

With rumors rife about a Facebook phone, Google Voice delivering network-agnostic telephony applications and Mobile VoIP gaining traction, its time for the network operators to do or die, says Scott Stonham

# Battling against disruptive technologies since 2005 — What's changed?



Scott Stonham: The real threat comes from brand erosion

As far back as 2005 the research firm Evaluateserve predicted that the emergence of VoIP as a disruptive technology would significantly and permanently reduce overall operator profit and revenues to the tune of 22-26% and 5%, respectively, by 2008.

However, the intervening years have seen a marked shift in the composition of operator revenues. Voice is still at the core of revenue generation but is widely seen as a rapidly commoditising service, regardless of the disruptive influence of VoIP providers. While we thought the competition was about voice revenues; that hasn't turned out to be the case. The real threat comes from brand erosion and the costs operators have to bear in maintaining a network to support the service and data delivery of third party applications from Over-The-Top (OTT) providers, such as Google, Skype, Facebook and many others.

The effect of those services is far more acute than simple loss of voice revenue. Figures from Bernstein Research have uncovered that an iPhone user consumes between five and seven times more bandwidth than the average voice subscriber and double that of an average smartphone user. The firm also states that in the period 2006-2009, consumption of data bandwidth at AT&T has grown 50-fold while its data revenues have only increased 250%. Meanwhile, the operators have to build and maintain networks and call centres to support that growth.

Skype is illustrative of the potential impact on operators of OTT providers. Recent research from TeleGeography says that international Skype traffic amounted to 54bn minutes in 2009. Whilst the number of minutes is substantial, the revenue generated by Skype and

consequently lost to operators has not, to date, confirmed the worst fears of early predictions. For the first half of 2010, Skype reported an almost insignificant profit of just \$13m on \$406m of revenue, 87% of which was generated through SkypeOut credit sales. With the remaining 13%, or \$52m of its total revenues, being attributed to its other services, such as conferencing, SkypeIn and voicemail, what is all the worry about?

The concern with Skype, Google Voice and other OTT providers, including Facebook, is not restricted to simply revenues; it goes much further than that. The worry is that large numbers of subscribers are choosing to use third party applications instead of those offered by the network operators, and this in turn impacts the operators in a plethora of ways, of which only one is revenue.

If you take Google Voice as an example, it is clear how the compounded effects can easily add up to be a much greater threat to the sustainability of today's mobile operator business model than simply lost voice revenues. Google's Google Voice gives users one number that is portable across any network, mobile, VoIP or fixed line; inserting a layer between the subscriber and the operator that, when supplied with the other network-agnostic features it offers, such as voicemail, call history, conference calling, call screening and blocking and voice transcription of voicemail messages, completely decouples the subscriber from the network. The subscriber associates value with the Google applications, not the underlying network. In fact, with Google's positioning, in the eyes of the subscriber, the network provider becomes simply a cost rather than a value-add. The Google Voice mobile application, which is already approved by Apple for the iPhone, also allows for unlimited SMS messaging and, with Yahoo Mail now also offering SMS, this crucial revenue stream is once again being targeted. Once a user associates Google as its voice, messaging, data, email and apps provider the role of the carrier beyond being the commoditised provider of a broadband connection or a SIM card looks significantly threatened.

If that wasn't enough, beyond the decoupling, or isolation of the subscriber from the network, the operator becomes burdened with not just providing front-line support for these applications, which according to one operator executive can cost £50 per support call, but also providing for and supporting the rapidly increasing bandwidth requirements. The relationship between high data use and reducing revenue per user is clearly indicated by some recent analysis from Gap Gemini.

Gap Gemini recently researched the impact of increased data usage on the earnings before interest

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and taxation (EBIT) of a sample European broadband operator in the period 2009-2012. The analysis found that for customers with 1GB of average usage per month EBIT margin declines from 50% to 20%, for users with 1.6GB of average usage per month EBIT declines from 45% to around 10% and for users with 2.4GB of average usage per month EBIT falls from 35% to minus 10%. This clearly illustrates the growth of the loss making customer as operators take the hit for supporting the services of YouTube, Facebook, Google, Apple and Skype. As an example of the scale of the problem, the many discussions I have had with network operators suggest that Facebook usage accounts for 40 to 60% of mobile network traffic. Look at that another way; one application that the operators do not control, that they make no money from yet still have to support and in doing so are being marginalised is taking up almost half of their primary asset — that would be like Shell giving half of its oil pipelines to BP.

These factors all beg the question why are operators being so passive in the face of this onslaught from OTT service providers? Ten years ago the operator sector was ruthless in its sustained resistance to Microsoft entering the market yet, while OTT providers have helped made the case for the existence of mobile — and fixed — data networks, operator businesses are now being ruined by unmonetised traffic over which they have no control. Operators continue to be ill-equipped to deal with this kind of threat and appear to be sitting back and relying on the prospect of regulation to sort the problem out for them. Having welcomed Google, Yahoo and Facebook as generators of data traffic and shunned Microsoft as a potential competitor, operators now need to work out how to monetise OTT traffic while continuing to provide decent service to their customers. Concerted action is becoming imperative and it is my belief that operators need to do something soon or die. They can't rely on yesterday's defences, such as regulation or high cost-to-entry, since the smartphone boom and open-access high-speed networks have rendered these obsolete.

Yet this is not an area in which operators have been naturally strong. Their network-centric view has caused them to invest in new networks without having fully-developed business cases to support them and that attitude has seen the OTT players welcomed with open arms on the basis that any traffic is good traffic. Unfortunately the congestion time-bomb was not identified and operators have not made sufficient moves to differentiate themselves from their competition through providing relevant, revenue generating applications. The moves they have made have been flawed as operator groups have attempted to deploy

application ecosystems across their entire business. Those applications and platforms have failed to attract users and therefore haven't generated the revenues envisaged. Operators keep trying to play the applications game and keep failing at it.

I think the reason for that is that operators attempted to do too much and lost focus and relevance. It is worth remembering that Facebook, Skype, Google and others started off in a small way, bringing their offerings to market gradually and making them available to a small subset of users, often as beta offerings. Take Vodafone 360 as just one example of how the mobile network operators approach innovation. This has been the exact opposite of their OTT competitors — the company brought an entire suite of applications to market for all its users, in five languages and in several countries all at once.

Instead, operators should focus on doing something small and targeted that will be well received, generate revenue and be easy to set up. In our exploration of Skype revenues earlier in this article, one factor that is apparent is that it is professionals that are paying Skype for applications and services. Many of these are professionals from the small and medium sized business (SMB) sector that are currently, erroneously, viewed and served by the operators as if they were traditional consumers. They want enterprise-grade messaging, productivity and communications services and are prepared to pay for these but the operators simply aren't making them a relevant offer in spite of the fact that these users are already prepared to pay for applications and services. Such professional consumers or prosumers currently have no option but to pay Skype, Google and others for the services they need but can't readily get from their operator. The longer that their operator fails to address their needs the more entrenched these users become with the services and applications of web companies and the OTT community.

The SMB sector is a perfect and ready-made opportunity for operators to focus on and CommuniGate Systems can help deliver solutions targeted to the SMB's needs that are easy to deploy and sell under the operator's own brand. Operators already have significant SMB subscriber bases with current estimates stating 60% of consumer tariffs are being used by SMB employees. SMBs have clear requirements and operators can start with a simple, small deployment before rolling out, larger more comprehensive products as they gain traction and experience. That will allow them to avoid the big bang approach they have previously stuck with for consumer application launches that has to date resulted in their service and application strategies blowing up in their faces.

At CommuniGate Systems we have been working with our carrier partners across the world to help answer these questions and better equip them with the tools and technology they need to compete with these disruptive technologies. In the coming weeks I'll be chairing discussions along these lines at Global Telecoms Business' 40 Under 40 event in London on September 27, 2010 and at CommuniGate Systems' own event on October 4, 2010 in Bodrum, Turkey, for more information visit [www.communigate.com/bodrum](http://www.communigate.com/bodrum) ■