



European Mobile Industry Observatory 2011

Executive Summary

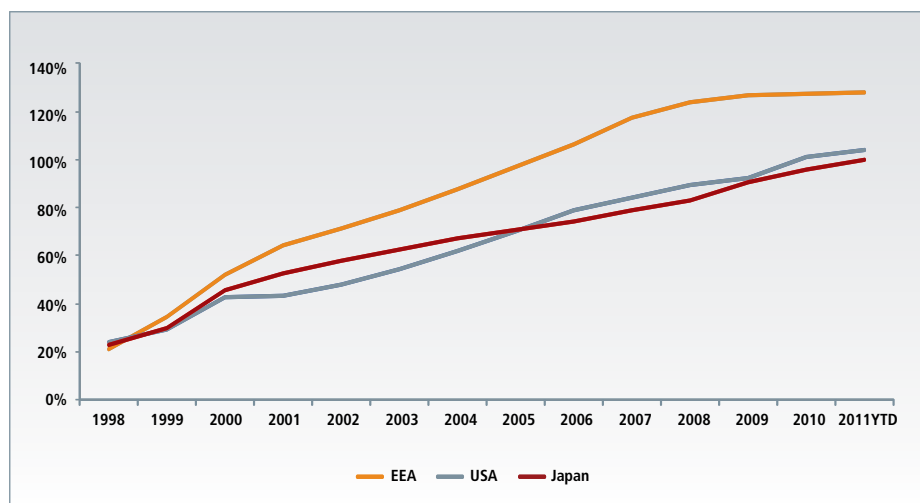


Driving Economic and Social Development through Mobile Broadband

The European Mobile Observatory was first published in 2008, and later in 2009, as a comprehensive review of the European mobile communications industry. This 2011 report updates the Observatory with the latest statistics and market developments, providing a reference point for participants in the mobile industry, for policy makers and other interested stakeholders. It covers the state of the industry, including the evolution of competition, innovation in new products, services and technologies and the industry's contribution to social and economic development in Europe.

Mobile communication is now a key European industry, comparable in size to aerospace and larger than pharmaceuticals,¹ with total revenues amounting to €174 billion in 2010. Today, mobile services are ubiquitously available, with a population coverage rate of nearly 100% and a mobile penetration rate of 128% in Europe (versus 100% in Japan and 104% in the USA). This represents 656 million individual subscriptions (measured as active SIM cards) held by an estimated 456 million Europeans (89% of the population), many of whom have more than one subscription. Mobile services are now being used across all age groups and socio-economic segments of the population. Indeed mobile services are often the only regular communication services for some socio-economic groups.

Penetration Rate of Active Subscriptions in the EEA, USA and Japan



Source: Wireless Intelligence; EIU



Innovative mobile data services are changing the dynamics of the industry and the way consumers use their handsets. Mobile Broadband is becoming widespread, with 92% growth per year since 2006.

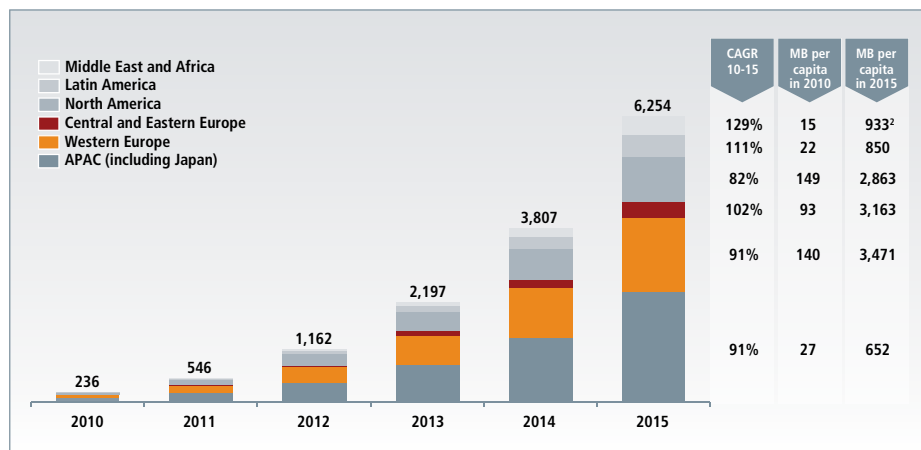
Smartphones, which are forecast to grow at 33% per year, and more recently tablets, which are forecast to grow at 57% per year, are further driving an explosion in mobile data traffic. According to Cisco, mobile data traffic volumes are expected to increase by over 90% each year for the next 5 years. By 2015, Europeans will consume more data than any other region on a per capita basis.

Investment and innovation in new technologies and services (e.g. LTE networks) is supporting this growth. Traditional mobile companies such as network operators, handset manufacturers and infrastructure suppliers are contributing to this end but no longer fully define the mobile market. Expanding content and service offerings, new software and user interfaces, and easily accessible distribution channels are creating a consumer-driven mobile ecosystem with a diverse set of players – all of which will drive future growth in mobile data.

¹ Aerospace market in Europe is estimated at €47 billion (Source: Aerospace Global Report 2011, IMAP). Pharmaceutical and Biotech market in Europe is estimated at €5 billion (Pharmaceuticals & Biotech Industry Global Report — 2011, IMAP)



Global Mobile Data Traffic by Region and Per Capita, in Petabytes per month

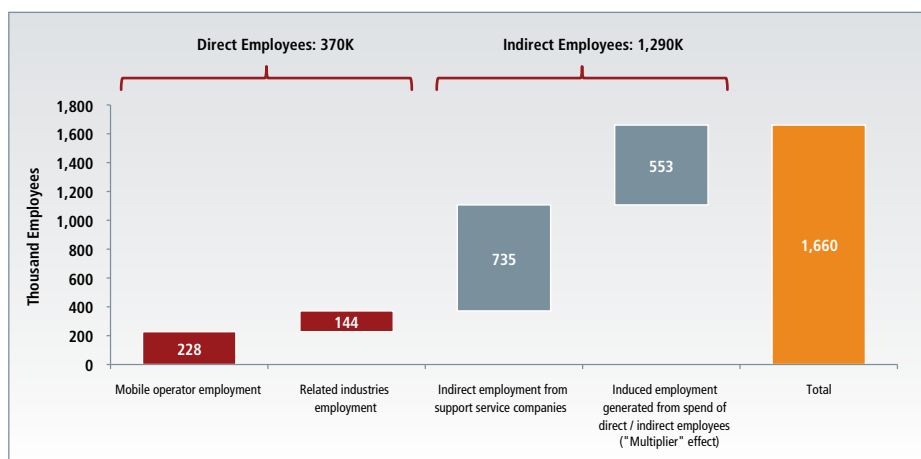


Source: CISCO VNI, 2011; EIU

Voice call volumes grew by an average of 13% per annum from 2000 to 2011, with European consumers making an estimated 144 minutes of outgoing mobile calls per head of population per month in 2011. The growth in mobile messaging traffic (SMS and MMS) was very strong until 2010, with growth of 23% per annum from 2000 to 2009. Since 2009, growth in mobile messaging has slowed to 2% per annum, due to the use of social media and instant messaging services as alternatives to SMS and MMS.

Despite the economic climate, mobile services continue to make a strong socio-economic contribution to Europe. The mobile industry supported an estimated 1.7 million jobs for Europeans in 2010 and mobile operators contributed €174 billion (1% of total EEA GDP) to GDP. Contribution to public funding amounting to approximately €65 billion – plus a further €18 billion estimated as the indirect contribution from related industries.

Direct and Indirect Employment created by the European Mobile Industry, 2010



Source: Operator provided data; Wireless Intelligence; IDC; EIU; A.T. Kearney analysis



Fierce competition in the mobile market is driving down prices. Across the EU27, mobile prices fell by an average of 11-13% per annum between 2006 and 2010. In comparison, fixed line prices fell by only 5% a year from 1998 to 2010. Telecommunications services are one of the few household services that have declined in price over the past few years. By comparison, between 2007 and 2010, European Union consumer prices for energy and food increased by an average of 4% and 3% per annum respectively.³

Annual Price Reductions for Baskets of Mobile Services in the EU

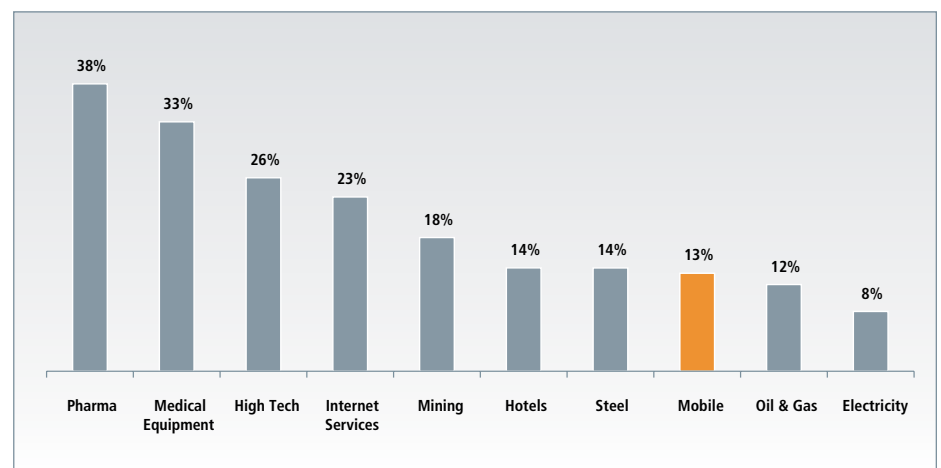
Price Basket	Region	Period	Average Annual Growth Rate
OECD domestic mobile medium usage price basket	EU27	2006-2010	-11%
OECD domestic mobile high usage price basket	EU27	2006-2010	-13%
OECD domestic residential fixed line price basket	EU15	1998-2010	-5%
OECD domestic residential fixed line price basket	EU27	1998-2010	-3%

Source: Telecoms Price Developments from 1998 to 2010, Teligen for the European Commission; A.T. Kearney analysis

Despite these price declines, usage growth enabled the mobile industry to enjoy strong revenue growth, averaging 9% per annum, from 2000 to 2008. In the recent recession, however, revenues declined by 3% in 2009 and remained relatively flat in 2010. It is expected that mobile operators' revenues will continue on this trend through 2011, especially as economic conditions continue to deteriorate in several countries. The economic climate has also intensified trends already seen in a mature and intensely competitive market, for instance consolidation across the value chain – including operators and their vendors.

Data for 2010 suggests that operators generated profits at a similar modest level to 2007 and 2008 – with returns on capital employed (ROCE) of 13%. Contrary to popular belief, such returns lag those of numerous other sectors, as illustrated in the exhibit below.

ROCE for Mobile and Other Industries (Europe, 2010)



Source: Confidential Operator data; Bloomberg; A.T. Kearney analysis

Mobile operator revenue growth rates have been declining for the past few years due to the economic climate, market maturity and greater regulatory interventions. Cautious consumer spending and reductions in business expenditure, as a result of the uncertain economic climate over the last few years, are continuing to pressure revenues. The European Commission has also targeted mobile termination rates, seeking to introduce major reductions by the end of 2012. These factors can be seen in the fact that European ARPU declined from €27 per month in 2006 to €20 per month in Q2 2011. Recent IDC data estimated that 2009 and 2010 saw a 10% and 7% decline in mobile voice revenues respectively.

Mobile data revenues are partially offsetting reductions elsewhere with strong growth in broadband connected to sales of smartphones and dongles. Data now represents 12% of mobile operator service revenues, having been only 4% in 2007. Mobile operators are also facing strong competition for consumer spending and share of total industry margin from other industry players, such as fixed line operators, device manufacturers and developers of operating systems, applications and content.

To ensure competitiveness and reignite long-term revenue growth, the mobile industry continues to invest in product and service innovation. Investment in research and development of mobile services can be very high. In 2010, Telefonica invested €4.8 billion in technological innovation, of which €800 million were directly allocated to R&D. Over the last few years, mobile data services have begun to yield the impressive results awaited for many years – a trend that will only continue as new data-oriented products, content and services emerge. As these new services are increasingly “bandwidth hungry” they will require investments into new, higher capacity networks. Mobile operators have already started deploying new technologies, such as Long Term Evolution (LTE), to satisfy the future requirements for mobile voice and data services.

Mobile industry investment in new technologies and infrastructure can also act as part of economic stimulus to help promote economic recovery. According to the ITU⁴, investments in ICTs can play a large role in generating economic recovery given their strong externalities, high multiplier effects in returns on investment and reduced leakages. Social returns to investment in ICT infrastructure are likely to exceed the individual private returns on investment, suggesting that the private sector alone is unlikely to generate the socially optimal levels of investment. Infrastructure investments are also likely to generate more robust and durable economic growth than other types of stimulus measures.

If given the right opportunities, the mobile industry is expected to continue investing strongly in new technologies and new services.

Support of future technologies, by operators, vendors and regulatory stakeholders such as the European Commission, is vital for future economic growth.



For further information please contact:

info@gsm.org

GSMA London Office

T +44 (0) 20 7356 0600

www.gsmworld.com

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Authors:

Martin Whitehead, Director, GSMA Europe
mwhitehead@gsm.org

Tom Phillips, Chief Government and
Regulatory Affairs Officer

ATKEARNEY

A.T. Kearney

Lansdowne House, Berkeley Square
London W1J 6ER
United Kingdom

www.atkearney.com

Authors:

Mark Page, Partner, Communications,
Media and High-Tech Practice
mark.page@atkearney.com

Dr. Maria Molina, Consultant,
Communication, Media &
Technology Practice
Charlotte Wood, Consultant