# Time to accelerate growth

*How telcos can fuel growth via 5G and diversification*

Executive summary - TIME global report

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Arthur D Little

# Executive summary

## Introduction

The "scissor effect" of a widening gap between revenue and investment means that the pressure on telecom companies' cash flow has never been so intense. Left with limited resources to invest into the industry, telecom executives have their backs against the wall, trying to deliver growth while juggling both increasing capex and investor unwillingness to cut back dividends. The COVID-19 pandemic has not helped. As data traffic has soared and for the first time exceeded supply, telecom network upgrades have been high on even governmental agendas. The 2020 edition of our flagship report focuses on a solution to these challenges – unlocking value through asset reconfiguration in order to finance growth and transformation via 5G and diversification.

Our study represents a truly global view, with over 100 C-level interviews conducted between March and September 2020. Our analysis shows that over 90 percent of respondents have considered alternative options to unlock value from network assets. However, it also shows that while most, if not all, telcos have tested the waters of asset reconfiguration, there is incremental value to be extracted as models evolve. In addition, many other questions of value creation remain an executive priority, but are unclear, including ways of monetizing 5G and future value chain positioning of telecom players.

This report proposes means by which telcos can unlock incremental value and reinvest it in high potential growth areas. We hope this will serve as guidance on how to succeed going forward.

## 5G as an oxygen boost to the economy

With the 5G journey at its start, disruption and innovation will occur in three key value-creating business segments:

- In order to unlock the potential of 5G from a B2C perspective, telco and media companies need to form alliances to create compelling use cases for consumers. It is often not the novelty of the commercial setting, but rather, the added value of the content, experience, or device that creates excitement among consumers. Bundling these three areas and engaging with consumers in a different manner offers opportunities for monetization. We predict that launching 5G premium bundles for content will be the most value-creating option for telcos, and may lead to an enterprise value (EV) increase of more than 10 percent.
- From a B2B perspective, while there is €60bn to be captured in the mobile private networks (MPN) space, competition from non-MNOs is heating up. To compete effectively in this market, telcos will need to provide an end-to-end value proposition, enriching their vendor portfolios and seamlessly integrating various wired and cellular technologies in both an IT and OT environment. Beyond MPN, network slicing represents a substantial opportunity to capture

incremental value. We expect to see both single-tenant and multi-tenant slices, though we suggest that telecom operators initially collaborate with a relatively small set of customers while preparing for others to come: railways, energy and utilities, blue-light organizations and broadcasting companies to begin with, followed by transport & logistics, healthcare, traffic management, drone operations, financial services and others.

- Furthermore, the substantial investment in 5G networks requires telcos to think beyond B2C and B2B business models. A key enabler to tap into further potential value creation is structural separation into ComCos and NetCos. The NetCo can be used as a base to kick-start new wholesale business across multiple 5G models by positioning itself as a neutral infrastructure provider. Such positioning could deliver an overall enterprise value increase of up to 60–75 percent, partly through financial engineering, but mostly due to unlocking new wholesale revenues.

## Beyond telcos' core strategy: How to succeed?

Telcos have tried to develop new opportunities beyond their core businesses for decades. While the array of diversification opportunities is vast and players are becoming ever more radical in their efforts, the more important question to resolve in order to create value is ***how*** to diversify. Arthur D. Little's benchmark of telecom diversification initiatives shows that less than 15 percent of initiatives are generating sizable revenue 24 months after launch. Most of the time, revenue contribution of "Beyond Core" initiatives remain highly marginal as telcos are facing multiple internal challenges, which bring down the initial ambition.

To succeed in implementing a successful Beyond Core strategy, a telco should first adopt a "test and fail" mind-set. During the concept selection phase, the Beyond Core team should think in start-up mode and ensure that concepts meet three requirements: they answer a client need with tangible benefits; are aligned with the telco core strategy; and are not immediately replicable by competitors. Once the business potential and telco legitimacy are confirmed, the concept needs to be actioned. Diversifying means that teams will enter unknown territories. Early-stage engagement with potential partners – in particular, disruptive solution providers – provides an opportunity to proof-test concepts, strengthen them, and optimize the utilization of internal resources.

Overall, in order to successfully diversify, the telco needs to follow four priorities: target sizable revenues, but also have a clear growth plan per diversification domain; build a multi-model approach combining internal and external resources (beyond M&A); set up a diversification office structured in private equity mode; and follow a phased and agile approach in execution with sequential prioritization of concepts.

## Asset monetization: More than ever, now is the time to reconfigure telco assets

Asset reconfiguration has been accelerating over the last years, with ever more complex models emerging. Reconfiguration has unlocked value for shareholders in multiple ways: securing new funding, increasing consolidated EBITDA and revenues, and increasing overall enterprise value.

TowerCos have spearheaded value creation with multiple benefits – from cash proceeds for the MNO to dynamic development of TowerCo infrastructure assets delivering very high multiple valuations. Looking forward, TowerCos could expand their services in the infrastructure market along several paths, such as entering the active infrastructure layer and expanding horizontally into new asset classes. Beyond TowerCos, telcos are looking towards more comprehensive asset reconfigurations, including legacy fixed networks, mobile radio access networks and edge data centers, as new growth areas.

Telco asset reconfiguration can drive value creation in six ways: accelerating deployment by lifting financing constraints, increased asset utilization, de-risking investment, strengthening the wholesale value proposition, increasing management focus on the distinct core businesses, and possibly preempting unfavorable regulatory decisions. While some of these benefits can be enjoyed through network-sharing agreements or internal governance changes, asset reconfiguration offers a way to capture all these full benefits. However, asset reconfigurations also have their own challenges, and the value creation equation needs to be carefully assessed based on the specific market context of each telco.

Shareholders need to be aware that with NetCo and ComCo reconfigurations, telcos are shifting away from yield stocks to infrastructure rollout stocks and growth stocks. On the one hand, the cash flows of NetCos will need to be isolated to match the investment profile of greenfield infrastructure investments, i.e., massive upfront investment followed by a stable yield over the long term. On the other hand, without a (passive) network, the ComCo will have to justify its capex level and therefore face a choice: become a growth stock or stay a yield stock.

# Authors

**Karim Taga**
Managing Partner
TIME*, Vienna
taga.karim@adlittle.com

**Gregory Pankert**
Partner
TIME, Brussels
pankert.gregory@adlittle.com

**Paul Desjonqueres**
Principal
TIME, Paris
desjonqueres.paul@adlittle.com

**Christoph Uferer**
Principal
TIME, Vienna
uferer.christoph@adlittle.com

**Gabriel Mohr**
Principal
TIME, Vienna
mohr.gabriel@adlittle.com

**Bela Virag**
Managing Partner
TIME, Vienna
virag.bela@adlittle.com

**Glen Peres**
Senior Manager
TIME, Vienna
peres.glen@adlittle.com

**Dobromira Boyadjieva**
Principal
TIME, Dubai
boyadjieva.dobromira@adlittle.com

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*TIME: Telecommunications, Information Technology, Media & Electronics

# Contacts

If you would like more information or to arrange an informal discussion on the issues raised here and how they affect your business, please contact:


**Austria**
Karim Taga
taga.karim@adlittle.com

**Belgium**
Gregory Pankert
pankert.gregory@adlittle.com

**China**
Yusuke Harada
harada.yusuke@adlittle.com

**Czech Republic**
Jiri Steif
steif.jiri@adlittle.com

**France**
Julien Duvaud-Schelnast
duvaud-schelnast.julien@adlittle.com

**Germany**
Michael Opitz
opitz.michael@adlittle.com

**India**
Barnik Maitra
maitra.barnik@adlittle.com

**Italy**
Giancarlo Agresti
agresti.giancarlo@adlittle.com

**Japan**
Shinichi Akayama
akayama.shinichi@adlittle.com

**Korea**
Kevin Lee
lee.kevin@adlittle.com

**Latin America**
Guillem Casahuga
casahuga.guillem@adlittle.com

**Middle East**
Andrea Faggiano
faggiano.andrea@adlittle.com

**The Netherlands**
Martijn Eikelenboom
eikelenboom.martijn@adlittle.com

**Norway**
Lars Thurmann-Moe
thurmann-moe.lars@adlittle.com

**Poland**
Piotr Baranowski
baranowski.piotr@adlittle.com

**Russian Federation**
Alexander Ovanesov
ovanesov.alexander@adlittle.com

**Singapore**
Tomasz Izydorczyk
Izydorczyk.Tomasz@adlittle.com

**Spain**
Jesus Portal
portal.jesus@adlittle.com

**Sweden**
Agron Lasku
lasku.agron@adlittle.com

**Switzerland**
Michael Opitz
opitz.michael@adlittle.com

**Turkey**
Coskun Baban
baban.coskun@adlittle.com

**UK**
Nicholas Johnson
johnson.nicholas@adlittle.com

**USA**
Sean McDevitt
mcdevitt.sean@adlittle.com