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Major Wireless Carriers Flexing Their Muscle
Smaller Carriers Face Costly Upgrades, Reduced Revenue

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Myriad challenging issues face workout professionals dealing with wireless telephone companies. These issues, which include the industry's rapid pace of change, make navigating the current business environment extremely difficult.

From a "big picture" perspective, consolidation in the industry appears to be picking up, most significantly with the proposed merger between Cingular and AT&T Wireless. Also, time division multiple access (TDMA), a technology used by wireless companies, is disappearing, resulting in fewer technological choices for consumers and the prospect of costly conversion requirements for already cash-strapped carriers.

Major carriers have accelerated their build-out over the past several years so that they are no longer just in the metropolitan areas and along interstate highways, but are accessible in suburban, exurban, and even rural areas. Finally, carriers are heavily marketing nationwide calling plans that feature significant rate discounting in the form of minute bucket plans.

The proposed Cingular-AT&T merger, therefore, is not simply a combination of two major industry players. It continues a trend toward ubiquitous coverage and service in fewer technologies throughout the United States. The merger would reduce not only the number of national players, but also the number of nationwide wireless service providers using global system for mobile communication (GSM) technology. Such consolidation, from the perspectives of numbers and technology, has created a segmented market. If the Cingular-AT&T merger is completed, there will be two nationwide companies using GSM, two using code division multiple access (CDMA) technology, and one, Nextel, that uses integrated digital enhanced network (iDEN) technology.

Revenues Squeezed

Fewer nationwide players and technological choices create significant pressures on roaming revenues because carriers can cut deals with fewer other carriers to achieve nationwide coverage. Leverage in negotiations over roaming rates is often heavily weighted toward nationwide players. As a result, roaming rates have dropped precipitously over the past several years, causing severe reductions in revenue and earnings before interest, taxes, depreciation, and amortization (EBITDA) for second- and third-tier entities, such as Dobson, Western Wireless, and many other smaller private companies that have relied on roaming revenues to survive.

As a result, banks have seen covenant violations and payment defaults from these smaller companies. Yet these same borrowers need additional capital to contend in an increasingly competitive environment. Turnaround professionals are often brought in to work with smaller wireless companies that are facing reduced revenues from roaming charges, pressures on average revenue per unit/subscriber (ARPU), and bloated expenses. At the same time, many of these companies need to upgrade their plants because of the industry's move away from TDMA technology, to comply with FCC requirements, or to handle more voice and data traffic.

Faced with such situations, turnaround professionals often must raise capital or prepare for a sale while stabilizing cash flow and addressing employee morale. With the arrival on the scene of a turnaround professional, lenders and investors investigate the business practices of their clients in a more objective light. At the same time that smaller wireless providers face these difficult industry issues, practices that previously had been "under the radar screen," such as bloated payrolls, outdated marketing, troublesome intercompany relationships, outdated billing systems, and lack of network capacity, are often cited as some of the more common issues.

Dealing with the company-specific issues in the context of a rapidly changing environment typically proves very challenging. Significant investment in new equipment, new phones, and new marketing materials is required if many companies are to remain competitive. However, with revenues squeezed by lower rate plans, reduced outcollect roaming due to lower rates, and increased incollect roaming due to the overbuilds by the major players, a cash crunch often results.

Typically a turnaround professional starts by concentrating on the "low-hanging fruit" — previously hidden flaws. For operations, the focus is on personnel expenses, including commission structures, health care and other benefits, and hidden perks that often built up over the years in a less competitive environment. Marketing efforts should be focused locally, and community involvement should be emphasized. Creative work should differentiate the company from its nationwide competitors, while at the same time conveying the smaller wireless carrier's ability to provide the same capabilities.

The network is often a difficult issue, but capacity upgrades should be made to the extent possible, particularly in key coverage areas. Because the cost of new equipment has dropped sharply, it is less expensive to improve service in the current environment.

Internal Changes

An important aspect of improving operations is changing the internal workings of the company. Typically, a turnaround professional finds that different areas within a company do not communicate with each other. Fiefdoms have been established over time to protect specific people or to convey power. To compete successfully in an extremely competitive industry, however, free-flowing communication within a company is crucial. Data must be shared so that issues are fully understood and the best decisions possible are made.

Breaking down barriers between groups is crucial. This is particularly true for the finance department, which often is viewed as the enemy and therefore is been shut out of the information loop. Because decisions ultimately must be justified from a financial perspective, the finance department must become fully involved in the decision-making process rather than merely providing data after the fact.

Weekly group meetings are an important part of creating an environment in which information is shared and communication is increased. In addition, the dynamic of these meetings often needs to be changed to more adversarial, give-and-take discussions on particular items. Senior-level managers must believe that they have a voice in the outcome of these debates, particularly during difficult times for the company.

A key issue for a turnaround professional is often increasing employee morale. Two discussion tracks should run concurrently, one with top-level executives and one with the company's remaining employees.

Top-level executives clearly should know that significant problems exist. These individuals should be kept abreast of the company's progress and most often will be involved in discussions with potential investors/buyers. It must be made clear to the company's rank-and-file employees that changes are being made to benefit them and that they should spend less time worrying about the health of the company.

An example of positive change is modifying compensation structures to make them more incentive-based so that good performers can make more money. This is typically a positive change for both the company and its employees, at least those who are important to the company's future. Another positive change is elimination of policies for benefits such as vacation or sick time that were put in place on a whim and reflected one person's idea of appropriate procedures, as opposed to industry norms. Changing such policies to reflect industry norms benefits employees and is therefore good for morale.

Perhaps the most difficult issues to address at the company level are those that create conflicts between short- and long-term objectives. For example, initiating changes in rate plans, which often are long overdue, may have a short-term negative impact on churn. Although this may be troublesome in the short run, it may have a positive effect over the long haul. Similarly, a shift in a company's credit scoring policy or in its prepay and credit-limit products also may produce negative short-term results while providing a more stable long-term revenue base. In making such changes, issues need to be fully vetted and communicated to the various constituencies.

Consolidation Continues

To help in calibrating the impact of these decisions, a turnaround professional must keep in mind the company's ultimate objective and the time frame for achieving it. Typically, the overriding goal of the parties involved is either to raise capital or to sell the company.

As analog and TDMA roaming revenues continue to decline, wireless companies that have TDMA networks will face severe difficulties in raising capital. Raising capital to upgrade a TDMA network is very difficult given the capital required and reduced roaming revenues inherent in the business model as the company moves to CDMA or GSM. Companies that have original CDMA or GSM networks and are faced with the need for costly upgrades may find raising capital a bit less challenging. Often, however, such a company is sold to a larger industry player that can afford to upgrade the system and fold a troubled company's operations into a much larger entity. As a result, consolidation of small wireless carriers seems destined to continue.