

Motorola at Risk in Nextel Strategy It Would Lose Exclusive Deal on Phones If Sprint Gains Merger

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Sprint's negotiations to buy Nextel have ignited fears that Motorola will lose its exclusive deal to supply phones and equipment to Nextel.

That loss could mean gains for Lucent Technologies and Nortel Networks, which are the main suppliers of wireless network equipment to Sprint.

The possibility of a union between Sprint and Nextel is "a bonanza" for Lucent and Nortel, said Susan Kalla, an analyst who covers the companies for Friedman, Billings, Ramsey. If a merger occurs, she and other industry analysts say, Sprint will induce Nextel's more than 15 million subscribers to turn in their handsets, which use an unconventional technology called iDEN.

Sprint is likely to encourage these customers to buy its own handsets, which use a more common technology known as CDMA, or code division multiple access. And to handle the influx of millions of extra customers, Sprint will probably have to order more base stations, switches, routers and other equipment from Lucent, Nortel and other vendors.

Kalla said she expected Sprint to take as long as five years to shut down the iDEN network, giving it time to expand its CDMA network without pressuring Nextel customers to swap handsets. Sprint may also introduce dual-mode handsets that would allow its customers to roam between CDMA and iDEN networks. Such a phone does not now exist.

Since last Thursday, when news first broke that Sprint and Nextel were in merger talks, investors have focused most on the potential damage to Motorola. Its shares fell 7.8 percent on Friday, but they rebounded on Monday on news that Motorola had won a contract to supply equipment to China Unicom.

Shares in Lucent and Nortel, by contrast, have been little changed. This is because the benefits of a Sprint-Nextel union are "just too subtle of a story, and we're not talking about gobs of money," said Brett Azuma, the head of research at RHK, a telecommunications consultant.

"In the near term," he said, "everything is a bit murky. But it is logical that Sprint will move all its customers over to its own network."

How Sprint ends up persuading Nextel's customers to switch to CDMA phones will help determine how large a windfall Lucent and Nortel might see, and how soon. Companies in such situations try not to set hard deadlines for cutting off older services because customers may rebel by switching carriers. At the same time, it becomes expensive to continue operating a network that is used by fewer and fewer customers.

Some wireless carriers, for instance, still operate networks that allow customers with older analog handsets to talk, even though most new customers are buying handsets for use on digital networks. As has been the case in other mergers,

Sprint would most likely offer customers with iDEN handsets financial incentives to give up their phones when their contracts come up for renewal, analysts say.

Sprint may subsidize the price of the new phones and offer discounted service plans, especially for businesses with many phones on their accounts.

Steve Levy of Lehman Brothers says he expects former Nextel customers to begin shifting to CDMA phones in 2006 if a Sprint deal goes through.

Sprint could also concentrate on improving its "push-to-talk" service, which allows a cellphone to double as a walkie-talkie. This service has proven immensely popular at Nextel. As of June, Sprint had signed up 360,000 subscribers for its version, which it calls Ready Link, though customers have to pay a \$5 monthly fee to use it, unlike at Nextel.

No matter how Sprint chooses to handle these issues, it ultimately would need more capacity to handle the extra customers. Nextel's 15.3 million subscribers would make up about 40 percent of the merged company's customer base. Lucent and Nortel have not been able to provide equipment to serve those customers because of Motorola's exclusive agreement.

"There's only upside for Lucent and Nortel" because they do not sell iDEN equipment, said Edward Snyder, a cellphone industry analyst at Charter Equity Research in San Francisco. "The first step will be getting subscribers to roam between the two technologies, and so you'll see the deployment of CDMA base stations next to iDEN base stations."

Given all the unanswered questions, industry analysts say it is hard to predict how much money Sprint will have to spend to expand and transform its network. The company said last week that it would invest \$3 billion during the next three years to enhance its network to provide high-speed Internet access.

Sprint could scale back these plans and use the savings to instead expand the capacity of its current digital network, or explore technology that allows for high-speed data connections and voice service on one network.

Either way, analysts said Sprint could end up spending billions of dollars more during the next several years as a result of a merger with Nextel.