

Box 1

Implications of the UMTS auctions for monetary and financial developments

Many governments of euro area countries are currently organising the sale of third-generation UMTS (Universal Mobile Telecommunications System) mobile telephone licences. In Finland and Spain the licences were allocated free of charge or for a very modest fee; the auction in the Netherlands, which was completed in July 2000, raised €2.5 billion. The German auction for UMTS licences finished on 18 August 2000, with the proceeds reaching a total of €50.8 billion. In view of the significant amounts of funds involved, this box takes the German case as an example and elaborates on the expected implications for developments in M3 and its counterparts and for the bond markets.

Impact on euro area M3 and its counterparts

The financial flows triggered by the German UMTS auction will be reflected in euro area M3 and its counterparts from the August data onwards. The payments of the licence fees to the German Government were due at the start of September. While most firms waited until that date to make the payments, some funds had already been transferred by the end of August. Regarding the sources of financing, it can be assumed that firms relied on their own funds, bank loans and funds raised via bond issuance or new capital. Some of the funds were probably transferred from outside the euro area. As firms most likely had to hold some funds in the form of short-term assets shortly before the payments were due, the possibility of a slight upward effect on M3 in the August data cannot be ruled out. Furthermore, the data for loans to the private sector and net external assets of the MFI sector (reflecting transfers of funds from outside the euro area) are likely to be affected from August onwards.

The transfer of the proceeds to the German Government implies, *inter alia*, a shift of deposits from the private sector to the central government sector. As the deposits of central government are not included in monetary aggregates (since they do not usually exhibit a close relationship to government spending behaviour), this transfer implies, *ceteris paribus*, a reduction in M3. The German Government announced that it will use the licence fees exclusively for the redemption of debt. However, the greater part of these redemptions cannot be carried out immediately. The major transaction foreseen, for example, is the redemption of €33 billion of a floating rate note relating to the Currency Conversion Equalisation Fund, which will not take place until the start of 2001. The redemption of debt by the German Government will most likely be reflected, in particular, in a decrease in the deposits held by central government and in credit to general government. However, this should not be expected to have a significant effect on M3, because a large proportion of the government debt to be redeemed is held by MFIs.

All in all, it is quite possible that the M3 data in August, and other items of the consolidated balance sheet of the MFI sector for some time, will be affected by transactions relating to the UMTS auction. Consequently, due caution should be exercised when interpreting these data in the coming months.

Impact on bond markets

Bond markets have been influenced in recent months by expectations of shifts in relative supplies of government and corporate bonds related to the UMTS transactions. In particular, expectations of dwindling supplies of government bonds and increasing supplies of corporate bonds have prompted a widening of spreads between government and corporate bond yields, as well as between yields on government bonds and swap rates (see Box 3 in this issue of the ECB Monthly Bulletin). To the extent that proceeds from future UMTS auctions in other euro area countries exceed market expectations, this is likely to put further upward pressure on yields in the corporate bond market as well as additional downward pressure on government bond yields and, hence, bring about a further widening of spreads.

The amounts reached in the bidding process exceeded initial market expectations. It is likely that the yields on corporate bonds issued by telecommunications companies are being affected by additional risk premia in connection with the increase in the leveraging of these firms. In addition, concerns might have increased among investors that the amounts paid by successful bidders may have been excessive in relation to the earnings which are expected to be generated from the licences. This type of influence has been particularly apparent in the downgrading of credit ratings of telecommunications companies and in recent declines in the stock prices of successful bidders.