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Cutting the Cord: Investing in Wireless

By Glynn Key, Wilmer Cutler Pickering Hale and Dorr

With the dynamic growth of the wireless industry in recent years, more and more private equity investors are looking to wireless technology and services as an avenue for expanding their portfolios. The attorneys at Wilmer Cutler Pickering Hale and Dorr know this well, having represented both industry and investors. But what should investors know before pumping their money into this rapidly expanding market?

Glynn Key

We recently met with industry and government leaders to explore the current issues facing private equity investment in the wireless industry. Executives from Nextel, JPMorgan Partners, the FCC, The Carlyle Group, and Telecom Ventures weighed in on the topic from their respective industry perspectives. Our discussion identified some key considerations for potential investors.

First and foremost, investors should grasp just how quickly the market is expanding. According to CTIA, as of last summer there were more than 170 million cell phone subscribers in a nation of almost 295 million people. "Given the large percentage of the population that has access to wireless devices, U.S. wireless is the growth industry for the telecom industry in both equipment and services," says Atish Gude, vice president of strategic planning and corporate strategy at Nextel. "The focus for the private equity world in wireless is increasingly becoming applications and middleware-centered driven."

Some statistics to mull over when considering industry and investment potential: Verizon announced last month that 45% of its revenue comes from its wireless services unit, Nextel's third quarter profits are up a whopping 69%, and Cingular just received clearance to complete its $41 billion merger with AT&T Wireless, creating a wireless giant that is banking on the bundling of broadband services to its 46 million subscribers. In addition, Lucent recorded its first annual profit since 2000, fueled by rapid growth in the wireless telephone division.

An investment plan cannot be composed of statistics alone, however. What do these stats mean for the private equity investor and how do private equity investors then take this knowledge and transform it into a savvy investment strategy? Michael Hannon, a partner and co-head of the Telecommunications, Media and Technology practice at JPMorgan Partners, points out that domestically, wireless applications are attractive, but on the international market, JPMorgan leans toward services. "Europe and Asia are the hot spots for 3G and component technologies," he says. "Private equity/buyout opportunities in wireless are best overseas in places with relatively stable government environments and solid financial sectors where multiple platforms, like IPOs or strategic buyers with capital, are in place."

Dr. Rajendra Singh, CEO of Telecom Ventures and co-founder of Teligent and LCC International, has some prescient advice for those interested in getting into the wireless market. Telecom Ventures specializes in early to mid-stage investment in wireless system operations and emerging wireless technologies, a several hundred million dollar family investment vehicle. From his position, Singh observes that there are four trends in the wireless industry of which potential investors should be aware:

• First, cultural change is significant and being driven by youth's consumption and use patterns. If you don't know how a young person uses technology and how important wireless is to that experience, Singh suggests you quickly learn.

• Second, enabling wireless technologies are a growth sector because of the need for wireless applications and content to be easily accessible for consumer use. This means more focus on wireless middleware opportunities.

• Third, a marketplace mindset has been established where the cell phone is not just a communication device but a device that enables the exchange of ideas and also, increasingly, goods and services.

• Finally, today, nearly all networks are hybrids, composed of wireless, cable coax, copper, and fiber. In hybrid networks, the value added comes from taking a position that takes advantage of the hybridization instead of fighting against it (e.g. content or applications have to flow across all elements of the hybrid network instead of being stove-piped).

Glynn Key is a partner at Wilmer Cutler Pickering Hale and Dorr. She represents public and private companies, private equity firms and emerging technology companies. She may be reached at glynn.key@wilmerhale.com

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195 Broadway, 9th Floor, New York, NY 10007 • (646) 822-3043