

Traditional Financing Instruments for ICT Projects

Among the more traditional financing instruments available for both large and small projects are the following:

Foreign donors and lenders

There is a broad network of international public and non-profit donors and financial institutions which play active roles in supporting the finance and development of ICT networks and services throughout the developing world. A comprehensive report on the status and activities of Official Development Assistance (ODA) and International Finance Institutions (IFIs) in the sphere of ICT financing was prepared for the World Summit on the Information Society by its Task Force on Financial Mechanisms (TFFM).¹ This report shows that, while some forms of direct donor financing of infrastructure, for example, have declined as market forces have taken precedence, these institutions continue to play a vital role in promoting market-driven development, sector reforms, and targeted direct assistance. The latter is increasingly taking the form of Output Based Aid (OBA), in which donor institutions link financial support to quantifiable and measurable results of infrastructure and service expansion plans, for example, through universal access fund mechanisms.

Loan guarantees

Some foreign donor agencies and government programs emphasize reducing investor risk over direct financial assistance. Loan guarantees represent an important element of this strategy, by helping start-up companies or those without strong credit histories to obtain commercial financing, subject to partial or total underwriting of those loans by the aid agency. This strategy can be especially helpful in supporting micro-finance institutions lending to SMMEs.

Vendor financing

Vendor financing has evolved over recent years to become a potentially attractive source of financing for many start-up ICT companies. Equipment suppliers historically

¹ <http://www.itu.int/wsis/tffm/>

have offered limited financing options (e.g., short instalment plans) to their purchasers. Recent changes in the telecommunications and Internet industries, however, have broadened the types of financing options offered by vendors, as competition has created incentives for suppliers to reach out to smaller and less established customers, to establish brand loyalty as the industry grows, especially in new markets in developing countries. Companies such as Cisco, Lucent, Nortel, ZTE, Huawei and others have provided attractive financing terms, even “free” equipment, to lock up new network operators for longer term upgrades and expansion deals. There are risks to these arrangements, of course, if the terms of financing arrangements hinder competition or inflate costs down the road. The downturn in the global technology sector in the past few years has led some suppliers to cut back on lucrative financing offers in emerging markets.²

The Valtron Rural Telecommunications Pilot Project discussed later in Chapter VIII is partially financed this way.

Public private partnerships (PPP)

A variety of practices and business-government arrangements fall under the term “Public Private Partnership” (PPP). Generally, the concept implies a coordinated effort between private companies and public agencies to pursue a given investment or business deal which neither party would be as likely to implement on its own. Under some PPPs, private companies act as “outsource” agents for government functions or otherwise obtain contracts to deploy specific facilities and services mandated (and funded) by government. In the case of ICTs, the more common model that is emerging involves government subsidy or co-financing of socially beneficial infrastructure projects, leading ultimately to private ownership and operation on a commercial basis. Examples include large-scale national and regional fiber optic backbone networks and Internet Exchange Points, which can be of value to the ICT industry as a whole, but may not be sufficiently attractive for any one operator to implement on its own.

Other types of PPP arrangements include:

² Ouida Taafe. “Low ARPUs, high hopes.” <http://www.itudaily.com/new/home.asp?articleid=4090911> 09 Sep 2004.

- Project Finance³, also known as "limited" or "non-recourse" finance, generally involves the establishment of a special purpose finance vehicle to develop, finance, construct and operate a specific project. The lenders in project financing look to the cash flow generated by the project as the source of funds for repayment of their loans and to the assets of the project as collateral for the loans (rather than to recourse from the shareholders of the company).

Unlike, for example, a project financing in the power sector, telecommunications projects do not tend to be based around a single asset, generating a single predictable revenue stream over a definite period. The dynamic nature of the telecom industry - a function of customer demand, technological advances and regulatory changes - all require that a telecommunications project be supple enough to react quickly to market forces, including through the addition of new businesses or services. Thus, in some circumstances there is conflict between traditional project finance requirements, which use a static business and quantifiable risks as a model, and the need of a company to operate and manage its business in the ever-changing telecom and Internet markets.

- Build Operate Transfer (BOT) schemes represent one form of project finance, except that after a period of time, when the capital costs of the project have been paid off, the ownership of the project can revert to the original owner, whether it is government or a private company. These arrangements were used extensively in some countries, for example in Thailand, to build out three million new customer access lines for the state telecommunications operators during the 1990s, prior to the opening of the markets to competitive, private entry.
- Export bank or credit agency financing whereby an ICT project involves the sale of goods and/or services from its country of origin to a foreign market the project. Such financing may be eligible for coverage by public export credit agencies (ECAs). Where the export content is insufficient, or the political risks are significant, multilateral credit agency (MCA) coverage may be available. The willingness of ECAs and MCAs to participate in projects provides significant encouragement to,

³ Glenn S. Gerstell and Alisa Fiddes. "Techniques for Financing Telecoms and Internet Infrastructure Buildout in Asia." http://web.ptc.org/library/proceedings/ptc2001/sessions/test_area/monday/m16/m164/

and is often a necessary prerequisite for private lenders and investors to be interested in participating in emerging market projects.⁴ The Chinese Sino Bank has been very aggressive in promoting the export of Chinese ICT equipment and services through these types of arrangements. The Ruralfone project described in Chapter VIII uses this type of financing.

⁴ Ibid.