Last year saw a significant increase in the level of M&A activity in the TMT sector and expectations are high for a repeat in 2015. The advancements in technology and cheap finance are driving deal making, especially in the telecoms and technology space where convergence is leading to a plethora of new types of deals. At the same time, there is widespread interest in the role that regulation will play in these combinations.

**68%** of those asked believe that mobile Telco consolidation – with a move from four to three operators – will strongly feature in M&A activity in the TMT sector this year.

**60%** believe that US/European telcos will be leading TMT consolidation activities in 2015.

Regulatory scrutiny is listed as the **#1** barrier to doing more deals in TMT.

Global Telecom Media & Technology (TMT) M&A saw deals worth $296 billion in 2014. Among the three sub-sectors, Technology led the sector in both the volume and value of deals, recording 479 deals valued at $166 billion and contributing 56% of the total value of TMT M&A in 2014. In addition to a surge in Technology M&A, 2014 also witnessed a notable trend in the convergence of Technology, Telecoms and Media into media conglomerates.

Against this backdrop, FTI Consulting in conjunction with TMT Finance surveyed the senior executives and advisors working in the TMT sector in order to establish the key drivers of TMT M&A deals in the coming year.
Telco consolidation and the role of regulation
a key feature for TMT M&A activity in 2015

More than half of all respondents expect mobile telco consolidation to feature strongly in 2015. Following M&A activity in the UK with Hutchinson Whampoa’s proposed purchase of O2, Hugh Kelly, Managing Director, Economic and Financial Consulting, believes that regulators may accept a reduction in the number of mobile phone providers from four to three and perhaps even fewer in many countries. “We’ll see some mergers getting approval because competition authorities will recognise that there are efficiency benefits that come with them,” he says.

When assessing a merger, competition authorities are concerned with the impact on competition and the potential harm to consumers.

“Where mergers are approved there will be a focus on remedies to address any competition concerns such as spectrum divestments and support for mobile virtual network operators,” says Kelly. Those managing M&A in the TMT sector will need to consider the impact of potential remedies which the authorities may impose to secure merger approval. They’ll also have to anticipate future changes to the regulatory environment, for example as signposted in Ofcom’s recent announcement. The emergence of fewer but bigger players may lead to a shift in the regulators focus, for example towards ‘bundling’ of services and customer switching, points out Kelly.

“In many areas the regulators are taking a “wait and see” approach but this means that all those in the TMT sector should pay careful attention to the mood music coming from the European Commission and others”, he says.

James Melville-Ross, Senior Managing Director, Strategic Communications, says “It’s still too early to say how last year’s reshuffling at the European Commission will change things. We’ve had mergers in Austria, Germany and Ireland in the last Parliament. It remains to be seen how the new Commissioner will look at the next round of deals against the changing market.”

Deal Drivers in 2015
Which of the following do you think will be leading TMT consolidation activities in 2015? (Please select all that apply)

- US/European telcos: 60%
- Internet big 4: 48%
- Middle East/ African/ Asian telcos: 35%
- Billionaires: 33%
- Private equity: 29%
- Other telcos: 18%
- Content owners: 14%
- Sovereign Wealth funds: 10%
- Other: 4%
- None: 1%

What types of TMT M&A do you expect will feature strongly in 2015? (Please select all that apply)

- Mobile telco consolidation: 68%
- Fixed/mobile telco convergence: 55%
- Telco infrastructure JVs/spinoffs: 50%
- Content/distribution convergence: 32%
- Internet company consolidation: 31%
- Cross border: 26%
- Tax benefits: 7%
- Semi conductor consolidation: 7%
- Other: 1%
Quad play offerings to increase

Efforts by operators to provide a quad play offering (mobile, fixed telephony, internet and TV) will continue and may well increase. “This reduces costs because customers only need one bill,” says Hugh Kelly. “But, more importantly, it reduces customer ‘churn’ because the more services a customer is signed up to in a bundle, the more inconvenient it can be to switch to new providers. That’s important because the cost of acquiring new customers in this sector, with offers such as six months free internet, is very high. However, barriers to customer switching will inevitably attract the attention of the regulator as it has done in other sectors such as banks and utilities.”

Level playing field

European telcos have been lobbying hard for a ‘level playing field’ to address concern that ‘over the top’ (OTT) internet service providers unfairly benefit from a less onerous regulatory regime. “The European Commission has started to consider how OTT providers have impacted the traditional telco markets. Ultimately the review could lead to reduced regulation of some services such as voice and texting” says Hugh Kelly.

Consolidation to lead cross border M&A

“Major content convergence is unlikely,” says Charles Palmer, Senior Managing Director, Strategic Communications. He notes that only a third of the participants (32%) believe that this will feature strongly among M&A activity in 2015. “Not only would the regulator be concerned but, as we’ve seen, ‘walled gardens’ don’t work.” He believes that open auctions such as the one that saw BT and Sky bid around £5.14 billion more likely to be the norm from now on.

He also argues that in the future M&A will take on a more international perspective with cross border acquisitions, although relatively few and far between at the moment, becoming more common. He points to the decision by Deutsche Telekom to retain 12% share in BT and the positive reception from the markets of a possible deal between Telecom Italia and Orange.

“There could be more mega-mergers in Europe to form global firms to stand toe to toe with the international gorillas like AT&T and China Mobile,” says Melville-Ross. “If you look at the US, their two largest operators are bigger than the top five in Europe. Once we’ve seen the current phase of in-country consolidation, we may well see the mega-mergers coming through. How the European regulators view these deals will be interesting.”

Net Neutrality - An important issue?

Net Neutrality seems one area where the Europe is taking a less aggressive stance than the US Federal Communications Commission (FCC) which recently approved a plan to regulate broadband internet like a public utility, using legislation passed in 1934, notes Michael Knott, Senior Managing Director and leader of FTI Consulting’s TMT practice in London. Charles Palmer points to a feeling within the sector that properly maintained net neutrality will reduce the need for further regulation in this area.

Strategic activity leads as PE activity declines

The majority of respondents expect that trade buyers are likely to dominate the M&A landscape in the coming year. The top three categories in our survey are trade buyers – US/European telcos, Internet companies and operators from the emerging markets – whereas Private Equity comes fifth. This is consistent with Capital IQ figures which suggest PE represented 15% of TMT deal values in 2014, down from 17% in 2013.
“With acquisitions it’s interesting to note the increase in companies buying companies rather than private equity,” says Michael Knott. “There are likely two reasons for this; private equity is worried about the macro economy where they believe that the current recovery is unproven, and secondly there is a belief that prices are a bit ‘frothy’.”

Acquisitions of tech start-ups by the major players is a trend that will continue and even increase, believes Knott. “Investing in start ups is how large companies innovate. The big names such as Apple have strong balance sheets and substantial cash reserves. They’ve also seen President Obama’s plans to stop US corporations avoiding the payment of taxes on overseas profits. They’re now looking at companies that are tangential to the main activities for example Google in mapping or Apple in eyewear. Mobile technology is increasingly interesting. Artificial intelligence and predictivity are also growing areas of attention.”

Charles Palmer adds that many start up tech companies will often end up being bought by larger tech companies with a global platform because they’ll get a better valuation than they would with an IPO where financial buyers will value future cash flow and profits rather than the potential of the tech stack on their platform.

Social and mobile are major themes, he says. “It’s increasingly about attracting an audience, advertising to them and then providing seamless payment systems. This will be a big thing in 2015/16.”

Asia Pacific and Africa expected to provide most opportunities for TMT expansion.

Opportunities for TMT expansion

Respondents consider Asia Pacific and Africa as providing the main opportunities for TMT expansion.

“Africa is higher than I expected as an area with opportunities for expansion,” says Michael Knott. “There are certainly some assets and hardware such as tower sales. There’s less competition for assets so companies might be looking to get a bargain here. Another area might be FinTech - we’ve seen the deal between M-PESA and Safaricom recently.

“Africa is an interesting one,” agrees James Melville-Ross. “On paper it’s hard to ignore the fact that it looks ripe for investment - low penetration numbers and great growth prospects - but the reality of doing deals in Africa is not straightforward.”

“There are considerable risks involved in doing business in Africa too” says Michael Knott. “It might be the case that companies are saying that they would like to invest in Africa in an ideal world, in other words, if these risks didn’t exist.”

RESEARCH METHODOLOGY

In conjunction with TMT Finance, FTI Consulting conducted online research from 25th Feb to 4th Mar 2015 with n=143 respondents involved in the TMT sector. These respondents were broken down into the following categories: ‘Working in the TMT sector’ (n=60 respondents): Fixed Telco, Mobile Telco, Content Provider, Technology Provider / Vendor, Other Media Organisation; ‘Working with TMT’ (n=74 respondents): Consultants / Advisors, Bank, legal Firm, Private Capital & the remainder (n= 9 respondents): Regulator & Other. The research included 20 questions. Further details of the results and methodology can be obtained by emailing Dan.Healy@fticonsulting.com