


How to build growth in emerging markets

It's a mistake to believe that emerging markets are years behind developed nations, and that the former will eventually look like the latter. In reality, operators in emerging markets are way ahead in extending the traditional role of an operator. This spurs business innovation and is a lesson to all.

 In emerging markets they know how to make money from customers who have practically no money at all. That's a feat in itself, but not enough. You also need to look beyond short-term profits. Let's look closer at how this can be done.

Low-disposable-income customers, people with USD 5 or less to spend per day, are the mainstream of Southeast Asia's emerging and high-growth markets today. Operators' Earnings Before Interest, Taxes, Depreciation and Amortization (EBITDA) figures are astonishing, with some currently achieving EBITDA of 60 percent or greater, as compared to 30–40 percent for Western operators.

With worldwide mobile growth approaching the 50 percent penetration mark, many people have speculated about the next billion subscribers. Growth will be coming from countries such as China, India, the United States, Pakistan, Nigeria, Brazil, Indonesia, Bangladesh, Mexico, and Iran.

According to Portio Research, the Asia Pacific region will account for 65 percent (980 million) of the global net additions from 2007 to 2011. China and India have always been popular examples of tremendous market growth opportunity in the Asia Pacific region. I would like to focus on the Southeast Asia market as a dynamic illustration, where much will apply to similar emerging markets in the rest of the world.

Southeast Asia, with a population of 750 million, presents an attractive 65 percent untapped market for mobile ser-

point

» **Low-income, mainstream customers are central to the mobile business in emerging markets, but high-end users can provide a stable source of revenue. You need to understand both.** «

vices. The region records the highest Short Message Service (SMS) growth globally, from the Philippines, which sets a global benchmark for high operator margin as well. Mobile operators Smart and Globe generate an EBITDA of 60 percent and above, respectively.

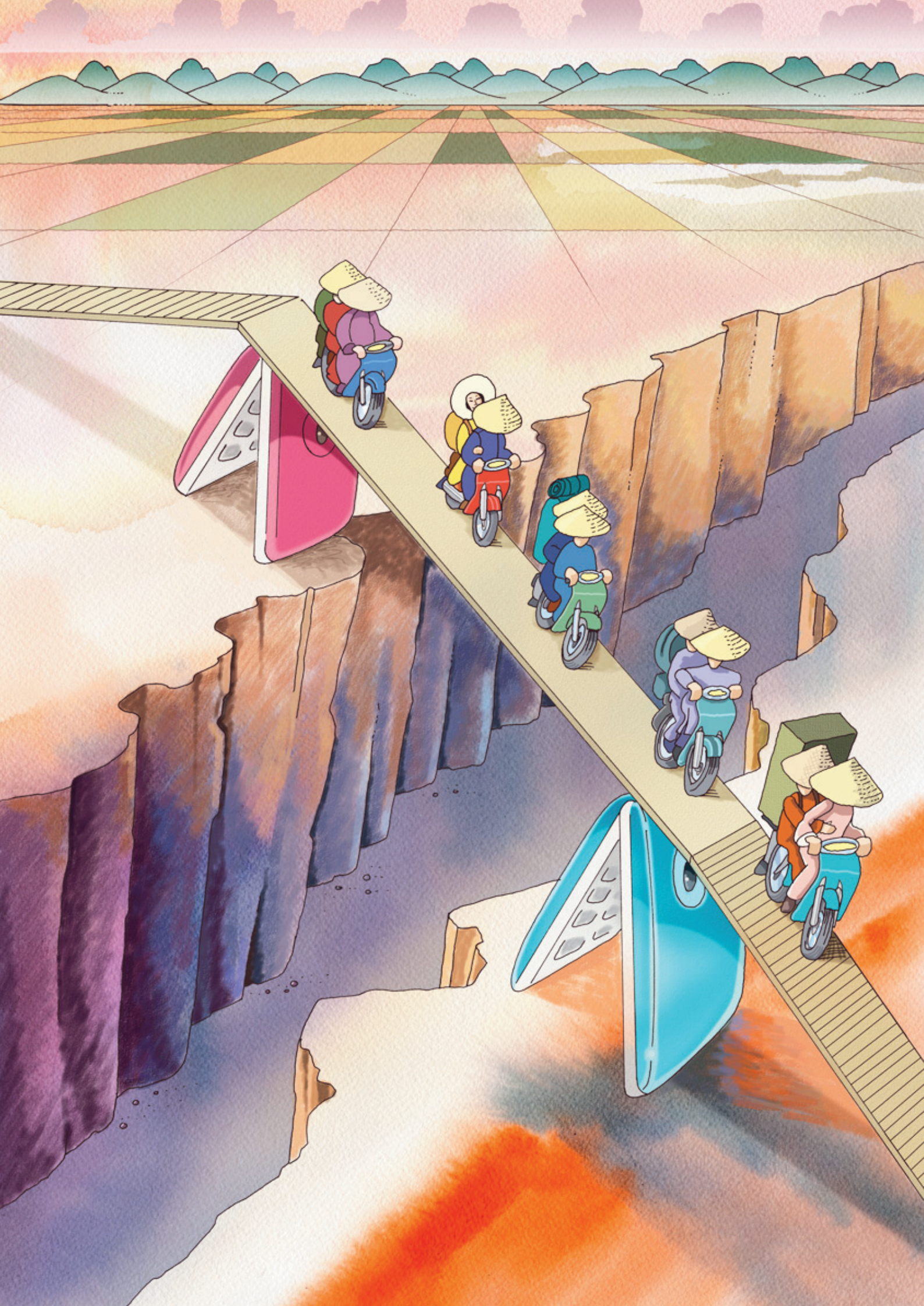
Low income is mainstream

Most mobile users today come from the cities: youth, young professionals, micro-entrepreneurs, and average users. In general, the mobile generation consists of highly educated young people and singles in the 25–34 age bracket, who usu-

ally have illiterate parents and grandparents. Status recognition and up-trended lifestyle are their key values.

Mobile users are usually early adopters of new phones and services and are receptive to technology and innovation, which indicates higher interest in advanced services than commonly found in developed markets. Advanced users, however, contribute only 5–20 percent to operator revenues. In mobile high-growth countries, such as Bangladesh, Indonesia, the Philippines, and Vietnam, the advanced mobile user segment represents only 5–10 percent of revenues. This market contributes more than 86 percent of current and future growth for mobile communication services. In more highly penetrated markets, such as Malaysia, Thailand, and Brunei, 10–20 percent of revenues come from the advanced user segment. In general, low-disposable-income mobile users in the emerging markets are the mainstream contributing to operator revenues.

Operators in emerging markets often believe that they can secure revenues from this segment by increasing penetration with competitive pricing, in conjunction with securing high Average Revenue Per User (ARPU) from advanced users by working with churn management, customer retention, loyalty programs, and Customer Relationship Management (CRM) initiatives. This is a delusion, in my opinion. I have seen many operators invest much in customer retention, reward programs, or CRM,



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STRENGTHS

- High economic growth market where users are increasingly better-off overtime
- High mobile penetration rate, large volumes – allows economies-of-scale
- Consumers desiring mobile services – a status symbol in developing markets
- High youth segment population hence uptake of data services is high and will be growing
- Highly profitable
- Operators and consumers are highly dynamic and open to new ideas

OPPORTUNITIES

- Opportunity for innovative services, solutions and business models with lower costs structure
- Due to a high volume environment, economies-of-scale to competition is realistic
- Opportunity to leverage revenues through new non-telco revenue areas
- Leap-frogging opportunities on mobile broadband, mobile commerce, mobile banking, mobile TV, etc.
- Luxury to leverage on unique local culture and global success stories
- To offer services on 2G, 3G, mobile broadband
- Foreign investment in the form of equity or technology

WEAKNESSES

- Low ARPU users with low income
- Market still quite strongly regulated
- Users can't afford to pay for more sophisticated mobile phones hence most mobile phones are basic
- Very competitive market with high churn rate
- Consumers and competitors are price-sensitive
- Primarily still a voice-based market
- Value-added services hindered by diverse languages and illiteracy obstacles

THREATS

- High barriers to entry with mainstream users living in rural environment with poor infrastructure, poor education system, little access to health care and locations with poor logistics
- Mainstream users earn USD 5 per-day hence operators need to be very innovative ensuring services meet priority needs
- A low-cost operating model – strong needs for low-end handsets and low-cost service solutions
- Political instability
- Regulatory interference

while internally cannibalizing their subscriber base through unsynchronized subscriber acquisition strategies with inappropriate pricing and packaging.

India's lifetime subscription plans show that, although they attract large volumes of new subscriptions, the ARPU is not sustainable. Mobile users in emerging markets are very price sensitive, so operators must realize that waging price wars to get new users is a short-term tactic that will not sustain revenue generation in the long run. Conversely, offering new empowering and innovative services that genuinely meet user needs will make a remarkable difference.

Though low-income, mainstream customers are central to the mobile business in emerging markets, high-end or advanced users can provide a stable source of revenue to help mitigate the volatility of the low-end prepaid private market. You need to understand both the mainstream and the advanced-user segments in order to achieve profit equilibrium.

The math of revenue growth

The challenge is to be profitable with the low-disposable-income customers growing wealthier in pace with their developing economy.

In the graph above is a strengths/weaknesses/opportunities/threats (SWOT) analysis that reflects the market opportunities and challenges for operators to shape the economics of the emerging market.

With a share-of-wallet spend of 5–10 percent on mobile communication by low-income customers, the Southeast Asia market is worth an estimated USD 13 billion per annum with the mainstream existing mobile users. Conservatively estimated, the market size could be USD 29 billion per annum by 2011.

There is so much more to make money from

Opportunity exists not only to harvest the mobile communication needs, but also to expand growth by connecting the unconnected in the emerging market, to

truly shape the economics of the developing economy, quality of life, and the economic pillars. There are many cases where operators do not just play a traditional role but look beyond it and act as innovative service providers.

For instance, Smart and Globe in the Philippines act as financial service providers, facilitating foreign money remittance and mobile commerce as successful bankers in that market. Indeed, there are more mobile service retailers than bank branches in the Philippines.

Operators have a chance to shape and expand consumers' share-of-wallet for communications from 5–10 percent to 20 percent and beyond, through financial, retail, and other services. This is what I call "leveraged revenues." Note also that customers' disposable income will grow with the prospective prospering economy.

The fact that operators start off with a large volume of users, providing economies-of-scale, will help them build further with more revenue streams, adding more services to the basic ones. Lower network cost will help bring mobile services to the masses and more leveraged revenues later.

What do low-income earners want?

Mobile phones have become an important communication tool for people in rural areas. They help bridge the gaps in the everyday living environment. It is crucial to note that in many cases a village's family breadwinners are living in other countries as foreign labor to ensure that they can support their families or their children's education. This is especially common in the Philippines, Indonesia, Bangladesh, Cambodia, India, Malaysia, and other countries in the Asia Pacific region. Low-income earners' needs are unique and focused specifically on improving quality of life. I classify this in five categories, see next page.

Empowering services are important for addressing the user's fundamental needs, which can be communications or something else. Many traditional operators fail to realize that, for this group of

users, mobile communication isn't just communication. Examples of empowering services that successfully meet users' needs and wants include:

- G-Cash by Globe — meets the needs of 8 million Filipinos abroad, who remitted USD 13.4 billion per annum.
- Cellbazzar by GrameenPhone — a social empowerment service in Bangladesh that gives rural users an opportunity to generate revenue by making their stocks available via mobile to the urban entrepreneurs at cheaper cost.
- Bubble Talk, a VoicesMS service by Digi — a Malaysian operator helping many meet their love and belonging needs. Language is no barrier to expressing feelings.
- SmartLoad by Smart — in the Philippines, stimulates usage with convenience. Top-up of mobile communication value in a smaller denomination helped create small retailing business opportunities and reduce the operator's operating expenditures.

Users can of course only spend within their means. Empowering services that meet these needs specifically and are affordable for low-income users will stimulate their willingness to spend.


Assuring profitability

Many mobile operators wanting to break into emerging markets and rural areas complain about the difficulties. For instance, lack of basic transportation makes it difficult to set up base stations. High roll-out costs make operators unwilling to invest. But dynamic new market entrants view the difficulties as opportunities to get in and engage with the consumers. They have often succeeded and forced the incumbents to follow. The incumbents' risk aversion often gives a first mover the advantage.


The following classic example applies to both the emerging and the developed markets. Sensis, one of the largest publishers in Australia, is also a mobile advertising pioneer in Australia. Sensis owns the local mapping, yellow and white pages directories, as well as other vertical business directories such as job

Low-income earners' needs


Strengthening social networks



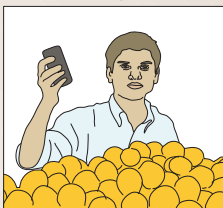
An alternative for immature infrastructure



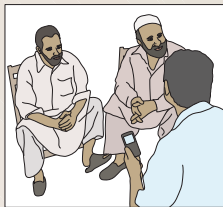
Contacts for security & survival



Generating income



Aspired status or modernization...



search, accommodation search, and the local professional e-community.

Sensis competes with Google with its online and mobile location and contextual search. Google is, of course, well known for its international search business and wants to get more local in order to create more value for advertisers and get closer to sales and transactions. Because Sensis was acquired by Telstra Group (the incumbent in Australia), Sensis was forbidden to partner with other mobile operators providing advertising offers across all Australia, which weakened its business core strengths to the advertisers. Telstra did not understand the advertising industry, and therefore unwittingly created a foothold for Google to craft a good market proposition and grow its mobile offerings.

This is a common behavior of most communication incumbents, and it created a global market opportunity for Google to partner with all mobile operators, thereby creating a major threat to Telstra and many other operators globally.

I asked a number chief marketing officers, business development directors, and marketing directors in the key operators of the Asia Pacific region how they achieved their high EBITDAs and what they have done to keep operating costs

down. My findings are summarized below.

1) Balance costs and revenues

To succeed in the low ARPU market requires balancing low- and high-end user segments to help control the key instruments in business operations, such as communication revenues, leveraged revenues, and operating and capital expenditures (OPEX, CAPEX). The graph on page 60 illustrates this further.

Operators generally have a higher margin from the high-end users in the high-growth market. Churn management or brand loyalty schemes are sometimes effective means of addressing high-end users, and maintaining and growing ARPU in this segment if the overall acquisition strategy is aligned with customer retention acts. The ability to cross-sell and up-sell relevant services to this group of subscribers will help increase revenues and margin.

A large subscriber base helps lower the overhead cost per subscriber and allows the operator to remain competitive. This is useful when price war tactics are needed. Over time, user volume increases with the market penetration rate; hence, leveraged revenues can be generated.

Revenues can be injected with further



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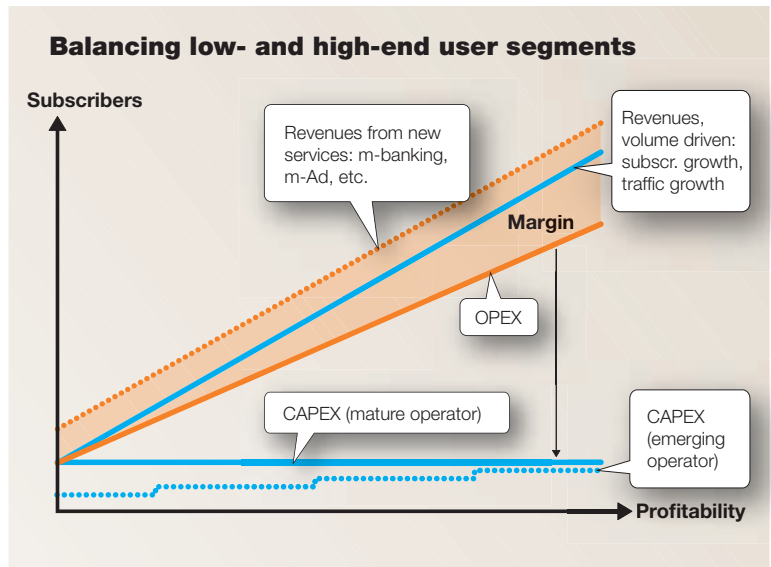
forced penetration rates via service offerings that lower the barriers to subscribe, such as prepaid sachets or low-denomination top-up cards, shared mobile phone or credit sharing, and so forth. Other services that can increase leveraged revenues are those beyond communications, such as mobile commerce, mobile banking, and mobile advertising.

To lower production costs, there are many options to consider. Managed or shared services, for example, help reduce capital spending yet reach new customers and obtain larger volumes.

Innovative low-OPEX operators such as Smart and Globe in the Philippines, Telkomsel and Excelcom in Indonesia, and GrameenPhone in Bangladesh are industry leaders with OPEX as low as USD 2.6 and below per subscriber per month. They use OPEX reduction tactics such as e-refill (or electronic prepaid mobile balance top-up) and build in-house distribution networks to reduce dealer commissions. Some keep customer care costs down by using a Wireless Application Protocol (WAP) portal and website instead of keeping a full customer service front to address inquiries. And having no subsidies on handsets is a major low-cost tactic that allows emerging market operators to take advantage of low labor costs.

Market leaders are built for low-end users but target high-end users for a better margin. Operators such as Smart and GrameenPhone desire to grow toward rich media, content, and services, looking beyond what a traditional operator would do:

- In 2000, Smart Philippine was granted an award by the GSMA for mobile banking. It did not gain much attention or profitability at first but today it is enjoying its harvest.
- Similar principles apply to GrameenPhone's Cellbazaar, which believes in looking beyond communication needs. Cellbazaar is a mobile directory service that helps connect farmers and fishermen in the village with the buyers in the city for trading stocks at lower prices.



- Smart Philippine was given an award for its new innovative services on mobile advertising in November 2007.
- Bangladesh's GrameenPhone is now exploring mobile advertising (for example, classified advertising via mobile) after its first attempt on Cellbazaar.
- Dialog GSM in Sri Lanka pioneered mobile insurance in third quarter 2007. Now this insurance sales channel is growing at a consistent rate.

2) Balance the service portfolio mix

There are two categories of service that a dynamic operator can offer:

empowering services that address the low-disposable-income user needs to improve the quality of their daily life; and innovative services that address the wants of those who are not constrained by their income for the basics.

My Competitive Service Portfolio Quadrant, on the following page, is a help to better position services.

No wonder operators complain of decreasing ARPU despite their growing EBITDA and total revenues. How can ARPU increase if the majority of services are low in ARPU? But there are more competitive empowering services available, such as credit sharing, which are

flexible and affordable and can drive penetration.

Look at the empowering services quadrant on the left. Many such services are transactional by nature, which means that subscribers will only use them when required and if they are affordable. If an operator uses empowering services solely to attract more subscribers, ARPU will inevitably decrease and become non-sustainable. This is because empowering services are easily substituted as a commodity by competitors. Besides, ARPU as one of many key performance indicators does not necessarily reflect the true state of an operator's business growth and may not be meaningful in the emerging market.


Operators must realize that services such as village phones, credit sharing, and low-denomination top-up are commodity services that facilitate communications. To expand new-subscriber share-of-wallet spending beyond communication, operators must further explore this group's needs.

Innovative multimedia services beyond voice and text are crucial for growing revenues from various customer segments. Low-cost players need a data strategy precisely because they are focused on the low-end mass market. Hence, offering data services to the high-end segment and the business segment

will help stabilize sources of revenue and mitigate the volatility of the low-end prepaid market.

3) Invest and make partnerships to scale up quickly

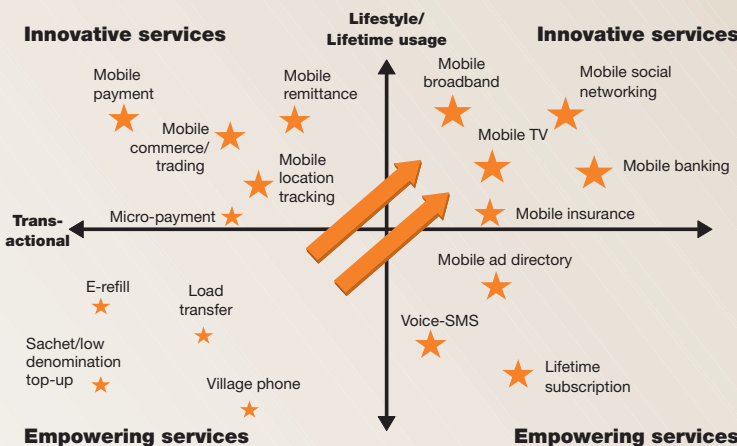
Philippine operator Smart has three times received awards from the GSMA for innovative services, even before they harvested anything from the market. First it was Smart Reload (an e-refill service that started in early 2000), then Smart Money, and then Smart's mobile advertising services. Proactive players know what they need to do next. They recognize that there are seasons in business life just as in human life: seasons of seeding, nurturing, and harvesting. I have witnessed wise operators strategically increase CAPEX and OPEX when preparing to battle and to later harvest. Evolutionary ideas can't pay off at once. In emerging markets, in particular, when a new business opportunity becomes apparent, several companies crop up to capitalize on it.

Being insensitive or irrelevant to customer needs is dangerous in any market, but especially in emerging markets that are generally dynamic and volatile. Essentially, the operator's role in emerging markets is often more challenging than first thought, yet the rewards are greater. What they are doing successfully is to evolve this role beyond merely providing communications to also becoming an integral and indispensable part of private life, social life and not least, their countries' economic development. 

Sources:

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 Analysis on Operator's Interviews 2007 and SEA low-ARPU market studies
 Best Practices from key performing operators researched 2007
 Bangladesh Infocom study 2007, ConsumerLab
 Driving growth in an expanding market study 2007, Ericsson
 Ericsson Strategic Focus low ARPU High Growth study Feb 2007

Competitive service portfolio quadrant



Empowering services that have proven to meet the needs of low-disposable-income earners are listed below.

- **Security and survival services that meet security needs:** e-Refill, load transfer, mobile remittance, mobile commerce, location-tracking services, logistic or inventory-tracking services, emergency services. **Note:** Location tracking of mobile doctors in South Africa is critical to treating AIDS victims.
- **Affordability and flexibility services that fulfill love and belonging needs:** micro-prepaid, low-denomination recharge, collect-call/SMS, accrual recharge, credit sharing, voice SMS, advertising subsidized services. **Note:** These services lower the barrier to adoption, hence drive penetration. Mobile broadband potentially can be packaged using similar tactics to help rural users gain access to the internet for meeting many of their needs, including belonging and self-actualization.
- **Aspirational services that fulfill the status and self-esteem needs:** acquisition of high-end phones in mobile communication plans and packages, mobile TV, downloading of ringtones, wallpaper.



the author

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