Paul-Louis Caylar and
Alexandre Ménard

How telecom companies can win in the digital revolution

Digital McKinsey September 2016

For telecoms, making smart use of digital technologies calls for a wholesale digital transformation. Five steps are needed to make it happen.

Telecom companies face increasingly tough times as digitization reshapes the industry landscape. In fact, telecoms come second only to media in the ranks of sectors expecting moderate or massive digital disruption over the next 12 months, according to a 2015 cross-industry survey of senior industry leaders.[1]

In the past five years, the telecom business has entered a period of slow decline, with revenue growth down from 4.5 percent to 4 percent, EBITDA margins down from 25 percent to 17 percent, and cash-flow margins down from 15.6 percent to 8 percent.[2] Competitive boundaries are shifting as core voice and messaging businesses continue to shrink, partly under regulatory pressures, but also because social media is opening up new communications channels. Among US telecom companies, for instance, landline and mobile voice now account for less than a third of total access, down from 55 percent in 2010, while data revenue has risen from 25 percent of total revenues in 2010 to 65 percent today.

But digitization is not just a threat; it also offers telecom companies an opportunity to rebuild their market positions, reimagine their business systems, and create innovative offerings for customers. Not surprisingly, most executives consider digitization to be one of their top priorities,[3] but few companies are close to capturing its full potential. We calculate that digitization could enable telecom operators to improve their profits by as much as 35 percent, yet the average improvement achieved is just 9 percent.

So how can companies bridge this gap? We have identified five ways to come out on top of the digital revolution.

1. Reinvent the core

Digitization touches almost every aspect of a telecom operator's business:

Omnichannel sales. Today's consumers engage with multiple channels during their customer journey. Customers increasingly visit stores to look at products before buying online, but even

---

[1] In a survey of more than 2,000 C-level executives from 15 industries, 64 percent of telecom executives (and 72 percent of media executives) expected to see moderate or massive digital disruption in the next 12 months. See Rhys Grossman, "The industries that are being disrupted the most by digital," *Harvard Business Review*, March 2016.

[2] Figures for 2010 and 2014.

[3] According to McKinsey's TMT Extranet Survey of more than 250 respondents from telecom, high-tech, media, cable, and Internet companies worldwide, conducted in November and December 2014.

more do the opposite, researching products online before completing their purchase in a store. Great customer journeys call for excellence in every interaction, clear cross-channel pathways, and a seamless customer experience. Stores need radical reform, too, not just to reduce their footprint but to transform the customer experience they offer. Investing in digital sales has enabled some leaders to increase revenues by 30 percent and reduce commercial costs by a similar proportion.

E-care. Digital is now the leading channel in many customer-service transactions, too. Among a sample of telecom companies in Western Europe, 89 percent of service journeys occurred partly or entirely online (Exhibit 1). Customers prefer digital service, with 76 percent of telecom customers satisfied with digital-only journeys, compared with 57 percent for traditional channels. However, few service journeys are entirely digital as yet: just 15 percent are digital from start to finish, while 41 percent begin on an e-care platform and then switch to traditional channels. For telecom operators, migrating to e-care can reduce call volumes and operating expenses by 25 to 30 percent. One company that launched an e-care effort as part of a broader digital sales transformation saw a 40 percent reduction in customer-care costs as well as a rise in customer satisfaction.
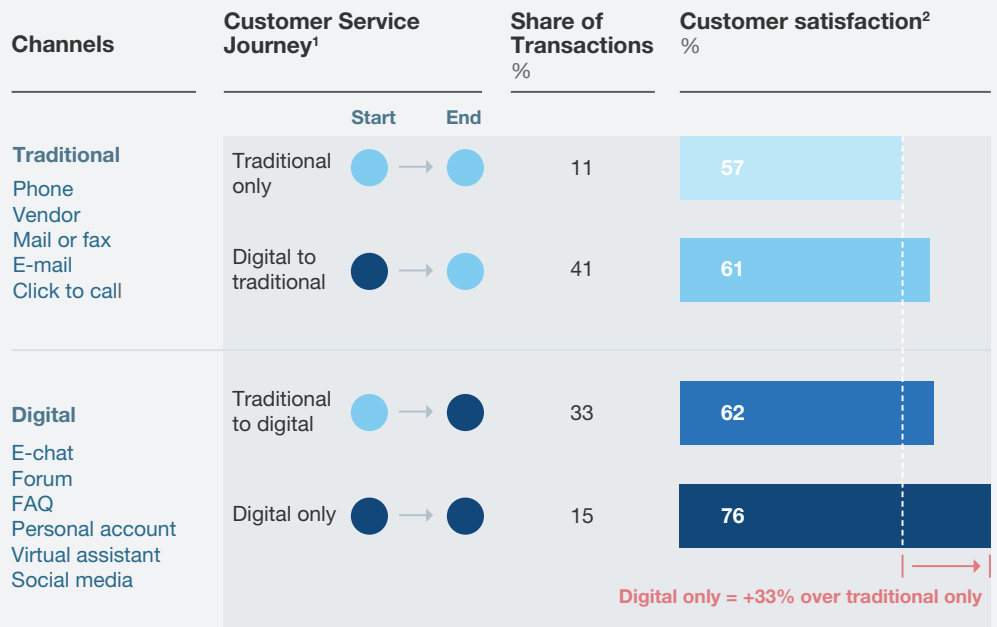
Digital processes. Today's customers expect an easy-to-use interface across all channels, an exciting in-store experience, and fast service 24/7. Yet many operators, especially incumbents, struggle to meet these expectations because of slow design processes, limited customer input, and rigid legacy IT systems. They need to overcome these barriers and invest in effective customer-relationship-management systems to track customers' digital footprints, reduce costs, boost customer satisfaction, and improve brand advocacy and differentiation. Digital touchpoints now influence customers' preferences across the whole decision journey (Exhibit 2). Among these touchpoints, websites have by far the most influence on customers' brand preferences, with mobile apps a distant second because of their limited reach (only about 10 percent of the target population). Social media play a part only when negative coverage harms customer acquisition. In the near future, telcos will be able to use real-time 360-degree data on individual customers to personalize promotions, campaigns, and service interventions along the entire customer journey.

Analytics. Network operators can use analytics to reduce customer churn, make better marketing-spend decisions, improve collections, and optimize network design. For instance, customers at risk of defecting can be identified even before they consider doing so, enabling operators to target their retention efforts, reduce spending, and maximize impact. One company raised its telephone-outreach hit rate from 60 to 480 at-risk customers out of every 1,000 calls, and reduced its attrition rate from 24 percent to 20 percent a year. At the same time, network operators can optimize their marketing spending by using advanced analytics tools, such as forecast simulators and econometric models, to predict acquisition and retention at the level of individual advertising channels instead of relying on predefined

Exhibit 1

The more digital the journey, the higher the satisfaction.

Example: telecom customers in Western Europe

Channels	Customer Service Journey[1]			Share of Transactions %	Customer satisfaction[2] %
		Start	End		
Traditional Phone Vendor Mail or fax E-mail Click to call	Traditional only	● →	●	11	57
	Digital to traditional	● →	●	41	61
Digital E-chat Forum FAQ Personal account Virtual assistant Social media	Traditional to digital	● →	●	33	62
	Digital only	● →	●	15	76

Digital only = +33% over traditional only

[1]4 service journeys were identified based on an analysis of 11 touchpoints spanning traditional and digital channels. For traditional-to-digital journeys (and vice versa), the first channel switch was used to allocate the journey.
[2]Respondents who ranked their satisfaction in the top 3 on a 7-point scale, where 7 = most satisfied.

Source: McKinsey e-care survey of c. 2,000 telecom customers in Western Europe; Francesco Banfi, Boris Gbahoué, and Jeremy Schneider, "Higher satisfaction at lower costs: Digitizing customer care," *Digital: From enabler to shaper, Recall*, No. 22, McKinsey & Company, May 2013

McKinsey&Company

---

percentages or gut instinct to allocate their ad budget and ceding the details to an agency. In collections, meanwhile, operators can use analytics to identify customers at risk of default and optimize outreach for those they wish to retain. One company created an algorithm that sorted late-paying customers into three groups—self-cure, in need of reminders, and bad payers—and targeted each group with different measures. The new approach cut churn among these customers by 90 percent. In network design, clustering customers according to their daily travel patterns has enabled some operators to fine-tune their geographical networks to optimize customer service and investment. One company increased the ROI of network deployment by 10 percentage points and reduced capital spending by 38 percent.
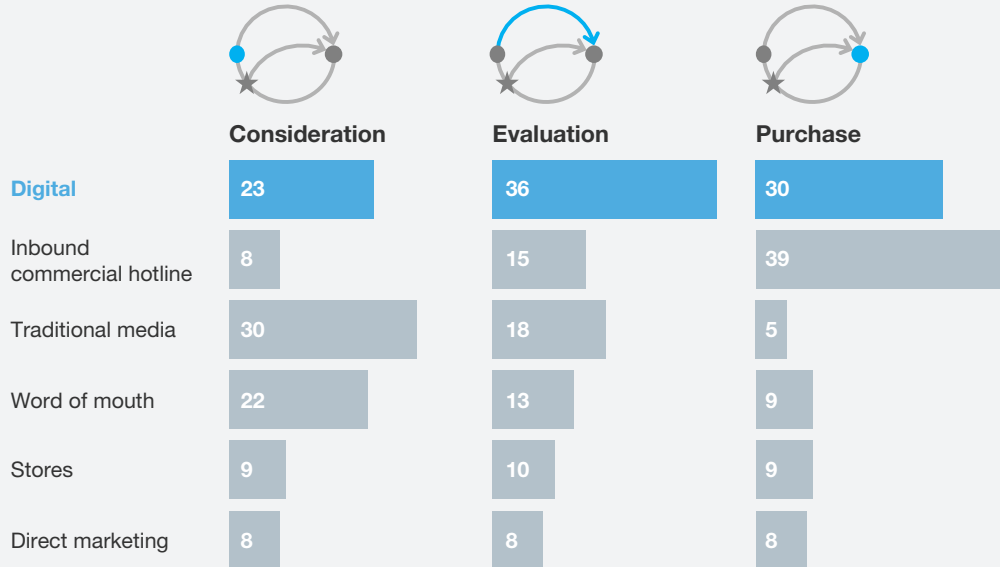
2. Pursue adjacencies

A third of the respondents to our TMT Extranet Survey were preparing to move into adjacent businesses such as financial services, IT services, media, or utilities in search of new opportunities and revenue streams (Exhibit 3). Some top-tier telecom companies

The customer decision journey has radically shifted toward digital touchpoints.

Derived influence index

	Consideration	Evaluation	Purchase
Digital	23	36	30
Inbound commercial hotline	8	15	39
Traditional media	30	18	5
Word of mouth	22	13	9
Stores	9	10	9
Direct marketing	8	8	8

Source: Francesco Banfi, Paul-Louis Caylar, Ewan Duncan, and Ken Kajii, "E-journey: Digital marketing and the 'path to purchase,'" Recall, McKinsey & Company, January 2013

McKinsey&Company

have set up dedicated digital business units with funding for internal R&D to create new services. Most companies are in the early stages of developing their digital-services portfolios, though some have offered a limited set of services for years. Such offerings usually involve partnership with third parties that bring specialist expertise to complement the telcos' strong customer relationships and broad reach. A notable example is in media, through partnerships with companies such as Netflix, Deezer, and Spotify.

To become a successful multiservice provider, telecom companies should seek to:

Create a focused offering for promising adjacent opportunities, with clear positioning, a well-defined value proposition, and a carefully targeted customer segment. Such an offering should rely on standardized IT products and services and existing platforms where possible.

Develop platform-based solutions in disruptive technology areas that are close to the core business but provide additional growth potential. Telecom companies should also consider how to derive additional value from their existing assets and competitive advantages.

Minimize costs in production and delivery by using automated and "low touch" processes to avoid building in extensive personnel requirements and increasing speed to market with a product that is not fully integrated in existing legacy systems and potentially running on a separate infrastructure.

Exhibit 3

Some companies are planning an imminent move into adjacent businesses.

% of respondents, n=104

We will move into new verticals	33
Financial services	33
IT services	32
Media	30
Heathcare	26
Utilities (eg, smart grids)	26
Automotive	26
Retail/ e-commerce	20

McKinsey&Company | Source: McKinsey TMT Extranet Survey, 2014

Drive sales by starting with a basic portfolio of services to gain traction and then developing one or two solutions with demonstrable advantages for a particular business. As customer demand increases, telcos can improve their responsiveness by implementing lean approaches and speeding up processes though multiskilling and dedicated presales and sales support. They should also capture synergies with their core business in areas such as local presence, customer access, and industry knowledge.

3. Build talent and capabilities

Many operators realize they need to work on building essential digital capabilities (Exhibit 4).

We recommend they focus more on agility and learning than on forecasting and planning, which become less relevant and reliable as technology-driven change continues to accelerate. They also need to foster a mind-set geared to learning, experimentation, and iterating with the customer. That means going to target customers at an early stage to test their appetite and price sensitivity, and then scaling up promising options fast.
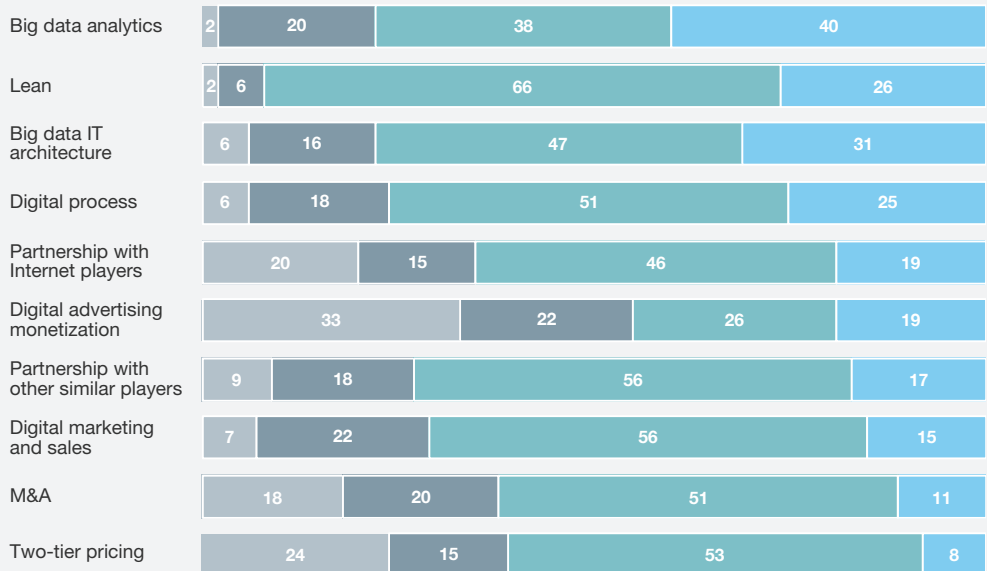
4. Revamp IT

For most operators, streamlining their application landscape and standardizing and automating their IT infrastructure will be a priority. Aging and complex legacy IT applications

Exhibit 4

Some digital capabilities are in short supply.

% of respondents, n=55

■ Not important ■ Important but external ■ Important and in-house ■ Important and in short supply in-house

Capability	Not important	Important but external	Important and in-house	Important and in short supply in-house
Big data analytics	2	20	38	40
Lean	2	6	66	26
Big data IT architecture	6	16	47	31
Digital process	6	18	51	25
Partnership with Internet players	20	15	46	19
Digital advertising monetization	33	22	26	19
Partnership with other similar players	9	18	56	17
Digital marketing and sales	7	22	56	15
M&A	18	20	51	11
Two-tier pricing	24	15	53	8

are a major hindrance in competing against nimble digital rivals. A recent McKinsey IT benchmarking study of 80 telecom companies worldwide found that top performers had removed redundant platforms, automated core processes, and consolidated overlapping capabilities. Such an effort enabled one South American telecom to free up the equivalent of 31 percent of its full-time employees, gain a unified view of customer billing, resolve customer issues faster, and reduce service errors. Inefficient IT processes are another obstacle.

The top-performing companies in our benchmarking study have simplified and automated backbone IT processes and systems such as server deployment, load balancing, and service-ticket management, saving costs and enhancing their ability to adjust capacity and load volumes. In emerging markets, where some telecom operators are adding as many as one or two million subscribers per month, the ability to automate capacity, server throughput, and storage has allowed senior managers to focus on business growth instead of scrambling to augment their IT infrastructure.

5. Start with the customer and work back

Most operators think of the customer experience as a series of touchpoints—individual interactions between the customer and different parts of the business, such as products,

customer service, sales staff, and marketing materials. But this misses the crucial part of the picture: the customer's whole experience of the company. Only by walking in the customer's shoes along the entire customer journey from beginning to end can operators truly understand how to improve their performance. What would an ideal journey feel like for the customer? What processes would support it? How would they intersect with social, mobile, and cloud technologies? The goal is not to digitize multiple elements but to deliver a superior customer experience. Companies that excel at this focus on singling out the handful of customer journeys that matter most to key segments, mapping how these journeys flow across functions, channels, and devices, and identifying and eliminating the biggest pain points.

■　　■　　■

Making smart use of digital technologies across the whole business is an imperative for telecom operators that want not only to combat the declining growth, shrinking margins, and intensifying competition of recent years, but also to seize opportunities that could make them stronger and more profitable than before. Getting it right will involve a wholesale digital transformation that starts with full commitment and strong leadership from the top. ❑

Paul-Louis Caylar and **Alexandre Ménard** are partners in McKinsey's Paris office.