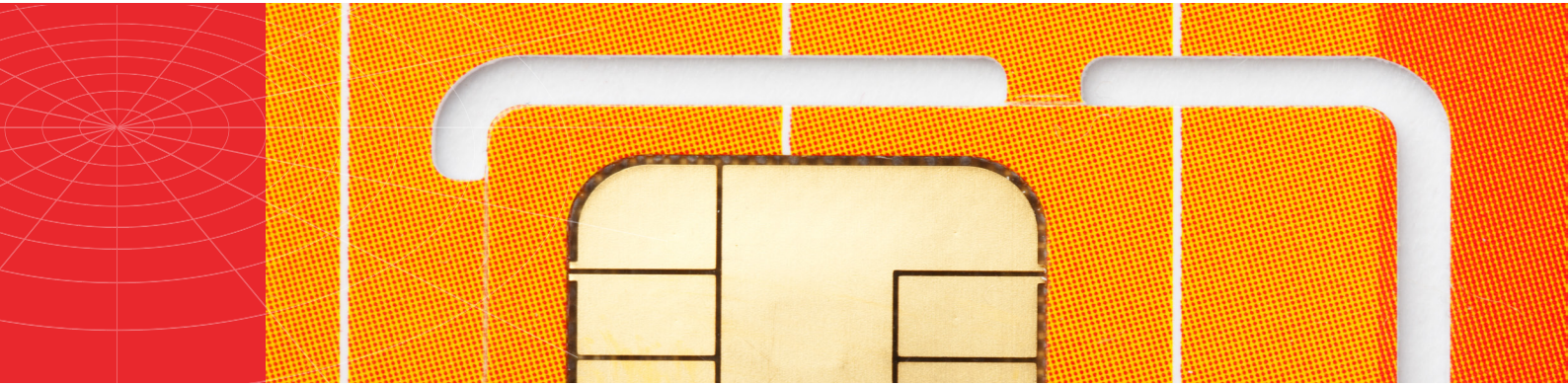


Ring up profits: How to crack the post-paid segment in emerging markets



By Piotr Markowski and Shaowei Ying

One of the great changes in modern times has been how fast and how widely the communications revolution has spread. Even in urban squatter settlements or remote villages in the poorest countries, it is routine to see people talking on cell phones.

So far, mobile usage in emerging markets has been associated with the pay-as-you-go (or “pre-paid”) model, in which consumers pay for a set number of minutes and then top them up as required. As incomes rise and prices fall, however, consumers are likely to shift to the contract (or “post-paid”) model, in which they pay a regular fee, typically by the month. In the Philippines, for example, post-paid service has been growing at 7% a year, more than twice as fast as pre-paid.

The advantages of having a larger percentage of post-paid subscribers are considerable. For a start, operators are assured of a more stable revenue stream and lower churn rates. Operators also capture back the margins given to the third-party channel distributors, which are extensively used in emerging markets for selling prepaid top-up airtime. Such margins could range from 10% to 20% of face value. In addition, with access to important information, such as mailing addresses and usage patterns, smart companies are in a position to

create targeted campaigns that offer differentiated services.

There are also risks, though. Post-paid service is costlier to provide and the risk of bad debt is higher. Moreover, companies can lose good consumers in the transition.

Here’s how telecoms providers can get ahead of the curve and manage the migration to the post-paid world.

1. Create a compelling value proposition: Companies need to evaluate how to increase the relative attractiveness of the post-paid value proposition. Options include enhancing the range of handsets; introducing hybrid tariffs; and experimenting with customizable price plans.

The key is to find the optimum balance between a low cost of acquisition (potentially even including subsidizing the price of the handset) versus the expected average revenue per user. To some extent, this will be a matter of trial and error, but there are examples to follow. In 2010, for example, one Asian provider launched its post-paid service by giving customers flexibility to mix-and-match plans and add-ons. The company also spruced up its stores, and retrained staff to do more consultative

selling. In a single year, it increased the number of post-paid subscribers by 21%.

Hybrid pricing is one way to ease consumers into the post-paid world. As the name implies, “hybrid” pricing combines elements of both kinds of service. In a hybrid model, consumers might make a short-term commitment (seven to 20 months, or even a set number of recharges) rather than a longer one. Or they might be allowed to opt for limits on costs, by topping up the fee after a set value has been reached. In another example, a Slovakian provider offers two low-cost contracts (10 euros and 15 euros); when the monthly credit is used up, it can be recharged via the Internet, ATMs, scratch cards and other venues.

In the Czech Republic, consumers have proved skittish about switching to post-paid phones. So one company created a menu of 2,600 options; customers create their own service (or can choose one of 10 standard options). Because users make their own recipe, in effect, they set their own monthly fee. They can also change the terms of service at any time.

2. Choose your customers—and check them out: Untargeted campaigns are unlikely to be profitable; it makes much more sense to find, select and evaluate sub-segments of customers.

This is a three-stage process. First, test a sample of consumers, by running relevant pre-paid to post-paid campaigns on a representative sample of, say, 10,000 users. Then, identify promising sub-segments by finding patterns between identifiable user data (location, tenure, spend level etc.) and the elasticity of the revenues. Finally, roll out below-the-line campaigns to the most promising sub-segments.

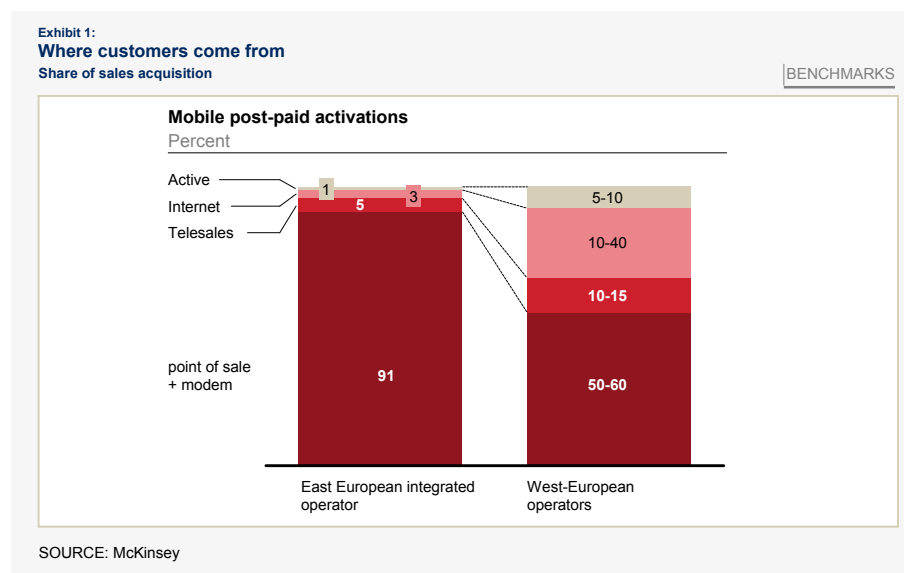
As part of this process, certain financial facts of life must be acknowledged. First, post-paid service works best with those who are connected to the formal financial system, in the form of bank accounts, credit cards and checks. And second, just as in wealthy countries, there are going to be a certain number of deadbeats—although credit and fraud verification systems may not be as sophisticated.

Hard experience has found that bad debt rates for new post-paid subs can be double or triple that for the rest of the subscriber base. Worse, while “indirect” channels like direct mail and the Internet are growing fastest, they also have the highest churn rates.

It makes sense, then, to make acceptance of new customers conditional. While most carriers examine customers purely on their credit score, actual customer behavior is more complicated. In addition to credit score, channel, and geography, regression analysis has identified age, handset selling price and tariff plan as major factors that influence fraud probability:

A credit infrastructure is crucial to a modernizing economy, so companies should also help to spearhead efforts to develop a national credit database.

There are also fundamental differences in economics between migrating own prepaid subs to postpaid, and acquiring



new (or competitive) subs as postpaid rather than prepaid. If current subscribers migrate to post-paid, value could actually be destroyed if increased costs – in the form of bad debts and higher subscriber acquisition and retention costs—offset the benefits of better post-paid margins and longer tenure. On the other hand, acquiring new or competitive subs on makes economic sense if the postpaid offerings help to “lock-in” customers and create higher revenue per user.

3. Leverage retail operations: In emerging markets, traditional retail points of sales, such as operator-owned stores, still play the primary role for both pre- and post-paid services. In Central Europe, for example, 80% of post-paid subscriptions come from single-brand points of sale (compared to less than 30% for Germany, Spain or the Netherlands).

Having an extensive network of physical stores is costly but necessary. It’s worth noting, for example, that brand-name retail outlets have the best record at signing up reliably paying consumers. And, of course, while the Internet may seem ubiquitous, it isn’t quite, and people

in emerging markets may also have heightened concerns about security and delivery. So the better option is to accept, and build on, the human dimension. In training store staff, for example, shift the incentives in order to link dealer and store commissions to post-paid value created. Another approach is to use tele-sales to generate leads that sales agents fulfill. This also helps to reduce the risk of companies cannibalizing their own prepaid subs.

Pursuing an aggressive post-paid strategy in emerging markets is fast becoming an important source of competitiveness. Done right, the post-paid segment could confer significant economic advantages, including higher profit margins and stronger connections with consumers.

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