

# INNOVATIVE FINANCING TO END DIGITAL EXCLUSION

*In May 2021, Intelligens Consulting wrote about the need for a radical rethink to end digital inclusion with a focus on innovative commercial models that go beyond relying on market forces alone. This follow-on article – with input from Portland Advisers – sets out our thoughts on a UK Government approved approach that can be implemented by landlords to combat market failure and stimulate the roll out of fibre networks to social housing tenants.*

## STRUCTURED FINANCING IS THE KEY

In our article of May 2021, we wrote that landlords such as local authorities, social landlords, and housing associations will need to ‘step up’ to combat market failure and deliver future-proofed fibre connectivity solutions using innovative commercial models that leaves nobody behind thus combating digital exclusion.

Stepping up requires social landlords to embrace innovative commercial models and requires significant amounts of up-front capital investment typically unavailable from the public sector. That means any capital investment must come from the private sector (typically an operator) and structured finance models are essential vehicles for to enable that private capital investment.

Although a wide variety of structured financing models are known and have been tested, this article describes the development of a Joint Venture (JV) model which has peaked our interest for several reasons:

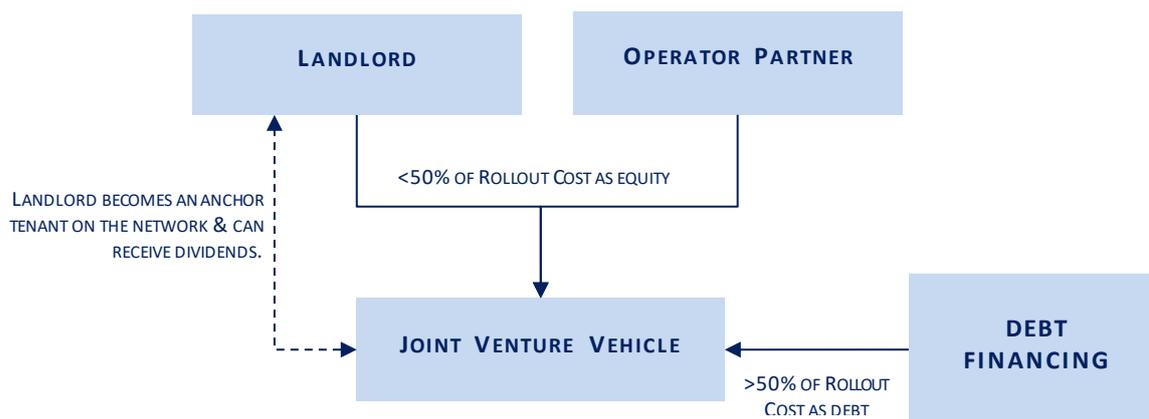
1. Although JV models are rarely considered in the public or third sector, such an approach would make it more attractive to landlords and would attract private sector capital investment.
2. The JV approach is similar to that currently under consideration by the UK Government’s department for Digital, Culture Media and Sport (DCMS) to deliver Project Gigabit.
3. A JV could deliver affordable gigabit capable fibre connectivity to the most vulnerable sector of the public.
4. A JV approach could reduce the need for cash strapped landlords to source up front capital while creating the potential to generate a commercial return for the landlord.

## A JOINT VENTURE APPROACH CAN ATTRACT INSTITUTIONAL FUNDING

The JV model builds upon a type of public private partnership (PPP) with addition of the landlord as anchor tenant where the landlord creates a JV or Special Purpose Vehicle (SPV) with the private sector investor. The JV or SPV would invest in, and provide, broadband infrastructure services to end users while both parties would own equity and split the investment risk and financial reward. Such a JV can attract institutional funding substantially decreasing the costs to the public sector as shown in **Figure 1**.



Figure 1: Overview of JV anchor tenant model



### KEY ISSUES TO BE ADDRESSED

The JV anchor tenant model above can be fine-tuned to deliver the required economic and social benefits to various stakeholders, provided that the following issues are properly addressed:

- **Levels of market risk the JV is taking:** the level of guaranteed revenue in the JV provided by the landlord (as an anchor tenant) has to be carefully calibrated. If levels of guaranteed revenue are acceptable, project financing lenders may lend at a debt-to-equity ratio of about 60/40, though even higher levels of debt leverage are possible where the market risk is very low.
- **Landlord's return requirements:** The landlord's up-front capital contribution must be balanced against available dividends from the JV to generate the required return for the landlord.
- **Operator's partner's return requirements:** The operator partner's up-front capital contributions must be balanced against the projected revenue in the JV, considering the mix of social versus private tenant customers using the network.
- **Subsidy control:** Subsidy Control, the successor to EU State-Aid regulations, is still a work in progress but is likely to contain many of the same features as the previous regulation. Consequently, limiting market distortion is likely to remain a key factor in limiting regulatory challenges. This might be achieved by intervening at the wholesale level while providing open access services to ISPs.

This JV approach, if properly negotiated and structured, will remove the financial roadblocks to the delivery of affordable fibre networks to the, as-yet, unconnected 1.5 million UK households.

Please contact us should you wish to learn more about this approach and its benefits.



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