

Sell 4G in Closed-Bid Auction

One reason Russia's economic policy often falls short of the mark is because the government believes that it is unable to carry out the recommendations it receives from economists. It decides that ignoring the recommendations is better than implementing half-measures. For example, in winter and spring 2009, the government considered a range of infrastructure investment projects similar to the "financial stimulus" measures in China that would have eased the burden of the financial crisis. However, those projects never got off the ground, in part because the government had no illusions about its own limited capabilities.

Perhaps this is the reason Prime Minister Vladimir Putin decided not to hold an auction to allocate frequencies for Russia's fourth-generation radio networks. After all, everybody knows that participants reach secret agreements beforehand, eliminating the competitive aspect of the bidding.

In fact, with only one exception, all major privatization auctions have suffered from this problem. These auctions were carried out English-style, not through sealed bids, and the item on the block went to the person who made the highest verbal bid. Controlling stakes in the two main production assets of the former Yukos oil company — Slavneft and Yuganskneftgaz — were sold at auction this way in 2000. Neither auction was competitive.

What is the problem with English auctions if bidders can theoretically reach agreements before any type of auction? The bids are made in the open, and each participant is able to make sure that the others are upholding their end of the bargain. But if one buyer breaks the prior agreement and raises the bid above the agreed limit, the others can join the fray and drive the price through the ceiling just for spite. Whoever finally does win will have to pay far more than was planned. Knowing that, participants tend to uphold the terms of their secret agreements and bid low.

But when the bids are submitted in sealed envelopes, all bets are off. The temptation to break prior agreements is much greater because the high bidder's real intentions become known only later. This kind of auction makes it much harder for participants to "fix" the results in advance.

The only example of a successful privatization auction in Russia took place in 1997 when a blocking stake in Svyazinvest was auctioned off through closed bids. The winner, George Soros, offered \$2 billion, an enormous sum for that time, and later bitterly regretted having overpaid.

But if the government — or in a broader sense, the public — is the auctioneer, we should be glad to have put so much money in state coffers. Another proof that the auction was truly competitive is that the losing bidders proceeded to unleash a media campaign against the government aimed primarily at former First Deputy Prime Minister Anatoly Chubais.

Conducting such an auction for 4G networks would require political courage. But without such courage, effective government is impossible.

09 September 2010
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