HD **Telstra stuck at growth crossroads**

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TELSTRA is laying bets on new technologies and **acquisition** targets that it hopes will bring in its next wave of growth.

As it lays bets on new technologies and acquisitions, the $68 **billion** telco is struggling to explain where the next wave of growth is likely to come from.

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While there's no shortage of ideas or new businesses opportunities for Telstra to pursue, the unanswered question remains: will any succeed?

If you ask Telstra chief executive David Thodey, he will answer with an unequivocal yes.

But with the looming loss of its fat-margined fixed-line telephony business to the National Broadband Network in return for $11.2bn, and a slowing mobile market, the reality is that Telstra's long-term future is up for grabs.

Telstra has of course seen this movie before. Almost a decade ago, when it was under the leadership of now-NBN Co chairman Ziggy Switkowski, the telco posted its biggest ever profit as a privatised **company**: a $4.45bn bonanza.

It was a time of fixed-line telephones, dial-up internet connections and mobile phones as big as bricks, but even back then there were signs the telco's rivers of **gold** — its fixed-line voice business — were fast drying up.

At that time, investors and analysts wanted to know how Telstra would grow when those rivers finally dried up. The answer then? Telstra's world-beating Next G mobile network.

That network — and sustained **billion**-dollar investments in it each year — laid the foundation for Telstra's explosive growth through its mobiles business, which now boasts more than 16 **million** subscribers who annually pour in $9.67bn of revenue into the **company**'s coffers.

But with Thodey acknowledging this week that the mobile wave is slowing, the telco again finds itself at the crossroads.

The critical question now is whether Telstra can take on the protean shift needed to grow new businesses and its bottom line. Thodey is adamant it can.

"For Telstra we know if we don't reinvent ourselves, if we don't continue to innovate in some way, that our customers will tell us and they'll leave us, and when they leave us we don't have a business," Thodey told guests at a business lunch in Sydney this week.

Big change of course requires big bucks. But if there's one problem Telstra doesn't have, it's a cashflow one.

The telco had $7.4bn in free cash floating on its balance sheet at the end of the 2014 financial year thanks to its 70 per cent **sale** of its Sensis directories business as well as its 76.4 per cent **stake** in **Hong Kong** mobile service business CSL for about $2bn.

While Telstra has already returned $1bn of that to investors through a share buyback and spent close to another billion on small-scale acquisition throughout the last 12 months, much remains for the telco to spend.

However, before Telstra starts splashing its cash to fend off internet giants like Google and Facebook, it would be instructive for the telco to heed the lessons of its past.

Chief among such lessons was Telstra's troubled relationship with its print directories arm Sensis, the home of the White and Yellow Pages.

Like Telstra's monopoly copper network, the Yellow Pages was a cash cow, generating margins of more than 60 per cent.

But rather than another river of gold Sensis ultimately turned into a symbol of one of the telco's biggest failures to deliver shareholder value as the telco missed key opportunities to sell the moribund business at its peak. In 2005, in the days before Sensis was forced to weather attacks from Google and smaller and more nimble online competitors, the asset was valued at close to $12bn.

At the start of this year Telstra sold a 70 per cent stake in the White and Yellow Pages publisher for just $454 million, giving Sensis a total value of just $649m.

Thodey, however, reckons the days of Telstra laying big bets on high-margin businesses are behind it.

"We went through a stage saying that unless we can find something with equal margins that we've got today, then we wouldn't do anything.

"That's just an unrealistic expectation now," he told analysts and investors at the telco's annual strategy update in Sydney this week.

The new reality is that any businesses that attract Telstra's burgeoning cash reserves will have to be operations with small profit contributions and high hopes.

"In five years' time we will have new business revenue streams with lower margins. But hopefully they will get better returns as we go forward," Thodey said.

Some of the focus of Telstra's recent investment activity has been on smaller and more agile software developers, which offer services targeting the big drivers of internet consumption such as video and increasingly healthcare applications.

In August, Telstra paid an extra $US270m to lift its stake in Silicon Valley-based video platform maker Ooyala from 23 per cent to 98 per cent.

The acquisition of Ooyala — which helps media companies such as ESPN and Bloomberg to stream videos to smartphones, computers and tablets — is just one of many new digital vehicles being targeted by Telstra as new growth areas.

Local interests include a $100m investment in its freshly elevated health-services division — which includes e-prescription exchange provider Fred IT and health appointment marketplace Health Engine — as well as investments in online restaurant reservation Dimmi, digital signage outfit Mandoe Media and cloud-based communications software provider Whispir.

These string of investments all come with the possibility that they could fail and cost Telstra hundreds of millions of dollars in writedowns. The write-off of its $302m investment in two Chinese mobile companies, Sharp Point and China M, is a case in point.

But like most big incumbent telcos around the world, Telstra is desperate not to be sidelined by software and tech firms like Skype and Whatsapp, which are eagerly eating the telco's voice and messaging lunches.

The other area that remains ripe for Telstra to gamble its cash on is investment into new businesses that leverage the company's existing strengths.

One such area is in cloud computing, and the telco's fast-growing Network Application Services, both of which are now being pushed through Asia where the telco hopes to tap in to demand from big-ticket corporate customers.

A key battleground for Telstra is Asia where the telco hopes to become a dominant technology and services company for the region's burgeoning middle class.

The telco is putting aside up to $1bn to spend on overseas acquisitions, partnerships and infrastructure investments in the region to establish its presence in the region.

While it seems like the days of Telstra dropping **billions** on a mammoth **acquisition** are far behind the telco, some growth it has to be said is better than no growth. Or through one of the smaller bets, the telco might be on to something.

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