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WiMax and VoIP… similarities?

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Following its recent lackluster IPO (ClearWire has fallen about 20%, as of this writing, from its IPO price of $25), it's tempting to compare WiMax service providers such as ClearWire with companies represented by previously fallen IPO stars, such as, say, Vonage (which has lost over 75% of its value since its debut). After all, both types of service are retail telecom oriented, relying on a subscription model, both are fierce burners of cash, both value cases require real paradigm shifts in consumer behavior, and in the cases of the specific companies mentioned, both had high profile IPOs for about half a billion dollars. We think, however, that important fundamental differences between the two business models warrant very different analyses.

To take the example of Vonage, only as a way to generalize for its broader sector, the company has performed similarly to many other non facilities based service companies. With the exception of Virgin Mobile, the Mobile Virtual Network Operators (MVNOs) have often been the subject of considerable investor disdain, following in the shoes of non-facilities based CLECs, long distance resellers, and similar telecom "bubble" products. (To be fair, Vonage does own some components of its network, but still largely relies on others to carry its traffic.) With this dependence on third party networks, Vonage and similar competitors are in the situation of paying ~60% of revenues from each customer to the owners of those networks, which can limit financial flexibility and the benefits of growth.

ClearWire offers investors substantial comfort through the durability of its assets, and so a repeat of the Vonage debacle is quite remote.

The real issue though, from our perspective, is that at the end of the day non-facilities based operators are only as strong as their customer relationships, which in turn reflect a combination of loyalty (carrot) and switching costs (stick). Like its competitors, Vonage is trying to form bundling arrangements with other service providers to deepen these customer relationships, most notably Earthlink. However, if investors ever start to feel that customer relationships could be at risk (or, alternatively, that the service offered is fungible), then they may soon conclude (as they had done with other telecom "resellers" before) that there "isn't a lot of there, there." It certainly doesn't help when it is official government policy (through number portability) to lower those switching costs. (Additionally, VoIP in general also suffers (fairly or not) from some quality perception issues, though over time these are becoming less prominent.)

While WiMax faces many of the same issues (broadband is, after all, becoming increasingly a commodity), its VoIP offerings are inherently a double play (bundled with broadband connectivity), vs. pure VoIP providers' single play service. This can make the offerings of ClearWire and similar companies stickier, and with higher ARPU makes their customers more valuable.

More importantly, ClearWire and similar WiMax business models have a lot more than customer relationships to cite on the asset side of balance sheets. There is owned infrastructure, and, probably the most important asset of all, there is licensed spectrum – the value of which has been validated in recent spectrum auctions that attracted some of the telecom sector's deepest pockets (27 billion mHz-POPs of spectrum fetched $14.7 billion). Such assets for ClearWire but also many other WiMax projects represent inherent barriers to entry that the likes of Vonage and other VoIP resellers would clearly have benefited from. As a downside mitigant, therefore, there is an asset value that underpins at least a portion of invested capital.

So, while the business model for WiMax broadband offerings is far from proven, and (using ClearWire as a proxy for the overall sector) the stock performance out of the gate is shaky, we think ClearWire and similar WiMax initiatives may offer those investors wanting to participate in the growth of wireless broadband services substantial comfort through the durability of an asset base versus comparable non-facilities based telecom services like many VoIP providers.

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