Over the Top
Operator Threat and Opportunity

By Michael Dargue and William Wadsworth

Recent years have seen the rapid consumer adoption of over-the-top applications for voice and messaging communications. Initially seen as a disruptive force from outside the industry, operators are now launching “Over The Top” (OTT) apps of their own.
OTT Communications: Where Did They Come From, Where Are They Going

Communications over IP networks have been disrupting established businesses for many years. The original OTT communication – the email – was a major factor in the decline of global postal letter volumes\(^1\). More recently, VoIP applications like Skype have taken a bite out of the fixed telecoms market, and now the fortunes of mobile operators are firmly in the spotlight.

Last year saw OTT messaging take off on mobile, as predicted in Cartesian’s 2011 Year-End Thoughts. The popular multimedia messaging application, “WhatsApp”, was carrying 10 billion messages per day alone by mid-2012\(^2\).

Some 75% of operators have expressed concern about losing revenue to OTT players\(^3\). Forecasts predict that by 2016, lost revenue to OTT services (see Figure 1) will be worth 7% and 28% of projected voice and messaging revenues respectively\(^4\).

\(\text{Figure 1: Worldwide Operator Voice and Messaging Revenues Lost to OTT Applications}^{4}\)

This growth in OTT services has been enabled and driven by a range of factors (see Figure 2), many of which have the potential to underpin yet stronger growth in the future.

\(^1\) Cartesian Viewpoint – Postal Operators: Delivering Success through Telecom Strategies (2013)
\(^2\) WhatsApp (August 2012)
\(^3\) European Communications (2012)
\(^4\) Ovum (2012), Cartesian (2013)
Operators on the Defensive

Mobile operators have mounted defences against the OTT threat, with varying degrees of success.

In select parts of the world, the incumbent operators have been shielded from the full impact of OTT through national regulations, for example in China and the Middle East. While this rarely manifests as a complete ban, and restrictions in some markets (e.g. Egypt and UAE) have been relaxed over time, this has provided operators in these markets with temporary breathing room.

Elsewhere, some operators have chosen to enforce their own block of OTT apps on their networks; attempts have also been made to disable handsets from supporting them. Such moves, however, can give rise to consumer disapproval and potential regulatory intervention.

Where operators have no choice but to support third-party OTT apps, new pricing strategies have been deployed. Rather than compete head-to-head in a price war with the OTT entrants, many operators have instead structured propositions to offer ever-larger bundles of minutes and texts – effectively at marginal price of zero without wider value destruction. This offers a partial solution when coupled with usage-based

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2 Cartesian, IDC, Ericsson, IHS iSuppli, company websites
pricing of data. Some price differences will persist though – particularly for roaming, where use of OTT is particularly popular.

If You Can’t Beat Them, joyn Them

In addition the defensive responses, several operators have launched OTT services of their own or have partnered with existing players. Developing an OTT offering allows operators to leverage the wider capabilities of smartphones, enriching core communications services for existing subscribers and enabling off-net users to be addressed. Secondary benefits include gaining deeper insight into OTT usage and contributing to wider OTT-community fragmentation.

**Figure 3: Examples of Operators Finding Opportunity in OTT**

<table>
<thead>
<tr>
<th>Operator</th>
<th>Opportunity</th>
</tr>
</thead>
<tbody>
<tr>
<td>bobsled</td>
<td>• Enables users to make and receive calls and texts to/from other Bobsled users on any network using a mobile device or web portal</td>
</tr>
<tr>
<td>TU</td>
<td>me</td>
</tr>
<tr>
<td>voopee</td>
<td>• Enables Malaysian expats to be reached on a local number • Allows an MNO to tap a foreign market without MNO/MVNO launch</td>
</tr>
<tr>
<td>BT</td>
<td>• Enables BT’s fixed customers to use their landline tariff plan on their mobile • Provides alternative mobile entry option</td>
</tr>
<tr>
<td>TELKOMSEL</td>
<td>• Telkomsel has created a special unlimited data plan that includes unrestricted use of WhatsApp and Opera Mini services • The value of the overall customer proposition is enhanced</td>
</tr>
</tbody>
</table>

The market for OTT applications is crowded, yet 42% of operators claim that they could develop a better OTT application than an independent OTT player could. Operators bring a number of key assets which many independent OTT players cannot offer: an existing billing relationship; a trusted brand; extensive customer insight; and a considerable subscriber base to market to.

Operators are also better positioned than pure OTT players to form partnerships with other operators when developing OTT applications, as exemplified by “joyn”, the Rich Communication Suite (RCS) service including multimedia call and messaging options to be offered by Deutsche Telekom, Orange, Telefonica/Movistar, Vodafone, SK Telecom and others.

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6 Cartesian, company websites, press releases
7 Amdocs survey (2012)
So far, operator OTT apps have achieved moderate adoption – Bobsled with 2 million users, SK Telecom’s version of Joyn with 1 million, and TuMe with 600,000 – although this could appear insignificant when compared to third-party OTT applications such as WeChat (300m users⁸) and WhatsApp (estimated 200-300m users⁹).

Success, however, cannot be measured in subscriber numbers alone. A carefully positioned OTT play can deepen the relationship between customers and the operator’s brand: raising loyalty, reducing churn, and even creating an enticing point of differentiation for new customers. OTT may also be used to target a niche segment, for example operators seeking to serve ex-pat communities overseas may chose OTT entry over MVNO. Alternatively, OTT can be used in combination with MVNO to reduce airtime costs, as demonstrated by Republic Wireless in the USA.

A Holistic Operator OTT Strategy

To be effective, an operator OTT strategy will need to generate tangible benefits to the operator’s balance sheet by tapping new revenue streams, improving loyalty and decreasing churn, lowering costs, or growing market share.

Revenue Streams

Operators that have already launched OTT apps have typically decided to launch first and monetise later. T-Mobile’s Bobsled, for example, had an initial aim of capturing a share of users, intending to charge for premium upgrades, and/or use as a platform for adverts and sponsorship. Telefonica’s TuMe also launched as a free-to-use service, but may later offer premium functionality. Chargeable options could include charges for certain destinations and premium services such as local contact numbers and voicemail. Termination and interconnect fees are another important component where dial-in is provided.

Brand Loyalty and Network Effects

A well-implemented operator OTT strategy can have other benefits beyond simply providing new revenue streams. Through their OTT app, an operator may be able to build relationships with subscribers on other networks: 95% of Bobsled’s users are not T-Mobile wireless subscribers¹⁰. It remains to be seen whether these external customers can be monetised effectively, or even persuaded to churn completely and become full T-Mobile customers.

Single-operator initiatives (such as those highlighted in Figure 3, above) increase inter-operator competition; cross-network partnerships such as joyn reduce it. Working across traditional operator boundaries is expected lead to much greater network effects and form a stronger “defence” against the threat from external OTT players, but requires a high level of operator cooperation and provides less scope for differentiation.

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¹⁰ T-Mobile (July 2012)
Entry Options

Operators have three options to assess when evaluating an “own OTT app” strategy. The decision will ultimately come down to the unique needs and position of a given operator, as each option brings its own set of benefits and risks:

- **Build** a bespoke OTT application in-house, as T-Mobile did with Bobsled, and as Telstra plans to do in the future. This offers complete control and full customisability, but at the potential expense of time-to-market and higher development costs.
- **Buy** a ready-developed OTT system, perhaps by acquiring an existing OTT player, as Telefonica did by acquiring Jajah. Offers a fast solution, but integration may be complex.
- **Partner** with an established OTT player, either by taking a white-label solution, or on a joint-branding basis such as Skype/Three or Google Voice/Sprint. A partnership requires less capital investment from the operator, but may create a conflict over customer ownership, especially when using a co-branding model.

Cartesian Experience and Support

An operator’s OTT strategy should be tailored to its individual circumstances: the most appropriate response depends on factors such as the operator’s market share and positioning, the competitive threat in their home market, their international reach, mobile communications usage patterns in their market, and the availability of Wi-Fi to their subscribers.

Cartesian has deep experience in assisting operators achieve their strategic objectives, having worked with numerous incumbents, challengers and MVNOs around the world to help them achieve their goals. Our experience in the OTT space has included assessing the competitive threat and developing response strategies for major international players. We can support across a number of areas, including:

- Assessment of the evolving competitive landscape and identification of appropriate response
- Strategy and business case support, including detailed cost and revenue modelling
- Strategic pricing evaluation for communications services
- Navigation of complex regulatory issues
- Vendor or partner identification and evaluation
- Acquisition target selection and deal development
- Innovative monetisation strategies, including data analytics and monetisation
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