Analysis

TELECOMS INSIGHT THAT MATTERS

GERMAN BROADBAND

The return of king Congster

T-Online has launched a no-frills broadband offer to fight against increasing competition in its home market

DEUTSCHE Telekom used to be the broadband steamroller of Europe, driving millions of standard DSL connections on top of its standardised network. Now it looks more like a scalpel-wielding surgeon, carefully selecting those customers needing most attention, and fashioning new product for them.

But analysts think there could be a price to pay.

Last year, T-Online, Deutsche Telekom's ISP division, was seeing high-end broadband customers migrating to lower-priced competitors in its home market. Deutsche Telekom took the plunge and announced its own low-cost broadband provider for 2005. At a time when the German incumbent is foisting its "T" branding on its overseas subsidiaries, it has for the first time launched a no-frills service called Congster, alongside the T-Online brand in Germany.

'Broadband is moving towards the mass market and different segments have to be served individually'

Germany has fallen behind many of its neighbours in terms of broadband penetration, which stood at 9.12% as of March 2005, according to Point Topic. But T-Online's senior management says that the market is mature enough to respond to segmentation.

"Broadband is moving towards the mass market," says Ranier Beaujean, CEO of T-Online International. "This fact implies that different customer segments have to be served individually."

Analysts say despite market domination, T-Online risked losing high ARPU customers to competitors. While Deutsche Telekom was able to hold its German DSL market share of 48% in 2004, it lost 1% market share during Q1 2005, according to German telecoms consultancy WIK.

"The floor was dropping out," says Dan Bieler, research director at Ovum. "Deutsche Telekom was once again late in reacting," he adds, but "it has now done what it had to do."

"They think the T-Online brand has a certain quality appeal," says BMP consultant Stephan Jay, adding that the no-frills service required a different image.

Congster, aimed at cost-conscious tech-savvy individuals, is a stripped-down broadband Internet access offer, without hardware subsidies or extras such as email addresses, free customer support or anti-virus software. The service came quietly to market at the turn of the year and, following a viral marketing campaign, is believed to be seeing some success.

"They're very cagey about [progress]," says Bieler, "but reading between the lines Congster is doing quite well."

According to Credit Suisse First Boston, although T-Online claims that less than half of Congster subscribers signing up in Q1 migrated from the full T-Online service, that is "still enough to be significant."

Consequently, Bieler thinks T-Online faces a Catch-22 with Congster: if it pushes the low-cost brand it loses margins; if not, it loses those customers altogether.

T-Online downplays the significance of customer migration. "Congster attracts most of its customers from our competitors, as well as new customers (non-churners) from the market," says a spokesperson for T-Online.

However, BMP's Stephan Jay believes T-Online is more concerned with keeping subscribers that would have considered churning than poaching customers from rivals. "Purely price-sensitive customers would have selected another provider," he says. While Congster is cheaper than T-Online, having launched with a €10 per month flat-rate service and low-priced volume-based tariffs, he says "it's not the price-breaking brand."

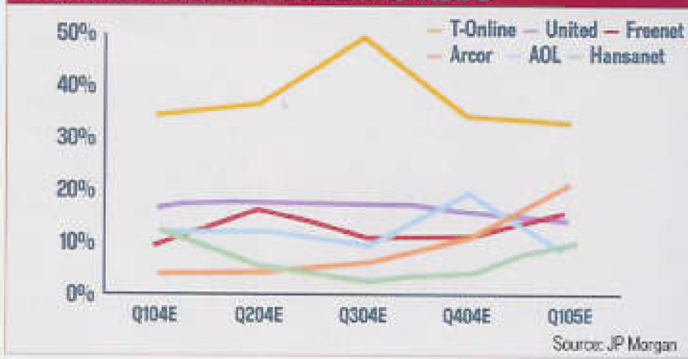
Peter Stamm, senior economist at WIK, notes that Germany's second largest broadband provider, United Internet, introduced a €6.99 flat-rate tariff in March this year, an offer that was matched by Congster in May. Arcor upped the stakes in July by halving its flat-rate tariff to €4.95. United Internet's GMX brand currently offers flat rates between €4.99 and €9.99, while Strato also has a €4.99 offer, says Stamm. In addition to GMX, United Internet offers higher-end consumer broadband services via its 1+1 brand. "Our activities were surely the reason for T-Online launching Congster," says a spokesperson at United Internet. He says that T-Online got the idea to do something below their existing price segment.

T-Online is also prepared to tough it out when it comes to pricing. In July 2005 the ISP slashed its retail flat-rate DSL prices from €29.95 to €14.95, a move it claims will shave €400 million off its 2005 sales, reducing its forecast to around €2.1 billion.

Ovum's Bieler says Deutsche Telekom's domestic mobile arm would do well to follow in the footsteps of T-Online by tailoring services to specific market segments. "T-Mobile is where T-Online was a year and a half ago," he says.

T-Mobile is suffering from a declining share of net additions in Germany, to the extent that its market-leader position is under threat from Vodafone. CSFB says that between Q4 2004 and Q1 2005, Deutsche Telecom has made a concerted effort to take a more consistent approach to its growth strategy in

GERMAN RETAIL BROADBAND ADDS



German mobile, cutting back prepaid SACs. This has affected T-Mobile's share of net adds over the last six months, falling from 20%-30% in the previous year to 5%-8%, and contributed to its service revenue growth slowing to around 1.5% in Q1 2005, say the analysts.

"[T-Mobile] pulled the brake too early," says Bieler. He concedes that the move may still boost T-Mobile's margins, but notes that it still lost out on "a few hundred thousand" late adopter subscribers that signed with Vodafone, O2 and E-Plus.

"Similar segmentation to Congster can be seen in the mobile market with E-Plus' no-frills brand simyo," says WIK's Stamm. Third-placed E-Plus says there are more sector-specific offers to come (*TTM*, 1 July 2005, p.16). "T-Mobile sooner or later will be forced to adopt a similar strategy," says Bieler. ■

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BROADBAND BUNDLES

In tune with the times

KPN is trying to capitalise on the popularity of VoIP by launching a naked DSL-based IP telephony bundle

IF YOU want to defeat your enemy, sing his song. This in effect was the concept behind KPN's recent groundbreaking voice service launch. Faced with declining voice revenues and VoIP based competition, KPN has retaliated with a naked DSL-based service and its very own consumer IP telephony bundle.

In the Netherlands, KPN is battling four other DSL networks, strong cable penetration, and renewed interest in consumer FTTH initiatives. In addition, wholesale line rental should be introduced by the end of this year, which will threaten voice revenues further. Cableco UPC has said it is adding 5,000 new VoIP customers every week.

KPN's service, called InternetPlusBellen, gives consumers broadband DSL and unlimited fixed line VoIP calls throughout the Netherlands. More importantly, the service is a naked DSL offering, as PSTN line rental is not obligatory.

Packages range from €34.95 for Go, which includes 800 kbps DSL and unlimited weekend calls to fixed lines, to €89.95, depending on usage and for higher speeds up to 8Mbps. For €2.50 per month more, users get unlimited evening calls or for €10 per month more, they get unlimited domestic fixed calls. There are varying call set-up tariffs ranging from 5-10 cents (see table, p.10).

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Users receive a free Experia integrated access device. KPN believes the array of value adds like WiFi, caller ID, messaging and conferencing and video calls will attract customers.

According to Morgan Stanley the overall price for the InternetPlusBellen bundle is between 7%-20% cheaper than if broadband and voice were subscribed to separately.

Ovum suggests the VoIP service to be relatively expensive, meaning KPN must beware of the impact cheaper alternatives may have on uptake. "Skype's international calls cost about half of KPN's," says Ovum's research director Dan Bieler. KPN's international calls start at 4 cents a minute. But he adds that it is difficult to compare directly as users typically still pay line rental fees when using Skype-like services.

Luis Prota, equity analyst at Morgan Stanley, believes the discount against current KPN tariffs makes sense as an initial pricing strategy, because high competition makes the Netherlands less profitable than other European countries. "We think it is better to retain the customer with an attractive offer rather than losing their whole revenue," he says.