

# THE PROCUREMENT VALUE IN TELECOM

UNLOCKING FURTHER POTENTIAL AND ENSURING ACTUAL  
FINANCIAL IMPACT

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## EXECUTIVE SUMMARY

Telecom operators are facing strong financial pressures due to shrinking commercial margins and rising operating costs and investment demands.

As in other industries, telecom operators have put in place procurement departments to obtain significant savings through negotiation and panel rationalization. External spend – opex and capex – is a major component of the cost base, accounting for up to 40% of revenues, and can often be leveraged during difficult times. However, in the face of more diversified and complex purchasing portfolios, more concentrated supplier markets and faster technological shifts, traditional sourcing optimization initiatives seem to be reaching their limit. Today, very few operators have successfully boosted purchasing performance through more sophisticated approaches on a large scale.

Reaching the full potential of sourcing optimization requires going beyond traditional negotiations, obvious panel consolidations, and basic supplier management. Successful companies develop cross-functional collaboration between buyers and various business stakeholders, and their procurement departments are involved in the early stages of specifications design to enable total cost perspective and determine best suppliers' relationship models. Most importantly, savings generated need to be integrated in the budgeting process to ensure credible impact.

When successfully executed, this proposition can yield up to 400+ basis points in cash flow for telecom operators. Optimized procurement also generates significant side benefits such as improved risk management and identification of faster growth opportunities through enhanced supplier relationships.

# 1. PROCUREMENT: A STRATEGIC LEVER TO MAINTAIN PROFITABILITY FOR TELECOM OPERATORS

Telecommunication operators are facing significant financial pressures. On one hand, they have never experienced such a decline in revenues, a trend that is here to stay. On the other hand, there is a clear need to continue investing in network development and new services within a highly regulated environment.

In this context, external spend optimization is a strategic lever to ensure profitability. As external spend can account for around 40% of revenues, saving just 5–10% means 200 to 400 additional basis points of cash flow.

In more mature markets where revenue began to stagnate a couple of years ago, most operators have already engaged in procurement cost optimization initiatives. In fast-growing markets, operators are strengthening procurement capabilities to support rapid expansion and prepare for when business conditions worsen. Whatever the context, basic procurement strategies and levers are no longer effective.

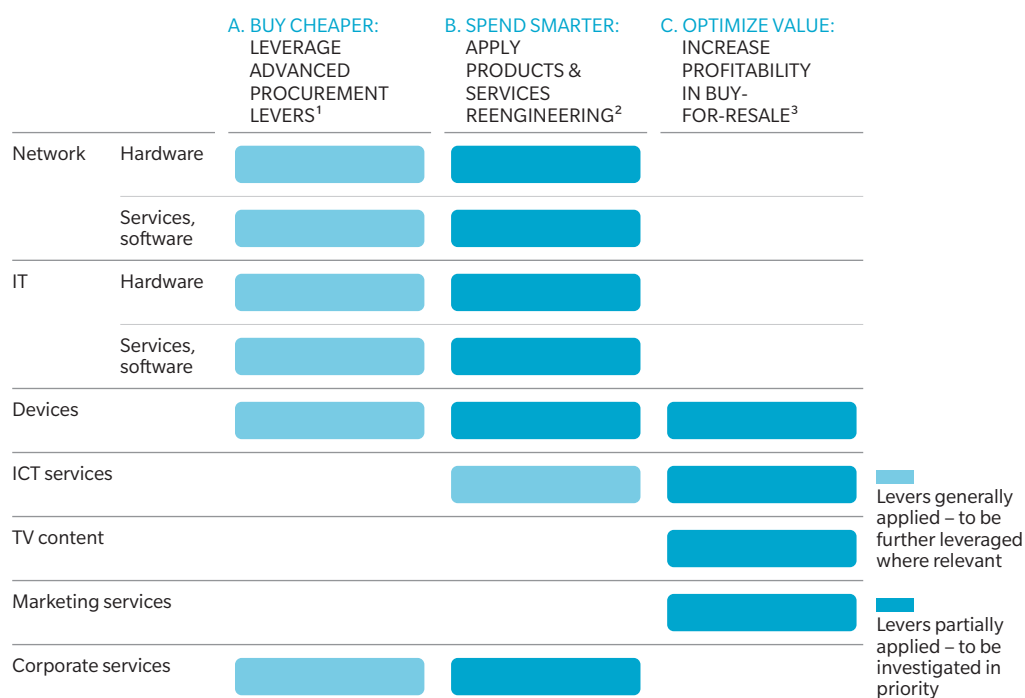
Indeed, the procurement environment has become more and more complex in the past years:

- Purchasing portfolio of operators has become increasingly diverse. It has evolved from relatively simple network elements (e.g. switches, routers) to a much wider array of products and services (e.g. software, maintenance, full solutions, TV content, set-top boxes, IT equipment for resale).
- Technologies are more complex, and technological shifts are very rapid, requiring operators to be flexible and react quickly. Suppliers' markets dynamics are changing, and telecom operators are now dealing with industries with low profit levels. Traditional vendors like AlcatelLucent and Ericsson have seen significant drops in their margins, due to fierce competition from new players like Huawei or ZTE. In the handset arena, Apple and Samsung have captured a major part of value, leaving only a very small share of the profit to others.

In this context, telecom operators need to shift gears in terms of procurement optimization through advanced practices, products and services redesign, and margin engineering on resale. It is also critical to obtain savings integration in budgets by the finance department. This requires overcoming existing silos between procurement and other parts of the company.

## 2. THREE KEY LEVERS TO UNLOCK THE VALUE

For a telecom operator, the purchasing portfolio typically covers seven major spend areas. According to their respective maturity levels, operators can apply three main macro-levers:



1 Unit price reduction, supplier panel consolidation, advanced supplier relationship management, ...

2 Specifications right sizing, redesign to cost and TCO/process optimization, consumption policy review, ...

3 Offer profitability improvement, customer investments optimization, ...

### A. BUY CHEAPER: LEVERAGE ADVANCED PROCUREMENT LEVERS

Over the past 10 years, most operators have taken measures to upgrade their procurement capabilities. However, in an increasingly complex environment, mature companies are taking traditional procurement practices one step further to optimize their TCO (Total Cost of Ownership) and capture more margin from supplier markets, as illustrated through the following examples.

#### MOBILE ACCESS NETWORK DEALS

Some emerging vendors have offered very aggressive entry deals to gain market share, applying a ‘razor-blade’ strategy. In many cases, some “great” deals actually turn out to be more expensive than expected. Indeed, precise network deployment scenarios, deep technical understanding, and robust modeling (e.g. via an “image network” methodology enabling apple-to-apple comparisons, or advanced benchmarking of deals and frame agreements) are critical to avoid pitfalls, align on best prices, and maintain bargaining

power. A clear sourcing strategy is essential. A “buy-as-you-grow” model supported by a robust technical roadmap could end up being more efficient than a poorly planned multi-year volume commitment strategy. In short, procurement strategies must always be considered in a TCO perspective.

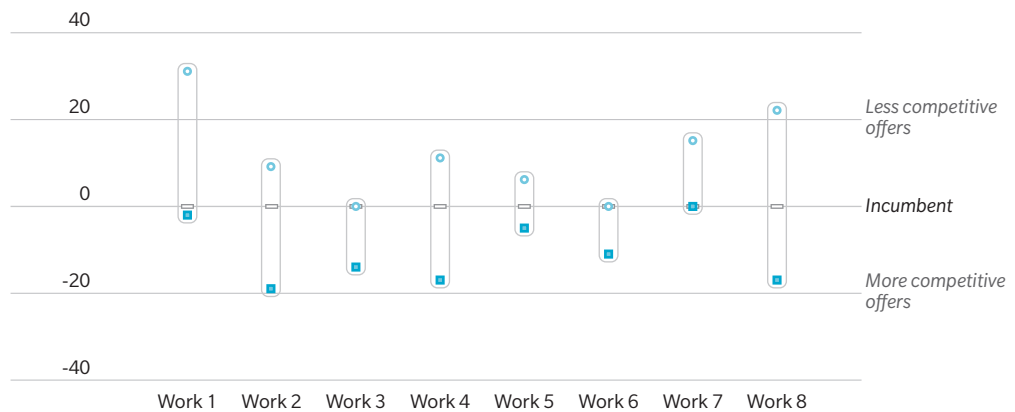
## FIELD OPERATIONS

Despite a significant part of labor-related costs, recent achievements have demonstrated that significant savings can still be obtained by consolidating the supplier panel and optimizing unitary prices through supplier cost structure analysis. Best practices also allow for further cost reduction and increased quality by reviewing key processes with suppliers (e.g. new FTTH and multi-technology deployment process, increased focus of dispatch by sending expensive splicers only when needed). They also seek continuous functional specifications simplification by aligning processes across technologies and products, and better adapting SLAs to value.

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### EXHIBIT 1: FIELD OPERATIONS – SUPPLIER PANEL REVAMPING CAN PROVIDE SIGNIFICANT OPPORTUNITIES

CIVIL WORKS PROVIDERS PRICE SPREAD VS. INCUMBENT  
PRICE SPREAD



## SOFTWARE APPLICATIONS

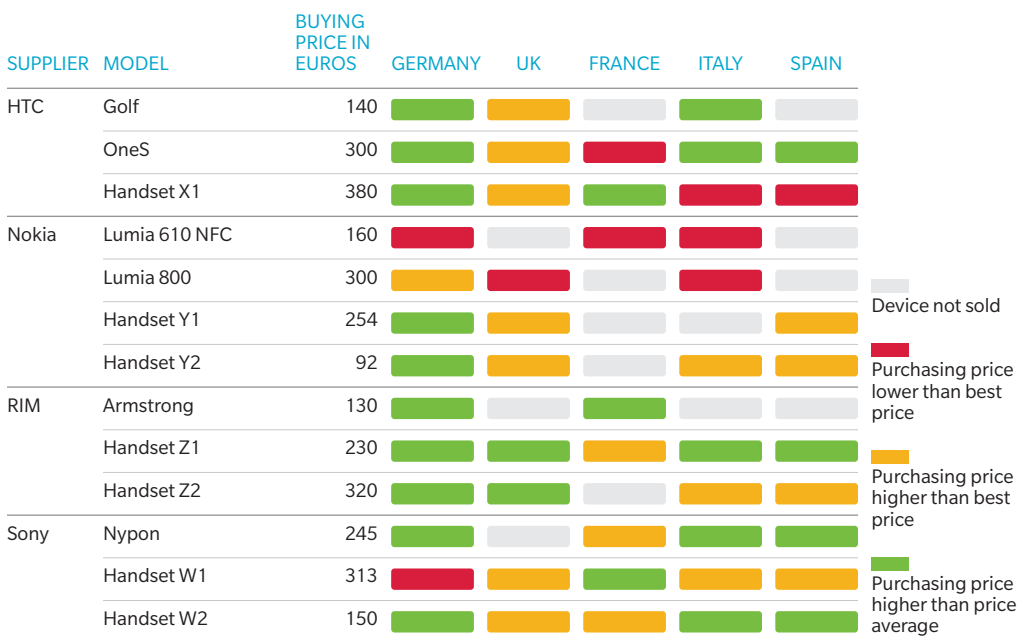
Traditional sourcing levers such as daily rate negotiations and offshoring development bring limited savings and are complex to implement in scattered application footprints. Supplier panel consolidation per application domains (usually from three to eight) can bring savings up to 30% from implied process simplifications such as decreased pre-integration work, avoided duplications between operator and vendors, reduced workload on tests. Such thorough review allows for make-or-buy optimization and the development of strategic supplier management.

## HANDSETS

Supplier market is difficult to address from a strict procurement perspective as some manufacturers struggle with reduced or negative margin, while a few others leverage leading positions to impose their conditions. Taking a broader perspective of costs helps activate levers such as on-going net price alignment on best market conditions and advanced forecast and ordering management to improve supplier demand visibility.

### EXHIBIT 2: HANDSETS – IMPROVE NEGOTIATION PREPARATION THROUGH ABSOLUTE BENCHMARKING

#### ABSOLUTE DYNAMIC MARKET-PRICE BENCHMARK



## B. SPEND SMARTER: APPLY PRODUCTS AND SERVICES REENGINEERING

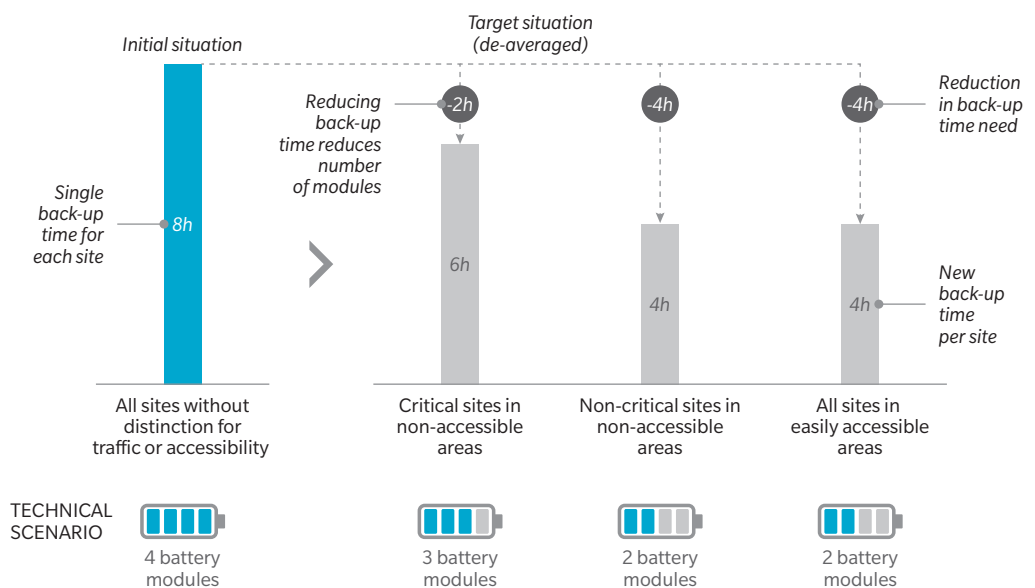
A large part of telecom operator's purchases is made of projects with lifetimes spanning several years (e.g. network, set-top boxes). Choices in terms of functional requirements and technical specifications therefore need to be optimized from the outset and, when possible, regularly challenged. Procurement departments play a key role in value engineering for telecom operators, just as they have done for years in more advanced industries like automotive.

## NETWORK

On the structural part of the network, specifications can only be influenced at the initial design stage. Strong upfront collaboration with suppliers in the design phase, sound demand planning, and understanding of the “on the field” usage allow to right-size network requirements. Leaders in this domain manage to build a clear vision on the expected service level and strike the right balance between business objectives, engineering constraints, and sourcing requirements. Other network components (e.g. batteries, HVAC ...) are also optimized via Value Analysis and Value Engineering in a TCO perspective. For example, some operators have deployed one unique battery per site instead of one per service, or adapting the power level to the exact needs of the site. Operators managing multi-geo networks can also leverage feedback from early deployed countries to optimize deployment specifications in the others.

### EXHIBIT 3: VALUE ANALYSIS AND VALUE ENGINEERING ON MOBILE SITES BACK-UP POWER SYSTEM

#### BACK-UP TIME AND BATTERY MODULE EVOLUTION FUNCTIONAL NEEDS



## SET-TOP BOXES

In a segment where components' prices are decreasing and the supplier market offers a reasonable number of alternatives, finding the right supplier and negotiating the right terms usually yields good initial results. There is, however, more to achieve by actively working on the product range, developing entry market simplified boxes and without hard drive, for example, and aligning box releases with market cycles to benefit from electronic component's price decreases.



## C. OPTIMIZE VALUE: INCREASE PROFITABILITY IN BUY-FOR-RESALE

Some purchased products and services are meant to be resold. Buy-for-resale mechanisms leave little room for price negotiation, making it critical for operators to optimize value (costs vs. revenues) to improve their margins.

### CUSTOMER PREMISES EQUIPMENT (CPE)

Subscriber Acquisition Costs (SAC) and Subscriber Retention Costs (SRC) can massively deteriorate margins if not managed tightly. Optimization requires 1) a scientific understanding of customer behaviors (e.g. segments, price and choice elasticity) to identify best return on investment opportunities, 2) the ability to handle big data, and 3) the implementation of decision support tools to make right choices on a day-to-day basis.

### ICT SERVICES

Equipment, which accounts for 40 to 60% of total costs, is often selected by clients and purchased on their terms. As a consequence, purchasing price or specifications are rarely influenced. In-depth deal and client margin analysis allow the optimization of sourcing channels (e.g. reducing broker usage by improved order planning) and service costs (e.g. leveraging own spare parts to avoid back-to-back reinsurance) or the improvement of service delivery efficiency (e.g. team specialization and training).

### TV CONTENT

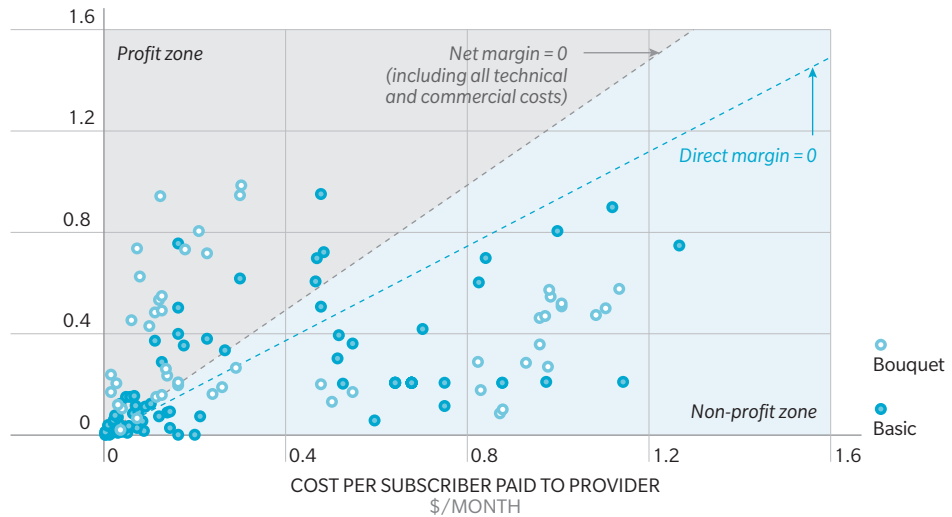
The challenge for telecom operators who have developed a TV offer now lies in increasing or maintaining profitability once market share is established. The first step consists of moving from a pay-per-viewer cost model, generally used at the development stage to avoid the burden of fixed costs, to a fixed fee model. The second step aims to optimize ROI using analytical techniques to calculate individual margin per channel. Then the last step is about understanding the true value of content, assessing its impact on acquisition or churn, based on quantitative, in-depth customer studies. This supports the decision to prune or replace unprofitable channels and develop undisputable negotiation arguments to increase profitability.

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## EXHIBIT 4: TV CONTENT – TV OFFER MARGIN OPTIMIZATION

### TV CHANNEL PROFITABILITY ANALYSIS

REVENUE PER SUBSCRIBER  
\$/MONTH



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## 3. HOW TO MAKE IT HAPPEN: ACCURATE MEASUREMENT OF FINANCIAL IMPACT IS CRITICAL

Most CFOs recognize that they struggle to reconcile savings from external spend and what they see in the books. This is even more difficult for telecom operators where a large part of the overall stakes is not year-on-year spend (CAPEX, project-driven expenses). However, in the context of increasing pressure on margins, it is now critical to demonstrate the actual and accurate impact of procurement initiatives.

Usually, savings are not properly integrated in budgets, resulting in frequent “consumption” of the cash and, ultimately, a massive decrease of the actual net financial impact.

A cross-functional approach based on pragmatic principles guarantees the impact of procurement initiatives:

1. Have procurement and business stakeholders define and agree on comprehensive yet simple saving calculation rules
2. Build a budget spend baseline by consolidating business needs in an environment characterized by non-recurring purchases and obsolescence-driven price decrease. For more than any other industry this requires:
  - To implement a robust “demand plan” process that will capture at a detailed level business requirements in terms of volume and mix, at current unit price
  - To give a sourcing guidance which includes main market price trends (mostly technology obsolescence) in order to adjust expected unit prices
3. Feed and manage a pipeline of actions which target savings are then integrated into budgets
4. Track completion of actions and savings realization to measure procurement performance
5. Measure P&L and cash evolution and compare it against savings declared by procurement

Beyond short-term benefits, validating savings by finance increases the commitment of all stakeholders to continuously pursue external spend performance improvement.

## CONCLUSION

In a context where the scissor-effect undergone by telecom operators shows no signs of going away, leveraging sourcing is a must-do. The good news is that more sophisticated approaches can generate a significant upside and relieve financial pain. The challenge is that in order to produce expected results, these levers need to be embedded in proven methodologies and tools and supported by a holistic operating model.

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Our approaches are built to deliver sustainability and avoid the black-box effect:

- Knowledge transfer: it is embedded in our way of working. Through formalized methodologies, supporting tools and processes and continuous coaching and training, we make sure each organization takes full ownership of our recommendations and is equipped to sustain them over time.
- Proprietary tools: Our approach is not a theoretical construct but rather a toolbox we have built a number of proprietary tools – from diagnostic (GSM Oliver Wyman tool ©) to consolidation (APD © and Levers periodic table ©) and performance measurement (SATT ©). This enables us to be immediately operational.

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