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presents:

SOEs and competition policy in China

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Since China's Anti-Monopoly Laws ("AML") bill passed in 2008, competition policy in China is thoroughly analyzed by antitrust practitioners around the world. The rulings by the Chinese antitrust enforcement agencies are often compared with rulings by competition authorities in developed economies. These comparisons may not properly take into account the major distinction of the Chinese economy. Namely, China's economy is still in the transition from a planned economy to a market economy. As such, state owned enterprises ("SOEs") play a much bigger role in China than in developed economies.

Given the important role played by the SOEs, Article Seven of AML provides that:

"With respect to the industries controlled by the State-owned economy and concerning the lifeline of national economy and national security or the industries implementing exclusive operation and sales according to law, the state protects the lawful business operations conducted by the business operators therein. The state also lawfully regulates and controls their business operations and the prices of their commodities and services so as to safeguard the interests of consumers and promote technical progresses." In addition, Article Seven of AML stipulates that *"The business operators as mentioned above shall lawfully operate, be honest and faithful, be strictly self-disciplined, accept social supervision, shall not damage the interests of consumers by virtue of their dominant or exclusive positions."*

Article Seven of China's AML has received considerable amount of criticism as it does not clearly stipulate which are those industries concerning the lifeline of the national economy and national security. While SOEs dominate in these industries, SOEs are also active in many arguably nonstrategic industries, such as real estate development.

This paper examines the SOEs and their effect on China's competition policy and projects future relations between SOEs and antitrust policy in China.

I. BACKGROUND

Among the major economies in the world, the Chinese economy is the only one that is still in transition from a centrally-planned economy to a market economy. A unique feature of this transitional economy is the overwhelming presence of SOEs. Different levels of government supervise SOEs. The largest SOEs, such as the three big oil companies (Sinopec, China National Petroleum, and China National Offshore Oil), are under the supervision of the State-owned Assets Supervision and Administration Commission (SASAC), whereas the large state owned financial companies, such as the four major national banks (Industrial and Commercial Bank of China, China Construction Bank, Agricultural Bank of China, and Bank of China), are regulated by the China Banking Regulatory Commission.

SOEs are dominant in many strategic industries such as banking, insurance, telecom, transportation infrastructure, oil and gas, and utilities. Table 1 presents statistics of Fortune Global 500 companies in China in 2012. Among the 73 Chinese firms listed on the Fortune Global 500, only five firms are privately owned companies and the highest rank by a private company is 242. On the other hand, 68 SOEs are included in the Fortune Global 500 ranking, among which, 43 SOEs are administered by the SASAC.¹

¹ See SASAC press release at <http://www.sasac.gov.cn/n1180/n14200459/n14669156/index.html> (in Chinese).

Table 1: Statistics of Fortune Global 500 Companies in China in 2012

	Number	Highest rank
SOEs	68	5
Under supervision by SASAC	43	5
Private	5	242
Total	73	

Sources: Fortune magazine's 2012 Global 500.
<http://money.cnn.com/magazines/fortune/global500/>

Table 2 presents the statistics of Top 500 Enterprises in China in 2012. SOEs account for 310 and private companies account for 190 in the ranking. SOEs not only dominate in terms of quantity, but also in size. The top 30 companies are all SOEs. In addition, SOEs are very active in merger and acquisition (M&A) activities. 110 SOEs in the ranking conducted 918 M&A activities, while 44 private companies conducted 193 M&A activities. SOEs accounted for 86 percent of the 1111 reported M&A activities among the top 500 Enterprises in China.

Table 2: Statistics of 2012 Enterprise Top 500 in China

	Number	Top Rank	Merger and Acquisition
SOEs	310	1	918
Private	190	32	193
Total	500		1111

Source: 2012 Enterprise Top 500 in China.
http://www.cec-ceda.org.cn/more_new.php?sid=6

Despite its dominant position in the market, and its active role in M&A, very few SOEs are being challenged by the three main AML enforcement agencies, namely Ministry of Commerce (“MOFCOM”), the National Development and Reform Commission (“NDRC”), and the State Administration for Industry and Commerce (“SAIC”) since the inceptions of AML in China. For example, MOFCOM has issued a number of rulings regarding M&A, but only one restriction involved an SOE (e.g. GE/ Shenhua case).²

A number of reasons explain this inactivity by the AML enforcement agencies against SOEs. First, Article Seven of the AML provides SOEs with certain legal protections. For example, if a SOE operates in an industry concerning the lifeline of national economy and national security, it cannot be investigated by AML agencies. At this moment, there is no clear definition of strategically important industries in the AML statute.

Second, SOEs have a very deep connection with various levels of government agencies. These deep political connections make it harder for AML enforcement agencies to prosecute anticompetitive practices by SOEs.

² See MOFCOM press release at <http://fldj.mofcom.gov.cn/ztxx/ztxx.html> (in Chinese).

Third, the executives of large SOEs are at the vice minister level in the Chinese bureaucratic system, which ranks SOEs above the AML enforcement agencies, such as MOFCOM's antimonopoly bureau. Chinese political culture makes it therefore very difficult for a lower ranked agency to prosecute a higher ranked agency.

II. New Developments

Several recent developments indicate a changing attitude towards SOEs by the AML enforcement agencies. The first widely reported antimonopoly case against an SOE in November 2011, the investigations against China Telecom and China Unicom over suspected price-discriminations in the broadband market, resulted in an announcement by the two companies that they would increase broadband speeds and reduce service charges, in order to settle the investigations by NRDC.³ These recent developments are encouraging, because it seems that SOEs are under scrutiny by AML enforcement agencies. These changes are mainly driven by the following crucial transformations.

First, the Chinese government recognizes that SOEs need to improve efficiencies in order to improve the overall efficiency in the economy. As China is moving away from a low income country to a medium income country, future growth in the economy will need to come from efficiency gains, rather than from further increases in capital and labor inputs. Thus, improving efficiencies at the SOEs level is critical to sustaining future growth. The main objective of the AML is to increase efficiencies in the economy by promoting competition. Therefore, the government has incentives to use AML to increase competition in the market and to improve the efficiency of SOEs.

Second, public opinion plays an important and increasing role in government decision-making. For example, the investigation by NDRC is prompted by public dissatisfaction with SOEs monopoly in the telecom market, which results in poor service quality and higher prices.

Third, competition between SOEs may lead to increasing roles by AML enforcement agencies in the future. Although, SOEs are all state owned, the management of SOEs enjoy considerable and exercisable power. In addition, SOEs are under supervision by different levels of the government. Hence, competition between SOEs can be very intense sometimes. AML enforcement agencies will therefore face growing demand in the future from competing SOEs to maintain a level of competitiveness.

Fourth, competition from private and foreign owned firms in China will influence how AML agencies handle SOEs. Private and foreign owned companies are the fastest growing sectors in China. Both private and foreign owned companies have recognized the power of AML in order to protect their own interest.

Fifth, as SOEs become multinational companies, SOEs face examination by competition authorities from other jurisdiction. As part of SOEs growth strategies, more and more SOEs adopt a "go abroad" policy by investing in developed economies around the world. The expansion of SOEs in developed economies will bring SOEs under supervision by foreign competition authorities. For example, the European Union Competition Commission carefully

³ See press release at China Telecom website:
http://www.chinatelecom.com.cn/news/02/t20111202_80346.html

reviewed the proposed acquisition of Elkem AS by China National Bluestar Group Co., Ltd,⁴ and the joint venture agreement between Sinochem Group (Sinochem, China) and Koninklijke DSM N.V. (DSM, Netherlands)⁵ in 2011. The lessons learnt by SOEs from acquisitions in developed economies will affect their behavior in the domestic market as well.

III. Conclusion

China's competition law is a key piece of legislation, which aims to build a market-based competitive economy. At its early stage, China's AML enforcement agencies have been trying to standardize competition policy. At this moment, SOEs have not been aggressively challenged by AML enforcement agencies. However, as market participants gain a growing awareness of AML, SOEs will face increasing pressure from the public and AML enforcement agencies.

Given the speed at which AML enforcement agencies are expanding their capacity and the greater use of AML by market participants, it is likely that antimonopoly cases against SOEs will accumulate.

⁴ *Case COMP/M.6082 China National Bluestar/Elkem*

⁵ *Case COMP/M.6113 DSM/Sinochem/JV*