulator should be agnostic regarding technology choice, and that China's 3G policy, including timing and number of licenses should be announced as soon as possible.

Factory Inspection

We have been informed that the China National Certification and Accreditation Administration (CNCA) has issued a new policy, which clearly indicates that in principle, all initial factory inspections should be conducted by the Chinese certification organizations themselves. Only under extreme circumstances (e.g., a delay in receiving the products would impact a major project in China), will CNCA allow the accredited certification organizations to subcontract the initial factory inspection to a foreign organization. This action creates serious delays for U.S. manufacturers in obtaining the CCC certificate, due to China's cumbersome internal approval process for overseas trips and related U.S. visa process issues. (It often takes months to schedule visa interviews.)

Certification

We note that China has engaged within the Worldwide System for Conformity Testing and Certification of Electrical Equipment (IECEE) Conformity Body (CB) scheme for safety test report acceptance, which is essential for market access and to eliminate redundant testing of products at multiple laboratories. However, laboratories in China are not making the best use of these international programs, requiring additional samples and repeat testing, resulting in substantial delays. The product testing and certification process in China is significantly more difficult than in other markets, which increases the cost of imports. Additionally, we note that China has opted out of the CB scheme for electromagnetic compatibility (EMC) testing, with the result that such testing must be done in-country. EMC requirements emerged out of a collective international effort and most of the world participates in the EMC component of the CB scheme and accepts CB scheme test reports generated by other participating members. We encourage the Chinese government to improve the application of the IECEE CB Scheme by accepting CB Scheme reports by national laboratories and eliminating the need for additional samples and redundant testing. We would also welcome China's participation in the IECEE CB Scheme for EMC.

Standards:

China has uneven and unclear requirements for inclusion of foreign-invested companies and institutions in technical committees that devise nationally adopted standards. TIA urges the Chinese government to publish a standard that indicates clearly how technical committees are constituted and who may participate, as well as the rights of participants. TIA recognizes that China has made significant strides to conform to their obligations under the WTO TBT Agreement to base their technical regulations on international standards. However, we are concerned that China continues to define "international standards" as only those developed in international forums like the ISO, IEC and ITU. China's narrow interpretation and acceptance of "international standards" is inconsistent with the spirit of Annex IV of the TBT Agreement, and negatively affects many U.S. and

other global manufacturers that rely on international standards developed outside of the Geneva-based organizations. China is currently in the process of revising its "Standardization Law."

Imports and Import Discrimination

China has met its commitments to the WTO Information Technology Agreement (ITA) by reducing tariffs on the great majority of information technology products to zero between the years 2002-2004. However, we urge the government to include Multi-Chip Packages (MCP) in the products to which zero-tariff status has been extended. MCPs are simply a more advanced form of integrated circuits, which already have received zero-tariff treatment. With respect to import discrimination, in key telecommunications sectors, China continues to struggle with economic inefficiencies, exacerbated by preferences for domestic industries and pricing and procurement practices that discriminate against imports. Specifically, it appears that in some telecom procurements, companies are ignoring their published criteria for bid evaluation, resulting in the selection of "national" champions, which are state-invested enterprises. As a result of these practices, importers have been excluded from the market.

Conclusion

TIA thanks the Commission for this opportunity to testify on U.S.-China trade relations. As you can see, China is an important market for TIA member companies. China's market opening and investment on telecommunications infrastructure have created significant business opportunities. In addition, the country's rapid economic growth, large population, and rapid uptake of next generation products and services also make China an appealing market. As discussed, however, significant impediments remain. TIA works closely with the U.S. government, through the SED process, for example, with the goal of creating a favorable trade environment. We very much look forward to this timely study, and we would be happy to work with you and your staff throughout the project.



APPENDIX

Table 1
U.S. Exports of Telecommunications
Equipment by Leading Countries
(\$ Millions)

Country	2004	2005	Percent Change
Netherlands	1,318	1,793	36.0
Canada	1,727	1,683	-2.5
Mexico	1,747	1,672	-4.3
Japan	1,246	1,035	-16.9
United Kingdom	967	839	-13.2
China	664	703	5.9
Germany	484	523	8.1
Hong Kong	479	443	-7.5
South Korea	504	440	-12.7
Australia	363	438	20.7
Top-10 Total	9,499	9,569	0.7
EU Total	3,924	4,441	13.2
World Total	15,461	15,757	1.9

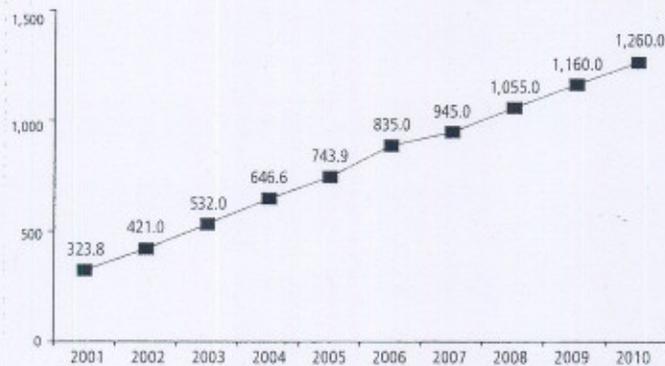
Source: TIA's 2007 Telecommunications Market Review and Forecast based on U.S., Department of Commerce data

Table 2
U.S. Imports of Telecommunications
Equipment by Leading Countries
(\$ Millions)

Country	2004	2005	Percent Change
China	9,203	14,057	52.7
South Korea	8,619	6,378	-26.0
Mexico	6,048	5,508	-8.9
Malaysia	2,625	4,485	70.9
Canada	1,883	2,291	21.7
Thailand	1,135	1,890	66.5
Japan	1,413	1,575	11.5
Taiwan	965	1,311	35.9
Sweden	775	1,164	50.2
Brazil	342	737	115.5
Top-10 Total	33,008	39,396	19.4
EU Total	2,576	3,378	31.1
World Total	36,783	43,804	19.1

Source: TIA's 2007 Telecommunications Market Review and Forecast based on U.S., Department of Commerce data

Figure 1 Telephone Connections in China (Millions)



Source: TIA's 2007 Telecommunications Market Review and Forecast

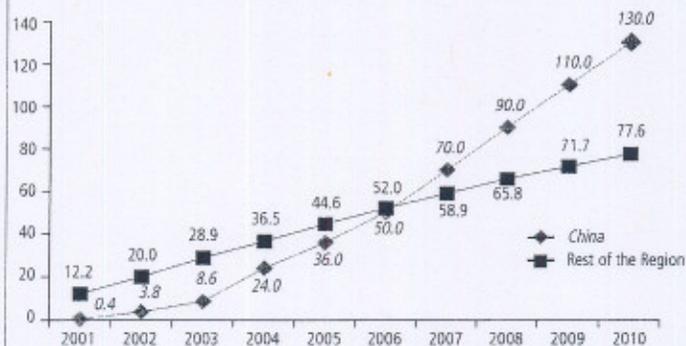
Table 3

Wireless Subscribers in Asia/Pacific (Thousands)

Country	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
Armenia	26	71	114	203	320	440	550	650	750	850
Australia	11,132	12,575	14,347	16,480	18,420	19,000	19,400	19,700	20,000	20,200
Azerbaijan	730	794	1,057	1,457	2,242	3,000	3,500	4,000	4,500	5,000
China	144,810	206,620	268,690	334,824	393,428	450,000	530,000	610,000	690,000	770,000
Georgia	301	504	711	841	1,459	1,750	1,900	2,050	2,200	2,350
Hong Kong	5,776	6,396	7,349	8,214	8,635	8,700	8,750	8,800	8,850	8,900
India	6,432	12,688	26,154	47,300	76,000	129,000	175,000	215,000	260,000	300,000
Indonesia	6,521	11,700	18,800	30,000	46,910	60,000	72,000	84,000	95,000	105,000
Japan	74,819	81,118	86,655	91,474	94,745	98,000	101,000	104,000	107,000	110,000
Kazakhstan	582	1,027	1,331	2,759	4,955	5,800	6,500	7,200	8,000	8,500
Kyrgyzstan	27	53	138	263	542	800	1,000	1,200	1,400	1,600
Malaysia	7,385	9,053	11,124	14,612	19,545	21,000	22,000	23,000	24,000	25,000
New Zealand	2,288	2,449	2,599	3,027	3,530	3,700	3,825	3,925	4,000	4,050
Pakistan	812	1,699	2,404	5,023	12,771	20,000	25,000	30,000	35,000	40,000
Philippines	12,159	15,383	22,510	32,936	32,810	40,000	45,000	50,000	55,000	60,000
Singapore	2,859	3,345	3,477	3,861	4,385	4,475	4,550	4,625	4,700	4,775
South Korea	29,046	32,342	33,592	36,586	38,342	40,000	41,500	43,000	44,500	46,000
Taiwan	21,786	24,391	25,800	22,760	22,171	22,300	22,450	22,600	22,750	22,900
Tajikistan	2	13	48	135	240	350	475	600	725	850
Thailand	7,550	16,117	24,864	27,379	31,000	33,500	36,000	38,500	41,000	43,500
Turkmenistan	8	8	9	50	100	150	200	250	300	350
Uzbekistan	128	187	321	544	720	820	920	1,025	1,125	1,225
Total	335,179	438,533	552,094	680,728	813,270	962,785	1,121,520	1,274,125	1,430,800	1,581,050

Source: TIA's 2007 Telecommunications Market Review and Forecast

Figure 2 Broadband Subscribers in Asia/Pacific (Millions)



Source: TIA's 2007 Telecommunications Market Review and Forecast



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