



Evolve or Perish

Digital Darwinism for telecom companies

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Introduction

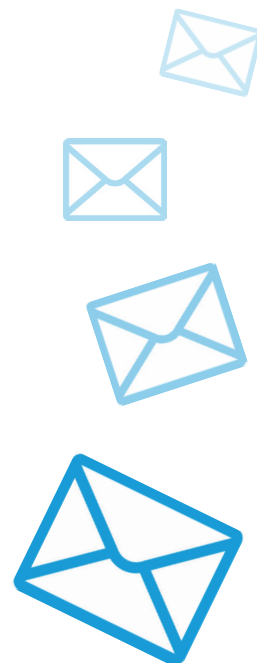
Studies of the digital economy all confirm the importance of the Internet and digitization as material contributors to economic growth¹. Consumers deserve much of the credit as they are “always on”. A recent 2012 ITU statistical report states that at the beginning of 2012, fixed broadband Internet subscribers were roughly 600 millions worldwide, with active mobile web access subscribers reaching already 900 millions.

Consumers are researching online with 1.2 trillion searches conducted online in 2012, according to Google Zeitgeist, are buying online, reaching the threshold of US Dollars 1 trillion sales lately according to global research site, internetretailer.com. Consumers are also conversing about as well as recommending brands forcefully: 22% of brand recommendations explicitly include the word “love” according to BazaarVoice.

Yet, although the Internet is now 20 years beyond when the first dial up connection was made, there has not been a comprehensive study of how digitization has evolved in consumers and has affected the bottom-line of companies. Crucial questions such as: are sales being cannibalized by online? Is brand competition tougher than before because of online? do not have definite answers. Companies obviously need to know how digitization affects the way consumers interact with brands and conclude purchase, and how digitization affects their true profitability in order to best compete and be at the winning or losing end of e-commerce and of the digital revolution.

Our study sought to close the gap. We undertook online market research in Western Europe to evaluate thousands of internet users' purchase journeys and ten times more in terms of consumer traditional, offline and digital touchpoints leading directly or indirectly to sales. The focus of this article relates to telecom products and services. Our research allowed us to develop a unique, high-resolution picture of how consumers interact with telecom brands, and how digitization affects those interactions. The picture that emerges is multifaceted:

1. Telecom consumers are already involved in many brand conversations and put brands in frequent competition especially in active evaluation to buy.
2. Brand conversations and comparison increase with digitization, and occur through a plethora of digital touchpoints increasingly outside of the control of brands, with experience matching, even surpassing the user experience offline, thus creating a more challenging environment for brands to conclude sales. Telecom brands must be loved before the active evaluation process, otherwise, this is too late for conclude sales- and worse, to feed social media after sales.
3. Only a few telecom companies have recognized the challenges and taken powerful digital actions to re-capture, or create unique dialogue with consumers. They're finding that their efforts are rewarded: the fringe of best companies is reaping large benefits, converting more sales than before. The effect could be large — powerful digital telco brands can generate 2 times more than the brands fully stuck in the past model of offline interactions.



1 Pélissier du Rausas, M., Manyika, J., Hazan, E., Bughin J., Chui, M. et R. Said, (2011), « Internet matters: The Net's sweeping impact on growth, jobs, and prosperity », McKinsey Global Institute, May 2011 and Jacques Bughin and Steven Spittaels, « L'impact de l'Internet sur l'économie belge », August, 2011
2 <http://www.itu.int/ITU-D/ict/wtim12/index.html>

As a case in point, consider a French brand like Free- which has been leveraging its unique “no frill” renowned brand to launch its SIM-only mobile offering in France in early 2012 and exclusively via online social media. Currently, the brand share in active evaluation is leading against all traditional mobile incumbents in France -even against other SIM-only brands launched at same, even lower, price point as, than, the Free Mobile offering. A brand like Telenet in Belgium has made a conscious strategy to reinforce its digital touchpoints, and to secure an online mindshare higher than the one it has already achieved offline for its triple play telecom offering.

It is also clear that the strategy of Free and Telenet, with their launch of King and Kong, resides, not only on digital, but in forward pricing much lower than the current price corridor. The fixed customer base they have combined with low price allows a quick mobile penetration in their broadband base, which ultimately allows them to phase their network development in medium term, - either through network sharing with mobile competitors under pressure, or via better and better wholesale deal by playing against a multitude of players, the increasing weight of their mobile retail base. This supply side strategy obviously puts pressure on incumbents, obliged to adjust price in the hope of only downselling versus losing customers, but the odds is that the mobile entry at low forward pricing is likely to spread in other markets too. This is because more and more, long duration, protective mobile contracts, are being challenged on a regulatory basis; because price per bits remain much higher today than in fixed, and because market is rebalancing to mobile internet, creating a disruptive moment for customer choice of mobile brands. Those changes also inevitably lead to more digitization, with customers waking up to decide more quickly on brands to continue, given more flexible contracts, and willing to re-balance voice versus data needs. The web is an easier way to get informed and an easier way to chase social media opinions without too much polluted communication from the old incumbents.

The message is thus clear: digitization is a crucial process of interaction of consumers with brands, mandating companies to transform themselves quickly and effectively. This is a matter of digital Darwinism, with digital leaders recapturing a significant part of the customer choice. Weaker brands fighting to stay relevant to an increasingly digital consumer will have no choice to embrace the digital revolution.

A. A HIGHLY ENGAGED TELECOM CONSUMER

1. The vast majority of consumers engage in telecom brand conversations

Consumers actively provide and seek word-of-mouth recommendations. For example, about 76% of Belgian consumers converse about brands, and 26% of them proactively recommend (and 20% criticize) brands to others, mostly friends (68%) and family (66%). In France, 64% converse about telecom brands, and 34% recommend to buy brands. Those conversations are not only frequent, but are specifically undertaken as part of the fundamental act of purchasing. We found that, in telecom 41% comment and converse about brands with the main intent of receiving information and feedback from others to help them with purchase decisions. This underscores that word of mouth remains the most relevant touchpoint to sales, especially in telecom with 47% of the telecom category purchases we analyzed relying on brand conversations.



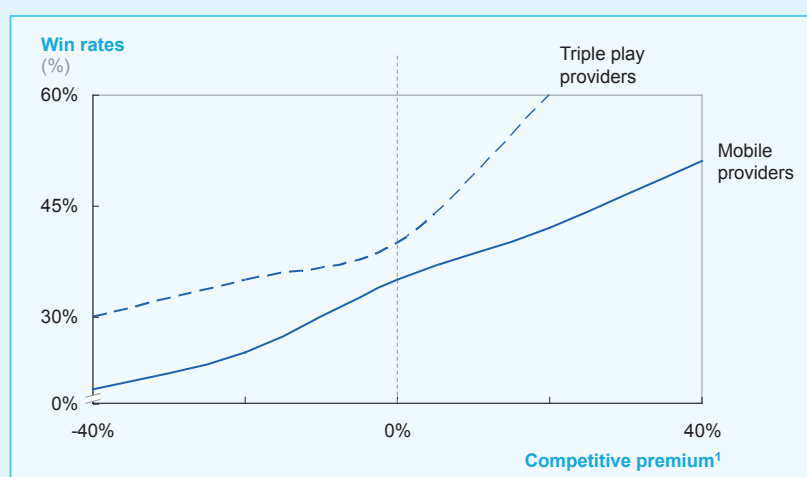
2. Telecom brand competition is quite prevalent, especially in the active phase of purchase evaluation

Consumers typically are aware of 5-7 consumer brands—and in industries such as cars or clothes, up to 8 brands are considered. In telecom, typical awareness is 3 to 4 brands. When it comes to the actual purchase, about 5 brands are initially considered for cars, and the lowest brand consideration relates to investment products (1.4 for bank investment product and 1.8 in life insurance) as well as telecom (1.7 for mobile provision, and 1.7 for triple play telecom services).

Not surprisingly, brands that emerged as winners in this consumer brand competition capture the most sales. And the difference can be large: the most competitive brands generate 30% more win rates than their fair share, while the weakest brands give up 30% of anticipated sales. In telecom triple play products, the major brand competition arises at the moment of active evaluation by the consumer—consumers compare actively brands in about 60% of the cases—further, the most competitive brand in triple play telecom (respectively, in mobile services) can generate 100% higher win rate (respectively 65% higher win rate) than the least competitive brand in the consumer active evaluation process, just before purchase (Figure 1).

Figure 1

Best competitive telecom brands generate highest win rate percent, Belgian telecom brands, 2012



1 Market share in competitive purchase versus fair stock market share

SOURCE: McKinsey

B. DIGITIZATION MAKES SALES SUCCESS MORE DIFFICULT

How does the brand engagement/competition change under digitization? We found that not only has digitization become an irreversible trend for customers but that this creates more challenges for brand sales success as well.

1. Digitization has become mainstream and will continue to gain traction

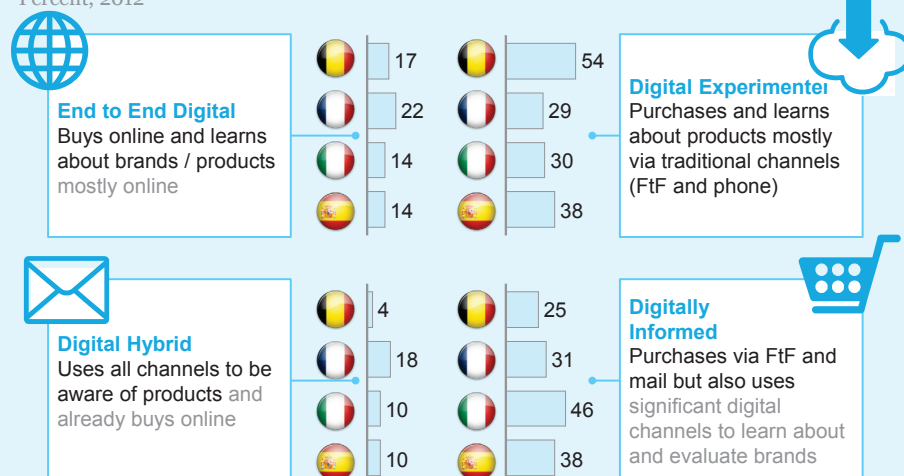
Digitization is already part of the mainstream path to purchase, with major digital touchpoints including search, social media, e-commerce, branded content sites, ad displays, and YouTube videos. In Belgian telecom for example, we found that 29% of all touchpoints in the initial consideration phase of the customer purchase process are digital touchpoints. Digital touchpoints become more dominant (33%) in the critical active brand evaluation phase and account for 24% of the actual purchase decisions. The proportion of digital touchpoints to actual sales for triple play has grown at about 18% a year, growing significantly in importance in recent years.

The intensity of consumers' digital interactions is not uniform, however (Figure 2). Looking at how again Belgian telecom consumers digitally interact with telecom brands in their decision journey, we can identify four segments reflecting different digital behaviors: Digital Experimenters, Digitally Informed, Digitally Hybrid, End to End Digital. Overall 51% of Belgian Internet users, when it comes to fixed telecom and 54% when it comes to mobile voice service, are still what we call "Digital Experimenters". Those consumers, when they engage in purchasing, use the Internet primarily and many (35% of cases) only during initial consideration of the purchase process, when they select the set of brands out of the larger list of brands they are aware of. Further, for Digital Experimenters, the active evaluation of brands and final purchase remain exclusively offline. This offline proportion may seem large, and indeed in Spain, the proportion of Digital Experimenters is significantly lower at 38%, even at 30% in Italy for both mobile and fixed telecom products combined.

Figure 2

Digital interaction types for mobile services purchases

Percent, 2012



SOURCE: McKinsey digital matters survey 2012

In France, the share of Digital Experimenters is less than 24% for mobile voice or mobile data. The major change that happened in France is the aggressive entry of Free Mobile, offering mostly a model of distribution via online, which pushed broadband uptake via online, and now pushing it aggressively for people shifting their mobile subscription to Free Mobile.

The other three segments of Internet-using consumers that make up the remaining already use in aggregate more digital than offline touchpoints along their paths to purchase. Where they differ is in the extent to which they use e-commerce to complete the full telecom product purchase cycle.

Our research revealed that in a quite advanced digitized market such as France, about 31% of consumers are in the Digitally Informed segment and are leveraging the Internet for awareness and active evaluation, but not for purchase online. Another sizable portion of consumers — 31% for broadband in France, and up to 52% for mobile — are using digital channels to conclude their purchase process. Regarding the mobile segment in France, a segment of 29% can be categorized as End to End Digital, using digital channels to initiate, progress, and complete 100% of their sales for mobile in France. The other part, 18% of French telecom customers, are Digital Hybrids, using digital channels throughout the cycle but still generally moving offline for their final purchase.

The evolution of digital touchpoints is quite important. First, digitization touchpoints to sales have continued to increase thorough years, roughly at 20% a year. Second, as shown above, supply side dynamics in the market can quickly create a major acceleration in digitization- see France. This digitization is quickly built up, because, the major natural fishing pond of the attacker, is its broadband base, already well online. Also, the low price entry offering is usually done via SIM-only, - simplifying the case for purchasing online.

Looking at the digital mix, in most of Europe, we notice that branded operators web sites and online search are leading the digital touchpoints in reach and frequency, only to be bypassed by offline word of mouth. Typically, call centers are the fourth touchpoint in importance.

Online search continues to grow in importance, not only because online is increasing, but because, it is also the leading gateway to other information. Among all searches, 20% of online searches are linked downstream to information on physical store locations, and 16% to social recommendations in both France and Italy (Figure 3). Also, a large part of the reach of branded operators web site is not direct traffic, - a lot remains due, - between 30-60% - to search traffic upstream. This has consequence for the distribution model of the telecom in the future. The reach of branded web sites exceeds that of branded stores, by a factor of 2:1 in France for all telecom products, in the purchase process. Further, frequency through web sites is 20% higher than it is when it comes to visit a telecom store, and the relevance of online visit is as strong as relatively less frequent visits to stores. Consequently, the experience of digital touchpoints clearly surpasses the experience of offline touchpoints such as stores for telecom consumers, leading to possible re-arbitrage in the long-term between expensive offline channels and online.

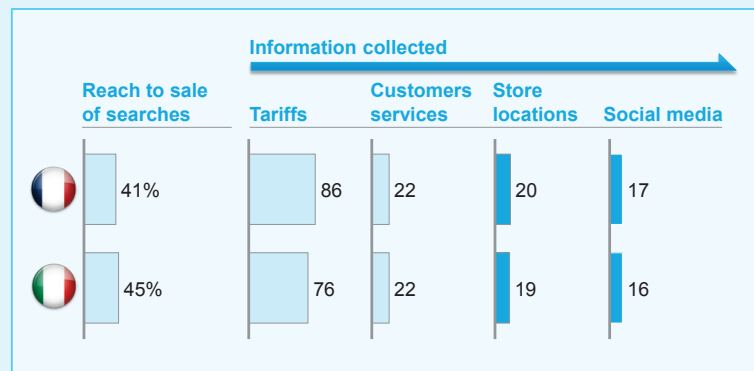
One exception of online trialing offline but quickly vanishing: offline word of mouth,



Figure 3

Online searches is a gateway to other touchpoints

Percent, 2012



SOURCE: McKinsey digital matters survey 2012

with up to 40% reach, continues to have higher reach and to deliver better experience than online when it comes to active consideration and evaluation of telecom purchase, but this is quickly changing. Nearly 30% of telecom post-purchase leads to word of mouth, and the online reach is closing its gap with offline. With 35%-50% of customers annually updating or churning their telecom offering, this means that the post purchase cycle feeds 10% of new word of mouth, on an actual stock of 40%. In a few years, the total word of mouth base of information will be easily depreciated and fully renewed, with an increasing proportion of online.

2. More digital consumers mean more telecom brand competition

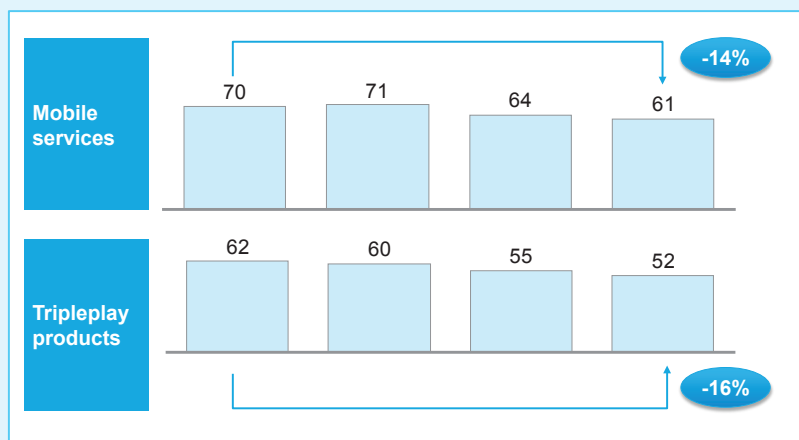
In addition, the greater the number of digital interactions a consumer has, the more intense the brand competition. We found that the average brand conversion in the purchase funnel is in general 20% lower for the End to End Digital segment than for the Digital Experimenter segment for telecom products (Figure 4). This lower digital conversion is due to four factors:

1. Facebook, Twitter and other communities and blogs have added platforms by which people can connect and converse among each other. We find that in telecom, the digital brand conversations already capture one third of the reach of offline word of mouth when it comes to actively recommending telecom brands. While Facebook brand fans only account between 0.5% to 1.2% (depending on countries analyzed) of a telecom brand customer base, this fan base is an effective ambassador to actively induce other consumers to reconsider their brand choice for purchase—roughly the average twitter account has 150 followers in US, and the average Facebook account has 160 friends, with roughly same amount through weak links.

Figure 4

Brand conversion decreases with digitization in triple play and mobile

Probability of being selected, Percent



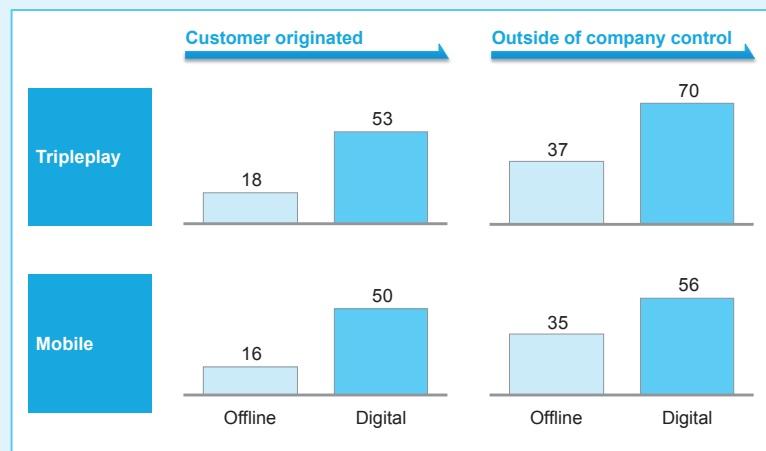
SOURCE: McKinsey digital matters survey 2012

2. The number of digital touchpoints to sales increases by roughly 20% for telecom products, with users exhausting all types of digital touchpoints—from search, to brand web sites, to social. With so much input, users may be more likely to encounter a “deal breaker” along the digital byway that de-rails their purchase intent. In fact, we find that digital information retrieval is intense, and is very large-price information is collected for 86% of the time for telecom products. Further, 50% of the time, data are collected on product quality as well as 36% of the time when it comes to provider services excellence.
3. A larger percentage (53% for telecom triple play products, 50% for mobile services) of digital interactions is driven by consumers (versus 18% and 16% for offline touchpoints). Simply put, the majority of digital telecom brand interactions are actively initiated directly by users. Adding all other messages received via word of mouth and other consumers, 70% (56%) of digital triple play (mobile services) touchpoints take place outside the control of telecom companies, versus 37% (35%) only when it comes to offline touchpoints to purchase triple play products (mobile services) (Figure 5).
4. Not least, digital touchpoints are more often used by churners than loyal customers. Churners are thus more in a mood of comparing, then the other types of customers. In telecom, we find an interesting patterns; the lead touch—point for consideration is search for loyal customer, it becomes price comparison site for telecom churners, and is morphing to digital social media for entirely new customers.

Figure 5

Digital touchpoints in telecom are much less within companies' control...

Percent



SOURCE: McKinsey digital marketing survey 2012

C. REINVENTING BRAND INTERACTIONS

Given the rise of digitization, the future seems more complex for telecom brands but this also opens the opportunity for brands to reinvent their interactions with customers. This form of digital Darwinism is the essence of competition and would thus benefit digitally-savvy brands. What is clear from herebefore is that the arc of consumers' evolutionary cycle is bending toward digitization, thus to survive telecom companies will need to adapt their brand interactions to this new environment.

1. There are some digitally savvy telecoms—but on average, companies are lagging beyond consumers digital preferences

What is a digital savvy telecom company? Given the above, digital savvy companies are those that are able to **a)** attract more than their fair share of digital savvy segments in brand awareness, **b)** serve customers digitally in the process up to purchase, **c)** generate good to great customer experiences, at least as good if not better than offline, and **d)** see customers comment extensively online about their experience to influence others to consider and purchase their telecom brands.

We find that, for the average telecom brand analyzed, between 30-70% of brand sales are driven by digital touchpoints, that about half of those digital touchpoints lead to a sale online (the balance leading to offline sales), and that 20% of those digital-induced sales lead to a positive recommendation online.

Recall however that consumer behavior and preferences are such that 50% are digital in Belgium, and up to 70% in France, that is interaction preferences are more frequent

than what the telecom providers conversion figures above. This means supply lags demand.

In general, across all consumer products, we found that barely 20% of companies matched the consumer preference benchmark, meaning that those companies are proactively interacting digitally with customers. Roughly the same is true for telecom services — with a long tail of companies, mostly telecom incumbents, is lagging the latent demand expressed by consumers, — and to their peril. In contrast, a small numbers are aggressively pushing online: In France, a company such as Free exceeds the average benchmark, as is a company such as Mobile Vikings in Belgium. Those companies have quite strong conversion cases in the sales funnel and a much higher proportion of customers voicing their positive experience to social media.

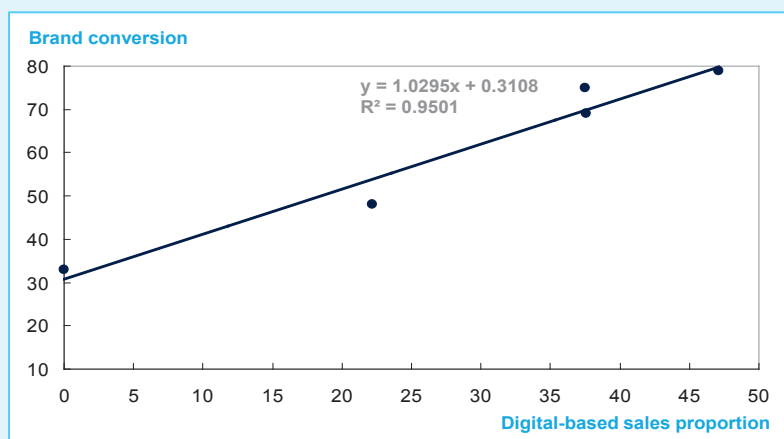
2. Companies that master digital interactions convert more sales

Is the push to adapt to digitization bad or good for sales? Are Free or Mobile Vikings correlated higher sales conversion rate in the purchase funnel with higher digitization, an exception?. Our study is the first that demonstrates what many suspect: companies that are better in digitization also enjoy the highest sales conversion rates. This holds true across all brands and sectors, including telecom services (Figures 6 and 7).

Figure 6

Digital-based sales leads to higher brand conversion subscription

Percent



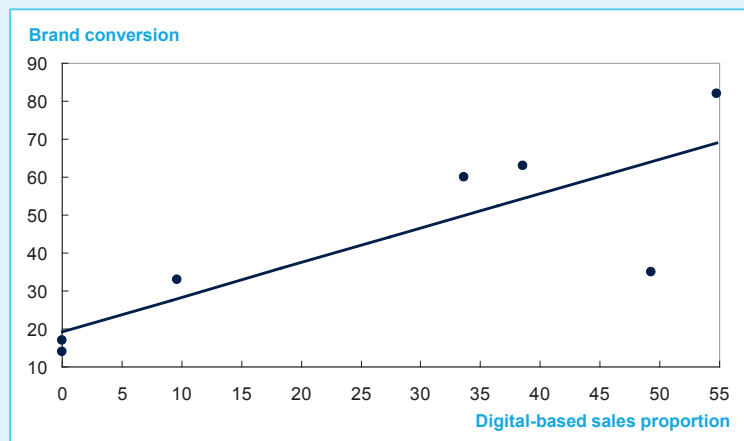
SOURCE: McKinsey digital marketing survey 2012

In Spain, Jazztel has been the fastest growing broadband player in the last year, with also the largest share of customers using online end to end for their telecom decisions. We find for example in Belgium that as a measure of improved digital capabilities, any 10% increase in digital touchpoints to mobile and fixed triple play sales results respectively in 5% and 7% more sales conversion success. This relationship is very strong, — explaining 90% of difference in brand conversion variance among mobile

Figure 7

Digital leads to higher brand conversion per industry – Trypleplay

Percent



SOURCE: McKinsey digital marketing survey 2012

providers and 67% in fixed triple play. This is furthermore one of the most robust relationship among the 27 product categories we have analyzed. This relationship is furthermore consistently driven by amount of brand searches and of online media, — in some cases, with online advertising too.

Consequently, our research offers compelling evidence that telecommunication companies need to recognize that they are in the throes of digital Darwinism, and make plans to adapt.

D. THE PATH TO DIGITAL REINVENTION

Darwin famously noted that it is not the strongest of the species that survives, nor the most intelligent, but the one most responsive to change. What should telecom companies do to make sure they are among the survivors of digital Darwinism? We suggest five actions tightly linked to the market research findings — more actions are possibly needed but not covered in the scope of this research.

1. **Focus on the future, not the legacy.** Companies in even the most traditional sectors have adopted new digital models. In the telecom sector Mobile Viking designed itself as a purely digital company, as has Free Mobile in France. Both companies enjoy very strong brand conversion (in our data, more than 80% conversion in the purchase funnel for Mobile Viking, versus 52% for the mobile services industry in Belgium; 64% for Free Mobile in mobile, versus between 28%-42% when it comes to traditional mobile brands in France).

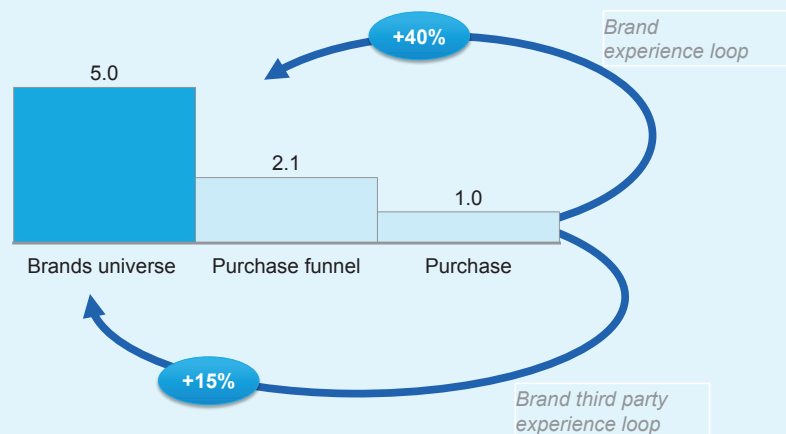
Digital telecom players do this by delivering a unique value proposition in terms of client service, community interaction and brand association. For example, without significant marketing budget, Free when launching Free Mobile, deployed

a smart digital campaign that cleverly combined traditional websites, blogs and social media websites to create one of the most positive buzz so far achieved in the French market. On the service side, both companies are able to create an atmosphere and digital channels where customers help (digitally) each other.

2. **Start experimenting fast.** Polarization is already occurring between digital savvy companies and the others as two types of feedback loops amplify the benefits reaped by early adapters. First, digital savvy companies are creating a stock of valuable recommendations to nudge prospective customers to buy. We found in telecom that about close to 50% of consumers provide feedback after purchase, much of it on social media properties. When read and positive, such feedback increases the probability of a sale by about 15%. Second, digital savvy companies increase the “stickiness” or repeat purchase potential of customers. A positive experience in telecom sales conversion increases by 40% the chance for the brand to be reconsidered and actively kept as preferred brand in repeat purchase. Those two reinforcing loops make clear that early success in digitization breeds long-term success. There is no time to waste (Figure 8).

Figure 8

Two reinforcing feedback loops affecting consumer telecom purchase



SOURCE: McKinsey digital matters survey 2012

3. **Identify and build the digital touchpoint ecosystem appropriate to your category.** While we believe that digitization is in general a “no regrets” play, some channels are more important than others, depending on the product category. For example, social media is twice as effective in converting consideration into sales between top brands in retail. In contrast, online search was found to be five times more effective in creating new sales between two of the main Belgian banks. In telecom, an inappropriate or subpar digital channel can spell disaster. In mobile services, a poor brand web store is actually systematically reducing sales conversion, implying that the web store experience did not meet consumer expectations. The keys are to know your customer and figure out which digital

medium they use for which purpose, and build the first iteration of an ecosystem on these insights. . Also, the real question is to understand the real sequence of touchpoints that will maximize sales conversion- as said earlier, search is a strong touchpoint in reach and frequency in telecom, but also it acts as the gateway to other crucial touchpoints such traffic to telecom web sites.

4. **Do not forget social media.** Even as the number of Facebook users tops one billion worldwide, the telecom sector has still a minor presence on social media. We found that the activation via social media varies a factor of 1-5 between the worse and best brands in telecom. The absence or poor activation can stifle interactions and inhibit the creation of a stock of valuable feedback.

A challenge we once provided one triple play telecom client of ours was to ensure its online presence in major digital platforms was as big as its brand presence offline. This was a challenge given an arguably more complex setting, given less controllable messages and interactions with customers, and the presence of third party web sites capturing a lot of gateway information for telecom brands such as search, price comparison sites, etc. The telecom triple company did so, by systematically communicating via social media, by asking feedback through its online community services, such as online gaming, and OTT vide platform. Achieving the milestone of brand likeness as strong online than offline, the company noticed it could not only sustain, but extend its leadership in triple play sales conversion. Its current extension to mobile products leverages digital social media too- in three months of launch, the buzz volume is already higher than the number 2 mobile service provider and only 10% lower than the incumbent market leader. The valence (ratio of positive volume



Consumers are digitizing more facets of their paths to purchase every day, in nearly every sector. These changing digital behaviors present challenges for telecom companies to engage and maintain dialogues with consumers as many crucial touchpoints are less in their control. Yet, our research shows that the opportunities are also significant. Companies that invest in understanding today's digital consumers and adapt to the new realities of digital Darwinism are the ones matching the preferences of digital-shifting consumers, - the benefit is already tangible with much higher brand recognition, brand valence expression and ultimately much higher brand sales conversion rates.

to negative) has already reached the ones of incumbents. From the above, this is sure symptom of success for this telecom attacker.

5. **Accept and adapt to user conversations.** Criticism or inaccuracies about a brand can be hard to take, yet because so many brand conversations happen outside of the purchase funnel it pays to become part of the conversation — even a difficult one. Investing in creating a first-class online customer experience that engages the customer and allows companies to solicit, listen to and respond to feedback is better than stifling conversation. The key is to use and adapt to feedback to stay ahead of the competition.
6. **Move from experimentation to strategy.** Many companies have launched various experiments in digital channels, however they find it hard to institutionalize and anchor these initiatives. We observe that leading companies invest in bringing in fresh digital talent, create a continuous digital monitoring and measurement process, and implement a fast-paced “test & learn” mechanism. Advanced “big data” analytic techniques allow companies to glean insights about website behavior, social media buzz and search behavior. Ongoing tests of small enhancements coupled with constant monitoring of digital reactions can reveal which actions are truly relevant and improve the digital environment for consumers and companies.

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