

## France Telecom warns of hard times ahead

> **France Telecom** has warned the industry that its coming year will be tough as it tries to rationalise and build a global business that has a fully integrated network across its entire operation.

The slowdown in growth that it saw at the end of 2005 is set to continue through 2006, the company said, with the rationalisation of its infrastructure and personnel being key to improving its position.

Camille Mendler, VP international telecommunications strategies at Yankee Group, said: "It is undergoing a major integration. France Telecom wants to become an integrated operator which means a lot of restructuring. Part of that restructuring is putting together the French business teams with Equant and building a global business organisation that addresses not only multinationals but also SMEs in those countries where it has a national network footprint."

France Telecom is looking at accelerating the integration process this year by rolling out programmes which will simplify its brand portfolio and by unifying network and customer relations in each of the countries in which it operates.

Cesar Bachelet, analyst at Ovum, said: "A lot of duplication within France Telecom will be eliminated. Not just at the personnel level but at the network level as well. The aim is to rationalise the business, which will enable them to reduce their costs and this reduction in cost hopefully will happen quickly enough to offset the revenue decline."

This is France Telecom's second warning in four months. It cut its revenue growth forecast for 2005 to between 2% and 3%, from a previous figure of "nearly 3%". It had already cut its sales growth target in October last year from 5% to 3%.

Mendler said: "I think that the strength of the management team is absolutely key in the integration. The management team will have to devise a strategy that allows for this transformation to happen." ■

## Analyst's Eye >



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## ALL EYES ON VIDEO

### DAVID BALLARINI MULLS OVER THE FAR-REACHING RAMIFICATIONS OF CISCO'S ACQUISITION OF SCIENTIFIC-ATLANTA

> **Cisco's announcement** on November 18 last year that it would be acquiring cable and video equipment leader Scientific-Atlanta in a \$6.9 billion deal is perhaps the most interesting major technology deal of 2005, in what was a busy year for technology deals. And it's the most interesting deal from two very different angles.

Firstly, it is a radical departure from Cisco's long-held acquisition approach to gobble up relatively small but promising technology start-ups. From the mid 90s onwards Cisco has bought a large and diverse range of small companies – a range that includes Kalpana for its light-switching technology, Grand Junction, the company that invented fast Ethernet, and Netsys, a developer of network management software.

Scientific-Atlanta by contrast is a company of long standing: it has been at the heart of the American cable industry since 1951, it employs 7,500 people around the world, and it will certainly pose organisational integration complexities that transcend anything in Cisco's experience to date.

Perhaps this move is a sign of the times at Cisco, which has slowed down to the low teens in revenue and profit growth rates as its core data networking business has matured. Its price/earnings multiple in the low 20s now looks more like that of an industrial company than that of a technology company.

Perhaps the senior executive team at Cisco recognises that future value creation will depend on their company's ability not to develop new data networking technologies but to successfully consolidate equipment vendors that add noticeably to revenues, and contribute proven products and sizeable customer relationships.

Equally interesting, the combination of Cisco and Scientific-Atlanta has enormous potential to create probably the best-positioned vendor in a period of market development in which cable companies, telcos and internet content companies are all rapidly adopting new services and technology strategies to provide interactive video, voice, wireless and data offerings over converged, IP-based networks.

Scientific-Atlanta's head-end and set-top products, together with Cisco's IP routing and Linksys home wireless networking systems could, over time, be developed into converged, "quadruple play" offerings that suit every type of service and content provider.

And the investment market seems to like the story – during the last couple of months Cisco shares have recovered well from the minor drop that they experienced immediately after the merger was first made public.

Then there's the question of what activity the combination of these two giants will prompt from other companies operating in the sector. Given the potential that Cisco now has to be able to marginalise other vendors in the video equipment space, it would be natural for first tier players such as Motorola, Thomson, Nortel and Alcatel, as well as secondary players such as Harmonic, Arris, C-Cor, Tandberg TV, Seachange, Concurrent, Terayon and Tivo to consider some strategic mergers and partnerships of their own in order to create stronger companies with more coherent, integrated offerings.

In this investor's opinion at least, that above list of players will certainly be shorter by the time we get to 2007. ■