Surviving and Thriving in 2023

Don't look to a polarized Congress, possibly deadlocked FCC, or a chance for peace in Ukraine to make your business plans work. Fortunately, you may not have to. At least a partial cure lies in good contingency planning and exploration of new financing methods. Here's how to get it done.

By Steven S. Ross / *Broadband Communities*

The year ahead offers enormous opportunities but serious hazards for broadband deployers. Interest rates are high and may continue to climb a bit more. Aside from state and federal largess, money is becoming harder to get. Shortages of labor, electronics and fiber can only get worse. Design, software and engineering talent looks to be in adequate supply. Availability of management, legal and business consulting talent also looks OK, although only in some places. But thanks to over-the-top streaming, the business case has never been easier or potentially more profitable for all but the national carriers.

On the plus side, about $50 billion in federal money is on the table to fund deployments, and about $30 billion is spread over the next five years or more in direct subsidies to broadband customers or from the FCC to broadband operators.

But none of the paths are straight or well-marked, and almost all are subject to nasty events worldwide and in the U.S. Deployers calling me for advice are not as well schooled in the history or implication of shortages, inflation or high interest rates as they should be. Those familiar with the stagflation of the 1970s and shock of 2007–2009 do not fully grasp the sources of today's problems, or the solutions.

I hear far too many glib solutions from politicians of all stripes. Republicans complain about inflation but offer no real solutions. Many Democrats believe that a dollar can be spent more than once and refuse to set priorities.

INFLATION ISSUES

There are no real solutions right now. The causes of today's inflation rest mainly in the COVID-19 pandemic and in Russia's invasion of Ukraine. Inflation rates are already trending down in the U.S., but inflation has been and will remain more onerous among all major U.S. trading partners. All of that adds up to confusion.

If inflation lessens in the nation, it would be reasonable to expect, for instance, that the Federal Reserve would slow, stop or even reverse the 2022 interest rate hikes. But if the rest of the world continues to suffer, central banks elsewhere will raise their interest rates. That would tend to weaken the dollar, so buying goods overseas will get more expensive for Americans.

Oil does not count, because it is almost universally priced worldwide in dollars anyway. But part of the reason oil and natural gas prices have not risen even higher is that China is not producing goods at full capacity as it continues COVID-19 lockdowns. That, in turn, produces scarcity that raises prices of those goods.

If the Ukraine war suddenly ended because of, say, a leadership change in Russia, then energy prices would immediately plummet. Food prices would soon follow. We can hope, but we cannot plan for it.

In the U.S., prices are not likely to fall as far as elsewhere, because labor shortages here have helped drive up wage rates for lower-paid service workers. That, in turn, makes broadband deployment labor pricier.

The argument that out-of-control federal spending, mainly on COVID-19 relief the Republicans scream about and the 2017 federal tax cuts Democrats dislike, has added to inflation does not seem to hold much water. For one thing, inflation heated up this year as the federal annual deficit dropped by well over a trillion dollars. For another, again, inflation has been worse elsewhere. And though the federal debt grew, private debt shrank.

Debt creation does add to the supply of money, which normally increases inflationary pressures, but the Federal Reserve compensated somewhat. And controversial spending as for infrastructure (including broadband) theoretically makes the economy more efficient, reducing prices.

Some federal actions, such as forgiving student debt, cost less right now than one might imagine – the money has already been spent on college tuition, so the real "loss" is the interest the government won't collect going forward. But forgiving student debt makes the students more creditworthy so *they* might be expected borrow more.

All this raises the cost of broadband deployments. If a deployer borrows at 7 percent to build a $10 million system that won't reach cash flow breakeven for three years, servicing the debt adds about 20 percent – the interest rate times the extra loan period to the capital cost. The $10 million system now costs $12 million to build. Deployers have a way to reduce that now. Serving bandwidth only, neighborhood fiber can be lit as it is built. One would expect that this would increase marketing costs, but it hasn't. The most savvy deployers are just marketing door-to-door and letting local officials publicize and take credit.

DELAYS

Breakeven can also be delayed by equipment and labor shortages, and those delays take time to calculate. I discussed this in an earlier column (bbcmag.com/community-broadband/bandwidth-hawk-financing-just-got-extra-complicated-broadband-communities-has-your-back) and a workshop at the **Broadband Communities** Summit last May in Houston.

Obviously, delays can be expected to increase when $42.5 billion in federal funds begins flowing this summer through state offices established in the Broadband Equity, Access, and Deployment (BEAD) Program (see bbcmag.com/multifamily-broadband/bandwidth-hawk-federal-broadband-funding-time-to-act). Chinese production snags for equipment are likely but labor shortages are even more likely as demand rises 20 to 25 percent throughout the expected five-year BEAD buildout. Remember that $10 million system? The rise could now be closer to $14 million! There is some room for negotiating payment upon delivery.

ALTERNATIVE FINANCING

That, in turn, leads to deployers exploring other financial alternatives. One example: have builders of new multiple-dwelling-unit (MDU) complexes or planned unit developments fund the deployment. The broadband carrier that would normally deploy now earns its keep by offering turnkey management. Would the pricing be bulk? It depends. Low-income tenants, for instance, are eligible for a $30 monthly federal subsidy paid directly to the deployer. Doing that when broadband is part of the rent still needs to be sorted out. MDUs and rented single-family homes are clearly the deployer sweet spot. For details and data, see bbcmag.com/multifamily-broadband/bandwidth-hawk-new-broadband-deployments-for-new-housing-yes-but-dont-believe-everything-you-hear.

If available, condo homeowner associations could use their funds to pay for the deployment. Because they tend to run at breakeven, they cannot take advantage of depreciation as a tax deduction. The deployer and its financiers can. So these deals tend to have the deployer take the money, lease the system back to the condo (with the lease payments covering the condo's loan costs, if any) and hand over the fully depreciated system after five years (the IRS limit) or a bit longer. Deployers can often work through consultants, state officials or local bankers to help arrange investments.

Major carriers entered what quickly became a high-interest environment in 2022 with bloated balance sheets that they generally want to reduce in size. The normal way to do this is to have smaller local carriers, often with federal funds available, build systems and establish cell sites, then lease them (or at least backhaul) to major carriers. The national carriers provide sure cash flow, making smaller carriers' lenders more comfortable. Leases must be carefully structured to keep them off the major carriers' balance sheets.

The profit problem for major carriers is that they must own an exclusive cell site to establish a competitive advantage that doesn't involve price cuts to customers. But federally funded BEAD projects must be open-access, with nondiscriminatory access to all carriers. So expect major carriers to apply for federal funds themselves and eventually lobby for rule changes. Local deployers must work in their states to achieve the right balance.

The FCC model, using Universal Service Fund money from (disappearing) voice phone fees to subsidize operating costs but not build systems, seems to be outdated. And the fund itself is evolving to tax broadband traffic rather than voice. But as 2022 ends, the FCC is hobbled by the lack of a working majority. The two Republicans and two Democrats on the commission have been more cordial than many other niches in the federal government but cannot act boldly enough. As this article went to press, a full Senate vote on the Biden nominee, Gigi Sohn, has been blocked for a year. The nomination dies unless she is approved in a lame-duck session before the new Congress is seated in January.

At the very least, some additional funds could be reallocated to subsidize telemedicine and remote mental health access. Those programs have been successful but underfunded and judging by the applications, could easily make good use of twice the roughly $1 billion allocated to them now (see fcc.gov/connecting-americans-health-care).

Deployers and potential deployers must pay extra attention to the new FCC broadband availability maps that were due to be formally released just before Thanksgiving and finalized late this coming spring.

All of this requires that federal and state governments pay more attention to the *availability* of money, not merely its cost as expressed by interest rates. The Federal Reserve, for example, needs to lighten up on funds for building infrastructure such as broadband that lead to overall cost savings in the economy. And no infrastructure returns calculatable economic benefits faster than broadband. All that new federal funding can't help deployers unless the deployers can raise their share. Fortunately, many states have indeed stepped up with their own funding mechanisms. ❖

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