

Chinese operators reap the rewards of rising smartphone penetration

"China has an unusually large number of potential first time smartphone buyers, and that's not lost on us," Apple CEO Tim Cook [told investors this week](#). He added that the firm had recently lowered the price of the iPhone 4 in China to make it "even more attractive to those first-time buyers."

China was a bright spot in an otherwise [mixed set of financials](#) for the iPhone maker, its Greater China unit (which includes Hong Kong and Taiwan) the only region to increase sales over the sequential quarter. The region contributed \$8.2 billion in revenue, "our best quarter ever in Greater China," according to Cook, accounting for about 19% of Apple's total.

And yet Apple is still a minor player in China's vast and fast-growing smartphone market, with the country's (and world's) largest mobile operator, China Mobile, not even an official Apple distributor. And despite Apple now being able to discount earlier models, the iPhone's premium price points mean it will likely struggle to grow its market share beyond the estimated 10% it currently commands.

Instead, the market is dominated by Android, which powers about four in five smartphones in China, and has been the driving force behind China becoming the world's largest smartphone market. Among the Android vendors, Samsung – the world's largest handset maker – [is the market leader](#), but domestic vendors such as Huawei, ZTE, Lenovo and Coolpad are all major players. The choice is often vast: China Telecom, for example, claims to have a portfolio of 380 smartphone models on its books.

The three local mobile operators – China Mobile, China Unicom and China Telecom – are benefiting greatly from the country's smartphone revolution, as rising smartphone penetration accelerates uptake of their respective 3G services. As a result, all three players have enjoyed strong revenue growth over the last two years with 2012 sales rising by 6.1% at China Mobile (to CNY560.4 billion), by 19% at Unicom (to CNY248.9 billion) and by 15.5% at China Telecom (to CNY283.1 billion). China Telecom was the only one to report lower annual net profit than a year earlier, significantly linking this to the ["short-term pressure" on profitability](#) related to promoting the iPhone, which it began offering in March 2012.

But it also cited the iconic device as responsible for a significant uptick in mobile data traffic and revenue; China Telecom's data traffic almost tripled in 2012, while data revenue surged almost 50% to CNY43.6 billion and now accounts for 47% of revenue on the mobile side.

It is a similar picture at China Unicom, which reported a 185% annual increase in data usage by 3G smartphone users in 2012 - the average user consuming 256MB a month. This enabled 3G to become Unicom's largest revenue contributor in 2012, surpassing 2G service revenue in Q4 2012.

Unicom is already selling more smartphones than its rivals and has recently said it is [targeting sales of 90 million this year](#), which would be a 50% increase on the 60 million shipped in 2012. While Unicom has deals in place with international vendors such as Apple, Samsung and Nokia, its smartphone growth is coming mainly at the low end; it responded to the loss of its exclusive

hold on the iPhone last year by offering low-cost smartphones priced at CNY1,000 (\$160) or below to boost the “quality-to-price ratio and competitiveness of its terminal products.”

As well as boosting smartphone penetration, this focus has allowed Unicom to lower its smartphone subsidies relative to 3G income. Its 3G handset subsidy as a percentage of 3G service revenue dropped from 17.7% in 2011 to 10.2% last year.

The situation at China Mobile is more complex due to it using the homegrown TD-SCDMA standard for its 3G network, which requires specially adapted devices. Partly as a result, China Mobile enjoys nowhere near the dominance in the 3G space as it does in the market overall; its share of the total market was 64% at the end of 2012, but only 38% in terms of 3G connections. 3G accounted for 12% of China Mobile's connections base at year-end, compared to 32% at Unicom and 43% at China Telecom.

However, China Mobile has recently talked up a “thriving” TD devices ecosystem, noting that “mainstream chipset and device manufacturers [are] involved in R&D of TD products [and that] chipset manufacturing technology, power consumption and product quality [is] equitable with that of competing standards.” One notable vendor supporting the standard is Nokia, which has released [several TD versions of its flagship Lumia smartphone](#) range for the operator.

China Mobile launched 242 TD devices and 138 smartphones in 2012; it shipped 56 million TD devices in total, about 60% of which were smartphones. It is [targeting 120 million TD device sales this year](#), with smartphones estimated to account for 80%.

The market leader is already looking ahead to the forthcoming launch of its TD-LTE 4G network, signing up compatible devices from the likes of [Huawei, HTC, LG and ZTE](#). It will reportedly [launch a major 4G terminal tender](#) this month, aiming to buy 160,000 TD-LTE devices.

		China Mobile	China Unicom	China Telecom	Total
Smartphones					
Shipments (million)	2012	34	60	41	135
	2013E	96	90	-	
% 3G devices	2012	60%	-	60%	
3G					
Technology		TD-SCDMA	HSPA	EV-DO	
Connections (million)	2012	87.9	76.5	69.1	233.5
% 3G	2012	12%	32%	43%	21%
Base stations	2012	280,000	331,000	-	

China, smartphone shipments and 3G connections by operator

Source: *Wireless Intelligence, company data*