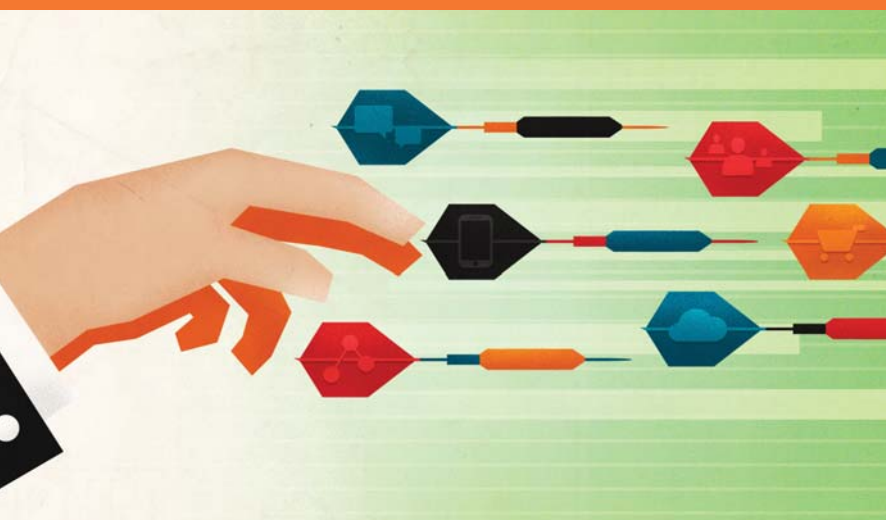Telecommunications, Media, and Technology

Change the channel: A new multi-touch point portfolio

By: Paul-Louis Caylar /// Mikhail Dmitriev /// Ben Fletcher /// Pascal Grieder

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The war for telecoms value has shifted to a multichannel theater of operations that promises new opportunities for telecoms players willing to capture them.

With the many serious challenges telecoms leaders face today, the question of how best to utilize the multitude of new channels they have at their disposal might not be getting the attention it deserves. That's a mistake because this new multichannel world – now an undeniable reality – brings both serious competitive threats and new growth opportunities. To navigate this complex new landscape effectively, however, companies need to understand where they stand at a granular level – one that involves micro-regions and per-product transaction types. They should also develop a coherent and rigorous execution plan capable of turning their multichannel strategy into effective practice.

Acknowledging the new multichannel reality

Today, telecoms players can interact with their customers through an ever-growing variety of channels. From call centers and brick-and-mortar stores to Web sites and social networks and beyond, consumers expect to be able to connect with their telecoms providers in multiple ways. In fact, 70 percent of customers currently visit at least two channels to collect information, and 50 percent of European consumers research using one channel and then purchase through another.

Mastering the multichannel world can open a variety of new opportunities for industry players. It can help companies boost revenues as they migrate customers to channels that offer the greatest potential to capture value or increase offer success rates by delivering more (and better) information about the telco's products and services. Operators can optimize their cost to serve customers via multiple channels by enticing them to move to more efficient

sales and service venues. They are also useful in capturing back-office synergies, enabling companies to deploy common processes and simplify procedures. Another benefit is the ability to improve customer satisfaction if telcos can seamlessly integrate subscriber experience across channels. Ideally, operators will develop a single, multichannel profile for each subscriber that contains key information about their needs, preferences, and value as a customer.

An effective multichannel strategy can increase revenues, reduce costs, and boost competitiveness by improving brand value

While a multichannel strategy can reduce costs, it can also burnish a telecoms player's brand. Research shows that telecoms distribution channels provide an effective way for companies to differentiate their brands from competitors' and at the same time improve customer experience. McKinsey recently surveyed European consumers regarding the comparative importance of the "touch points" where telcos interact with consumers. Ranked in terms of their statistically derived importance, retail stores and online channels ranked first, while call centers came in third.
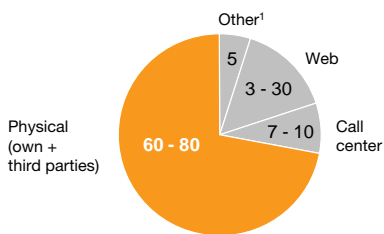
A number of channel trends are currently affecting the telecoms sector. In physical channels, which include telco-owned and third-party retail stores, companies are experimenting with new store formats and focusing on providing world-class customer experience with a strong educational thrust. They are also working to improve their retail performance by freeing up in-store sales consultants to spend more time selling and by taking steps to achieve higher service-to-sales conver-

The physical store still makes the largest contribution to mobile sales

ESTIMATE

Benchmark channel mix

Share of total mobile sales
Percent, average in Europe

Other[1]

5

Web

3 - 30

Physical
(own +
third parties)

60 - 80

7 - 10

Call
center

Rationale for relevance of the retail channel

Trust	▪ Still many customer segments prefer face-to-face advice before purchasing
Experience products	▪ Handsets increase in relevance as key buying factor (and touch & feel is preferred) ▪ Increasing number of other experience products in the offer (TV, iPods, etc.)
Complex offers	▪ Increasing offers of potential alternative services (add-ons, bundles, etc.)
Convenience	▪ Always a store near home, work, or along the shopping route

1 Including, e.g., direct mailing, D2D, SMS campaigns
SOURCE: McKinsey's benchmark run on declarations of 10 mobile operators in the EU and Russia, iConsumer 2012; research on 8 Western European countries

Exhibit 1

sion rates. Some players are launching additional retail brands to attract new subscribers from different consumer segments.

Remote channels are having greater impact by attracting more service transactions and online sales. Specifically, telecoms players have continued to utilize their call centers to make sales – with inbound calls targeted to make service-to-sales conversions, while outbound calls focus on cross-selling additional products or services that complement current customer purchases. Beyond these channel trends, some operators are taking advantage of the new multichannel reality by persuading customers to use more cost-efficient (and effective) channels for communicating with the company. Some are developing integrated methods to enable customers to interact seamlessly with them across multiple channels.

While all telecoms channels are growing, retail brick-and-mortar stores remain the most relevant in terms of their contribution to mobile sales. In Europe, for example, physical stores generated between 60 and 80 percent of mobile sales (Ex-

hibit 1). A number of factors explain the continued primacy of physical retail channels. Many customers still prefer to receive face-to-face advice when buying products, and with handsets increasingly seen as a key buying factor, shoppers want the opportunity to "test drive" them in person. Likewise, the availability of an increasing array of other "hands-on" products, from tablets to televisions to music players, plays to the retail channel's strength. Additional enabling trends include the move to more complex offers, which sales consultants can explain more effectively in person, as well as the convenience of stopping by the local neighborhood retail store.

Going granular to develop a multichannel strategy

Even though the multichannel phenomenon has become a telecoms reality, many companies lack a coherent strategy to successfully harness it. Creating one will require many operators to understand the details of their current situation at new levels of granularity.

Telecoms players that want to unlock their full multichannel potential need to answer several key questions: What are the economics and performance of different channels across a variety of transaction types? How does the company define a target channel mix that promotes sales, service, and information access, and how does it develop an optimal retail footprint? How does an organization enable cross-channel integration mechanisms? What are the implications of changing the channel mix for each channel? What approaches can help the company actually achieve its target channel mix? What are customer channel preferences across segments, and what barriers are preventing customers from adopting the most efficient channels from a sales and cost perspective?

A multichannel strategy has implications across the entire telecoms organization. A discussion that leads to fact-based answers of these questions will help operators develop an effective strategy with a number of critical end products.

Sales and service channel economics. The telco should have an integrated perspective on each channel's contribution performance (sales minus variable cost) as well as its costs and revenues. Business leaders should understand how much revenue and value all major product sales and service transactions generate, along with the associated channel costs for these transactions.

Defining the vision for channels and multichannel journeys. Companies develop a view on the future role and value proposition of each channel, then prioritize multichannel pathways.

Optimal sales and service channel mix. This requires operators to project their optimal channel mix over a three-year horizon for each product and service transaction and forecast each channel's three-year target economics.

Target digital model and levers to drive it. This includes the necessary changes to the digital channel along with initiatives to drive sales volume and digital self-care adoption.

Target retail model and footprint. Operators will want to determine not only the optimal number of brick-and-mortar locations but also their formats, operating models, and headcounts.

Insights regarding consumer channel preferences and behaviors. Here, the objective involves gaining a fact-based understanding of the ways consumers use and perceive each channel, identifying any barriers to adoption in the most efficient channels.

A concrete action plan enabling channel mix migration. The action plan should lay out the steps the company will take to facilitate consumer migration to the optimal channels and describe the organization, incentives, and infrastructure needed to enable cross-channel integration. Also, implementing a multichannel strategy usually requires a significant and separate transformation of company IT systems and capabilities.

Deriving sales and service channel economics

Companies need to understand the economics of integrated sales and service channels in detail. The most important concept in this regard involves each channel's contribution – in other words, its channel sales less any direct costs incurred. Elements of the sales part of this buildup start with the operator's payments from gross subscriber additions ("gross adds"), usually for a 6- or 12-month period (Exhibit 2). The next step is to add revenues from options and value-added services (VAS) activated through that channel, along with all equipment and the value of service, which equal the total value generated by the sales and service channels. To calculate the contribution from each channel, analysts deduct from the total sales all the direct costs associated with gross adds, options, VAS,

Operators determine each channel's business contribution by calculating its value from sales and service as well as its costs

Granular breakdown of a channel's revenues and costs reveals its precise contribution

Indexed

Legend:
- Prime cost[1]
- Commercial costs (sales and service costs)
- Allocated expenses on channel support

Gross add revenues	Options/VAS revenue	Equipment revenue	Service value	Total value from sales and service channels	Gross and costs	Options/VAS costs	Equipment costs	Service costs	Contribution
41	22	15	22	100	15 (7/4)	15 (4/7/4)	12 (7/4/1)	14	44

1 For instance, roaming, interconnect, COGS of devices
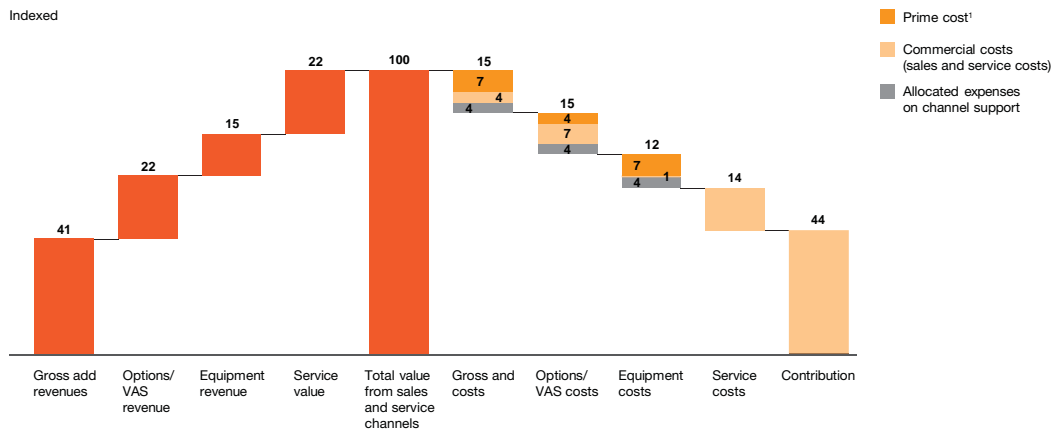SOURCE: McKinsey analysis

Exhibit 2

equipment and service. For accuracy, this analysis should include primary, channel-related costs and allocated channel support expenses. The telecoms organization should perform this type of sales/service mix analysis for each channel separately.

Many companies often struggle when dealing with the service part of channel economics. The following methodology allows them to quantify the value received from each service transaction (Exhibit 3). Analysts need to consider three value components.

Service-to-sales conversion. Service is an important generator of channel traffic, allowing operators to up- and cross-sell to customers. As a result, telcos need to understand the probability of any service-to-sales conversion along with the average sales value of each transaction type by channel.

Value from loyalty. Great service impresses customers, builds their loyalty to the brand, and has a direct impact on churn reduction. To quantify loyalty value, the organization first needs to understand the value of achieving maximum customer satisfaction. To do this, analysts take a sample

of customers who gave the company the highest satisfaction grade following a transaction and then compare the difference in their churn rates (i.e., either their declared desire in a survey or actual numbers) to the rest of the sample of customers who gave a lower grade.

Cost avoidance. Some service transactions gain intrinsic value because they allow a telecoms player to avoid the opportunity costs associated with churning customers. For instance, in prepaid markets, a transaction that involves replacing a customer's subscriber identity module (SIM) creates value simply by taking place. Otherwise, the operator risks losing the customer to a competitor or incurs subscriber acquisition costs when the customer buys an entirely new SIM.

Telecoms players should also take into account the frequency of different transactions when assessing their value. Some – like the cost-avoidance component of replacing a SIM – create value every time; others – such as prepaid balance check – do not necessarily avoid cost or boost loyalty every time they happen.

Applied methodology quantifies value of service based on loyalty value, service-to-sales conversion probability, and cost avoidance
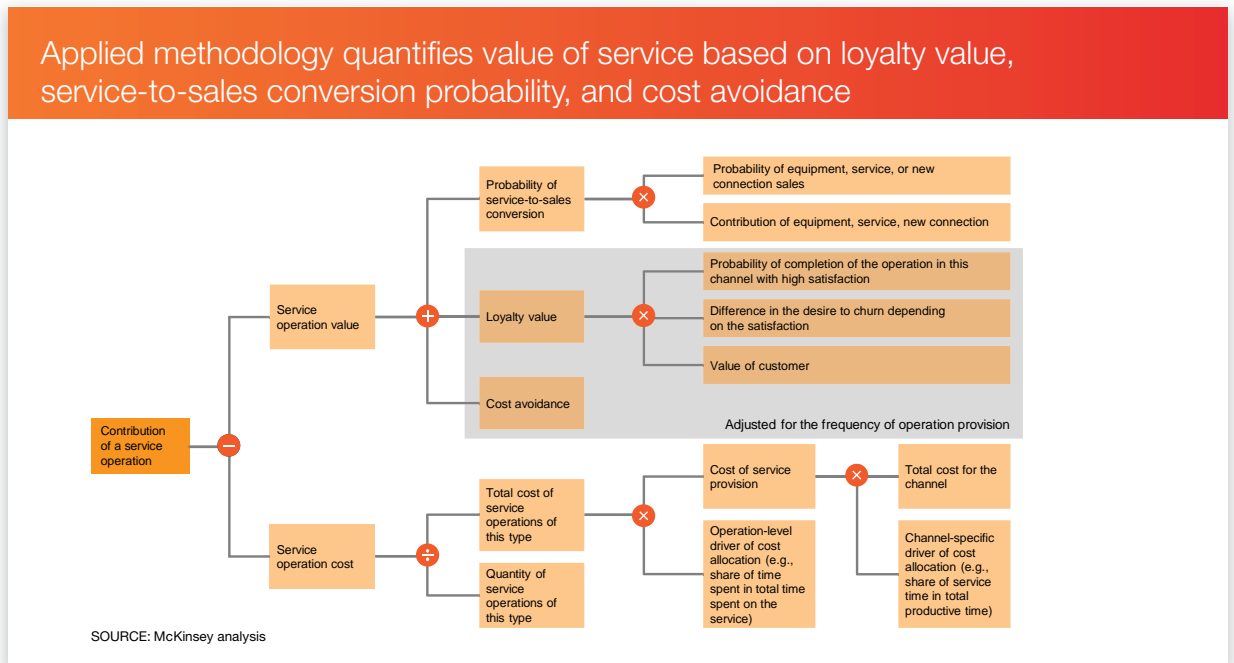

SOURCE: McKinsey analysis

Exhibit 3

Experience suggests that the most valuable insights typically emerge from examining per-product and per-transaction data, especially in terms of contribution performance. When analyzing sales transactions, companies often discover that some products actually destroy value when sold via certain high-cost channels. Per-transaction analysis of services also yields useful insights. At one operator, this revealed that one channel had the highest per-transaction contribution, although its transaction volume was still relatively low. Another showed high contribution performance in some operations that resulted from high service quality levels. The number crunching helped the company identify the transactions and channels that brought in the most value in service-to-sales conversions. As a result, the company decided it should not move these transactions to lower-cost channels.

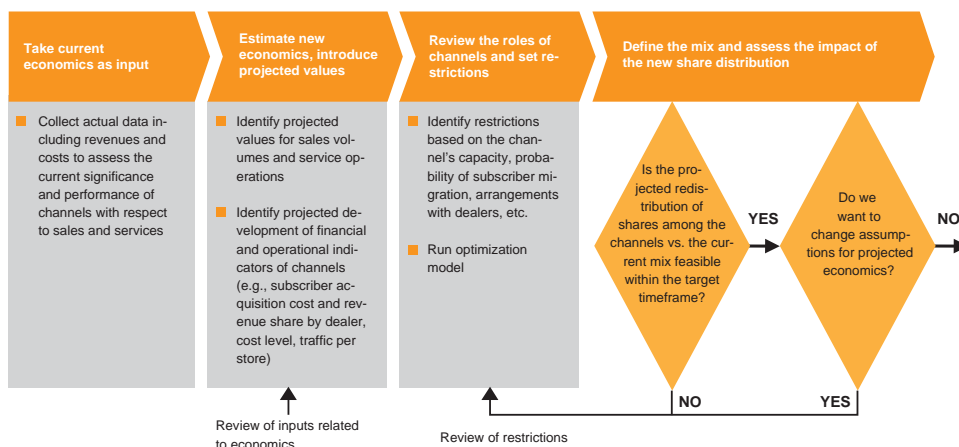## Defining the vision for channels and multichannel journeys

Operators should strive for a multichannel and multidevice model. This approach accommodates a journey in which customers conduct product research on the Internet and complete their sales transactions either on the phone or in the retail store. The model also enables an efficient and fluid customer experience across all of their devices that is also connected to the physical world.

The vision should have very high digital ambitions for both sales and service. It is already the case that at least 50 percent of customer billing inquiries, payment arrangements, questions about installation, ADSL gross additions, and mobile renewals are done online at some operators in France and the US.

Digital channels' value propositions should focus on simple and error-free digital journeys, easy and secure purchases, one-on-one personalization, and a direct link to physical stores. The value proposition of the physical channel is usually about providing more sophisticated expert support and customer education; an opportunity to test services, devices, and accessories; and personalized diagnostics to identify the offers best suited for a particular customer.

An iterative optimization model determines the optimal target mix

Take current economics as input	Estimate new economics, introduce projected values	Review the roles of channels and set restrictions	Define the mix and assess the impact of the new share distribution
■ Collect actual data including revenues and costs to assess the current significance and performance of channels with respect to sales and services	■ Identify projected values for sales volumes and service operations ■ Identify projected development of financial and operational indicators of channels (e.g., subscriber acquisition cost and revenue share by dealer, cost level, traffic per store)	■ Identify restrictions based on the channel's capacity, probability of subscriber migration, arrangements with dealers, etc. ■ Run optimization model	Is the projected redistribution of shares among the channels vs. the current mix feasible within the target timeframe? → **YES** → Do we want to change assumptions for projected economics? → **NO** **NO** ← → **YES**

Review of inputs related to economics

Review of restrictions

SOURCE: McKinsey analysis

Exhibit 4

Three consumer trends define multichannel pathways that really matter for telcos.

Web-to-shop/click-to-call. Web purchase is supported by shop pickup or telesales.

Showrooming. Customers use the shops to test their products before buying online.

Multichannel basket. Clients create a shopping basket on one channel. That same basket transfers to other channels.

Channel visions most telcos have developed include these three pathways in some way. In some mature European markets, they already constitute 30 to 40 percent of total sales transactions.

Optimizing channel target mix and deriving target footprint

Target channel mix can be simply set top-down; however, operators focused on determining an optimal mix of channels often find it useful to use an iterative optimization model (Exhibit 4). Such modeling often makes sense due to the complex influence changes in channel mix can have on channel economics. This is especially the case with captive channels such as the company's own retail and call centers due to fixed nature of costs and link between service traffic and sales through service-to-sales conversion. The four-stage approach described enables operators to assess their current channel economics, project sales and service values, review channel roles, and define and assess the impact of the new mix. They develop target channel mixes for both sales and service using the model, while taking any interdependencies into account. Optimizing channel mix can have significant bottom-line impact. One operator increased its channel contribution by 10 percent – a figure equivalent to over USD 300 million.

Data from surveys on consumer preferences and barriers to customer migration provides important input to the mix model, allowing leadership to set feasible optimization boundaries. It is also impor-

tant to consider the improvement potential of individual channels, since doing so can significantly influence results.

The model enables companies to arrive at an optimal product and service transaction mix across different channels and to calculate the most effective captive retail footprint size. Companies can, however, easily fall into a trap when sizing the footprint. If, for example, the model indicates the footprint size should be 200 stores smaller, many simply pick the stores with the poorest figures for closure. The risk associated with this sweeping but simple approach is that companies might close some poorly managed stores in good locations that actually stand a good chance of performance improvement. To avoid such costly mistakes, companies need to go deeper into the microregion and even to the store level to assess potential. One effective approach in this area involves point-of-sale (POS) regression modeling, which calculates each store's economic potential and compares it with the shop's actual performance. Companies can review their geographic coverage by employing the store catchment area concept, which can identify the best new store locations. This approach can also help them understand the revenue losses the company will suffer by closing specific stores. This way, a 200-store footprint reduction may, for example, involve closing 400 stores in total and opening 200 in new locations.

Successfully executing a multichannel strategy

Once it develops the robust multichannel strategy described, an operator needs to build a tailored organization and establish rigorous process and capable IT systems to execute the transformation.

First, significant changes might be needed in organizational design. The multichannel world requires cross-channel integration. For instance, many companies as a result of their multichannel strategy start thinking about their physical channel also as

an extension of online, with stores being pickup points for online orders and showrooms leading to sales online. For companies that used to think and manage their channels in separate silos, this means reallocating roles and responsibilities and redesigning incentives across channels to facilitate and reward cross-channel collaboration and cross-sales.

Second, delivering a multichannel strategy and enabling cross-channel customer journeys usually requires significant changes in IT platforms. Target IT capabilities to be developed include, among many others, a cross-channel product advisory engine, a fully multichannel architecture offering, an agile operations platform supporting real-time automated processing, fully online event-driven CRM, and a fully parametrical product catalog.

Finally, bringing the multichannel strategy to life leads to implementing dozens of specific initiatives across all channels and many functions. These initiatives support implementing organizational and IT changes and actions to enable and speed up customer migration across channels. They also support channel-specific actions to adapt each major channel to the new paradigm. A transformation of this scale usually requires setting up dedicated PMO capacity to rigorously drive and track implementation and impact.

Implementation of the multichannel strategy may require changes to organizational design and IT platforms

☐ ☐ ☐

Telecoms players compete in a multichannel world today; thus mastering the complexities inherent in this environment will set future industry winners apart. Leaders who actively take steps to optimize the mix of sales and service offerings deployed through each channel can turn the multichannel challenge into a significant opportunity.

Paul-Louis Caylar
is a Principal in McKinsey's
Paris office.
paul-louis_caylar@mckinsey.com

Mikhail Dmitriev
is an Associate Principal in McKinsey's
Moscow office.
mikhail_dmitriev@mckinsey.com

Ben Fletcher
is a Principal in McKinsey's
Sydney office.
ben_fletcher@mckinsey.com

Pascal Grieder
is a Principal in McKinsey's
Zurich office.
pascal_grieder@mckinsey.com