TELECOM, MEDIA AND TECHNOLOGY

GROWTH Q1 2016

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ALVAREZ & MARSAL

Telecom

The growth for mobile operators in the last quarter was driven by the increase in 4G/LTE customer base. The 4G/LTE global subscriber number exceeded 1 billion in Q4 2015 according to Ovum. Growing 4G subscribers, has led to higher data usage (1.7GB per month in the U.S. in 2015, according to Ofcom) especially driven by new unlimited data products. However in terms of revenue impact the picture is different. Most operators across Europe and North America decided to include 4G in their existing data products, with limited or no price increase. Price tiered by speed with systematic throttle has been the exception with Swisscom, the main European player opting for this strategy.

The very heavy investments in networks (4G, then 5G, fibre, etc.) have caused several Telecom businesses to spin-off their network assets from their operator business. Numerous examples include Telefonica, Telecom Italia, O2 Czech Republic and Vimpelcom. This separation allows operators to focus on products and services while network businesses focus on offering the best multi-network communication infrastructure. The trend has drawn significant interest from private equity buyers looking for long term stable returns.

While 4G already is a reality, three growth opportunities were the main topics at this year's Mobile World Congress:

- the Internet of Things (IoT) : Ericsson expect the number of connected devices to increase from 5 billion in 2010, to 25 billion in 2020
- 5G expected to deliver speed 10 times higher than 4G and very low latency: Some trials have already started in South Korea and the U.S., but its standard is only expected to be agreed by 2018
- Virtual reality: Highlighted by several key players, virtual reality is expected to be a growth opportunity across the TMT industry

A&M VIEW

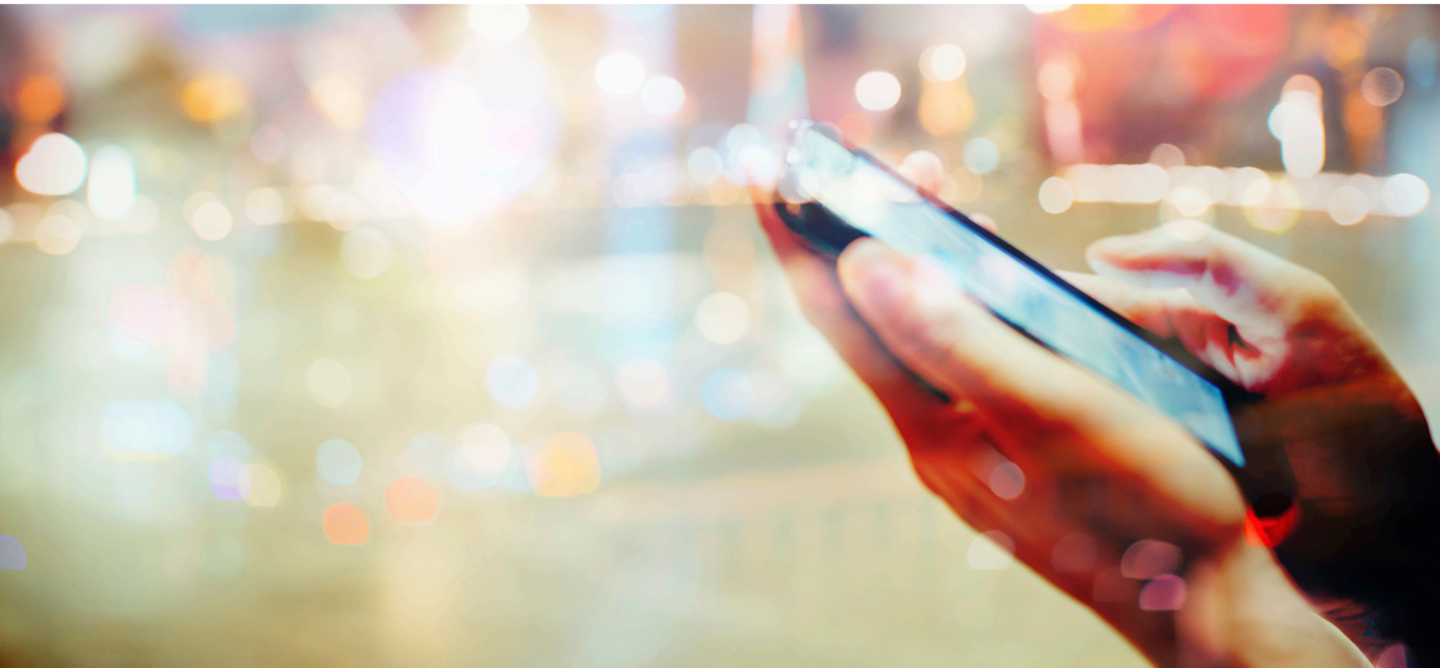
Monetisation and disruptive business models

Monetising 4G/LTE: 4G speed was generally added in the main operators' offers with limited monetisation. Only a few operators went for standard plans with unlimited data usage. Also, 'data only' plans have merely been progressively introduced. It is likely that 'all you can eat' data plans for mobile or fixed access, could offer major growth opportunities especially when shared for devices beyond the mobile phone i.e. tablet, laptops and soon cars and the numerous devices connected in an IoT environment.

Disruptive business models: Operators with disruptive business models such as Free in France and T-Mobile U.S. have been very successful at capturing new customers. Aggressive pricing, a basic product portfolio, effective marketing and transparency are the main components of their success. Our experience shows that this approach can be applied to other operators and generate significant gains especially for standalone (typically private equity owned) operators.

Customer experience is key for market leaders

Disruptive business models have proven successful for market challengers, we have seen market leaders focus on offering more sophisticated and segmented services and improved customer experience. As more Telecom groups spin-off their network assets and as products become more sophisticated (3Play 4Play), the ability to provide a multi-network, unified customer experience with a single view of the customer and sophisticated 'next-best activities' is a decisive advantage.



Media

Pay-TV subscriber numbers were significantly dented in 2015 (see chart on page 6). Pay-TV subscribers in the U.S. are trending down and according to Leichtman Research Group about 3 percent of the Q1 2014 customers have now left. Faced with this decline, pay-TV operators have taken the following steps:

- providing faster internet speed, especially to counter the Telecom operators such as AT&T and Verizon
- Investing in OTT (over-the-top) solutions to offer a multi-room and out-of-home experience e.g. Time Warner cable- TWC TV, Comacast X1, Directv, etc.
- Improving picture quality, for example Directv offer some of its programs in 4K
- Offering promotions and price reduction

Streaming businesses had a very active last six months with Netflix announcing in January at the Consumer Electronic Show (CES) it is now available in virtually every country on the planet. At the same time HBO was rumoured to be restarting an aggressive international roll-out for HBO GO. Amazon also announced record Christmas numbers as Prime Video views doubled compared to that of Christmas 2014. Sky made an investment in Asian streaming service iflix, a rival to Netflix.

On the film side, 2015 and Q1 2016 broke box office records in cinema driven by the almost simultaneous release of James Bond Spectre and Star wars - The force awakens.

A&M VIEW

More M&A ahead

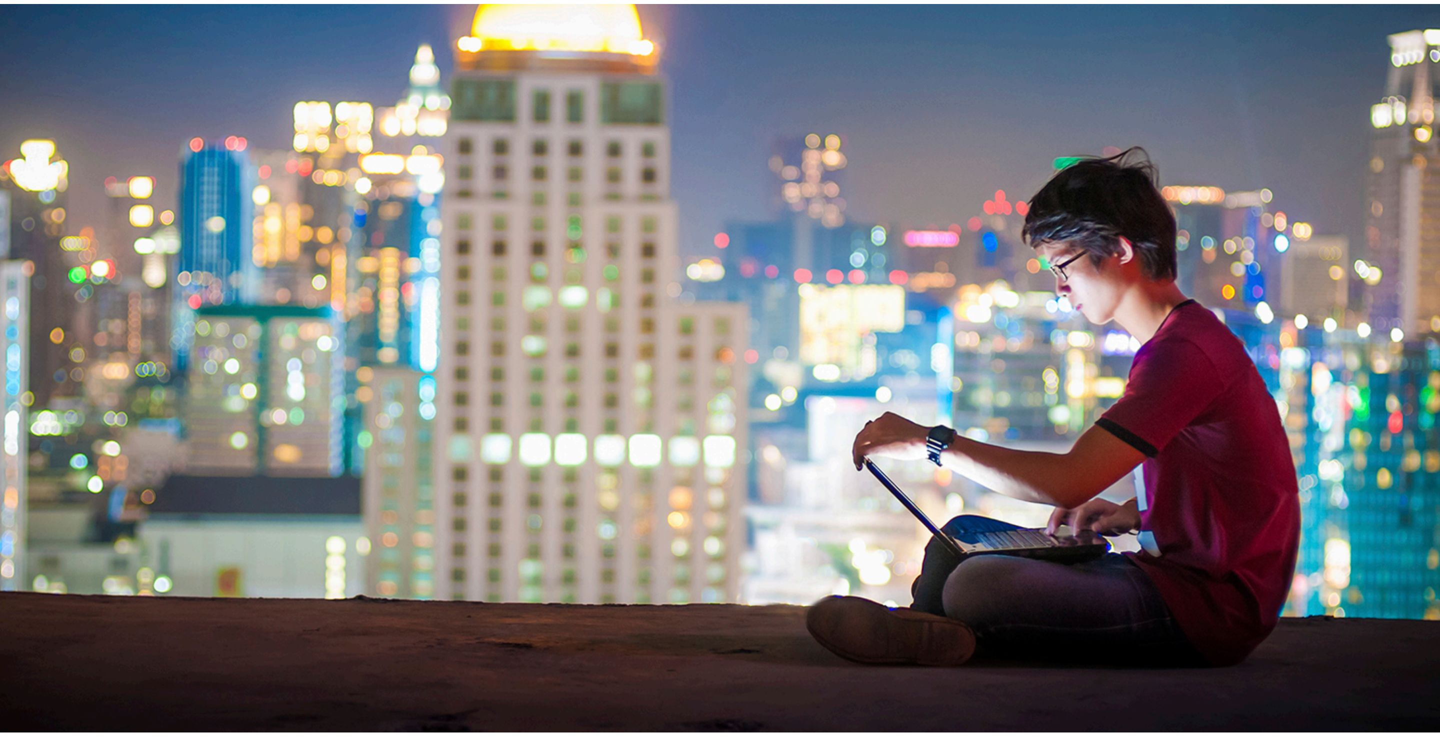
The consolidation of pay-TV operators is well advanced in the U.S. with several M&A operations in the past year. It may now reach Europe, as indicated in the latest Liberty Global – Vodafone deal in the Netherlands. This deal may end up being a template for a wider Vodafone- Liberty Global merger. The market response shows this may disrupt both the Telecom and pay-TV operator markets.

More OTT competition

Netflix has been the leading OTT business in the U.S. and now internationally. It seems that Amazon is now offering a credible alternative. Both provide an international multi-device ecosystem with original content and fast growing subscriber base. Amazon's 'The man in the high castle' is proving a hit comparable to Netflix's 'Orange is the new black' or 'House of Cards'. HBO is also ramping up its international efforts supported by the immensely popular 'Game of Thrones,' still the most pirated TV show on Earth.

Increased dependency to film franchise

The continuing success of film franchises (e.g. James Bond and Star wars) mean they are key areas of growth studios, but even more so for cinemas. Terra-Firma owned European cinema chain Odeon-UCI's turnaround was helped by a strong film slate in 2015 allowing its owner to consider a disposal process.



Technology

The mobile phone market is due for a change of direction in 2016. A study by IDC in March 2016 highlighted the end of double digit growth for smartphone as the market matures. The transition will be fast as global smartphone sale growth will almost halve from 10.4 percent in 2015 to 5.7 percent in 2016. Quick to recognise this change, Apple launched a new mid-range device priced at ~60 percent of the price of their flagship model. The new model is also cheaper than the previous mid-range model, showing a clear willingness to maintain presence in the mid-market where Apple historically held a weaker position than Android competitors.

The ad-tech industry was very much in the spotlight due to increased interest in ad-blocking. Ad-blocking was made possible on iOS (Apple) mobile software in September 2015. As a result, the use of ad-blocking apps increased from 28 percent of mobile users in Q3 2015 to 38 percent in Q4 2015, prompting claim this was a major risk for advertising driven business. Despite these marked increases, leading online advertising businesses such as Alphabet (Google) and Criteo reported they had not been affected.

Yahoo!, another large online advertising company, was at the centre of attention in Q1 2016. The business launched successful new products (mobile, video, native advertising, social) but faces challenges in its advertising/search business, while its share in Alibaba and Yahoo! Japan are said to be extremely valuable. Several large private equity firms (KKR, TPG) and corporates (Verizon, Microsoft, and Time) are said to be interested in the spin-off of some Yahoo! businesses.

Sports and sports technology still proved a fast growth sub-sector last quarter. Formula 1 revenues have increased 5-times in the past 15 years and it is now rumoured that CVC, its owner, will put its 35 percent share up for sale. Because of the growth in sports, the sale of Italy-based deltatre in Q1 2016 attracted interest from major players including Silver Lake owned WME-IMG, Providence owned Chime communications, EQT owned Sportsradar and WPP owned Bruin sports.

A&M VIEW

New growth opportunities

Smartphone growth is now more likely to come from emerging markets buying mid-range models, rather than high-end phones. This is likely to encourage a more diverse range of devices to cover multiple needs, as well as a more segmented approach to markets. While Android and Samsung are already well positioned, Apple will want its share too. The experience of cheaper Android tablets denting iPad sales (-20 percent in 2015 vs. 2014) was significant and Apple will no doubt actively protect their phone business.

Ad-tech is the new fin-tech

The proliferation of ad blocking devices and the dependencies on online and mobile advertising revenues by large tech player (e.g. Facebook, Google, and Criteo) mean that ad-tech is likely to remain very active with fast growth and M&A opportunities. Another ad-tech opportunity is programmatic TV advertising (targeted advertising based on actual TV viewing habits) underpinned by big data tools and techniques. It represented a $2 billion opportunity for tech businesses in 2016 and is forecast to grow to $6 billion in 2020.

M&A as growth strategy

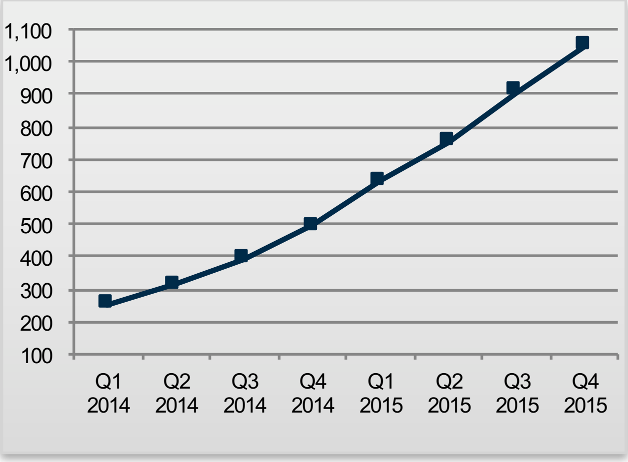
In several technology sub-sectors (e.g. software), the ‘buy vs. make’ decision is very often ‘buy’ in order to gain access to innovation and new products fast. This was illustrated by the recent Rovi talks to acquire innovative Tivo as Tivo has great user experience products and innovative search and recommendations software. Similarly several large tech businesses expressed interest in acquiring sport tech specialist deltatre to access their technology and industry contacts, especially in football and broadcast.

In the current TMT environment, many companies need the support of experienced professionals who can work alongside management to deliver solutions to complex problems.

Founded in 1983, Alvarez & Marsal is known for its distinctive restructuring heritage, hands-on approach and relentless focus on execution and results. A&M works with clients across the TMT investment life-cycle in the following ways:

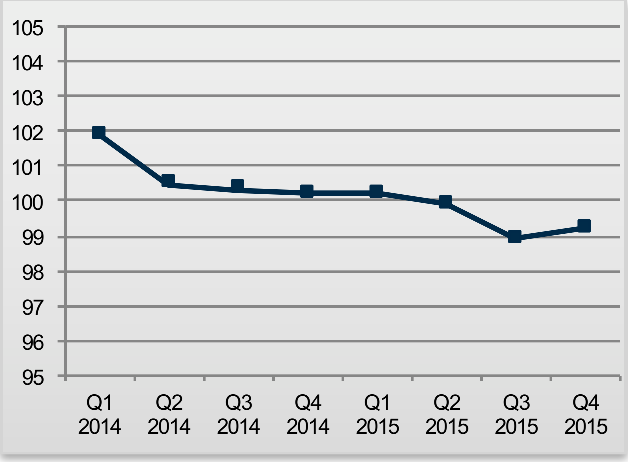
- Assisting companies pursue acquisitions, mergers or divestitures with financial and operational due diligence, valuation, tax structuring and acquisition/carve-out integration planning and execution.
- Working with management to grow revenue, optimise cost and CapEx, analyse asset performance and portfolio prioritisation, identify divestiture opportunities, and improve the company's planning and financial control processes and systems.
- Supporting management, legal and financial advisors of distressed companies to stabilise operations and cash flow, thereby extending their 'liquidity runway.'
- Providing interim management positions as appropriate.
- Providing expert advice such as on economic, accounting and forensic technology issues in relation to regulatory investigations and disputes.

4G/LTE Subscribers – Global (Million Units, Q1 2014–Q4 2015)



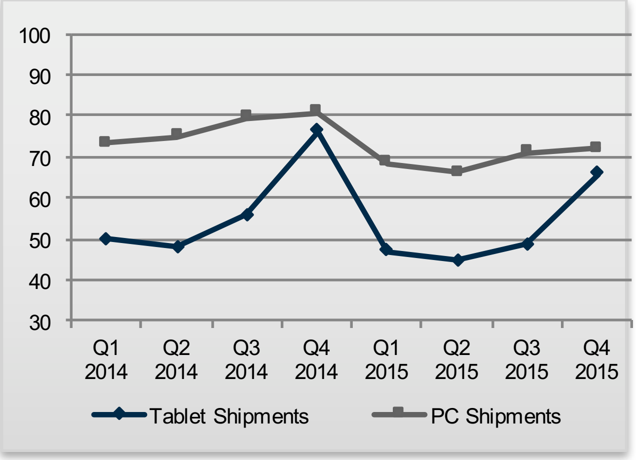
Source: Ovum

Pay TV Subscribers – US (Million Units, Q1 2014–Q4 2015)



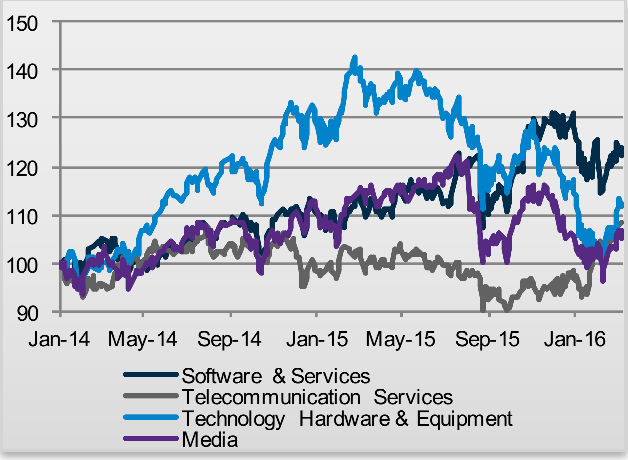
Source: Leichtman Research Group

Tablets & PC Shipments – Global (Million Units, Q1 2014–Q4 2015)



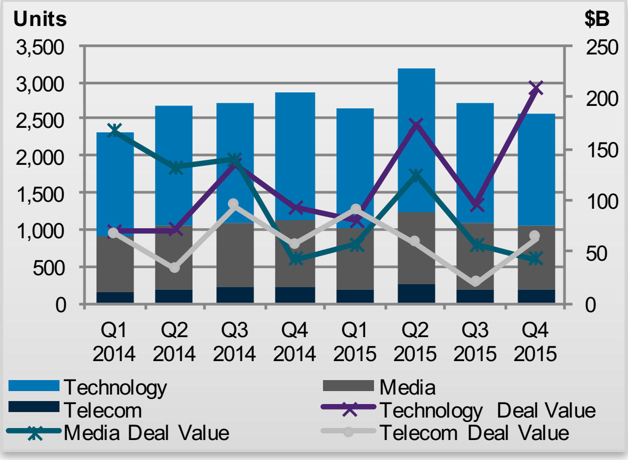
Source: IDC

TMT Stock Price Performance – S&P 500 ($, January 2014–March 2016 YTD)



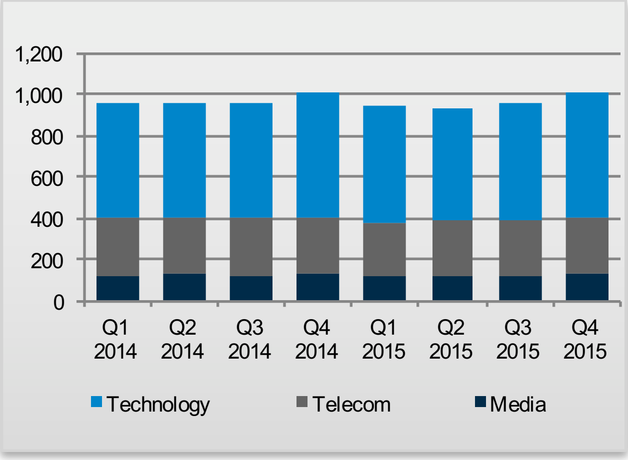
Source: CapitalIQ

TMT Deals and Value – Global (Units, $ Billion, Q1 2014–Q4 2015)



Source: Thomson One

Public TMT Companies Revenues ($ Billion, Q1 2014–Q4 2015)



Source: CapitalIQ

A&M in conjunction with Henley Business School have launched a detailed research study entitled '[Boards in Challenging Times: Extraordinary Disruptions](#).' Providing guidance on how Boards should address unique, extraordinary disruptions, the report analyses the real-life experiences of more than 70 seasoned U.K. Executive and Non-Executive Board Directors, and includes 4 detailed case studies, one of which looks at the transformation of [Skype Technologies](#) under Silver Lake ownership.

Below is a summary of the Skype Technologies case study:

Context:
- Private equity firm Silver Lake led a coalition of investors (eBay, Adreseen Horowitz and other) to purchase Skype in September 2009. However, the business needed attention: the founders had left, some IP was at risk, the strategic direction was unclear and the business had lost its focus on growth and products.
- The consortium purchased 65 percent of Skype for $1.9 billion.

Approach:
- Silver Lake and the investors' consortium led a transformation of the business to help it re-invent itself. They set up a new Board and hired a new Chairman to drive consensus between the very diverse shareholders. The new Board were able to:
  - Solve the IP issue in the first month and reengage the founders
  - Change and reinforce the leadership team to increase its transformation skills and industry insight. A new CEO was recruited with experience at Cisco, YouTube. He was supported by a Chief Development and Operations Officer from Silver Lake and a new CFO with Cisco and McAfee experience
  - Clarify the key strategic issue as to whether the business was a Telecom or a Technology business
  - Give a clear direction and sense of priorities
  - Empower the management to transform the approach to products with smaller teams employing an agile methodology

Outcome:
- Successful transformation during the course of 2010 together with a Carve-out from previous owner eBay.
- Skype was sold to Microsoft for $8.5 billion in May 2011.

Read the full case study [here](#).

Q&A with new-joiner David Evans

David, you started as co-head of A&M European Transaction Advisory Group (TAG) in January 2016. What drove your decision to join A&M?

I wanted to join a firm with the ability to deliver integrated transaction and operational support to both Private Equity Houses and Corporate clients on a pan European basis, and which had a strong and established presence in the U.S., given the trend for U.S. cross border investments in the European TMT sector. Since joining the firm, I have been impressed with the depth of hands-on expertise we have working across the TMT sector, both in Europe and Globally.

What is your background in the TMT sector?

I have been involved in buy side and sell side transactions in the TMT sector for the majority of my 20+ years in professional services, working with multinational corporates including Discovery, eOne, Liberty Global, ProSiebenSat.1, Sky and WPP and private equity houses including KKR, Advent, Francisco Partners and Vista.

What is your current perspective on the market?

The TMT sector has experienced a great deal of activity over the past 24 months and we continue to see a strong pipeline of assets coming to the market over the next six months. However, I do think we have hit that point in the cycle where there is a growing divergence on valuation multiples between buyers and sellers – with most of my private equity clients being more focused on exits rather than new investments in the short term.

What do you see as the growth opportunities in the TMT sector?

I think there will be more opportunities driven by the speed of development in 'Machine to Machine' or the 'Internet Of Things'. As new eco-systems emerge, they will present attractive opportunities for both telecom operators looking to differentiate their offer and private equity houses looking to fund the roll-out of consumer and business-to-business applications emerging in an increasingly connected, smart phone enabled world.

Also, I think that businesses in the sector that have successfully begun the migration from traditional license models to a subscription revenue models or traditional subscription businesses with strong content that have a clear strategy to take advantage of a digital world will continue to attract strong interest from private equity buyers.

CONTACT US

To discuss how A&M might provide assistance with Transaction Services, Operational Performance Improvement, Restructuring or Interim Management please contact any of the following:

European Key Contacts

Adam Bradley
Managing Director
+44 790 437 2660
abradley@alvarezandmarsal.com

David Evans
Managing Director
+44 207 663 0577
david.evans@alvarezandmarsal.com

Amit Laud
Managing Director
+44 790 824 7096
alaud@alvarezandmarsal.com

Martin McKay
Managing Director
+44 776 522 1489
mmckay@alvarezandmarsal.com

Renaud Fuchs
Director
+44 789 613 2614
rfuchs@alvarezandmarsal.com

North America Key Contacts

Byron Smyl
Managing Director
+1 305 798 0648
bsmyl@alvarezandmarsal.com

Tom Hill
Managing Director
+1 312 601 4226
thill@alvarezandmarsal.com

Middle East Key Contact

David Tusa
Managing Director
+971508133061
dtusa@alvarezandmarsal.com

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