Joint Committee on the National Broadband Network

Answers to Questions on Notice

Submission No. 3.3

Public Hearing 16 April 2012

Broadband, Communications and the Digital Economy Portfolio

Department of Broadband, Communications and the Digital Economy

Question No: 18

Hansard Ref: In writing

Topic: Private Equity – Debt Financing

The Joint Committee asked:

The department's submission notes that borrowings "are not precluded by the legislative framework" and that NBN Co's Corporate Plan 2011-13 plans for the introduction of debt financing mid-way through the rollout, i.e. commencing in 2015. Can you elaborate on these points?

Answer:

NBN Co has been established by the Commonwealth as a Corporations Act company. As such it is able to undertake all those activities the Corporations Act authorises companies to do, including borrowing money, unless otherwise constrained by other legislation, shareholder resolution or other policy parameters provided by Government.

The National Broadband Network Companies Act 2011 places a number of restrictions on the operations of NBN Co, in particular in relation to dealings in the share capital or equity of the company. These restrictions do not extend to placing controls on the ability of NBN Co to borrow, as long as share capital remains unconstrained. Similarly restrictions on borrowing are not imposed by any shareholder resolution or policy parameter. To the contrary, the Statement of Expectations, the Government's principal vehicle for the provision of policy parameters to NBN Co, extols the company to borrow at the earliest effective opportunities.

NBN Co's Corporate Plan 2011-13 plans for the introduction of debt financing mid way through the rollout that is commencing in 2015. This plan, which is supported by the independent analysis of Greenhill Caliburn and KPMG, is based on this timing being the earliest that the revenue generated by NBN Co would provide lenders with confidence that interest charges can be met and the borrowings repaid at the expiration of the term.

The analysis undertaken by McKinsey and KPMG in the Implementation Study for the NBN included an examination of an appropriate funding model for NBN Co. The results of this analysis including recommendations around the funding of the NBN and scenarios for taking on private sector debt are set out in Chapter 8, pp 367-415 of the Implementation Study:

'An appropriate funding model for NBN Co is one in which Government achieves its policy objectives and uses its resources efficiently. This can be achieved through the use of Government equity to fund NBN Co during the first 5 years of roll-out. In later roll-out (years 6–9), the company could begin to take on substantial volumes of private sector debt, as cash flows become available to support it. Government intends to privatise NBN Co, however, flexibility should be maintained in the timing and nature of privatisation.

Using private sector debt reduces the need for Government funding. While Government debt is less costly than private sector debt, private sector funding confers the benefits of greater financial discipline and a reduction in the use of Government funds, consistent with Government policy. Even though the debt would be held by a Government-owned entity, it is held by an independent company and secured against that company's assets and cash flow, so is not classified as Government debt.

Private sector debt would provide NBN Co with financial discipline and would reduce Government's funding requirement. The amount of debt that can be raised by NBN Co increases over the course of the project. Under the Funding Reference Scenario, as cash flows become available and grow, NBN Co will be able to support up to $25 billion in private sector debt by year 12. Given the size of the NBN initiative and constraints in the domestic debt market, NBN Co will need to access international debt markets.

NBN Co has a choice between multiple sources of debt capital. To reach the amount of debt funding contemplated, both bank debt and capital markets will need to be accessed. Project finance debt would be insufficient on its own. Finance from vendors and export credit agencies is limited to the physical equipment purchased for the network roll-out. The limited capacity of the Australian debt markets would likely force the company to tap international markets.
The debt capacity available to NBN Co is conditioned by the credit rating achieved (Exhibit 8–5 explains credit ratings). Although private debt lenders may only require NBN Co to sustain a rating over BBB–, a rating of A– or above is preferable when accessing large amounts of debt.