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Telecom operators in the GCC survived the financial crisis and maturing markets by adjusting to the end of explosive growth. How ready are they to adapt again to new industry trends?

After years of strong growth, Gulf Cooperation Council (GCC) telecom operators have slowly adapted to the new realities of their maturing markets. Rising oil prices contributed to sharp increases in the level of gross domestic product (GDP) per capita, creating an attractive telecoms market. Between 2004 and 2007, GCC telecom revenues grew 15 percent annually, with earnings margins hovering around 47 percent. Fueled by growing profits and healthy cash flow, GCC operators went on a buying spree across the Middle East, Africa, and Asia, acquiring existing operators or licenses to launch their own networks.

Telecom operators worldwide face numerous obstacles to their continued success such as stagnating growth, heightened competition, increasing investments in new technologies, and growing consumer sophistication. As these trends are still nascent in the region, GCC telecom operators have thus far implemented tactical, short-term initiatives to overcome these obstacles.

Opportunity abounds for GCC operators to prepare for future challenges by adopting a comprehensive cost management plan, addressing incremental efficiencies, process reengineering, and value chain restructuring. Operators that do not implement wide-ranging plans to manage their costs run the risk of steep declines in profitability.

Network costs are on the rise. An insatiable appetite for more data is forcing telecommunication companies to invest heavily in next generation networks. At the same time competition has gone global, creating enormous

price pressure in most markets. On the other hand, with declining revenues from traditional income sources such as wire line and wireless voice, the pressure is on to look for new products and services, but many are struggling.

GCC operators are now turning their attention outward again—adapting to new industry dynamics and getting ahead of the latest trends in the global telecom industry.

Data, more data

The Middle East has not been immune to the worldwide explosion in data, driven by data-savvy consumers and the deployment of a vast portfolio of mobile applications. Statistics from YouTube, which accounts for 24 percent of global mobile traffic, reveal that Saudi Arabia has the world's most YouTube clicks per Internet user (more than 90 million daily page views.) The Middle East ranks second after the United States in number of daily views, with 167 million video views per day. The Middle East and Africa are expected to have year-on-year data increases of 133 percent through 2014.

Technology

To meet the rising demand for data, operators must continually expand network capacity and roll out new technologies, such as fiber-optic networks and high-speed mobile broadband (4G), all while facing pressure from shareholders to limit capital expenditures and maintain healthy cash flow and attractive returns. Several GCC telecom operators have made huge investments in fiber networks and Internet Protocol television (IPTV) platforms, although the financial returns are not yet clear. Newer players are competing with embedded media ecosystems.

Aggressive OTT players

The rise of new competitors, broadly dubbed over-the-top (OTT) players, has the potential to impact the global telecom industry. They offer attractive services via their

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own platforms and ecosystems, including voice over Internet Protocol (VoIP), instant messaging (IM), and services such as TV, video, and music. And while subscribers pay telecom operators for fast connections, most revenue comes from pay-per-usage and advertisements. Operators benefit by charging subscribers for data consumption, but it is often restricted by data packages that offer unlimited data. As a result, the battle between operators and OTT players has begun for voice revenues (especially high-margin mobile international traffic), Short Message Services (SMS), and media.

Consumer behavior

Not so long ago, subscribers would make conscious decisions about which telecom operator to join, if they had a choice at all. Low-value subscribers generally chose the best value-for-money option, and high-value subscribers chose the operator with the best network and the most extensive portfolio of value-added services. Today's subscribers want the latest smartphones, tablets, applications, and content, most of which is neither owned nor sold by an operator.

How to adapt with new trends

Although some of these services have been around for a few years, operators have to actively offer value added services (VAS) such as M-Health, M-Education, and M-Banking. They will need to offer high quality voice solutions to limit the impact of eroding revenues and profitability from Voice-over-Internet Protocol (VoIP) players such as Skype.

To fight the decrease in SMS usage, operators need to consider offering enhanced functionalities in the instant messaging (IM) domain such as multi-user conversations, sharing of pictures, and status updates, by either partnering or entering alliances with other players, or by offering their own platforms.

The mobile telecoms market in the region continues to display signs of growth. Driven by strong mobile handset data growth, telecoms service revenue in the Middle East and North Africa (MENA) region will grow at a compound annual growth rate (CAGR) of 2.9 percent during 2013-2018 (mobile at 3.3 percent and fixed at 2.8 percent), to reach US\$96 billion in 2018.

Operators will need to also invest more in machine-to-machine (M2M) communication, which is expected to be a major growth market. The right partnerships to bundle connectivity with high value products (for example e-readers, cameras, laptops, cars and Internet of Things (IoT)) is critical.

Lastly, operators will increasingly need to enter the nascent, fast-growing cloud services market, which is opening up opportunities in consumer and enterprise businesses. Because the cloud market is relatively new, this is the optimum time for telecom operators to begin to capitalize on the opportunity with the right value propositions, the right technology and go-to-market partnerships and investing in large data centers.

Growth of mobile in MENA

The mobile telecoms market in the region continues to display signs of growth. Driven by strong mobile handset data growth, telecoms service revenue in the Middle East and North Africa (MENA) region will grow at a compound annual growth rate (CAGR) of 2.9 percent during 2013-2018 (mobile at 3.3 percent and fixed at 2.8 percent), to reach US\$96 billion in 2018.

The market will continue to be dominated by mobile. Mobile retail revenue will grow from US\$50.4 billion in 2013 to US\$59.1 billion in 2018. Growth will be driven by handset data spending, with smaller contributions coming from non-handset mobile broadband and mobile voice. The fixed market will also continue to grow in all countries—from US\$23.7 billion in 2013 to US\$27.3 billion in 2018, driven by fixed broadband and IPTV revenue, while fixed voice revenue will decline in most countries.

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At country level, five of the eight major markets that we model individually—Algeria, Morocco, Qatar, Saudi Arabia and the UAE—show strong net growth in telecoms service revenue. The fastest growing of these will be the UAE, at just over 3 percent CAGR, closely followed by Algeria and Saudi Arabia. In Kuwait, revenue will decline at a CAGR of -0.2 percent. Egypt will only experience marginal growth because of political instability.

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The power to survive

The GCC telecoms industry continues to be a highly dynamic sector and GCC operators are faced with considerable challenges in 2014 and beyond. Operators that act now will ensure they remain relevant and maintain healthy growth and profit margins.

Operators, particularly those in GCC countries, need to be prepared for the significant impact of over-the-top (OTT) messaging and eventually voice, as the penetration of smartphones passes the 50 percent mark. Early movers in 4G deployment should aim to maximize the initial opportunity for premium pricing for 4G, but international examples show that the 4G premium is not sustainable, so it is important to be realistic about the length of time this can be maintained. Alternative strategies to monetize mobile data are critical, as are strategies to accelerate revenue development from adjacent market partnerships and new business models. To cope with increasing network complexity, investment

requirements and the financial expectations of shareholders, GCC operators will continue to improve their balance sheets by off-loading assets and adopting a more asset-light model in line with developments in Asia, Europe, and North America. As a consequence, more managed services outsourcing deals of core activities such as network operations and maintenance are expected, as is the selling of assets, such as towers, to specialized tower companies. Operators will benefit from the scale and expertise of these third parties and be able to move from the traditional network and infrastructure focus to critical topics such as pricing, retention, customer experience, and digital diversification.

by **Omar Massaed**, senior director, Audit, Deloitte Middle East

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