

18 June, 2004

Office of the Telecommunications Authority  
29/F Wu Chung House  
213 Queen's Road East  
Wanchai, Hong Kong

Attn: Senior Telecommunications Engineer (Technical Regulation) 2

Dear Sir,

We refer to the Consultation Paper issued by the Office of Telecommunications Authority ("TA") dated 19 March, 2004 with respect to the Licensing of Mobile Services on Expiry of Existing Licenses for Second Generation Mobile Services. Based on our experience in financing mobile operators in Hong Kong as well as abroad, we would like to provide our views on the TA proposal as follows:

1. More competition in the already over-crowded Hong Kong market may damage the commercial viability of licensees and increase the risk to financial institutions which has existing exposure to the sector. We have already seen from the existing 2G situations that most of the existing incumbents required some form of financial support from vendors or parent group to compete/survive in the current market which is not healthy and not sustainable in the longer term. Consolidation has been widely expected for some time under the current competitive environment. However, there has been no consolidation to date among the six 2G operators and foreign investors are not interested to invest in Hong Kong due to the unprofitable outlook in the excessively competitive market.
2. Competition amongst the existing 2G incumbents are already fierce, particularly on prices. Some existing operators are reluctant to invest into new infrastructures and applications as profit margins are being eroded. They utilise existing network to maximise return from the "lowest tier" of subscribers who are not sophisticated and only require simple voice services. In the longer term, consumers could suffer, because of the lack of investment and promotion for non voice services, which is against the objectives of TA.

3. Over-fragmentation of the market and excessive competition (i.e. if more 3G licenses are granted) will further limit the ability of existing 3G incumbents to achieve economies of scale and generate decent profitability to make this a viable business and to continue investing into more sophisticated applications such as mobile data services, which is one of the priorities of TA.
4. All of the existing 3G licensees, except for one, had delayed the rollout of the 3G service in HK due to delay in enhancements to meet the evolving customer needs and uncertainty in customer demand. Introduction of further competition will create additional uncertainties for the existing 3G licensees and increase their reluctance to roll out their services.
5. From a financing perspective, while we applaud the absolute need for competition, the competitive structure of a market place without economy of scale and profitability could negatively impact the ability of incumbents/new licensee to raise bank financing to fund new investments on a standalone basis. Again, consumers may suffer in the longer term, as licensees are unable to obtain bank financing to fund their capital intensive investments to upgrade their network and applications.
6. With a small population of 6.8 million in Hong Kong, we believe it would be prudent for the Government to assess the potential demand and commercial viability within a commercial environment, after all four of the 3G licensees have rollout their services for a reasonable period of time, before considering the possibility of issuing an additional license.

In summary, we are supportive of the TA's objective to stimulate development of mobile data and related applications as well as enhancing Hong Kong's status as the mobile service hub in the Pearl River Delta and Asia as a whole. However, introduction of excessive capacity is likely to impair the commercial viability of the business and therefore, reduce the interests of the financial institutions to lend their support to the sector. This may, in the end, curtail the development of the domestic market and act against the stated objectives of TA.

We would be pleased to answer and clarify any questions you may have on our comments as mentioned above.

Sincerely yours,

Grace Fung Oei  
Head of Large Corporates & Public Sector  
Wholesale Banking