

## SHARE SWAP BETWEEN TELEFÓNICA AND CHINA UNICOM

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In 2005, Telefónica and China Unicom entered into a strategic alliance with the aim to operate jointly in the telecommunications industry. Initially, it took the form of a minority holding by the Spanish company in its Far Eastern counterpart when Telefónica purchased 5.38% of the Chinese operator's capital.

This initial operation was reinforced in September 2009 with a share swap between both companies, whereby Telefónica's investment rose to 8.06% of China Unicom's capital, whereas the latter acquired 0.9% of the Spanish telephone company. Through this new operation, Telefónica acquired a further 694 million shares, up to the aforementioned percentage, whilst China Unicom undertook to acquire 40.7 million shares in the Spanish company, which meant an investment by each party of one billion dollars (around 700 million euros at the prevailing rate of exchange).

The partners agreed to keep possession of the shares for at least a year, although the agreement included joint operations over the following three years, unless either one of the parties should discharge the contract with six months' prior notice. These joint operations included shared procurement, the development of common platforms for mobile phone services and the provision of services to multinational customers.

One of the agreement's clauses laid down a restriction on any investment in the share capital of each other's rival companies. According to this restriction, Telefónica would be barred from investing in the share capital of China Mobile and China Telecom, although it could enter into agreements with operators throughout the rest of the world. In China Unicom's case, although the agreement opened the doors to Western and Latin American countries, the restriction on forging new alliances was greater, as at that time Telefónica was operating in 25 countries.

At the time of this operation, Telefónica was the world's fifth largest operator in terms of the number of customers, with 264 million users distributed almost all over the world, whilst China Unicom was the fourth with 284 million users only in China. The top three were China Mobile (493 million customers), Vodafone (320) and China Telecom (288). The joint operations involved providing a combined service to around 550 million customers, almost 10% of the world's population.

At the end of September 2009, it was announced that the Korean company SK Telecom was selling its stock in China Unicom, which amounted to 3.78% of its shareholder capital. Once these shares had been repurchased, China Unicom decided to redeem them, which meant that Telefónica's true holding rose to 8.38% of the Chinese operator. SK Telecom's withdrawal led the Chinese operator to replace the CDMA technology standard in mobile telephony (used in the United States and in which SK Telecom had experience) with W-CDMA (used in Europe) and of which Telefónica has wide knowledge.

In January 2011, a new strengthening of the alliance was announced with the mutual commitment to invest the equivalent of a further 500 million dollars (around 367 million euros at the prevailing rate of exchange), whereby Telefónica's holding amounted to 9.7% of China Unicom's capital, whereas the latter now holds 1.37% of the former's. The increase in Telefónica's holding was made through the market

purchase of China Unicom's shares over the following nine months, whereas the increased holding by the Chinese company involved the purchase of shares from Telefónica's treasury stock.

The new operation meant a step forward in the reinforcement of the alliance by providing a seat for China Unicom's chairman, Chang Xiaobing, on Telefónica's board of directors, as consideration for the seat Telefónica's chairman, César Alierta, already occupied on the Chinese company's board.

However, in June 2012, it was announced the Telefónica's holding sale of 4.56% in the Chinese company, by a value of 1.128,9 million euros, so its holding was reduced to 5.01%. Despite this reduction, César Alierta remained within the company's board. This operation was carried out because the Spanish company had given priority to reduce its debt, which amounted to 57.000 million euros.

At 1 January 2012, the Asian company had more than 340 million customers, with 185 million mobile phones, 103 million landlines and 55 million broadband connections. China is the world's largest telecommunications market, with an enormous growth potential due mainly to the population's scant use of mobile phones and broadband.