Bottom Fishing in Latin America
Exploiting Sub-Prime Opportunities in Developing Markets
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In Latin America, a Cellular Need
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CARACAS, Venezuela, May 25 -- Communicating with the outside world has never been easy for residents of Nueva Tacagua, a remote neighborhood on the outskirts of Caracas dotted with crumbling government housing, rickety sheet metal shacks and pools of sewage. The area is an arduous ride from the city along an isolated road, and telephone wires have never made it this far into the hills.

Yolimar Zambrano, who runs a makeshift store in her concrete block home, says staying in touch with friends and relatives has been a lot easier in the last year -- thanks to her cellphone. But Ms. Zambrano, 30, admits that she and her husband spend as much on monthly cellular service as they do on two weeks of groceries.

''The signal doesn't even come in very well,'' she said, struggling to listen to voice messages, ''but it's the first time I've ever had a phone.''

Ms. Zambrano is part of an explosion in cellphone use in Latin America that has linked millions. Subscribers jumped from fewer than 40 million in 1999 to 118 million today, turning one in five Latin Americans into a cellphone user and making this a $20.4 billion market, according to Pyramid Research in Cambridge, Mass. Economic powerhouses like Mexico and Brazil have the biggest number of subscribers, but competition is fierce here in Venezuela, where cellphones are both a status symbol and a necessity.

Even after its economy contracted 8.9 percent in 2002 and 9.4 percent in 2003, Venezuela still has Latin America's second-highest rate of cellphone use, after Chile.

Driving the boom is an explosion in prepaid service that has made cellphones available to millions of low-income users, once excluded by monthly payments and credit checks. While in 1995 fewer than 2 percent of people in most Latin American countries had cellphones, the introduction of prepaid service has sent use skyrocketing, to 29 percent in Venezuela and 48 percent in Chile.

''Given Latin America's demographics, the cellular business couldn't take off until prepaid service made it possible'' for everyone, said Patrick Grenham, a telecommunications analyst with Citigroup Smith Barney in New York.

Although the cost of prepaid service can be 10 times that of traditional service, it attracts clients whose incomes are frequently too erratic to make a monthly payment.

Also driving cellular growth is a system that charges users only for outgoing calls, allowing them to receive unlimited calls free -- and thus keep their phone active even when the budget is tight.

With the right cost structures, providers can turn a profit within a year, even from users who make only a few calls. While Latin America's cellular providers once depended on upper-class users, revenues come increasingly from millions of low-income clients.

Fixed-line phones are found in close to 11 percent of Latin American households, according to figures from IDC, the research group. Many people simply do without fixed-line service to avoid large upfront payments, enormous delays and onerous monthly charges. To bring in users interested in having a home phone, providers in several countries now offer a home telephone that operates within a cellular network but at lower prepaid rates than mobiles.

The business of prepaid services has considerable drawbacks, like declining use during hard times and the constant cycle of users whose service is cut off because of inactivity. Providers still rely largely on revenue from customers with credit cards, many of them now using a service that allows paying bills by phone and creating closed-circuit group conversations.

Latin America's cellular market is dominated by Telefónica Móviles of Spain and America Móvil of Mexico, whose grip is likely to become even stronger. Led by the Mexican entrepreneur Carlos Slim Helú, the $7.5 billion America Móvil owns Mexico's largest service provider and has more than 46 million subscribers in seven countries.

Telefónica Móviles this year bought out BellSouth's cellular operations to give its Latin America subsidiary 41 million subscribers in 14 countries and potential revenue of $5.4 billion.

Telefónica Móviles will soon be operating Venezuela's leading provider, Telcel, which is battling for market position with Movilnet (owned by the Venezuelan telephone company CANTV) and Digitel (backed by Telecom Italia Mobile). Venezuela today has over 6 million cellular subscribers, and Telefónica Móviles expects this to reach 12 million within five years.

Status seems to play a big part in Venezuelans' use of cellphones. ''Venezuelans have always needed a public way to show their status,'' said the Venezuelan sociologist Leoncio Barrios. ''Thirty years ago, people would buy the fanciest car on the lot. But since times are tougher now, the best alternative is to have the newest mobile phone clipped to your belt.''

Venezuelans have become increasingly creative in getting more bang for their mobile buck.

Text messaging allows virtual conversations that cost much less than a call. The average Venezuelan cellular user sends 113 text messages a month, many between teenagers with too little money for calls. Providers sometimes face losses from text messaging, which can eat into profits by replacing calls.

''We have a phone in the house, but I'd rather send text messages to my friends,'' said Andreína Valerio, 13, who lives in the 23 de Enero neighborhood, a poor part of Caracas. She said this saves her money, but sheepishly admitted that her text messaging cost her parents more than $45 last month.

Dozens of Venezuelan radio and television programs allow users to participate in surveys or send in their opinions through text messages. The Miss Venezuela pageant, for example, allowed viewers (for 50 cents a message) to send suggestions for new beauty queen categories last year.

Cellphones have also been a boon to thousands of enterprising Venezuelans who buy prepaid phone time in bulk, then rent their cellphones by the minute, charging only 20 percent of what most users pay for a minute of service.

Gregorio Mayta, 33, who shut his carpentry business last year for lack of work, now sells calls on the Sábana Grande Boulevard in Caracas from seven cellphones displayed on a plastic picnic table.

''When business slowed down, I started selling the extra minutes on my calling plan,'' he said. ''These days it makes more than carpentry.''

Mr. Mayta spends over $200 a month to buy the cheapest prepaid minutes in bulk, then resells them in the form of one- or two-minute conversations purchased by an average of 500 customers a day.

But these alternatives have not damped Venezuelans' craving to have a mobile in hand -- even in areas of severe poverty like Nueva Tacagua, where cellular service is more consistent than running water.

For Yobran Nieves, the husband of Ms. Zambrano from Nueva Tacagua, cellular service is worth the sacrifice it entails. ''I feel like I'm getting robbed every time I put money into this thing,'' said Mr. Nieves, 25, scrolling through color pictures of the Eiffel Tower and the Golden Gate Bridge on the screen of his $375 mobile phone. ''But I still like having it.''

BACKGROUND
The above story was printed in May of 2003. Several years prior we conducted extensive qualitative research in Latin America for one of the providers mentioned, and recommended a strategy of targeting low income users in the region, like those profiled above. Obviously, this strategy was adopted, and the following reports on the original research that led to this adoption.

The Latin American telecommunications market is evolving from a monopolistic market into a free market environment. Brazil, as both the largest Latin American country and one where there was low mobile telephone penetration, is a very attractive market for providers.

To help a European client better understand the dynamics of this evolving market and to develop an entry strategy, we conducted qualitative research to analyze perceptions, attitudes and behaviors relative to existing and proposed new services and providers. We investigated two consumer segments in the top 3 Brazilian states:

- Current users in the upper/middle class who were technologically .sophisticated.
- Potential users in the lower classes (split between those who had a preference for a provider and those who were still undecided).

Bottom Fishing: Little Growth In Traditional Segments
Successfully entering the Latin American mobile phone service category is similar to "bottom fishing." As any fisherman will attest, the best catch is fish who live near the surface and have the highest commercial value. Typically, fish that live near the bottom are harder to catch, and have less commercial value. The only time fishermen will go after bottom fish is when the more valued species have been taken. Thus, the term "bottom fishing" refers to efforts that are directed at catching these less valuable fish.

Marketers are like fishermen in this regard. Their goal is to catch as many high-valued customers -- which in the mobile phone category is higher socioeconomic consumers -- as they can with the least amount of effort and expense. They tend to ignore potential customers who represent less value, i.e., lower socioeconomic consumers. Such consumers are the human economic equivalent of "bottom fish." Thus marketers who concentrate on developing business from low-valued consumers are said to be "bottom fishing." The implication is that they are doing so because the high-value customers have all been "fished out", i.e., taken by themselves and/or competitors.

This situation often exists for companies that are entering a market that has been dominated by established providers. Even though there is room for category growth, the highest-value customers may already be taken. While there may be an opportunity to "poach" a competitor's "catch" (i.e., take away market share), if customers are satisfied, and/or if there are barriers to switching, this may not be an effective business strategy. This is particularly so if the size of the existing market is small.

Thus new entrants to the market may find that the only "fish" left are the "bottom fish." Their business strategy must therefore be adjusted to develop tactics that efficiently exploit the more limited revenue and profit potential of such lower-value customers. However, as the client's experience in Brazil showed, a "bottom fishing" strategy can be turned to unique advantage. Although higher-value customers represent higher per capita revenues and profits, lower-value customers represent larger absolute revenues and profits by virtue of their greater numbers.

Cast A Deep, Wide Net

The economic value of the lower class consumer particularly applies in Latin America, where the percentage of population in the lower socioeconomic classes is much greater than in more developed economies. As the wireless telecommunications market has developed in Latin America, the relatively small percentage of populations that can afford such service have, for the most part, already obtained it from the existing providers. These providers enjoy an overall satisfied customer base among upper/middle class consumers, in large measure because they continue to offer more reliable and advanced technology and services. Further, there are barriers to change, such as the need to obtain a different telephone number if one switches service providers. Thus, there is little room for growth among this segment for new entrants.

Customers for a new service therefore need to come primarily from those who currently do not have wireless service. As the number of middle and upper class consumers who do not have wireless service is relatively small, the potential customers would be those in the lower socioeconomic classes, whose lack of disposable income and poor credit have not previously made them a segment of interest to the service providers.

What To Offer Then?

Mobile phone service providers have historically concentrated their efforts on first gaining penetration among the small affluent population, and then increasing revenues and profits by offering new technology and value-added services. They have also structured the service offering in a traditional manner by promoting a menu of subscription service contracts at various fixed monthly fees. These offers have traditionally included subsidized handsets and package rates that favor heavy usage.

A more recent development has been to offer pre-paid accounts rather than the traditional credit accounts. Such schemes operate much like the pre-paid phone card systems for wired telephones. These pre-paid plans have been popular with those who wish to budget or limit usage, and/or those who want to try mobile telephone service before making a commitment. They were not intended for those with a bad credit, or no credit. However, one of the unintended consequences of pre-paid plans is that it allows people to acquire a handset for relatively little money, and then use it for incoming-only service (like an enhanced voice pager). That is, many pre-paid users acquire a phone with a minimum amount of time pre-paid. When that time expires, the unit can still receive incoming calls, so they effectively have the use of a mobile phone for incoming calls at no charge.

How Is A Mobile Telephone Used?

The unique nature of mobile telephone makes it an enhanced communications device compared to wired service. Higher socio-economic users have a more sophisticated understanding of mobile's applications in contrast to the perspective of lower socioeconomic users. For lower socioeconomic consumers, mobile telephone is a basic service to be used sparingly in emergencies. Because of poor wired telephone distribution, mobile phone is, for many consumers, the only way to get telephone service. Thus, the new users from the lower socioeconomic classes will only demand basic service in contrast to the higher socioeconomic classes who need a variety of services.

How Then To Market It?
Mobile telephone initially was a service only the rich could afford, and this created an image of luxury. While it is no longer the case, the fact that only a small minority of the population uses it suggests that it is still a service most Brazilians cannot afford. Thus, among those who do not have one, a mobile telephone is seen as an indication of higher socioeconomic status. It has become an "aspirational icon" for those who strive for upward mobility. It also gives lower socioeconomic consumers the appearance of wealth and social position which for many is more important than meeting material needs. Therefore, marketing strategy should be tailored to the different classes. While higher socioeconomic classes find a sophisticated, value-added features approach appealing, lower socioeconomic classes need an approach that encompasses both the rational (a basic service that is better than wired), and the emotional (indicates higher socioeconomic status).

Who Is The Competition? Goliath v. David
In Brazil, there are multiple service providers in each state (the successor companies to the former state monopoly and private competitors). The successors to the former state monopoly are seen as the traditional companies that pioneered wireless in Brazil. They are the market leaders preferred by the higher socioeconomic establishment. While the quality of their service is high, they are also seen as expensive and somewhat arrogant. They have been vulnerable to more innovative and fleet-footed competition. The private competitors, seen as the "Challengers" are growing companies that are dynamic and enterprising. They are seen as the "people's choice" because of their more affordable prices and creative promotions. While innovative pioneers in new services, they are not as solid as the market leaders, and the quality of their service is not as high.

However, these providers all offer traditional business models that emphasize subscription service, and promote on the basis of offering innovative technology and new value-added services. While they have begun offering more basic services (such as pre-paid), their growth strategy is to concentrate on the quality of their customers rather than on the quantity. This means offering ever more value-added services in an effort to increase revenue and profits. They can be successful in this because they already have the bulk of the affluent population. Since satisfaction and barriers to change remain relatively high, the opportunities for a new provider are limited.

Future Services Opportunity?
A new service provider may think that their opportunity lies in being the leader in new technology, since consumers envision a future in which a whole host of new services can be delivered via wireless (e.g., video, electronic wallet, GPS). However, such new

technology will be relatively expensive, and is already being offered or envisioned by the current providers. Thus there is little incentive for customers to switch to a new provider. Even if there were such incentive, a growth strategy based on taking market share in a category with relatively little penetration would not be recommended.

Mobile telephone is now seen as a basic service in a free market, a normal service for which one shops. Thus, the opportunity is for a new service provider to capture a share of an expanding category with new users. The bulk of these will be novices, lower socioeconomic consumers who only want basic, affordable service.

Recommendations: Strategic Template

A high volume/low margin mass market strategy that offers mobile telephone service to lower socioeconomic users via innovative customer service and promotion is the recommended strategy. This is where the bulk of the population is, and they are currently not being served. By combining basic service and low price with innovative programs and promotions, a new provider can present itself to the mass of people as the alternative that breaks the existing duopoly. A new entrant should plan a strategy based on meeting the needs of the vast majority of consumers who so far have been under-served by the established providers. This requires the following:

- Focus on the working/poor classes.
- Offer low priced basic service on a pre-paid basis.
- Offer discount plans (e.g., friends and family) and a referral bonus.
- Sell through mobile sales offices that travel to the neighborhoods.
- Support the community via sponsorship, local event marketing, neighborhood
- media, etc.
- Position the product as a way for poor people to establish credit (e.g., after a certain period they can establish a credit subscription account).

Even if the net return is only half of what the other providers obtain, with a user base 34 times larger, the absolute business potential is substantial. By meeting the needs and aspirations of those who have been ignored because they have been deemed economically unimportant, a new provider can reap a bountiful harvest. As the saying goes, “fish where the fish are”, even if they are bottom fish.