

EXPLORING OPPORTUNITIES: IMPACTS ON THE DIGITAL INFRASTRUCTURE SECTOR (ASIA)

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Legal Briefings

The pandemic has reinforced the need for, and criticality of, resilient digital infrastructure.

How providers will innovate and adapt to changing business and consumer demands post-crisis remains to be seen.

What is clear, however, is that the disruption and uncertainty of the last few months has generated some exciting, if not necessary, opportunities for the sector, particularly in Asia.

CHANGING THE WAY WE COMMUNICATE

Social distancing, self-isolation and other measures implemented have radically changed the way we communicate and work.

With as much as one-third of the world's population in lockdown over the previous months, the demand for digital communications and the infrastructure services that underpin them has risen dramatically.

This increase in demand has placed significant and unprecedented pressure on existing infrastructure. As digital infrastructure providers transition from emergency response to "business-as-usual" (however that may be defined), they will need to adapt to sustained levels of demand and future-proof their infrastructure, service offerings and business models for a post-pandemic world.

THE CHALLENGES FACED BY DIGITAL INFRASTRUCTURE IN ASIA

Digital infrastructure providers have faced a number of significant disruptions and challenges due to the pandemic.

Telecoms operators have experienced greater pressure on their networks. Leading Asian mobile network operators (MNOs) have reported increases in internet traffic of up to 40% across their fixed-line and mobile networks. Mobile voice traffic has also boomed and there has been disruption to some voice services as regional MNOs have reallocated spectrum resources from voice to data. For some MNOs, already declining revenues have been further hit by lockdown restrictions prohibiting over-the-counter pre-paid top-ups.

Postponed 5G auctions and construction disruption have delayed the commercial launch of 5G, particularly in Southeast Asia. Stakeholders are encouraging regulators to host 5G auctions online as a health precaution and to avoid further delays to commercial launches. In contrast, the Chinese government has called for the accelerated roll-out of new digital infrastructure such as 5G networks and data centres, and the three Chinese MNOs aim to deploy over 550,000 base stations by the end of 2020, expanding coverage to an estimated 300 cities.

In Asia, remote working requirements and the use of videoconferencing tools and other digital applications have **dramatically increased the demand for computing and data capabilities**. This increase in demand has placed significant pressure on data centres to operate, and data centre operators have been forced to balance staff safety with availability and continuity of service obligations to customers. Some co-location providers have closed data centres to the public except for critical work. Several data centre projects have been paused due to safety concerns, including Facebook's data centre campuses in Ireland and Alabama. In Asia, some operators are accelerating the expansion of capacity at existing locations and looking to develop further locations.

Significant supply chain disruptions are also starting to emerge as a result of factory shutdowns and other lockdown restrictions in Asia, North America and Europe. Digital infrastructure providers are reviewing their supply chain arrangements and preparing for medium-term disruptions. Analysts predict that Covid-19 and underlying geopolitical trends towards fragmentation will accelerate the on- or near-shoring and diversification of supply chains and an overhaul of existing procurement policies.

The pandemic is a reminder of the critical importance of keeping digital infrastructure operational. In many countries in Asia, as in other parts of the world, fibre connections, submarine cables, telecommunications networks, data centres and their supply chains are treated as essential services and critical infrastructure. In parts of Asia, official exemptions from Covid-19 restrictions for supply chain participants have not been entirely clear cut, and suppliers have been unable to obtain or have experienced delays in obtaining the required approvals to continue to operate.

OUR POST-CRISIS INVESTMENT PREDICTIONS

The pressure that the pandemic has placed on existing digital infrastructure, providers and other key industry stakeholders has also highlighted growth and investment opportunities for the sector in Asia.

There is a clear need to reinforce existing infrastructure and roll out new infrastructure across the region – not only to address the pandemic, its aftermath and future pandemics, but also to support the ‘new normal’ in digital communications post-crisis. Greater investment is needed, from both the public and private sectors.

We set out below our key predictions for post-crisis investment opportunities in the sector in Asia.

1. STRONG POST-CRISIS INVESTMENT OPPORTUNITIES

Analysts predict that telecoms will experience some of the strongest post-pandemic investment because of the sector’s demonstrable resilience during economic downturns and the emphasis that some governments will give to 5G deployment and fibre in economic stimulus packages.

The pandemic has disrupted some M&A processes in Asia but appetite remains reasonably strong, particularly for mobile towers, data centres and subsea cables, as greater demand is placed on digital infrastructure services. There are at least four active tower deal processes underway in Asia at present, despite pandemic restrictions.

M&A activity is expected to pick up in the second half of 2020, driven in part by stimulus from central banks and distressed sales. The Malaysian government has pledged US\$92 million to expand the country’s telecommunications network and improve quality as part of a second stimulus package announced in late March. Bankers are expecting distressed sales in emerging markets in Asia in the coming months, with travel tech and digital marketplace businesses likely targets.

The priority for digital infrastructure providers will be to pump investment into their core infrastructure. For MNOs in particular, increased demand and declining revenues may require mergers and other investment opportunities in order to fund capex.

2. DEPLOYMENT BY INFRASTRUCTURE INVESTMENT FUNDS

Infrastructure funds remain the most obvious source of funding for the sector. Approximately US\$350 billion worth of dry powder is available for Asia-focussed funds to deploy, much of which is targeted at investments in the digital infrastructure sector.

Equinix and GIC have recently announced a US\$1 billion joint venture to develop and operate data centres in Japan, while Lendlease's data centre fund has US\$1 billion ready to deploy in completed assets and new development opportunities in the region.

Infrastructure funds that have historically invested in fibre and tower company separation projects in the region are expected to retain, and certainly appear to be retaining, their appetite for these projects. Fibre, in particular, will be a safe bet for infrastructure funds with the huge traffic demand on metro and residential fibre networks. The willingness of the global and regional tech giants to fund key infrastructure projects is particularly attractive to infrastructure funds.

3. DATA CENTRE GROWTH SET TO CONTINUE

Lockdowns may be delaying construction projects and disrupting supply chains but the data centres sector is likely to grow in the long term. The pandemic will accelerate the transition to the cloud, and everything "in" the cloud will need to be accessed from highly secure and resilient data centres and transported through resilient, high-capacity fibre networks.

Prior to the pandemic, construction of new data centres had been growing globally at a compound annual growth rate of 8.61% since 2017, and the Asia Pacific market alone was set to be worth US\$32 billion by 2023, second only to the United States.

The relatively new designation of data centres as essential infrastructure, coupled with growing demand from hyperscalers and tech giants, should continue that trajectory. Currently, there are a number of active data centre opportunities in Asia, particularly in China, attracting strong interest from strategic buyers and infrastructure funds. Virtual due diligence investigations of physical data centre sites and virtual technology audits are being carried out to progress deals, although deal origination is likely to suffer until lockdown restrictions are fully lifted.

4. DIVERSIFICATION OF REVENUE STREAMS

Telecoms operators faced with declining revenues and the pressure to invest more to deal with rising demand may do well to diversify revenue streams by tapping into adjacent markets. There may be opportunities for operators to pick up IT service providers, software developers, cloud-based services and e-commerce providers that may have previously been out of reach due to high valuations but have become distressed in lockdown.

Other attractive opportunities will lie with companies that provide remote communications services. Flickstree, an Indian AI-based video publishing network backed by Facebook's FbStart program, is currently receiving interest from international investors for its US\$20 million Series B round following a successful Series A round in February 2020 led by Samsung Venture Investment.

5. PREPARING FOR FUTURE HEALTH CRISES

The pandemic has demonstrated the key role that digital infrastructure plays in predicting and modelling disease outbreaks. The pandemic has created, and will continue to create, opportunities for digital infrastructure providers to work with governments and the healthcare sector to develop innovative tools, including community-driven contact-tracing technologies to combat and prepare for future health crises.

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