Chapter 3: Chunghwa Telecom Privatization Case

In an attempt to be practical in this study, we chose to examine Chunghwa Telecom’s privatization case in the hope to extract from this experience effective lessons that can be applicable for the government of Burkina Faso and ONATEL. Hence, this chapter emphasizes analyzing and understanding Chunghwa Telecom privatization experience, under its aspects of methods and formulations of business strategies.

1. Chunghwa Telecom General Overview

Chunghwa Telecom Company Limited is Taiwan's largest information and telecommunications services provider. It was incorporated in 1996 as a state owned enterprise with a registered capital at NT$96.477 billion. Its offers cover all the telecommunications services such as city calls, long distance calls, international calls, GSM data communication, internet services, broadband networking, satellite communication, intelligent network, mobile data and multimedia broadband to both residential and business customers in Taiwan. Chunghwa Telecom business lines include fixed line phones, mobile phones, and Internet and data services (Chunghwa Telecom website).

Since August 2005, the government’s shares ownership in the firm dropped below 50% with the sale of 17% shares by American Deposit Receipts (ADRs). Consequently it is now a privatized firm. It is listed on the Taiwan Stock Exchange and 25.5% of its outstanding shares are also traded as ADRs on the New York Stock Exchange. Currently, it has a workforce of 27,409 employees. According to its reported operating results for 2005, Chunghwa Telecom’s total fixed line subscriber base stood at approximately 13.3 million with revenue of NT$66.3 billion by December 31, 2005. As for the figures for the mobile services, the firm announced that at the end of 2005, the total number of mobile subscribers was 8.16 million with revenue of NT$3.2 billion. The company also reported 4.1 million subscribers and 3.65 subscribers respectively for Internet and ADSL by December 31, 2005 with revenue of NT$42.1 billion for these two services (Chunghwa Telecom, March 30, 2006).
2. General description of Chunghwa Telecom Privatization Process

Privatization and liberalization are two linked processes. They frequently go hand in hand. Countries reforming their national monopolies can choose to privatize these monopolies first before liberalizing the industries in which they operate. In this case, the process consists of changing the state monopolies into private monopolies in a first step. After which the liberalization of these industries is undertaken in order to bring in competition. This way of conducting economic reforms can have the advantage of speeding up the process of ownership transfer. However, some countries choose the option of liberalizing first before conducting privatization. In its attempt to reform the telecommunications sector, the government of Taiwan opted for the latter approach to implement this reform. This choice was partly motivated by the strong opposition of the Chunghwa Telecom employees to any idea of privatization, explains Dr. Mao. The opening up began with the mobile telephone sector. The wireless services were deregulated in 1997. The liberalization of this segment led to an increase competition on Chunghwa. Its mobile phone market share dropped from 100% to only 25% within two years following the move to liberalization, mainly because of the company’s lack of groundwork to face competition. Chunghwa Telecom also portrayed a certain slowness to respond to tariff cuts and to introduce prepaid services to match new market conditions. In addition, the firm faced a significant drop in revenues as a consequence of the Voice over Internet Protocol (VoIP) development that permitted people to make phone calls free of charge through the Internet.

Additionally, the fixed line telephony was due to be opened shortly to competition. In effect, the VoIP development resulted in a shrinking of Chunghwa Telecom revenues because, like any traditional telecommunications company, the voice transmission accounted for a great deal of its revenues. It is in such a difficult context that the market of fixed network telecommunications was opened up to competition in 2001 with the granting of licenses to three private operators. Chunghwa Telecom employees still strongly objected to the liberalization of the fixed line services. They advocated that the government should keep the fixed network under state control and only lease it to interested operators. Though there was not much they could do against the opening up; they worried about the job losses that come with it. But they had to make a difficult choice. They could defend their job security by
blocking the privatization. However, they would risk worsening the company’s situation that could in return lead to the same job insecurity. By this time the difficult situation of Chunghwa, as mentioned above and the existing competition undermined the employees’ resistance to the idea of privatization. Indeed, they felt afraid of seeing the company forced to go to bankruptcy, remarks Dr. Mao. The privatization became then a possible alternative to improve the company’s operations and performance, even if employees remained persuaded that it was not a good alternative. Thus, Chunghwa Telecom privatization course of action started in 2000 with the initial public offering of a small stake of the company (Taipei Times, Sep 11, 2005).

The main objective of the privatization was to enhance the company’s operating efficiency in order to sustain the competitive market. It was expected to give a boost to the development of Taiwan’s telecommunications market and bring the consumers both higher quality and diversified telecommunications services. Another target was to rest on the reduction of government involvement to expand the company’s space for market development at the national level and overseas market opportunities to the company as well. However it should be noted that the privatization was not free of constraints. Indeed, the powerful Chunghwa Telecom Worker’s Union regardless of the difficulties faced at that time by the company, still resisted to the process. When asked the reason of this opposition, the president of the company’s labor union, Hsu-Chung Chang, explained that for employees, the research of efficiency advocated to justify the privatization of Chunghwa Telecom was a pretext as the firm was successfully competing against private mobile telephone operators since the beginning of the deregulation of the sector. For him, the ownership had less impact on a firm’s efficiency. Hsu-Chung Chang believed that the true motivation for the government to privatize Chunghwa Telecom was rather to get proceeds from the sale of assets. In accordance with this conviction, the labor union undertook multiform actions to obstruct the process.

Among other actions conducted by union we can cite demonstrations, strikes, lobbying of politicians, sit-ins, petitions, etc. The workers’ union fighting tactics have been to seek for international assistance, show a strong unity of employees with charismatic leaders, to lobby
with all the major political parties (Chunghwa Telecom Workers’ Union, 2004). During the privatization process, the government also had to deal with political interferences. In fact, under the lobbying of Chunghwa Telecom Workers’ Union, there were lots of political interventions in the process from all major political parties. As an illustration, in June 2003 lawmakers required the government to hold 10 domestic auctions of Chunghwa stock before offering shares in the U.S. market as American Depository Receipts (ADRs) (American Chamber of Commerce In Taipei, 2004). At times, the process was even seriously delayed for political reasons. For example in 2003, the Ministry of Transportation and Communication urgently halted its plan to sell 180 million shares by stock floatation. Indeed, it did not want any overwhelming of this floatation with the 2004 scheduled presidential election, remarks the labor union (Chunghwa Telecom Workers’ Union, 2004).

3. Lessons from the Privatization Process
Since August 2005, Chunghwa Telecom is considered to be a privately owned company as more than half of its shares are in the hands of private shareholders. By analyzing the transfer of this company’s ownership, we can draw quite a few lessons from the process. We are especially interested in two types of learning. These lessons can be categorized into privatization methods lessons and lessons to minimize the social drawbacks on employees.

3.1 Lessons Regarding the Privatization Method
Chunghwa Telecom is just a partially privatized firm because the government through the Ministry of Transportation and Communication (MOTC) still owned a great deal of the company’s shares (more than 40% of the shares). This privatization process, like any other, revealed itself to be a time consuming one. The government chose to sell the firm by steps. Many reasons could explain this preference. First of all, the size of assets being sold was quite important. It would have not been easy to transfer Chunghwa Telecom to private at once. The government of Taiwan estimates that a progressive transferring of state assets of a certain size to private shareholders can reduce the impact of abundant state shares selling on the stock market (Council for Economic Planning & Development, 2002). In other words, this method aimed to protect the stock market from a massive release of state shares that can disrupt its
proper functioning. Another reason advocates to the idea of progressive privatization as the necessity for the government to implement its policy, especially in a strategic industry such as telecommunications. As explained in the literature review, many governments prefer to monitor companies operating in the so-called strategic industries from insight. By keeping part of the privatized firm’s shares, the government can have its representatives on the board or in the auditing committee. Thus, it can easily access information about the corporation and maintain a certain control on the partially privatized firm. In Taiwan, this willing is even codified in law. Indeed, it is clearly stated in the article 17 of the Statute for Transforming the SOEs into POEs (STSP) that the government can retain a “golden share” issued by the privatized utility or national defense related companies in order to veto the corporate decisions damaging national security or public interests (Council for Economic Planning & Development, 2002). Of course with time, the government can sell the totality of its stake or reduce it significantly, especially when the legal and regulatory framework is in place, well-established and well enforced. When the privatized firm gets over the transition phase and the government got experience in monitoring the industry, it is probably better to transfer the remaining state ownership to private investors.

The technique chosen to achieve the ownership transfer was mainly through Initial Public Offering (IPO). The company was first listed on the Taiwan Stock Exchange and then on the New York Stock Exchange as American Depository Receipts, respectively in August 2000 and July 2003 (Chunghwa Telecom Workers’ Union, 2004). Some people did not approve this way of selling Chunghwa Telecom shares. Among them is Dr. Mao for whom the option of “citizens preferred offering” would have been a good alternative. He explained that the handling of the privatization process was questionable under some of its aspects such as the fact that some families accumulated quite important portions of the firm’s assets at a discounted price. His idea is that the privatization should not mean “familization” where a state owned enterprise is transferred to one or few families. He believes that doing so leads to another monopoly with the only difference being it will be in the hands of some oligarchs. So was also the opinion of the company’s labor union, some legislators and even part of the general public. The union denounced what they called the ‘consortium rules and control’ referring to fact that significant parts of the company’s shares were released to banking
consortiums like Fubon and Cathay. The workers’ union criticized the fact that the Ministry of Transportation and Communication sold Chunghwa Telecom shares to these two financial groups at the price of NT$ 50.3 per share. In a report presented during the 2004 East Asia Telecom Union Forum, Chunghwa Telecom Workers’ Union argued that there were doubts in this stock floatation for three reasons. They explained that first of all, the transaction violated stock floatation planning originally made by government, where the stock floatation was to be sold to the general public first, and then by competitive auction mainly made by legal persons.

The second problem in the eyes of the union was that the deal price was a little higher than the bidding bottom, and was less than the NT$ 60 per share made in the budget of the Legislative Yuan. For employees, the last anomaly was the time from the announcement to the auction, which was only 8 days. The labor union considered that there was too short a time to arouse suspicions (Chunghwa Telecom Workers’ Union, 2004). Thereby, this was, according to the labor union, a proof of underground connections between government officials and some rich businessmen. However, the criticism about the amount of shares in the hands of financial consortiums is discussable. As long as the firm is listed on a stock exchange, it is quite difficult to prevent a specific investor from accumulating the company’s shares up to the quantity desired. In fact, any investor can buy the needed shares on the open market. In addition, having major investors could even be a guarantee that there will be a true and systematic monitoring of the firm management from the shareholders. Whereas a diffused ownership could lead to inefficiency as agency problems might arise if no investor holds enough shares that give him incentives to spend money and time on continuously gathering information on the company for monitoring and control purposes.

### 3.2 Limited Negative Social Impact

An interesting and important thing to be mentioned is that the privatization process of Chunghwa Telecom did not lead to any lay off of employees. While most of the time privatization means massive redundancies, this has been avoided in the case of Chunghwa Telecom. Many reasons could explain the minimization of the process’ side effects. The first explanation is the strong unity and dynamism of Chunghwa Telecom Workers’ Union. Indeed, from the beginning of the privatization up to now, employees showed a great solidarity in
their fight to defend their interests. This increases their bargaining power and allows them to obtain good compensations for those who had to take early retirement. In fact it was acknowledged that the wages for Chunghwa Telecom employees were too high and needed be cut. Therefore, it was necessary for the company to find ways to cut down its cost in the context of privatization, but also to promote workforce turnover, in order to enhance efficiency.

An early retirement program was then initiated. By the end of 2002, 7,000 employees applied for retirement with privilege. Thus the number of Chunghwa Telecom workforce was reduced from 35,000 to 28,000 (Chunghwa Telecom Workers’ Union, 2004). With this early retirement plan, remarked Mao, the corporation was able to save up to 10% of its total head count (Clark, 2002). President Hsu-Chung Chang agreed that their pay was quite high, but to him that was just a normal fact, because many of the employees were working for more than 20 years. He argued that it was rather the high number of managers that reflected the highest cost of the company. In effect, he asserted that some 13,000 managers work in the company and that any attempt to cut the operating cost of Chunghwa Telecom should start with the reduction of the number of managers. Such an option would at the same time result in more flatness in the firm, expressed President Chang. Nevertheless, he revealed that another voluntary retirement is currently being finalized where some 2,000 employees will leave with privilege compensations. This will allow hiring 1,000 new employees in addition to the 4,000 newly hired as an attempt to improve both personnel and payroll structure. However, regardless of the employees’ actions, this limitation of negative social impacts could have not been attainable without a true sense of consensus. Both the management team and the labor union have shown a great deal of responsibility in the negotiations to cut down costs. The search of consensus was important to both parties and highly encouraged by the government. The Council for Economic Planning and Development (CEPD) for example requires that all companies reach a consensus with their unions before submitting their privatization programs to the CEPD for review (American Chamber of Commerce in Taipei, 2004). In other words the completion of the privatization was not possible before a collective agreement was reached between employees and management on how to restructure the workforce of the company. The government motivation is to use incentives to curtail employees’ opposition to
its privatization program. The successful completion of any firm divesture process de facto strengthens the ongoing reform.

Moreover, the workers acknowledged and greatly appreciated their good collaboration with the management team. For Hsu-Chung Chang, his union has good working relations with the management. He hopes this trustful and constructive dialogue between Chunghwa Telecom employees and the management team can get to such a good level so that it can become a benchmark model for other state owned enterprises’ management and employees in their negotiations phase during the privatization process of their company. Another important reason in limiting the employee reduction in Chunghwa Telecom is certainly the quasi-monopoly that the company enjoys. It looks like the government made a trade-off between efficiency through the promotion of a true competition and a social commitment through the limitation of the job cut in the privatized firm.

4. **Lessons from Chunghwa Telecom strategies**

From Chairman Mao’s explanations, Chunghwa Telecom obviously was not prepared at all for the opening up of the telecom sector. Following the mobile phone segment liberalization, its market share in the mobile telephony evaporated. This lack of competitiveness was due to a number of problems. First of all, the company was unaware of its exact values and competitive advantages to be able to fully exploit them. Dr. Mao remarked that by that time, different employees in the company would have different answers to the question “what is Chunghwa Telecom’s business model?” Furthermore, the company did not identify its weaknesses in order to aim to minimize them. The organization of the company itself posed problems at that time. Indeed, it did not have any marketing department worthy of this name. Consequently, the firm situation at that period became very difficult. When Dr. Mao took the direction of Chunghwa Telecom, he made some important strategic moves. Among others, he cited the choice to stress on the fast development of the broadband rollout and, importantly, the revision of the corporate culture. In fact, one of the first innovations introduced by Dr. Mao was to initiate the transformation of Chunghwa Telecom from a traditional telecommunications company into a data company. He was convinced that the data business was a quite attractive “emerging submarket” in the telecommunications industry. Given its
assets, competencies and capabilities, Chunghwa was able to adjust its offerings to increase this new segment’s contribution to its revenue (Aaker, 2005). In addition, the then chairman initiated an aggressive development program of the ADSL on a massive scale.

Dr. Mao remarked that this strategic move was intended to position Chunghwa Telecom on a foreseen future strategic submarket so that the company could create new sources of revenues which could offset the lost due to the VoIP development. With the ADSL, the company could accommodate the introduction of new services such as the development of advanced voice, data and SIP\(^2\)-based multimedia services and IP/TV, believed Dr. Mao. Afterwards, the firm defined a strategic direction for each of the three major business lines which consist of the fixed line telephony, the mobile phone telephony and the data communication business. Thus, the fixed line business was set to develop and implement a defensive strategy. In effect, this segment was to be opened shortly to competition. Chunghwa Telecom was prepared to engage into a price war with new entrants in the market to make the competition irrelevant to them. Hence, the firm could defend and maintain its market dominance on the fixed line telephony.

As for the mobile phone segment that was already liberalized, the strategy was to ensure that it grows faster than competitors to regain some market shares and widen the subscribers’ basis, since this service was still in a growth phase in Taiwan. Lastly, the strategy for the data business was to create new markets and new possibilities for customers through value innovations.

The second important transformation undertaken by the company, under Chairman Mao, was about the corporate cultural change. Dr. Mao argued that without cultural change, it would have not been possible for Chunghwa Telecom to have such a phenomenal growth in its broadband rollout. To illustrate this cultural change, he cited the example of a campaign he launched just after he assumed the chairman position. In brief, the campaign consisted of asking every employee, including the chairman himself, to sell five mobile telephone numbers

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\(^2\) SIP stands for Session Initiation Protocol. It is according to Wikipedia a protocol that proposed standard for initiating, modifying, and terminating an interactive user session that involves multimedia elements such as video, voice, instant messaging, online games, and virtual reality.
in the market within a quarter. According to Dr. Mao, this was the first time the firm had this kind of all-out effort. By the end of the target period, the result was quite impressive. On average not only had every employee sold more than five numbers, actually the gross add was 800,000 and the net add was 600,000. After this campaign, a new kind of spirit started emerging in the company. Chunghwa Telecom employees were having a can-do and entrepreneurial spirit that were absolutely needed in a competitive market rather than the passive mindset which usually characterized the public corporations’ employees (Clark, 2002).

After these actions, the company stabilized its market position and started performing quite well. As of May, Chunghwa Telecom held a monopoly of more than 90 percent of Taiwan's fixed-line market and an 80 percent share in the broadband Internet connection market (Taipei Times, 2005). Contrary to the mobile phone market, the opening up of the fixed network market did not lead to a genuine competition in this segment as projected (Chunghwa Telecom Workers’ Union, 2004). It is certainly much more difficult and costly to build a fixed network for a telephony operator. Consequently, Chunghwa was able to maintain a quasi monopoly on services offer via the fixed network. It also enjoys a nearly 40 percent share of the mobile-phone market, with 8.1 million subscribers, according to the company's figures (Taipei Times, 2005). In a statement, Chunghwa Telecom announced that its current strategy in terms of business development is to focus on growth areas such as mobile services and Internet and data segments to compensate for losses incurred on fixed line business and on maintaining the top line. It plans to put tremendous efforts on implementing internal cost controls to reduce operational costs and to design a retraining program for employees so that they may contribute to these growth areas. Hence it can cope with its strategy to enhance its overall operational sustainability and effectiveness (Chunghwa Telecom web site).

One of the reported objectives for undertaking the privatization was to give the management more flexibility in term of investment decision-making. This is expected to give the company the possibility to consider engaging in overseas investments projects. Dr. Mao thinks that this should be the next move for Chunghwa Telecom. He highly advises it to seriously consider expanding its operations in foreign markets within a short period of time. The Taiwanese daily newspaper, Taipei Times, quoted him emphasizing that "internationalization is the route
to take and will provide Chunghwa Telecom with much-needed growth momentum. It will have to seize the opportunity and quickly tap into potential markets outside Taiwan before it's too late". The labor union also shares this opinion. According to the President of Chunghwa Telecom Workers’ Union, with the privatization, the company is projected to have enough flexibility to go international in order to open new sources of revenues and get international operations experience. In accordance with this orientation, it already opened an office in Malaysia.

5. Implications of Chunghwa Telecom Case

By studying Chunghwa Telecom privatization process, the goal is to see which lessons can be drawn from this experience for the ongoing privatization process of ONATEL. We are aware that there are so many differences between Taiwan and Burkina Faso that these possible lessons might not be transferable. They will probably need to be adapted to the context of Burkina Faso. Nevertheless, there are aspects in the way Chunghwa Telecom privatization process has been carried out that can serve as guidance for the government of Burkina Faso and the management of ONATEL. For sure, regarding the method there is less that can be imitated in the privatization of ONATEL because the economic contexts are just too different. Burkina Faso does not have any developed economy. Therefore, the country does not have an established and well-developed stock market or a developed capital market. In such environment, as mentioned by Bös, the evaluation of the company value could be very difficult. For example the IPO method applied in the case of Chunghwa Telecom ownership transfer cannot be a viable privatization method in Burkina Faso. The sale of shares on stock market is not feasible in Burkina Faso even if there is the possibility to do it on the BRVM3, the regional stock exchange based in Abidjan (Côte d’Ivoire).

Chunghwa Telecom privatization reveals that economic reforms are always time-consuming processes that require lots of determination and political commitment, which goes beyond partisan interests. Another lesson that can be drawn in terms of the liberalization model of the telecommunications sector in Taiwan is that, besides the mobile phone segment, the

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3 BRVM stands for Bourse Régionale des Valeurs Mobilières. It is the bourse that links the member countries of the West African Economic and Monetary Union (UEMOA)
The deregulation of the industry did not result into a competitive market. The explanation to this situation probably lies in the fact that the government did not set clear conditions to support new operators in their early stage to prepare them for competition. In addition, the time from the liberalization to now is short to see the development of new networks that can challenge Chunghwa Telecom. It will certainly take a long time to see the competition rise in fixed line business and in Internet and data communication, as these operations require heavy and massive investments. The government needs to find ways to give support to new operators for the development of their networks.

Moreover, it seems that Chunghwa is successfully pooling its human resources and its know-how to kill the competition in some of the business segments. It is being able to bypass the restriction on cross-subsidization, to distort the working of a competitive market. The president of the workers union acknowledged this fact during our discussions with him. The former state monopoly obviously uses its huge non-financial resources to sustain competition in competitive segments such as mobile phone business. It is certainly necessary to put further restrictions on Chunghwa Telecom regarding the cross-subsidization if the government really expects to see the competition playing the role of telecommunications’ development in Taiwan.

The most interesting lessons to be gathered from this Taiwan case for Burkina Faso, on how to succeed in the privatization of its telecommunications company, are based on the social impact of the privatization. Indeed, through a constructive dialogue between employees on one side and the government and the management team on the other side, the social drawbacks of the privatization were limited. The fact that Chunghwa Telecom privatization did not lead to any lay off of employees is a good example to be observed by a country like Burkina Faso where unemployment remains a serious problem. Therefore, implementing privatization without the consequences of a harsh lay off of employees should be an interesting experience to consider in the economic reforms of Burkina Faso.

As for lessons that can be drawn for the company, we can say that Chunghwa failed to prepare itself for the opening up of the industry to competition. Fortunately, it promptly
reacted to the difficult external environment thanks on one hand to a good leadership from the management and on the other hand to the scope of its resources that give it the possibility to undertake important investment projects allowing it to take great advantage of growth opportunities in value added-services areas.