News release

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Telecom Industry Challenges Lead to Overhaul: CAPEX Becomes a Main Priority

As telecom growth slows, industry focuses on the new drivers of EBITDA multiples

Telecommunication operators face intense challenges to obtain eearnings before interest, taxes, depreciation and amortization ("EBITDA") multiples and superior investor returns as the communications sector undergoes significant changes, according to a new PwC report entitled *Capex is king: A new playbook for telecoms execs*. Telecoms' previous reliance on rapid growth to obtain premium multiples is now deemed unsustainable as global telecom industry growth has dropped to less than gross domestic product growth.

"In the old days, telecoms could rely on strong revenue growth and EBITDA to provide premium EBITDA multiples. Today, we have segments like fixed lines in absolute decline and others like mobile that are expected to decline, said Pierre-Alain Sur, Global Communications Industry Leader, PwC. "Telecoms need to set aside their focus on EBITDA and cash in favour of capital return. It's about challenging telecoms' current internal decision making processes and resetting their expectations in order to get the EBITDA multiples they are looking for."

Challenges abound

Capex is king outlines the telecommunications industry's main challenge of slowed growth. Compounding the slow growth is the issue that there is no one complete solution that can replace profit declines with higher growth opportunities. Instead, a few segments that have been identified as growth areas – such as mobile advertising, cloud and Machine to Machine (M2M) – are not expected to entirely compensate for the decline. In 2015, mobile advertising opportunities are only expected to reach US$30bn, as the cloud will offer approximately US$35 billion and M2M is only expected to contribute US$13 billion. Even combined, these three segments are dwarfed by an industry worth US$2,000 billion that is facing threats to voice and message revenues among other issues.

Paradigm shift required

Progressive operators' best practices depend on a significant shift in thinking. Previously, expectations regarding capex were based on historical context, with departments expecting revenue would repeat year over year, based on the assumption of increasing traffic. Analysis for return on investment ("ROI") has not been employed systemically or rigorously.

In order to succeed, *Capex is king* reports that telecoms 'Product and pricing' questions regarding capital expenditures now need to center on more in-depth analysis including:

- Segments, products and price plans that drive ROI in each operational company ("opco");
- Capital allocation to each opco, which may appear stable over time, needs to be evaluated to determine how the ROI spread expected to change over time and how the capital allocation reflects that;
- The impact of service mix changes on different network elements
- Product ROI by month and how customers and traffic drive asset additions.

"Though growth opportunities still exist, it's simply not the same playing field as in decades past. Senior telecom leadership teams can't just control costs – their priority should be on creating value. It's time for telecoms to embrace capex best practices and not rely on the familiar measures of the past," added Sur.

Notes

For more information, visit http://www.pwc.com/en_GX/gx/communications/publications/capex-playbook-telecoms-execs.jhtml