## Cyberport in Abacus

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The government has recently announced that **the agreed value of the residential portion of the Cyberport land is HK$7.80B**. This would become the basis of its profit sharing with Pacific Century Cyberworks (PCCW), the investor of the project. Real estate professionals generally consider this figure to be a reasonable market price.

PCCW was listed in the stocks market soon after its Cyberport project got into fame more than a year ago. Now that it had succeeded in acquiring HK Telecom, the giant in communications, and hence transformed itself from a virtual concept to being a solid reality. It is therefore wise for PCCW not to drag on the question of land value with the government. After all, even with interest costs, the total investment of HK$15.80B in construction (6.1 on cyberport and 9.7 on apartments), could easily be repaid should the 4 million square feet apartments be sold at around HK$5,000 per square foot (ft2).

**From the viewpoint of the government**, however, the arithmetic is totally different. Despite an assumption of a stable residential market, promising $5,000 per square foot for instance, the government could share nothing in terms of profits. **The HK$7.80B (land) price tag is 'virtual' i.e. the treasury would not receive a dime should the apartment price level stay at HK$5,000/ft2**. Given this price level, all the apartment sales proceeds would be used to recover PCCW's investment, according to the terms of the joint venture contract. Hence, in forsaking the potential land sales income derived from the land, the government would only get, in return, the 100% ownership of the cyberport offices. Hence, there is a land cost on one hand, and office rental incomes on the other. Now let us work out the arithmetic of these costs and benefits.

On the **benefit** side, within the 1.6 million square feet of proposed gross floor area for the Cyberport, about 1 million would be office space. As the government tries to attract potential tenants by offering cheap rentals, these offices are insufficient to meet the pressing demand. Hence the government is planning to change other areas originally designated for hotels, houses and shops into offices. Using the current proposed rental of HK$8 per square foot per month**, the gross income of the cyberport would be in the order of HK$0.16B per annum**. This excludes maintenance and other miscellaneous operating expenses.

On the **cost** side, 10 hectares of residential land was valued HK$7.80B. Using this per hectare value of HK$0.78B, the 16 hectares occupied by the cyberport portion would be worth HK$12.50B. **These two lots, 10 and 16 hectares, with full sea views, would have cost the government HK$20B**. Receiving an annual rent of HK$0.16B over a HK$20B investment would imply <u>a rate of return of 0.8% per annum only</u> - a return far below annual interest costs.

The **objectives of the government** is, of course, not a mere 0.8% return over its investment; but are those '**invisible benefits** of attracting foreign investment, developing high technologies, and creating job opportunities'. Yet the question is whether these so-called 'invisible benefits' are real or virtual. Yes, international firms of modern technologies have shown their hands to move into the Cyberport. But on their balance sheets, are they entering the overwhelming value-for-money paid for the technological experts in Hong Kong? Or are they simply capitalizing their extra gains due to their savings in office rentals? Technological giants as large as Microsoft, or as new as tom.com, are all setting up major research offices in Shanghai and Beijing. Whereas in Hong Kong, major web-sites are all reducing their operations by cutting back staff. Then, what on earth is Cyberport's attraction to foreign investors? Land cost aside, the construction cost of the Cyberport offices is budgeted at HK$3,800 per square foot – doubling the newly built Cheung Kong Center in Central, while cyberport's rent is only one-seventh that of Cheung Kong Center! **In a nutshell, the cyberport is offering a Mercedes taxi service, but charges only one-seventh of the normal taxi fee!** This is clearly not a good business, is it?

Nevertheless, the objectives of 'attracting foreign investment, developing high technologies, and creating job opportunities' by offering cheap rentals may also be illusory. Exceptionally low rents may simply tempt some computer firms to move away from the CBD as these companies will simply close their offices in Central and Admiralty and move to the Telegraph Bay. <u>This could almost be a zero sum game</u>. The comparative advantages of the computer business in Hong Kong have always been the wide information network, advanced marketing techniques, and an efficient distribution center. These shop-window activities have existed in Hong Kong for ages. This has always been the means of survival of Hong Kong as a free entreport. Should this main trend continue, by the time Cyberport completes, it would become a Rolls-Royce shop-window paid for by the government, yet offered to brand named computer companies as their regional distribution centers, unfortunately at rentals levels of the Sham Shui Po Golden Shopping Center! Effectively, the Cyberport would be pouring millions of dollars of potential revenue for the Treasury into the pockets of computer companies. Yet there is one thing we should never forget: to the computer firms, business is business. We could neither force them nor expect them to use their extra profits to compensate all-too-certain losses in developing high technologies in Hong Kong. Nor could we expect them to re-locate their profitable research centers at other Asian cities to Hong Kong, where cost effectiveness is much lower.

By now, there is **no turning back** for the government. They would be forced to name this gold plated shop-window as a high technology center. It will certainly be a very tough job for the ministers, who are expected to make up stories for the emperor's new clothes. In my opinion, the government will be in a better position if the Cyberport is to be sold to the private sector when a suitable opportunity arises. The market is always in a better position to decide whether it should be a shop-window or a center of technology, given the specific circumstances of the market.

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