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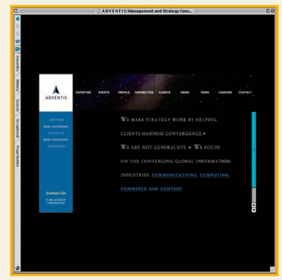


By Andrew Cole and Jennifer von Briesen

With the entrance of Virgin Mobile into the U.S. wireless market, much has been written about the emergence of MVNOs in the United States. And likewise, many have questioned the viability of the model as well as the reality of large-scale nontelecom brand entry into the wireless space.

We are here to confirm that significant behind-the-scenes deals are being struck with far-reaching implications for the entire industry. Adventis currently is helping craft the MVNO strategies for two *Fortune* 100 companies in the United States and four others in countries as diverse as Australia, the United Kingdom and Germany. We are in discussions with powerful entities in Canada, South Africa and Turkey. As a truly global trend, the entry of brand powerhouses into the United States and other markets will have a permanent impact on the very nature of wireless market competition and services.

Voice Is So *Last Century*

The current MVNO market can be characterized as the delivery of one common service or application, namely voice. And while voice service is compelling to all, its simplicity has made carrier differentiation almost impossible to establish. This in turn has powered intolerably high market churn and helped drive down per-minute pricing. So the industry continues to suffer from the vagaries of the old voice paradigm, and its salvation–which takes the form of value-added services–has so far failed to materialize. Because of this, a period of intense turbulence is embracing the industry, revising the requirements for success.

One of these fundamental shifts is the migration of inherent value from network ownership to the control of the customer. A second change–tied to the evolution of the value-added services, or VAS, market–concerns a new set of core competencies required for success. Successful VAS development demands marketing and service skills very different from those needed for simple voice services. As wireless value-added services become increasingly consumer goods focused, it is the traditional skills of companies such as Yahoo!, Sony Corp. and Walt Disney Co. that are needed. In addition, complex digital wireless networks require a different network management competency level, not to mention their dramatically higher costs of buildout and operation.

New Paradigm Means New Strategy

As the industry moves from a voice to VAS paradigm, many inevitable changes are occurring. First, network management is becoming a wholly separate and different business from the VAS business, ultimately leading to a complete separation. We expect the current networks ultimately to separate from their brands to optimize their networks. This brings us the second change. Networks cannot be satisfied with one wireless brand alone and instead require multiple brands to optimize capacity utilization. A third macro change also is evident. VAS development at its heart will drive uniquely personalized wireless services–services that resonate with the consumer in far-reaching ways. These personalized services will drive the fragmentation of the wireless carrier market into lifestyle brands where Gucci Mobile and Wal-Mart Wireless become a reality.

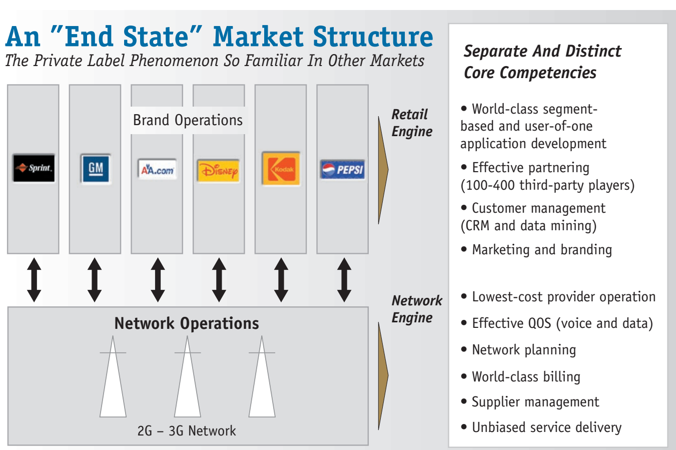
Large power brands are being driven to enter the wireless market as nonspectrum-owning virtual carriers. Many see the opportunity to benefit from a large opportunity, high-growth wireless Internet market. Others value the connectivity with the customer that comes through privileged access to the customer profile, while still others see control of the handset as a means to drive a fundamental shift in core business performance. Whatever the central driver, MVNOs from industries as diverse as retail, entertainment and auto manufacturing are rapidly establishing the operational requirements for success in the wireless market.

MVNOs Vs. Old-School Resellers

In our discussions with carriers and other vested interests, we have noticed a lack of understanding as to what an MVNO actually is. In fact, many carriers tag MVNOs as reseller organizations. Nothing could be less apt a description. While MVNOs do resell voice minutes, the core difference is that MVNOs craft unique VAS such as m-entertainment and m-gaming, and in doing so establish their own technology and content partners. In other words, MVNOs do not simply take a carrier's service and re-label it but instead create a suite of unique services targeted at their historic customer segment. Examples include America Online Inc., McDonald's and Ford Motor Co. MVNOs tend to control their own billing, customer care and all customer-facing capabilities. They leverage existing customers. The rest is left to the carrier.

An MVNO cannot exist, however, if the carrier does not allow the branded entity to access its network. Initially perceived by many ill-informed U.S. carriers as potential "Trojan horses," carriers have since progressed in their desire to support MVNOs, largely due to five major drivers. The first is a realization that the selective use of MVNOs in segments where carriers are either weak or perceived as unprofitable can drive subscriber adds that the carrier might not have otherwise enjoyed. MVNOs can make money where the carrier cannot–Wal-Mart and the low-income segment is a case in point. Secondly, carriers are increasingly understanding MVNO economics and seeing the potential for MVNO customers to have a larger earnings before interest, taxes, depreciation and amortization, or EBITDA, margin than existing carrier-branded customers.

Thirdly, as network investment and spectrum acquisition become ever greater, capacity utilization has become a key success factor. Additional capacity, particularly from MVNO customers that use nonpeak minutes, is highly attractive. Fourthly, the determination of heavy-hitting corporations to enter the wireless space is driving selective MVNO acceptance. Finally, the opportunity cost of going it alone has driven many European carriers–and their U.S. counterparts–to open their networks. As competitors embrace MVNOs, it becomes extremely difficult for carriers to ignore the trend for fear of being lost in the marketing noise.



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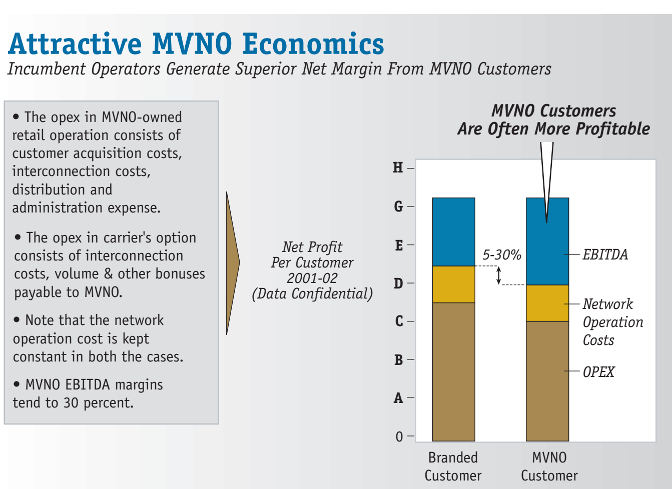

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It's Coming, Regardless

These forces are rapidly convincing U.S. carriers to open their networks to new MVNOs. For now, Sprint PCS and Nextel Communications Inc. appear to best understand the clear competitive advantage to be had from a rapid ramp up of the top MVNOs. Yet as in Europe, it is the largest U.S. carriers that continue to resist the trend. In particular Verizon Wireless has yet to wake up to the danger of its "laggard" strategic thinking.

While Verizon Wireless waits to determine its MVNO support strategy, others are moving ahead rapidly with initial discussions. These discussions are often precipitated by the compelling nature of some of the MVNOs coming to the table. Already large-scale businesses in their own right, organizations from different industries are combining to maximize impact and leverage existing strengths. Examples include joint ventures between retail players and global entertainment brands focused on key wireless segments. These players benefit from leveraging existing marketing budgets, distribution and consumer understanding to significantly alter the economics of the business. In this way there is more profit to go around, allowing the MVNO to make a 20 percent to 30 percent EBITDA margin and simultaneously pay the carrier its required return. This does not even consider the benefits from cross-business unit promotions and operational synergies that can transform MVNO economics still further.

Evidence from Europe has verified the theory that MVNOs make the wireless market more efficient. By reducing key cost elements such as distribution, while also reducing customer acquisition costs through the compelling connectivity of its brand to customers (thereby reducing churn), the MVNO can create a win-win economic partnership with its network carrier. Indeed, this relationship is at the heart of the MVNO concept and sets it apart from the traditional reseller market.

The MVNO trend is about to impact the U.S. market. Many drivers, including natural market evolution and fundamental economic efficiency, are encouraging major U.S. branded organizations to embrace the virtual carrier strategy. Meanwhile, U.S. carriers are moving fast to embrace these new entrants as partners. With the capacity to enable 10 large MVNOs, the U.S. market has both the inherent need and ability to power a new group of VAS players. Expect to see wireless services in a McDonald's near you by early next year. WW

Andrew Cole is global wireless practice leader for Adventis. Jennifer von Briesen is manager of the firm's Global Wireless Practice. Adventis is a management and strategy consultancy to the converging global information industries.