

# ANALYSIS-Motorola's Droid to help Verizon, hurt RIM & Palm

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WIRELESS/HOLIDAYSALES (ANALYSIS)

- \* Shoppers seen gravitating to Droid this holiday season
- \* Droid gains seen at expense of BlackBerry, Palm
- \* iPhone expected to stay strong
- \* Smartphone subsidies likely to hurt carriers' Q4 margins

By Sinead Carew

NEW YORK, Nov 23 (Reuters) - As U.S. consumers compile their holiday shopping lists, Motorola Inc's Droid smartphone is expected to feature prominently, at the expense of Palm Inc's Pre and Research In Motion Ltd's BlackBerry.

Heavy marketing by Verizon Wireless will help sales of what Motorola hopes is its comeback phone, though the Droid will still lag by far the total sales of BlackBerry or Apple Inc's iPhone, analysts say.

U.S. market leader Verizon Wireless, owned by Verizon Communications Inc and Vodafone Group Plc, is also looking for a bit of a comeback itself, having lost market share in the third quarter to iPhone carrier AT&T Inc.

"It sounds like early feedback from Droid has been pretty positive," said JPMorgan analyst Michael McCormack. "There's no question that we'll see better results from Verizon" than in the third quarter.

Motorola is expected to sell 500,000 to 1 million units of the Droid in the fourth quarter, according to estimates from four analysts. That would be a good start for a company that has been losing ground to rivals for more than two years.

"Droid's eating into competitor phone sales at Verizon," said Charter Equity Research analyst Ed Snyder, adding that Verizon's Droid promotions are a problem for RIM.

He said that RIM does not have as exciting a product line this holiday season as it did a year ago, when the BlackBerry Storm was the highest-profile phone on Verizon's network.

The Storm attracted attention because it was RIM's first touchscreen phone, whereas the latest batch of BlackBerrys are mostly just upgrades of older phones, analysts said.

"There's nothing new with the BlackBerry story right now," Snyder said. "Last year they were the only show in town at Verizon."

Top executives at RIM downplayed such concerns, saying last week that the Canadian company is used to tough competition in the cellphone market, where it has a strong following from business customers ID:nN17491172.

Broadpoint Amtech analyst Brian Marshall still expects RIM to have 6 million U.S. BlackBerry sales this quarter, but said that this figure could have been higher if not for Droid, which runs on Google Inc's newest Android software.

Marshall expects AT&T to report 2.5 million iPhone activations in the U.S. this quarter as Apple maintains a strong position in the smartphone market.

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Analysts also see the Droid stealing the thunder from Palm's latest Pixi phone and from its high-profile Pre, which are both offered only by Sprint Nextel Corp. Pre is expected to go on sale at Verizon Wireless early next year.

"Droid coming first will hurt Palm," said Broadpoint's Marshall who also sees other Verizon phone suppliers such as Samsung Electronics Co Ltd feeling the heat.

Since many people in the U.S. already have cellphones, operators are increasingly dependent on promoting the latest hot smartphones to win subscribers away from rival services.

But these advanced phones, while boosting subscriber growth, may hurt carriers' bottom lines in the short term as the carriers pay hefty subsidies on each phone -- and fork out for pricey advertising campaigns as well.

"I think you're going to see the potential for a little additional seasonal pressure for Verizon. You'll probably see some sequential margin pressure," said JPMorgan's McCormack.

He noted that Verizon Wireless could pull back a little on BlackBerry advertising to help mitigate the Droid's costs.

Verizon Wireless has long enjoyed the highest profit margins of the major U.S. mobile providers, but McCormack sees Verizon's margin slipping to 45.6 percent this quarter from 46.1 percent in the third quarter. He expects AT&T margins to fall to 38.3 percent from 38.5 percent.

Analysts see increasing competition boosting costs across the entire industry in the fourth quarter.

"Subsidies in the fourth quarter will be the highest we've ever seen them," predicted UBS analyst John Hodulik. "I don't think the other carriers are going to sit back and let Verizon Wireless take the market share." (Reporting by Sinead Carew, editing by Tiffany Wu and Gerald E. McCormick)