

Letter to the Editor of the Financial Times – published London edition 28 November and International edition 2 December 2002

Dear Sir,

Paul Klemperer (FT 26 November) argues that investment in 3G is ‘primarily motivated by attractive returns in the future’ and not by past investment, so the auction prices are irrelevant to the future of 3G. He also rejects the popular view that auction prices were overbid, but he fails to address how the former may have influenced the latter.

I have a partial explanation. None of the bidders seems to have seriously considered what they were bidding for. A 3G business is not a voice business, it is a data and Web-centric services business, and however ‘attractive returns in the future’ may be the simple fact is that they are irrelevant to the auction price, but not for the reason Paul Klemperer gives. They are irrelevant because winning an auction does not confer the right to run a data and Web-centric business. In an Internet world no licence of any kind is required to do so. The ownership of spectrum usage rights only confers the right to provide access to these services, and who actually provides them and bills for them is an entirely different matter in both logic and economics. Before the auction, British Government consultants using a net present value analysis estimated a value one-tenth the final outcome. After the auction, all the financial analysts in Hong Kong factored in the irrelevant future flow of revenues from data and Web-services and came to conclusions that according to my NPV estimations were again over the top by factor of around ten.

The Hong Kong regulator finally adopted my own proposal to run an auction based upon the royalties that bidders would pay from the turnover of their licensed business. (See http://www.trp.hku.hk/papers/2000/3g_response.pdf). The advantage of this approach is that it synchronizes the ability with the need to pay and avoids the debt problem. In the event four bidders for four licences paid the reserve price, which incidentally worked out at about one-tenth the financial analysts’ predictions.

Yours sincerely,

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