

# OVUM COMMENT

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## Deutsche Telekom profit warning – no need to panic

### **The recession brings its problems**

It is no surprise that the global economic downturn will have an impact on mobile operators and the wider telecoms industry. In our forthcoming report, *Mobile operators in a recession*: regional analysis, lessons and coping strategies, we analyze the different recessionary forces that are affecting mobile operators and what actions they are taking to mitigate the effect.

Yesterday's profit warning from Deutsche Telekom has laid the blame for the anticipated underperformance in Q1 2009 on the group's mobile operations in Poland, the UK and the US. In Poland, revenues from PTC are expected to take hit following a 26% decline in the value of the Polish zloty to the euro. Lower roaming revenues plus the fact that the pound is down 21% to the euro is having an impact in the UK. In the US, Deutsche Telekom is blaming a multitude of recessionary factors.

Admittedly, currency risk is a big concern. For those operators that have to generate revenue in local currency but then have to either buy network equipment or service loans denominated in euros or dollars, currency risks present a major headache. However, while this is of particular interest to shareholders and financial analysts, it is not a true reflection of the operational performance of mobile operators.

### **Competition rather than the recession remains the major problem**

Generally, the market dynamics have not changed much and competition remains fierce. In fact, we have yet to see any disastrous performance from a mobile operator that can be blamed solely on the economic crisis. Indeed, for each of the recessionary factors cited by Deutsche Telekom for its profit warning (apart from currency risk), it is possible to show a corresponding non-recessionary force at play.

For example, worries about the decline in business travel and its impact on roaming revenues understates the bigger impact from the EU mandated cuts in mobile roaming. In the UK, T-Mobile's surge in subscriber acquisition costs is to overcome a not-so-good performance throughout 2008. Of the four main mobile operators in the market, T-Mobile's organic revenue growth for each of the four quarters of 2008 was the lowest.

Likewise in the US, intense competition and the increased push for unlimited bundles is having a major impact on T-Mobile USA. Ovum's forthcoming report US prepaid mobile grows in strategic importance shows a growing prepaid segment in the US mobile market.

### **There is another side to the currency issue**

While shareholders in Deutsche Telekom may be worried about the impact of currency fluctuations on their expected dividend, there are three issues that should calm industry investors down. Firstly, currency fluctuations tend to even out. Whereas T-Mobile has highlighted the impact on the UK and Poland, its revenues in the US were significantly boosted by the strength of the US dollar against the euro.

Secondly, the same currency dynamics from T-Mobile UK that have hurt Deutsche Telekom will correspondingly have a positive effect on Vodafone from its operations in Germany, Italy and Spain. So in effect, any shareholder with a stake in both companies is hardly worse off.

Thirdly, and more generally, currency fluctuations can go up and down. Companies periodically enjoy a boom when the fluctuation favours them and should equally endure the pain when it hurts them. And in the wider economy, currency fluctuation has its positives and could present any disappointed shareholder with new opportunities, such as for tourism in suddenly low-cost foreign markets.

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