

# Analysis of celcom axiata investment in tune talk marketing essay



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Celcom Axiata is a member of Axiata Group is facing tough competition against the other major telecommunication rivals. Having coined as “ malay telco provider” that is, Celcom Axiata has weak penetration into some major markets and the strategy to overcome this is by appointing the Mobile Virtual Network Operators (MVNO) to penetrate into the identified markets using their own brand, look and feel.

Celcom Axiata business model for Tune Talk MVNO is by having 35% stakes in the company. After over 11 months in operation, Celcom Axiata is reviewing its position in this company whether to remain its stake, increase its shareholding or pullout.

Prior to making any decision with its investment, Celcom Axiata needs to evaluate the existing Tune Talk financial standing and its capability to provide the required return on investment as well as its ability to handle the issues at hands especially those concerning the cash flows.

## **Introduction**

Celcom Axiata is one of the 4 major mobile telecommunication companies in Malaysia. As at 31st March 2010, Celcom Axiata was ranked as second largest mobile telecommunication company behind Maxis, and ahead of Digi and U Mobile respectively. Celcom Axiata is a member of Axiata Group of companies who manage a group of Mobile Telecommunications in the Asia region. Axiata Group was previously known as TM International and part of TM (Telekom Malaysia) Group. The process of de-merger within TM Group saw the birth of Axiata Group, meant to focus on mobile telecommunications

arm of the corporation within the region whilst TM continue to maintain its fixed lines business as well as broadband provider.

According to the first quarter financial report, Celcom Axiata continue to show double digit growth on a YoY basis in all key indicators. Revenue was up 15% whilst Earning Before Interest Tax Depreciation and Amortization (EBITDA) increased by 16%. In tandem, Profit After Tax (PAT) was up 24% in the same period.

On a QoQ basis, Celcom continued to show positive performance. Despite coming off an

exceptional 4Q09, which recorded the highest ever quarterly growth, revenue growth was

marginal, but still up by 0.2%. Continued focus on costs saw EBITDA up by 2% with margins improving by 0.7 percentage points QoQ to 45.4%. PAT showed a robust increase of 7% to RM441 million (Celcom Axiata media release, 27th May 2010).

Celcom Axiata has been aggressively expanding its network and coverage to cater for the increasing demand by the customers. Despite its continuous efforts to penetrate into the various segments in this country, Celcom Axiata still lagging in some of key markets such as the Chinese market segment, immigrant market segment and student market or low income earners segment. These markets are predominantly controlled by Maxis and Digi and will be the key success factor for Celcom Axiata to capture in order to become the number one mobile telecommunication provider in this country.

One of the strategy to penetrate into these segments as single out by Celcom Axiata is by way of having a Mobile Virtual Network Operator (MVNO) approach. MVNO means Celcom Axiata will appoint a third party to run the mobile business using their own brand, leveraging on their own strength such as networking, channel of distribution, marketing and customer service. By doing this, Celcom Axiata can reduce its financial burden on the “ go-to-market” cost which in turn will be born by the MVNO partners themselves.

To date there are four MVNOs appointed and launched by Celcom whereby each of them is given different market segment to penetrate and capture. Each MVNO is treated as separate entity from Celcom Axiata where the respective MVNOs have full control over their own operations and management of the companies except for Tune Talk Sdn Bhd where Celcom Axiata has 35% share of the company.

Being different business model from other MVNOs, Tune Talk Sdn Bhd is seen as another Celcom Axiata joint venture company. Tune Talk is owned by the following shareholders as shown in figure 1 below :

Tune Ventures (owned by Datuk Seri Tony Fernandes and Datuk Kamarudin Meranun)

Individuals shareholders are Datuk Seri Kalimullah Masheerul Hassan, Lim Kian Onn, Jason Lo (the CEO of Tune Talk), Gurtaj Singh (the COO of Tune Talk) and Mark Lankaster (the CEO of Tune Hotels)

Celcom decision to have its stake in Tune Talk is to ensure it has some form of control as one the major shareholder. Although Tune Talk management

will have the control over the management of the company but the shareholders will have their voice heard during the monthly board exco meeting. Having represented by 2 permanent exco members from Celcom, it can ensure that Tune Talk business plan and strategies are in line with its goal to become one of the top mobile service provider in this country.

## **The Situation**

Tune Talk is approaching its first anniversary on the coming 19th August 2010. Celcom need to assess its investment and evaluate whether Tune Talk business is moving to the right direction and hence generate the desired dividends to shareholders.

In order to achieve the target, Celcom needs to keep track of Tune Talk management's way of running the business. The permanent exco members sitting in the boardroom must be able to drill down to the bottom line and analyze their way of spending their fund.

This is very important to Celcom as the major shareholder in Tune Talk so it can decide on the next course of actions such as to inject more fund into Tune Talk, or to remain its position without adding anymore cash or worst case decide to pull out from the pack.

Prior to such decision, Celcom needs to gather as much information as possible with regards to Tune Talk financial position, business directions, marketing strategies and other commercial matters which will be the key determination factors.

Based from the previous exco meeting it was learned that Tune Talk is facing difficulties to move forward with its business plans and marketing strategies due to shortage of cash flow. Tune Talk Chief Financial Officer (CFO) during his presentation to the board of directors highlighted the following scenarios :

### **a. Increase in Managed Services Costs**

Tune Talk adopted the managed services concept to deploy and maintain the Intelligent Network (IN) billing system, network related infrastructure namely Short Message Services Centre (SMSC), Home Location Register (HLR) and other Value Added Services (VAS).

Managed services concept is a new trend in telecommunication and information technology (IT) business whereby the customers or business operators do not buy outright the related systems but pay to the supplier or provider on usage based. This method saves the company from spending an upfront purchase of an asset, hence reduce the cash outflow. Managed services can help a particular company to avoid from having to allocate depreciation cost which may impact the company balance sheet.

In the case of Tune Talk the burden they are facing now is due to the increase in the amount to be spent on this managed services. The deal they are having right now is based on the number of subscribers using the system, the higher the number of subscribers the higher the managed services cost to be incurred. The amount will grow in tandem with the intake of new subscribers where the average cost per subscriber remain unchanged. Unlike buying own fixed asset, the average cost will tend to

reduce as the number of new subscribers grow until it reaches the economic of scales.

## **Increase in Channel and Distribution Cost**

In Malaysia, all the mobile operators are highly dependant to the normal traditional channel ie. mobilephone dealers to sell its SIM card and recharge vouchers.

Being too dependant to this type of distribution channel will increase the company's cost of sales whereby for every sales of SIM cards or recharge voucher the company needs to allocate some amount of percentage as an incentive for them to push its products over the competitors.

Traditionally, in mobile telecommunication business the channel of distribution consist of 3 layers :

distributors

master dealers

ordinary dealers

Normally only a handful of distributors are being appointed to distribute to the master dealers whom will then sell it through the ordinary dealers. Each of these channels will keep a small percentage as their incentive from the retail price.

Operators are normally stuck with this channel cost which they cannot run away with in order to push their products to the customers.

On average an operator will have to spend not less than 10% from its retail price being part of the channel cost.

## **Allocation for Marketing Cost**

As a new mobile operator in Malaysia competing against the other 4 major mobile telecommunications service providers Tune Talk is facing a tough time to introduce its brand to the market.

According to Nielsen Co Malaysia 2009 report (a research company), the telecommunication companies are among the highest contributor to the total advertising expenditure in Malaysia with Celcom leading the pack at RM 115. 8 million, followed by Telekom Malaysia at RM 94. 3 million, Maxis with RM 89. 7 million and Digi for RM 87. 1 million (see Figure 2 below). Newspaper and TV advertisement represent the top 2 categories for advertising followed by Radio, Magazine and Outdoor.

To date Tune Talk had already spent RM 2 million in their advertising cost through billboards, newspaper, TV and radio advertisements. This amount is rather very small compare to the amount spent by the big giants and it may not give the required exposure that Tune Talk expected to create its brand awareness to the market place.

Based from the report and dip stick survey conducted by Tune Talk marketing department their brand index is still very low and they would require more fund to be pumped in for this purpose.



## **Slow Moving of Customer Recharge Activities**

Tune Talk is only selling prepaid mobile and its main source of income is by selling the SIM card and recharge vouchers. As far as Tune Talk is concerned, the revenue generated from these sales is considered as their income (based on the generally Accepted Accounting Principle).

This is due to the fact the income will be reported when it is earned (Ross, Westerfield, Jaffe, Corporate Finance, 7th edition). The good thing about prepaid business is the transactions are in cash terms. This means Tune Talk will get to record the transaction into its book as and when the SIM cards or vouchers are sold to the distributors.

In accounting, the revenue from sales of SIM cards and recharge vouchers will only be realized upon usage and not upon sales. Nonetheless, as far as Tune Talk income is concerned, it has already acquired the money from the distributor and realized in its book as income as per GAAP.

As a rippling effect to lack of awareness of its brand in the market place, Tune Talk sales of SIM cards and recharge vouchers are moving rather at a very slow pace. Table 1 below is an example of the average sales and projected 1st year revenue from SIM cards and recharge vouchers :

Table 1

Items

Average Monthly Revenue

Projected 1st Year Revenue

SIM Cards

RM 500, 000

RM 6, 000, 000

Recharge Vouchers

RM 900, 000

RM 10, 800, 000

**Total**

**RM 1, 400, 000**

**RM 16, 800, 000**

This figure is far cry from the original budget that Tune Talk has to make which is RM 36. 0 million for its first year operation and increase to RM 50. 0 million and RM 72. 0 million in year 2 and 3 respectively.

### **High Customer Turnover or Attrition Rate**

It is common in the prepaid business industry that users tend to move or hop around from one operator to another operator to find for better offer and cheaper cost. Tune Talk is also affected by this game by the customers whereby the rate of customers churning out or leaving for another brand keep on increasing on month-on-month basis.

Malaysian prepaid business industry rate of customers staying in a particular operator (industry language is “ length of stay”) is in average of 6 months.

However in the case of Tune Talk its customers average length of stay is a mere 3 months which is about half of the industry average.

The impact of this short stay will cause a high acquisition cost to Tune Talk whereby its cash flow will be badly affected. In order to stay healthy, Tune Talk needs more than 3 months for each customer with average usage of RM 30 per month to recover its upfront acquisition cost such as the channel incentive, marketing cost and the other variable costs.

## **Shortage of Cash**

Tune Talk started off its business with RM 7.5 million worth of shares with 35% own by Celcom whilst the remainder are by several other individuals. After 11 months of operations, Tune Talk is now facing with the most critical moment in its business where their cash flow is deteriorating. Despite being a lean and mean in expenditure and had not spent any money on fixed asset, Tune Talk still face the cash flow difficulty.

An area that has badly affected Tune Talk cash flow is the channel incentive and the wholesale airtime rates that it has to pay back to Celcom. With intense competition Tune Talk needs to set its incentive on par or slightly better than the competition in order to get the channel attention and support.

On the other hand, the prepaid business market is competing on the call rates to be offered to the end users in order to beat the others. Since Tune Talk is buying its airtime from Celcom at fixed rate, the competition which had forced Tune Talk to also lower down its selling rate to the end users had cause Tune Talk margin to shrink and became smaller. The result is, the <https://assignbuster.com/analysis-of-celcom-axiata-investment-in-tune-talk-marketing-essay/>

income collected from the sales of SIM cards and recharge vouchers will have to be spent largely to incentive and wholesale airtime to Celcom, leaving only peanuts to Tune Talk to be used to re-generate its business. It is also better for Tune Talk to maintain a level of working capital that allows it to make it through those crunch times and continue to operate the business within tight budget (Cater McNamara, Authenticity Consulting LLC).

## **Action**

Celcom Axiata really need to review its investment in Tune Talk Sdn Bhd by looking at the present situation and its potential. It is a known fact that every new business need some times to be able to stabilize and start to show positive result out of its investment.

As far as telecommunication industry is concerned, a minimum of 3 years is required in order for a particular mobile operator to have a strong foothold and have substantial subscriber base to be relevant.

The question here is whether Tune Talk strategies are gearing towards the right direction which will guarantee to bear fruits at the end of 3 years? How much will investor need to pump in to ensure that Tune Talk can still survive until the 3rd year ?

It is imperative that Celcom Axiata representatives in the Tune Talk board of directors to insist Tune Talk management to review their existing business models which had obviously affected their cash flows. Serious attention must be given by Tune Talk management to revisit its dependency on the existing channel which will become its biggest threat in trying to minimize its cash out flows.

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Tune Talk management also needs to re-negotiate with its managed services provider to review the charges being imposed to Tune Talk for every new subscribers added into the system. The charges should be on decreasing trend as more customers being added.

Tune Talk may also want to consider finding new manage service provider should the negotiation come to a dead end. This is important in managing Tune Talk spending over the long run.

Prior to Celcom Axiata to make any decision with its investment, it needs to analyze Tune Talk financial condition. It is advisable for Celcom Axiata to scrutinize the Tune Talk financial management and ensure that all the monies are well spent and efficiently managed to protect its interest. Celcom Axiata finance manager needs to advice the Chief Financial Officer (CFO) of the real condition of Tune Talk by analyzing its financial statement cash flows.

Having spent for over RM 2. 6 million and holding 35% of Tune Talk shares, Celcom Axiata has the responsibility to report to its board of directors on the progress of its investment. The Celcom Axiata board of directors must be very interested to know whether the management of Celcom Axiata has made the right decision by investing in Tune Talk. One thing interesting in this business model ie MVNO is because the airtime being sold by Tune Talk (in this case the MVNO) is using Celcom network infrastructure. This means even though Tune Talk does not make huge profit and may not be able to provide the required rate of return in terms of dividends to the shareholders but as far as Celcom Axiata is concerned, it still make money from the

airtime sold. Thus, board of directors of Celcom Axiata may well be pleased by the increase in Celcom Axiata revenue alone rather than going down to the details of earning through the Tune Talk dividends.

Another area that needs special attention is to assess the existing Tune Talk management team style and business competencies. This industry is regarded as highly competitive and it takes excellent team to be able to compete with the big boys (as being referred to the seasoned mobile operators). Celcom Axiata representatives in the Tune Talk exco members must be able to provide information to the Celcom Axiata management whether there is an existence of conflict of interest in the Tune Talk management team. Although according to Vishny and Robert W, NBER Reporter, September 1989 said that the standard and ideally corporation allows management to have 5% of shares. This can be ascertained by judging into their way of running the business, their seriousness in fulfilling the required tasks as outlined in the business plans, their priorities in spending and handling the cash flows.

## **Conclusion**

It is probably premature for Celcom Axiata to make decision to pull out from this pack by merely basing on the first 11 or 12 months Tune Talk operation. However any decision to increase its capital in Tune Talk either by buying more shares or by pumping more money to support Tune Talk operations must be done with great detail analysis. It is not advisable for Celcom Axiata to simply inject more cash to Tune Talk without seeing any progress or improvement on some of the area of concern which have been highlighted in previous pages.

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The major issues that need to be really scrutinize by Celcom Axiata financial manager is on the cash flow management. The action items highlighted in previous pages suggested Tune Talk to improve the way it runs its business which will eventually give a positive impact to its cash flow.

It is said that high risk will normally generate high rate of return, but having said that, the save decision at the moment is for Celcom Axiata to remain its position without adding more cash but to continue to monitor Tune Talk progress and improvement. After all, Celcom Axiata is the one who makes more money from anyone else in the pack which is through the sales of wholesale airtime.

This investment although had not been able to generate dividends to Celcom Axiata but somehow has managed to complement the weak area that cannot be penetrated by Celcom Axiata using its own brand.