Industry Briefing

Economist Intelligence Unit The Economist

Europe telecoms: Crunch time

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FROM THE ECONOMIST INTELLIGENCE UNIT

Despite the growing popularity of smartphones and data plans, mobile operators are struggling to increase revenues.

It is hard to imagine that smartphones were once considered niche products for businesspeople and big spenders. In Germany, two out of every three mobile devices sold by Telekom Deutschland are now smartphones, with Apple's iPhone one of the most popular gadgets of all.

Telekom's mobile data plans are also in higher demand. Smartphone users like to browse the internet, share photos, download music and watch video clips, all of which chew up mobile data. If they are to get the most out of their snazzy smartphones, then, customers will have to fork out for a monthly data allowance. Telekom, during the nine months ending on September 30th 2011, managed to rake in €1.2bn in mobile data revenues, 30% more than in the same period of 2010.

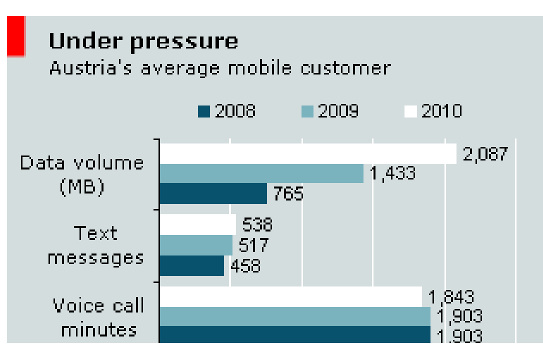
But that is where the goods news ends for Telekom, which has the biggest mobile-phone business in Germany (based on service revenues). Over the same nine-month period, the firm's overall mobile service revenues fell by 2.6%, compared with the first three quarters of 2010, to €5.15bn. A decline in revenues from voice calls and texting—still the bread and butter of the mobile-phone business—has more than off-set the mobile data gains.

Stiff competition partly explains the overall revenue drop—there are four mobile network operators in Germany vying for customers—but so do regulatory measures. In February, the Federal Network Agency (FNA), the German regulator for telecoms, slashed Telekom's mobile termination rates (MTRs) by nearly 50% to 3.38 eurocents per minute. Because they serve so many customers, large operators like Telekom terminate lots of calls from other networks, and so they suffer more from MTR cuts than their smaller rivals.

Squeezing it even harder, Telekom is being forced to make new investments to cope with the soaring volumes of mobile data traffic. According to the FNA, the volume of mobile-generated data was 65m gigabytes in Germany in 2010, a doubling of the previous year's amount. Telekom has added more capacity by upgrading its third-generation (3G) network and rolling out '4G' technology in urban and rural areas, but none of this comes cheaply.

Not just Telekom

The pattern of rocketing data traffic and subdued revenue growth can be found in other developed markets aside from Germany. In neighbouring Austria, RTR, the national regulator, reports that average revenue per user fell from €235 in 2009 to €215 the following year. Meanwhile, the average customer used 2,090 megabytes of data in 2010, up 46% on the previous year (see chart).



Another striking feature of the Austrian market is the drop in voice call minutes. That trend will likely be repeated in other developed markets where mobile data volumes are rising sharply. When customers begin interacting on social networking sites, or sending photos and video clips, they feel less need to make ordinary voice calls.

Over in Sweden, the Swedish Post and Telecom Agency (PTS) says national mobile data traffic

volumes jumped 91% to more than 53
terabytes during 2010. Overall revenues from mobile subscriptions (including voice and texts), however, rose by a more modest 14%. In the UK, Ofcom, the telecoms regulator, says that while mobile data volumes increased by 23 times between the fourth quarter of 2007 and the fourth quarter of 2009, mobile data revenues only doubled over the same period. The gap between growth in volumes of data traffic and an increase in revenues has been widening for some time.

It is going to get tougher

Large operators, already miffed by MTR cuts, face more regulatory intervention on pricing. In Europe, MTRs are calculated on the basis of cost modelling. Because network costs are being increasingly allocated to data traffic, the incremental cost of providing voice minutes is falling. This means—using the cost-model approach—that regulators have got more room to force MTRs down.

Ominously, for European operators, the European Commission (EC) has also drafted new 'roaming regulation'. The EC is turning its attention to the prices operators charge one another for carrying voice calls, texts and data services when their customers roam on to other networks abroad. Roaming charges for customers are also due to come under closer scrutiny.

Moreover, from 2012 the EC aims to make it compulsory for operators to wholesale network capacity to so-called MVNOs, or mobile virtual network operators. With no network assets of their own, MVNOs would be able to piggy-back on the network investment already made. If the wholesale charges are tightly regulated, network operators face the threat of increased competition on terms they cannot determine.

If operators are to have a mobile broadband business case, they will need to manage tightly the cost of carrying greater volumes of mobile data traffic. They will also, in all likelihood, need to attract a substantial number of customers that value the higher speeds of '4G' and upgraded 3G networks, and are willing to pay extra for this. Unfortunately, for operators, that is by no means certain.

Source: Industry Briefing