Chinese Handsets Get A Boost

by Paul DiPaola

Chinese policy makers have set out to nurture and support Chinese handset makers in the hope that some of them will ultimately emerge to compete in the domestic market. Given the strong position that MNCs already have achieved in China's GSM handset market, the embryonic CDMA handset market presents the best hope for Chinese handset makers. To accomplish this, Chinese regulators must create a vibrant CDMA wireless services market that provides Chinese handset makers with a large subscriber base, and maintain an environment in which the most hardy Chinese handset makers can build their capabilities and prosper.

The process of creating a vibrant domestic CDMA services market has begun. In 2000, the Ministry of Information Industry (MII) issued a CDMA licence to China Unicom, with hopes that it would emerge as a stronger No. 2 player. Unicom formally launched its CDMA commercial service on Jan 8, 2002, with an initial three-month pilot number release of 700,000 subscribers.

For Unicom, the launch of a CDMA network provides an opportunity to dramatically change the direction of its business. In a market that will ultimately have four competing mobile players, the majority of the industry's profits will go to the market leader and a strong follower with a disproportionate share of the high usage users. To date, Unicom has used its GSM network successfully to address price conscious consumers with lower priced value propositions and flexible prepaid options. In the long run, Unicom must increase its share of higher usage, higher margin customers if it is to build a sustainable business.

Given their high usage, these customers value higher levels of customer service, they are interested in having the latest handsets, and they also tend to be more comfortable with adopting new technologies. Therefore, Unicom will have to market CDMA's technological advantages over CMCC's GSM network. It will have to aggressively roll out CDMA's high-speed data capabilities in advance of CMCC's. It will have to offer excellent customer service and a wide selection of handsets. Ideally, these handsets would be subsidised to reduce the switching costs of high-end users already using the competitor's service. If Unicom is successful, China will become one of the world's largest markets for CDMA handsets with an estimated 50 million CDMA subscribers by 2005.

The MII has issued licences to 19 CDMA handset makers, 18 of which are local manufacturers. Motorola is the only foreign MNC amongst them. Success in the handset business has historically been dictated by four factors: access to handset technology, low-cost product design, comprehensive retail coverage, and brand building. For Chinese handset suppliers, the technology barriers have been dramatically reduced. Leading chip manufacturers are making core components readily available to local handset makers. Moreover, MNCs without licences are ready to provide the necessary technology through joint ventures or sell the technology outright.

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As a result, the 18 Chinese handset manufacturers are competing on the basis of low-cost product design, comprehensive retail coverage, and brand building. However, the number of licensed vendors is far greater than what the market can support. In a span of five years, the Chinese handset market will resemble most Asian handset markets that are more matured. Three players will likely account for 80% of the market—one or two of them are likely to be a Chinese manufacturer.

Currently, there are three types of aspirants: pure play handset makers such as Bird and Kejian, network infrastructure manufacturers such as Zhongxing and Datang, and consumer electronics manufacturers such as Haier, Hisense, TCL and Legend. Given the importance of low-cost product design, comprehensive retail coverage, and brand building, it is likely that a winner will come from the ranks of the consumer electronics manufacturers as they enter the market already in possession of these critical success factors.

The winning Chinese handset manufacturers will need to focus on low-cost product design while tailoring channel and marketing investments to meet the needs of distinct customer segments. Only then would the Chinese regulators have met their goals for a strong domestic wireless handset industry.