
Region in Focus

Latin America, Q1 2020

Covid-19 puts network resilience at the forefront

June 2020



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1

Key takeaways

2

Regional trends and developments

3

Global financial benchmarking

4

Topic deep dives

- Covid-19 impact: roaming, prepaid and handset sales most at risk
- Data traffic to grow fivefold by 2025
- Fintech is the star of venture capital as app usage growth accelerates

Defining 'Latin America'

Countries included:

Argentina, Bolivia, Brazil, Chile, Colombia, Costa Rica, Cuba, Dominican Republic, Ecuador, El Salvador, Guatemala, Honduras, Mexico, Nicaragua, Panama, Paraguay, Peru, Uruguay, Venezuela

All instances of \$ in this report refer to US dollars.

Network investments pay off as data traffic growth reaches new heights

- Data traffic growth around the world was already on the rise before the Covid-19 outbreak, which has caused a greater reliance on digital solutions in all aspects of life, including communications, education, entertainment and work.
- Investments in recent years across Latin America (e.g. rollout of massive MIMO) to ensure greater network capacity and coverage are paying off: traffic growth increased up to 30% for some operators in the region, with limited disruptions. However, the long-term impact of new consumer behaviours could mandate further network spend (both capacity and coverage) across the region.

Postpaid revenues on the rise as Covid-19 hits handset sales

- Stronger 4G adoption and high infrastructure spend to address capacity demands have had a positive bearing on top-line revenues. Many operators continue to push the migration from prepaid to postpaid, increasing the number of high-value customers, which has helped operators achieve a more stable revenue base.
- While Covid-19's impact on top-line revenues has been mostly limited so far, there has been a comparatively greater impact on handset revenues, as operator retail stores, a key sales channel for devices, have remained closed since around March 2020.

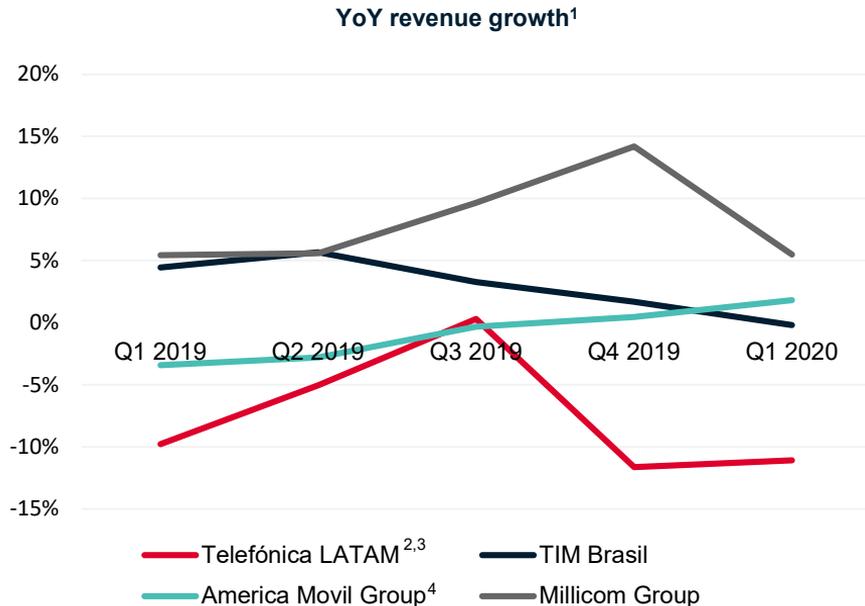
What opportunities lie ahead?

- As operators continue to support customers with free bundles and entertainment, they are faced with many challenges and opportunities. For instance, increased demand for security and cloud services create an opportunity for operators in the B2B segment.
- The pandemic could spark an acceleration of 5G. Higher speeds – a key 5G capability – play a key role in AI, IoT and big data, which are being used to help track the spread of Covid-19. However, the rollout of 5G depends on available spectrum and whether operators see such long-term investments as viable in a time of crisis.

Latin American fintech sector attracts investments despite geopolitical challenges

- In the last year alone, some 140 fintech deals, with roughly \$2 billion in investment (more than 200% growth year on year), were closed in Latin America. Brazil and Mexico's startups lead the way.
- This is testament to the growth in usage of fintech applications. A growing tech-savvy consumer segment, high smartphone adoption and increasing demand for banking without barriers are driving innovation, and investors have recognised the opportunity to fill the gap.

Regional trends: revenue growth stable but with an impending hit from Covid-19



Source: Company results, GSMA Intelligence

¹ Growth calculated in reported currency.

² Telefónica reports all markets in euros. FX impacts are not considered in this chart.

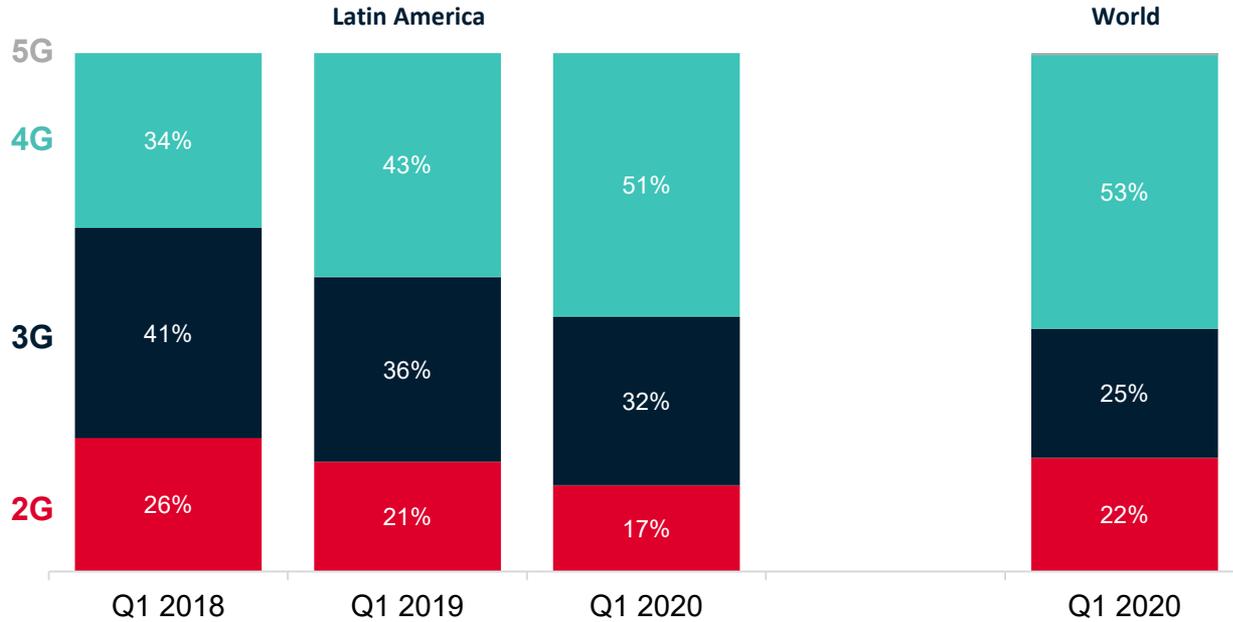
³ Telefónica LATAM includes Hispanic America and Brazil.

⁴ America Movil Group includes Europe and US operations, but more than 75% of the company's revenues stem from Latin America and the Caribbean region.

- Currency devaluation has affected operator revenues for some time, often impacting operators headquartered outside the region in particular and, to a lesser extent, those with earnings coming from outside of Latin America.
- Q1 2020 results have partially taken a hit, mostly from a decline in handset sales because of lockdown-related store closures. Around 40% of smartphone portfolios in Latin America are sold through this distribution channel (according to our Operator Device Survey 2020).
- Despite challenging economic developments, stronger 4G adoption and high infrastructure spend to address capacity demands have had a positive bearing on top-line earnings.
- Many markets have continued the migration from prepaid to postpaid, increasing the number of high-value customers. This has helped operators attain a more stable revenue base. Multiple operators in Brazil have already reported improvements of up to 30% year on year for mobile ARPU.
- Across the board, churn rates began to decrease in Q1 2020 as a direct result of the crisis, with consumers looking to avoid network disruption. This has reduced pricing pressure and further stabilised revenues.
- Additionally, with more markets in the region adopting a fixed-mobile convergence approach, total telco ARPU could improve as operators upgrade CRM and BSS solutions to streamline their offerings.
- Network sharing agreements in the region are gaining momentum as operators aim to better optimise capex. This is true for both large and smaller markets (a recent example being Peru), which are realising the potential benefits in terms of costs and accelerated coverage of hard-to-reach areas.
- However, this will not have a material impact on capex as a percentage of revenue (which remains at 19% in the long term), indicating a continued commitment from operators to improve infrastructure.

Regional trends: 4G finally becomes the dominant technology

Technology mix: percentage of total connections, Q1 2020



LATAM total connections

635.4m

Connections penetration

101%

Subscriber penetration
(% population)
Mobile Internet users
(% total subscribers)
Smartphone adoption
(% total connections)

Subscriber penetration (% population)	66%	67%	68%	66%
Mobile Internet users (% total subscribers)	77%	79%	81%	75%
Smartphone adoption (% total connections)	63%	66%	70%	66%

Technology

5G – Movistar has begun a 5G trial in the 3.5 GHz spectrum together with Huawei. The operator received a temporary permit from Colombia's Ministry of Information Technologies and Communications (MinTIC) to help control the spread of Covid-19. The first 5G pilot in the country outside of a lab, it enables real-time body temperature measurement via thermal cameras at control points at the District Health Secretariat and the Public Health Laboratory in Bogotá.

IoT – Nokia has signed deals with TIM Brasil and Telecom Argentina for its fully virtualised managed IoT service, Worldwide IoT Network Grid (WING). With recent upgrades to the WING architecture the service now includes 5G, soon to be followed by multi-access edge computing (MEC) technology. This is particularly relevant for TIM Brasil: as 5G spectrum is due to be auctioned this year in Brazil, this enhancement will enable the operator to support customer use cases for low latency and higher data speeds.

Regulatory

Brazil and Peru – Anatel, Brazil's national telecommunications agency, has approved a network sharing agreement between Vivo and TIM Brasil, which will allow the operators to share their radio access networks (RAN). The agency supports RAN sharing to expand coverage to less densely populated areas (less than 30,000 inhabitants). Similarly, Peru's Ministry of Transport and Communications (MTC) is a keen proponent of the private RAN sharing agreement between Movistar and Entel. However, it has stressed that the agreement will not exempt either party from the terms and obligations of their spectrum licences.

Colombia – Following the spectrum awards in December 2019, MinTIC delivered spectrum permits in the 2500 MHz band in May 2020. Claro, which won 30 MHz alongside Novator Partners, has already put the band in operation across its nationwide network. According to an ICT Minister, this allows the operator to offer twice the download speeds it was previously able to offer.

Competition

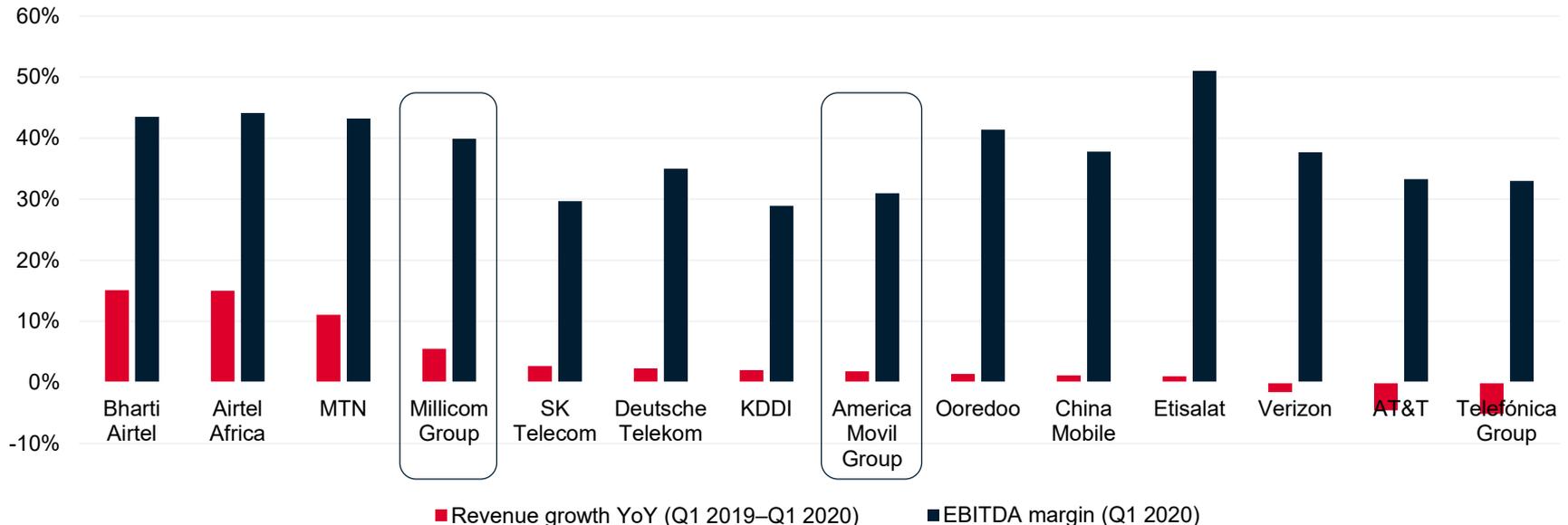
Argentina – After multiple acquisitions, Telecom Argentina upgraded its CRM and BSS solutions across its B2B and B2C units in partnership with IBM, Velocity and Salesforce. The newly implemented solutions give the operator a clean slate, as opposed to overlaying legacy systems with new ones. The upgrades further enable true quad-play offerings, fulfilling the objective of its acquisitions in the past two years.

Brazil – TIM Brasil and Vivo (Telefónica) have officially informed shareholders of their interest in initiating negotiations to target a potential joint acquisition of Oi Group's mobile business. The announcement notes that they are willing to acquire the business either in whole or in part so that in the event of the completion of the operation, each of the interested parties will receive a portion of that business. To date, Oi has not committed to any binding agreement.

Global financial benchmarking: Latin American groups fare well compared to global peers

- In Q1 2020, Latin American operators performed in line with their global peers in terms of year-on-year revenue growth (in reported currencies). This is partly due to M&A activity over the past year (e.g. Millicom's acquisitions across the region) combined with the region's digitally savvy consumer base (Latin American smartphone adoption rates fare well compared with advanced regions).
- Equally positive is the EBITDA margin in Latin America, with regionally headquartered operators performing on level with the global average and above some operators in developed Asia Pacific.

YoY revenue growth and EBITDA margin



Source: Company results, GSMA Intelligence

- According to the IMF, Covid-19 will contribute to the contraction of real GDP growth in 2020 by 5.2% in Latin America, as social distancing and travel disruptions will impact supply and demand for most of 2020. In markets where lockdown has been imposed and businesses (especially small businesses) are being impacted, government-backed remittances are key for survival. With a lack of such support, there will be a rise in unemployment.
- The telecoms industry supplies critical infrastructure, particularly during a crisis, so the financial impact on it has been limited compared to other industries. But there will still be near-term ramifications. As operators continue to support customers with free bundles and entertainment, challenges and opportunities lie ahead.

Challenges:

- Retail closures will result in **lower handset sales**. As economies weaken, a growing number of consumers will also hold on to their existing handsets to save costs. Additionally, new handset models due to be marketed could be impacted while manufacturing firms remain closed.
- **Roaming charges will continue to see a decline** as international travel remains restricted. The impact will be especially pronounced for countries highly reliant on inbound travel. Even with restrictions eased in some markets, travellers may put plans on hold because of a contracted economy and the risk of being stranded during a second wave of Covid-19.
- To a lesser extent, **prepaid recharges will take a hit** from retail closures and shrinking economies. This is a direct result of rising unemployment and falling GDPs and consumer purchasing power. Operators have already introduced measures to support low-income households through free data and voice bundle upgrades.
- A 5G network could significantly help combat the pandemic, but its rollout in Latin America will rely on available spectrum and whether operators deem such long-term investments viable in a time of crisis. Thus, **5G spectrum auctions could potentially be delayed** as operators weigh the risk of long-term investments across the region against current financial developments caused by the crisis.

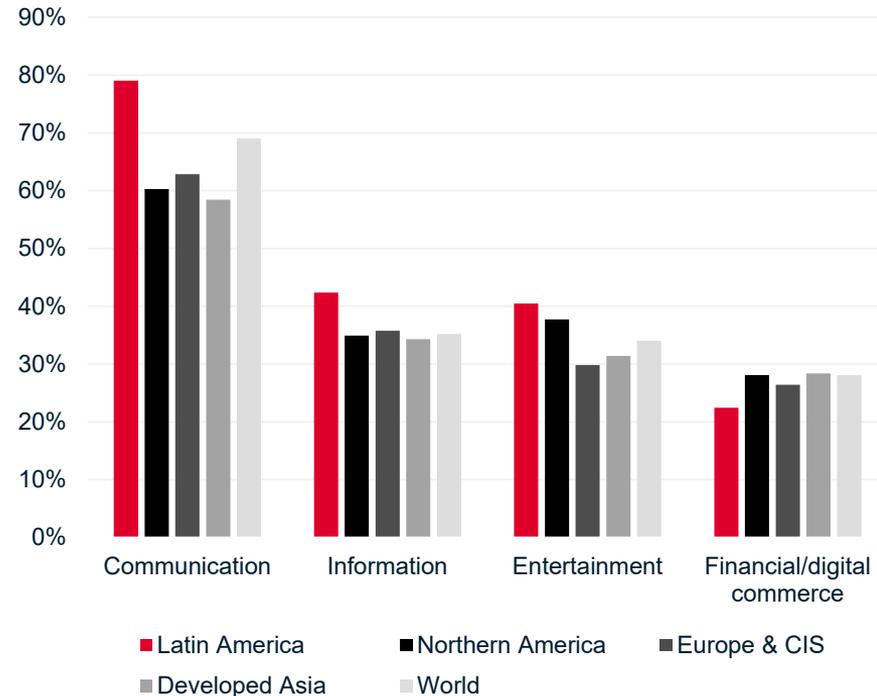
Opportunities:

- On average, B2B revenue equals around 10–20% of mobile operator revenue. While prolonged periods of remote working and business closures could be viewed as having a negative impact on this, there is **an opportunity for operators to increase B2B revenues** as businesses consider implementing security and cloud services for safer and more efficient teleworking. This is especially relevant for operators serving enterprises highly reliant on data and security e.g. businesses in the financial sector that will be facing payment backlogs due to office and store closures.
- Business closures create **an opportunity for operators to accelerate the migration of their remaining customer base onto digital channels**. In the past, this has allowed operators to decrease opex. It also improved operators' net promoter scores because these channels offer faster resolution times than traditional store visits or phone calls.

Data traffic to grow fivefold by 2025

- Mobile data usage in Latin America doubled year on year, reaching 4.7 GB per subscriber per month in 2019. And usage is expected to grow more than fivefold by 2025. Regular digital application engagement in Latin America is the highest in the world and a key driver for data traffic growth.
- This trend has been boosted by strong smartphone adoption rates in the region (around 70% at year-end 2019).
- With more people staying in and working from home, the current crisis is testing network resilience across the globe and accentuating changing data usage habits.
- Some operators in the region have seen data traffic increase by up to 30% compared to before the pandemic. Many operators have also increased mobile data packages to support teleworking and access to health and education services.
- Network investments over the last few years have allowed operators to handle this surge in data traffic with limited network disruptions.
- The application of massive MIMO in Brazil is a prime example of a network upgrade to address capacity demand. In response to data consumption growth tripling, TIM Brasil improved throughput per user (roughly 3 million users) sixfold in Copacabana in 2019.
- However, changes in traffic patterns (peak times and locations) and long-term changes to consumer behaviours because of lockdowns could further mandate network spend (both capacity and coverage) across the region.
- Against the backdrop of a challenging economy and growing data demand (both organic and driven by Covid-19), reliable networks and stable pricing are crucial for consumers. Operators' pricing strategies and network reliability will therefore be important both now and post pandemic when consumers reassess their subscriptions.

Latin America leads global digital application uses
% of smartphone users engaging in activity at least once per week

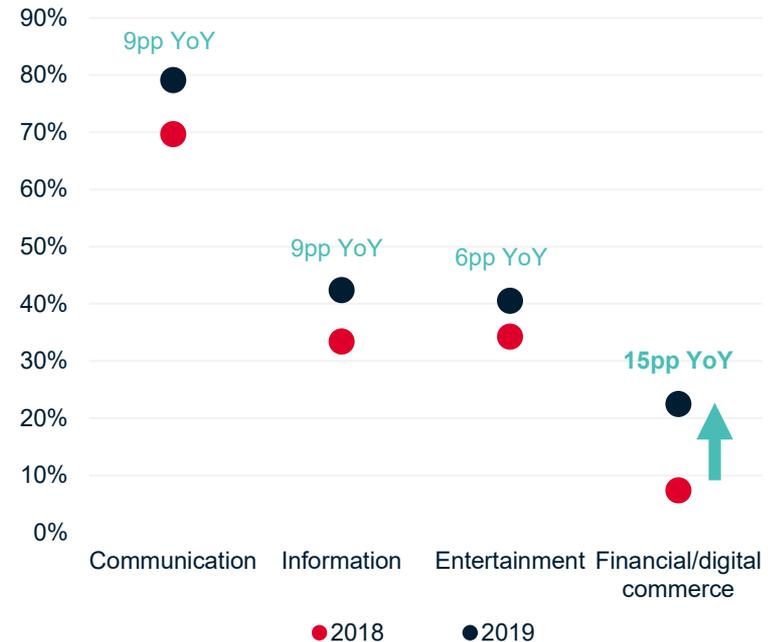


Source: GSMA Intelligence Consumer Insights Survey 2019

Fintech is the star of venture capital as app usage growth accelerates

- Despite foreign investors pulling out of stock markets in Latin America (due to the challenging geopolitical environment), the fintech startup community has seen growing attention from international investment, particularly for those in Brazil and Mexico.
- For example, Mexican banking startup Stori recently raised \$10 million from Bertelsmann Investments, while SoftBank increased its Latin American fund by \$1 billion (despite its WeWork-related losses).
- This is testament to the double-digit growth seen in fintech application usage in the region, driven by a growing tech-savvy consumer segment, high smartphone adoption and increasing demand for banking without barriers (a large proportion of the region's population remains unbanked).
- Barriers from traditional banking addressed by digital payment solutions include bill payments, high interest rates and low credit approval rates. To help remove barriers, changes in regulation have been put in place (e.g. Mexico's 2018 Fintech Law and CoDi platform). Such regulatory tailwinds allow digital players to recognise opportunities and provide easier access to industry.
- In the last year alone, some 140 fintech deals, with around \$2 billion in financing (over 200% growth year on year), were closed in Latin America (according to CB Insights).
- The push for mobile-led fintech creates an opportunity for operators to combine over-the-top innovation with the scale of existing capabilities such as mobile money. Operators benefit from a high level of KYC and can expand services beyond peer-to-peer transactional features to adjacent services such as credit, financial management, insurance and savings.

Financial and digital commerce app usage grows in double digits % of smartphone users engaging in activity at least once per week



Source: GSMA Intelligence Consumer Insights Survey 2019

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