

Telecom Italia's Sparkle operation is building new business opportunities around its backbone network and its data centres around the eastern Mediterranean, offering cloud and content-related services, says CEO Paolo Ferrari

From the Italian clouds to the sparkling Mediterranean, TI unit plans data moves

Paolo Ferrari: Services move operators up the value chain but you need to have a company culture to support that



Telecom Italia's international carrier business is fighting back against falling margins in the basic wholesale business by expanding into new services such as cloud and video.

And it is making the most of its position on the edge of the Mediterranean by developing links along the coast into Greece and Turkey, says Paolo Ferrari, CEO of Telecom Italia Sparkle.

"We have data centre operations in Sicily, in Athens and Istanbul," says Ferrari, speaking in an interview with Global Telecoms Business. The company is enhancing the data centres it already operates by providing new enhanced services "such as managed hosting all the way to cloud computing", starting with the Istanbul data centre at the end of 2011.

"The data centre that will be fully equipped to serve both international customers as well as corporate customers locally, with international connectivity as well as managed services."

The parent company, Telecom Italia, which is responsible for 25-35% of Sparkle's business, already has a service for clients in its home country called Nuvola Italiana — Italian cloud.

"We leverage our Telecom Italia group and Telecom Italia Sparkle knowhow and we leverage on our international connectivity to add significant value," says Ferrari. "That is significant investment, but is much less investment than if we were starting from scratch. It is a very good way to capture the innovation trends, while being conscious of the overall amount of capital that we can spend."

Ferrari has been with the Telecom Italia group for about a decade, starting as chairman of its office products retailer Buffetti. Later on he ran Hansenet, the company's broadband operation in Germany

— unfortunately for him at a time with the group decided to dispose of its operations outside Italy.

"It was a shorter project than expected as during my term TI disposed of the business," he recalls. "It was very good experience personally and professionally." The decision to sell "was the right one" because of to the competitive landscape in Germany.

He moved back to Italy to run Sparkle, which he describes as "the international services company of Telecom Italia".

A key goal is "to serve Telecom Italia as a customer" in areas such as "voice traffic management as well as connectivity management around the world", he says: "Telecom Italia is one of our biggest customers and is one of our priorities."

Third-party business

But the company has "a very large third party business" and is a generator of incremental revenue for the group "based on our international voice business, mobile data business, our data and IP and our multinational clients business", he adds. "We generate a large corporate business — multinational business that is still growing and will grow in the next few years." He estimates that "right now we do 65-75% of the business outside Telecom Italia.

But the international wholesale business remains a challenge — and the extent of that challenge is demonstrated by a continuing consolidation of operators, most recently the announced plans of Level 3 to buy Global Crossing.

Consolidation "is a consequence of what's going on in the market", says Ferrari. "Clearly consolidation is taking place because of the tremendous price pressure that we have — pretty much across all businesses. Maybe it's stronger or faster for voice because of price decline in the voice business, but the data and IP part is also experiencing a similar trend — with some years' lag."

Fortunately while prices in data and IP business are declining overall "in certain parts of the world [they] are still decent", he notes.

"But in general volume does grow significantly so these businesses grow in value, mainly driven by volume growth. This puts pressure on margins, pressure on costs and this is why a lot of companies are looking to consolidate."

Not long ago people were saying that, despite the pressures, consolidation wasn't as fast as expected — "then, bang, you have Global Crossing and Level 3 that shut everybody's mouth", he says.

Price pressure is one of the major challenges, but “the other challenge to me is the high investment — this is a capital intensive business”, he warns.

Cables are expensive. Four years ago it was not too difficult to present a case to build a cable from Europe to Asia, but now “the overall trend in prices doesn’t help”, he adds. “Right now it’s much more of a challenge to present a healthy investment case.”

Infrastructure investment

But Sparkle still invests “and the industry is still investing significantly in infrastructure — but you need to be more selective because of what’s going on in the market”.

And that’s why the focus by Sparkle and its rivals on services. That’s not easy, he notes: “In this industry it is a little bit tougher because you’re looking at services that are very different from what you used to do as a carrier.”

Services move operators “up the value chain and therefore you need to be ready for that”, he adds. “You need to have a company culture that supports that.” And “you need to have investment as well because some of this knowhow, some of these services aren’t developed internally, they need to be acquired.” A key factor is “how you partner with people”.

Cloud computing and enhanced data centre services are important, and they promise good returns. “The trading multiples of companies that do operate in these markets already are trading between 10 and 13 times ebitda, while the pure carriers trade between five and seven times ebitda. This is an area that a lot of people are working on,” says Ferrari.

“The other big area is content and video, which is a little bit more challenging. Somehow I think there is still an opportunity to play a role, not just in the value chain but in the content distribution but you need to invest into services, into platforms.”

This market is connected to the data centre business because the platforms to host content reside in the data centres, he notes, “and they need to be run in the proper way — everything is interconnected to some extent”.

It is an opportunity “but it’s also a challenge”, he adds: “Many others have invested in infrastructure, in cables, and to further develop their business as a carrier, [and] suddenly they have to develop a business that is different.”

Ferrari joined Sparkle formally in July 2010 but actually moved into the company two months later, to start work on a new business plan. “We are trying to address all the challenges. The price pressure and margin squeeze we clearly address by significant restructuring of our cost base. We are restructuring the company. In general we will have overall costs go down relative to the overall growth of the capacity that we manage and the overall business that we manage.”

He readily admits that Sparkle has “not been managing our cost base as much as the other players have done”. As a result he is “talking about the overall efficiency plan”, including general and administrative costs and a “rationalisation of our legal entities around the world” as well as “reviewing processes, managing vendors in a better way, so on and so forth”, says Ferrari. “I think we’re just a little late.”

Is he interested in any sort of consolidation. No, says Ferrari, “we’re not looking to sell or to dispose with regards to the network”, but he does “have a

voice business which is very large” and “we are trying to manage it from a value point of view rather than a volume point of view”.

What does that mean? “Certain relationships we had, that were many and each brought very little, we’re rationalising. We are concentrating on doing more business with fewer significant players.”

Outsourcing contracts

This means that Sparkle is interesting in doing some outsourcing contracts for other operators and managing their voice traffic. “That’s something we’re interested in.” The unit is already doing it for Telecom Italia and it is doing it for two French operators, Symacom and Virgin Mobile. “While we do reduce volume on very many small relationships we do compensate with bigger margin with fewer players.”

Ferrari has to argue hard for his investment with his parent company. “We are part of a group that has very a large pot of capex with a certain list of priorities. So we are very conscious of how we spend the money.”

But there’s money for acquisitions in that investment plan, he says. “We would like to for instance buy companies that bring us in one shot 50 data centres in Europe or round the world.” Are there any? “I don’t think the market has good value now,” says Ferrari.

Meanwhile, he says, the company’s business in Greece is going well — despite Greece’s economic difficulties. “If you are aggressive enough the tough times that Greece is going through [mean it] is exactly the right time if you want to invest,” says Ferrari. “This is why we’re doing it.”

And those investments give Sparkle access to the Middle East via the company’s submarine cable network that covers Crete, Cyprus, Turkey, mainland Greece, Italy and Sicily and its terrestrial network through Romania to Istanbul and to Frankfurt.

Sparkle’s MedNautilus backbone in the Mediterranean is paralleled by its LaNautilus backbone in Latin America, where “we are strong because we both have a captive business — TIM Brazil and Telecom Argentina”, both owned by Telecom Italia, and Sparkle has its own infrastructure.

“In terms of heavy investment and priorities, we’re certainly talking about the Mediterranean basin and Latin America.”

That’s supported by “our own proprietary infrastructure, South America Crossing, a ring of fibre that goes around South America, and we have a partnership agreement with Global Crossing — the northern ring, that goes from Latin America to North America”, he adds.

Which brings us back to the Level 3-Global Crossing announcement. “It was long overdue,” says Ferrari. “The market is moving that way for a reason. It does not surprise me that Global Crossing was part of it, because Global Crossing has had its own challenges over the past several years.”

And in the future? “It is going to be interesting to see what that means and how this unfolds and whether the consolidation process generates value or not. If it does, the industry will I think accelerate.”

But if there are challenges, “from an integration point of view [and] from a value generation point of view”, and then “maybe the industry will reconsider”, he adds. ■