

Europe's telecom sector has resilient ring

Acyclical performance, robust credit outlook matched by matured growth prospects



Europe's telecommunications sector has proved shock-resistant during the Covid-19 crisis with resilient revenues, but growth remains elusive despite surging data usage, according to latest figures from the region's regulators.

Telecom services revenues shrank by only 2% across Europe's biggest economies in 2020 compared with a near 8% decline in gross domestic product. Such resilience underpins our 'A' industry rating - a component in our assessment of business risk - for European telecom operators' credit outlook. However, we expect revenue growth to continue to undershoot long-run GDP growth as economies recover from the pandemic.

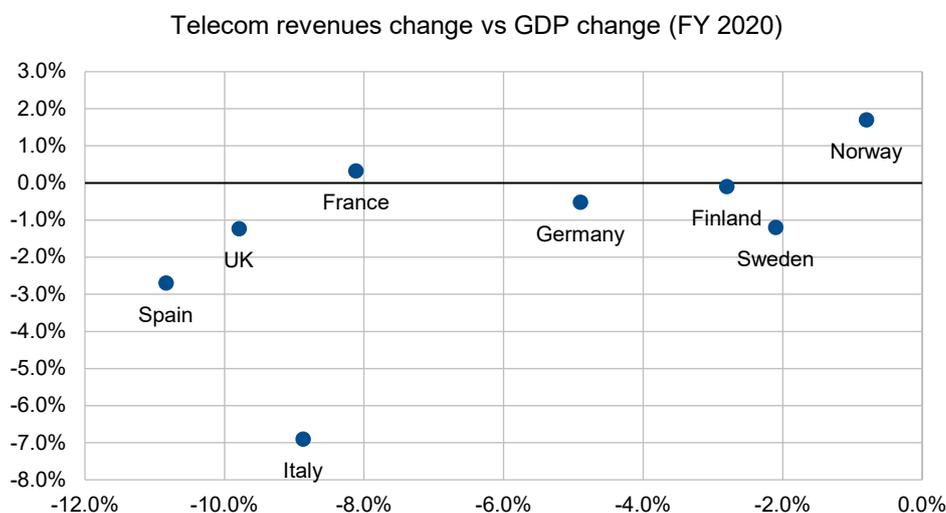
Latest data from Europe's telecom regulators show how resilient telecom services revenues were last year despite the deep recession in Europe. Most of European telecom regulators have now published their annual reports for 2020. The industry figures also support our view that exponential growth in data usage isn't translating into extra income for operators, even in the case of the mobile segment as 5G networks expand.

European economic growth has recovered swiftly this year, so it is worth remembering how deep the recession was in 2020. Output in the EU and UK contracted by 6.2% compared with 1.6% GDP growth in 2019 and the 2.2% five-year average growth rate.

We have focused on regulatory data from the four biggest EU economies - Germany, France, Italy, Spain - and the UK which together represent 63% of the broader region's population. In these five countries, the coronavirus-linked economic contraction last year was an even more severe 8.2% on average compared with 1.1% growth in 2019. Spain's economy was worst affected, contracting by 10.8%, whereas the recession was relatively modest in Germany, where output declined 4.9%.

In contrast, the decline in telecom services revenues was much more modest, though revenue growth before the crisis was running well below the expansion of the broader economy (see **Figure 1**). Telecom services revenues, on average, declined by 2.0% last year, ranging from a decline of 6.9% in Italy to 0.3% growth in France. Revenues fell 1.3% on average in 2019 and were down by average of 0.7% on a five-year basis.

Figure 1: Growth in telecom services revenues and GDP compared in 8 European markets: Finland, France, Germany, Italy, Norway, Spain, Sweden and UK



Sources: BNetzA, ARCEP, OFCOM, AGCOM, CNMC, PTS, NCom, Traficom, World Bank

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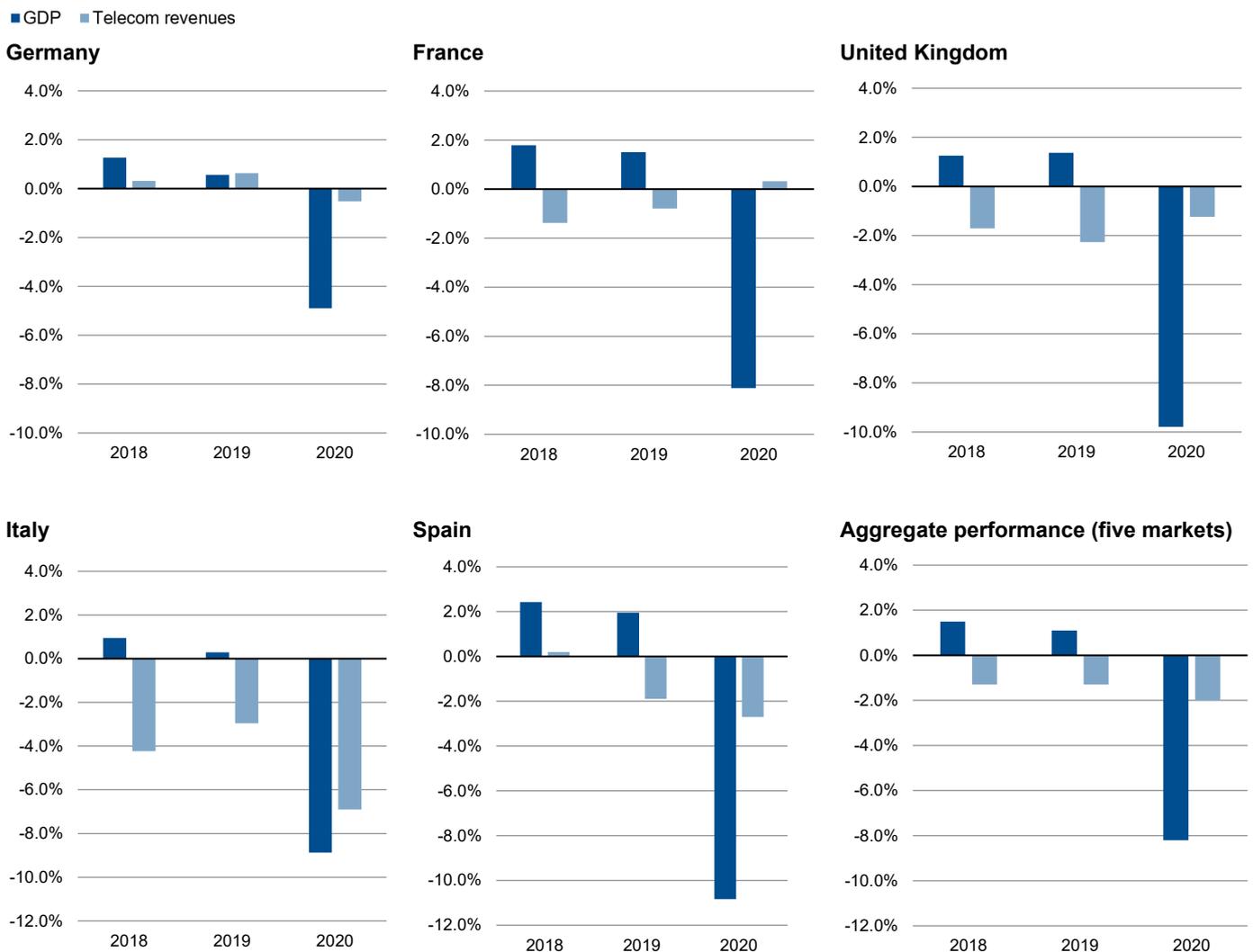
Telecom revenues held up relatively well during pandemic

Europe's leading markets typify sector's maturity

What is striking is that more than 9-percentage-point adverse shift in economic output between 2019 and 2020 coincided with a just a 0.7 percentage-point change in telecom services revenues in Europe's biggest economies, illustrating how non-cyclical today's industry is. In each of the five largest European countries, there was a small decline in telecom revenues growth (with the exception of France), but no material changes in the rhythm of growth compared with previous years, despite the disruption of economic activity from Covid-19 (see **Figure 2**).

We note that, excluding Italy where the market was unusually competitive with the recent entry of a new mobile operator, the average change in revenues in the other telecom markets was essentially zero, varying from +0.3% to -2.7%. The French market even recorded a slight 0.3% increase in telecom revenues despite the 8% decline in GDP. For example, French operator **Orange SA** recorded a 2% increase in service revenues - retail up 0.4%, wholesale up 6.7% - in France in 2020. In fact, in two out of the five countries, telecom revenue growth in 2020 was better than that recorded in 2019.

Figure 2: Growth in telecom services revenues and GDP in the five largest European countries



Sources: BNetzA, ARCEP, OFCOM, AGCOM, CNMC, World Bank, Scope estimates. Average sample is weighted by country population.

Fixed & broadband do better than mobile

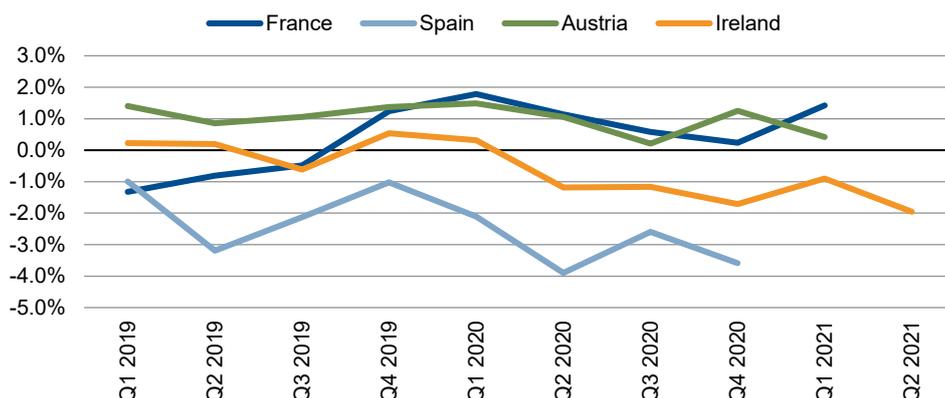
Looking at revenue trends within the telecom sector, the mobile segment contracted while fixed (fixed telephony + broadband) typically remained stable or displayed a slight increase, according to the most reliable, available regulators' data.

The difference partly reflects the relative ease with which mobile customers can switch providers, resulting in a higher churn rate than in fixed. **Deutsche Telekom AG** recorded an increase of 0.7% in telecom service revenues in Germany in 2020, with a 0.5% decline in mobile services revenue and a 1.2% increase in fixed. We also note that there was no significant uplift in corporate services revenues in line with the pandemic-related increase in remote working, as illustrated by the 2.6% in corporate connectivity revenues in France in 2020. In Sweden, the regulator reported a 6.5% decline in internet protocol virtual private network revenues in 2020.

Little change in revenue trends before, after pandemic shock

Looking at some national figures for telecom revenue growth during 2020 on a quarterly basis where they are available (France, Ireland, Austria, Spain; **Figure 3**), we can see that has been no significant change in national trends in each of these markets before and during Covid-19 crisis.

Figure 3: Quarterly growth in telecom service revenues in four European markets, Q1 2019 to Q2 2021 (%)



Sources: ARCEP, ComReg, RTR, CNMC, Scope estimates. Spain's CNMC has not published quarterly statistics since Q4 2020.

Finland, Norway, Sweden tend to be telecom trend setters

Advanced Nordic markets: maturity on display during pandemic

Another good barometer of the Europe's telecoms market is the Nordic region considering that the countries tend to be industry trend setters. Regulators' data for three of the countries – Finland, Norway and Sweden – show little change in telecom revenues in 2020, confirming that the mature European telecom market is characterised by low cyclicity.

Looking at individual Nordic markets (see **Figure 4** for Sweden), growth in telecom services revenues is running below GDP growth, typically by about 2 percentage points, as in 2019 (GDP: +1.4%, Telecom revenues: -0.5%), with the exception of two years of crisis where GDP declined significantly: 2009 and 2020. However, in 2020, when GDP declined by 2.8%, telecom revenues dropped only slightly by 1.2%, while back in 2009, where GDP declined by 4.3%, telecom revenues recorded a slight increase (+1.4%).

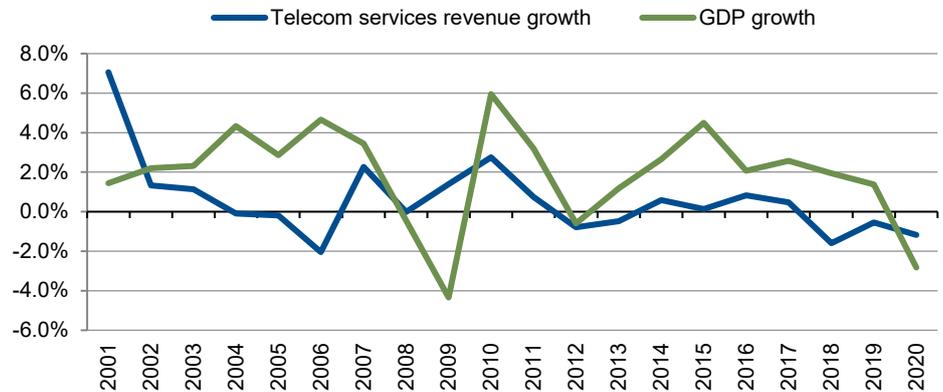
In Finland, the situation was similar, with telecom revenues declining by 1.2% in 2019 when GDP grew by 1.3%. The next year, telecom revenues were essentially flat (-0.1%) while GDP declined by 2.8%.

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Norway recorded telecom revenues growth of 1.4% in 2019 when GDP increased by 0.9%, while in 2020, telecom revenues increased by 1.7% as GDP declined by 0.8%.

Figure 4: Telecom service revenues growth and GDP growth in Sweden, 2000-2020 (%)



Sources: PTS, World Bank, Scope estimates.

Finland leads world in mobile data consumption

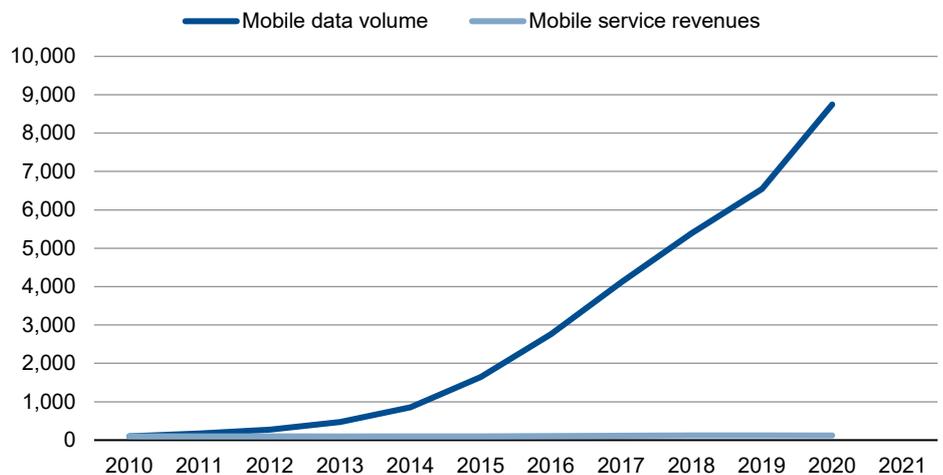
Mobile data conundrum: rise in usage disconnects from revenue growth

Finland is the world's most advanced market in terms of mobile data consumption, running at 29 gigabytes a month per subscriber in 2020, up 34% from the previous year, and well ahead of 8 GB/month in France, and 9 GB/month in the US - levels equivalent to Finland's usage way back in H1 2016.

Exponential growth in mobile data usage in Finland (**Figure 5**) has proved a poor catalyst for increasing mobile revenues at the country's telecom operators. Mobile data consumption grew 56% a year between 2010 and 2020, but mobile revenues grew just below 2% a year, with the number of mobile subscribers growing just 1% a year.

Finland's experience is telling for the rest of Europe, explaining why we believe that the introduction of 5G will have negligible impact on mobile revenues as indeed was the case for 3G and 4G. Finland, the first European country to introduce commercially 5G services in June 2018, has recorded no material change in mobile revenue trends since.

Figure 5: Monthly mobile data use per subscriber in Finland and mobile service revenues in Finland (2010=base 100)



Sources: Traficom, Scope estimates.



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