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Mobile Satellite Ventures and Inmarsat play nice

While many of you were enjoying holiday parties and eggnog, things got very interesting in Mobile Satellite Services (MSS). In particular, Mobile Satellite Ventures (MSV) managed to pull off a very interesting deal with their sometimes competitor, Inmarsat, LTD. When it was announced on December 21st, the market clearly liked the deal, sending the shares of Inmarsat up 7% and the shares of Skyterra (MSV's public trading vehicle) up a whopping 24% that day. This begs the question: Should it have? Let's take a look...

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To address this question, a little history lesson is in order. From the public filings of Skyterra, MSV and Inmarsat we can learn that these companies all share a portion of the spectrum known as the L-Band, (Mexico and Russia also have some use of the L-Band over North America). This sharing process is known as coordination, and through 1999 was governed through a process known as Spectrum Sharing Agreements, which were prepared annually. However, from 2000 through last year, no new Spectrum Sharing Agreements were reached, and interference complaint filings at the FCC were, to use a term, rancorous.

With no new agreements, MSV and Inmarsat remained bound by their last agreement, which was a product of its era in the sense that it did not anticipate the widespread adoption of WCDMA, UMTS and other 3G transmission formats that require large contiguous chunks of spectrum. (At the time, Inmarsat and MSV both operated earlier generation satellite systems that used narrowband channels.) Thus, while MSV did have nearly 20 MHz of contiguous spectrum, their remaining spectrum (approximately 10 MHz) was sliced into narrow intervals that had significantly less utility per unit of spectrum (and thus commercial value). Because these chunks were created by similar sliced portions of Inmarsat's spectrum, Inmarsat suffered a similar problem, albeit to a lesser extent. Thus, as technology evolved the 1999 agreement actually destroyed part of the spectrum value for MSV and Inmarsat.

Turning now to the agreement itself, it identifies several new spectrum plans (and associated payments) between the respective firms. While the timing and payments for the plans are explicitly



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specified in public filings, the actual spectrum plans themselves are not. To the extent that our conversations with MSV and the document allow, we also discuss what we believe to be the significance of each plan in the table below:

	Timing and Payments	Potential Significance
Phase 0 Plan	Immediate. Payment of \$31.25 million in stock (or cash if both parties agree) upon subsequent completion of MSV financing exceeding \$100 million.	MSV retains access to the same ~30 MHz of spectrum they previously claimed, but cleans up 1999 Spectrum Sharing Agreement to have both firms migrate their operations toward contiguous spectrum bands. We believe most (between 26 MHz and 30 MHz) of this spectrum becomes contiguous.
Phase 1 Plan	At MSV option, any time up until 9/1/2011. Initial payment of \$31.25 million in stock (or cash if both parties agree). \$250 million in additional payments over 24 months, plus a completion payment of \$56.25 million in stock (or cash if both parties agree).	The Phase 1 plan is an intermediate plan that probably provides MSV with accelerated access to the contiguous spectrum with much more favorable and flexible operating rules, but less aggregate spectrum than the 46 MHz of phase 2, by Inmarsat scaling back its expansion plans for BGAN service in the region MSV covers.
Phase 1A Plan	Same as Phase 1 except with 15 month timetable.	We believe the Phase 1A plan is very similar to the Phase 1 plan, but with slightly different implementation to reflect its further compressed timetable.
Phase 1 Alternative Plan	9/1/2011 if a Phase 1 option is not exercised by MSV by then. No additional payments.	We believe the Phase 1 Alternative Plan has greater contiguity than the Phase 0 Plan, but note that it provides for MSV to cede certain spectrum rights currently in dispute. As a consequence, we believe it preserves over 20 MHz of contiguous spectrum, but has somewhat less spectrum than Phase 0.
Phase 2 Plan	At MSV option, beginning 1/1/2010 through 1/1/2013. At Inmarsat option, beginning 1/1/2013 through 1/1/2015. \$115 million per year, with MSV retaining the right to terminate after 5 years.	Based on public documents, this plan provides MSV with ~46 MHz of contiguous spectrum. Given the magnitude of the payments involved, Inmarsat is probably deliberately ceding planned business in lieu of the magnitude of the payments.
Default Plan	Upon MSV default on its payment obligations following completion of transition to Phase 1.	We believe this plan is probably somewhat punitive to MSV, but that MSV would not have entered into the agreement if it did not preserve the 20 MHz of contiguous spectrum MSV currently controls.



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Alternative Default Plan	Upon MSV default on its payment obligations prior to completion of transition to Phase 1.	We believe this plan is probably similar to the Default Spectrum Plan, but is closer to the Phase 0 plan since it is implemented prior to the completion of Phase 1.
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Although there is substantial uncertainty regarding Phase 1, we know that Phase 2 provides for MSV to gain access to an additional 16 MHz of spectrum, and on a practical basis probably a bit more than that of valuable contiguous spectrum. If we compare that to the approximately \$1.25 billion present value of the payment MSV must make to secure this benefit, it comes to ~\$0.25 per MHz-POP. This is a modest premium to the valuation implied by the current trading price of Skyterra, MSV’s public trading vehicle, as well as recent transactions in the WCS band. Additional details regarding spectrum valuations will be discussed further in the forthcoming Near Earth LLC white paper entitled “Spectrum: Invisible Real Estate”, to be released shortly. For more details on the valuation case for MSS/ATC spectrum, as well as a full discussion of ATC in general, please visit www.nearearthllc.com to download our white paper “Mobile Satellite Service w/ Valuation of Ancillary Terrestrial Components (ATC)”.

So, quite apparently the MSV team is bullish enough to at least want to secure the option to that spectrum, which provides an excellent segue to another feature of the agreement – its built in optionality. As written, the plan allows MSV wide latitude to “bolt on” spectrum in two chunks, using three different time scales (admittedly at considerable and probably escalating marginal expense) as it evaluates its business case. In the alternative, this agreement resolves existing issues regarding spectrum, and through the phase 1 alternative plan caps MSV’s payments at \$31.25 million.

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Overall, at today’s valuations, we view the plan as a mild positive for both MSV and Inmarsat, but with substantial upside potential for both. To begin with, the plan makes for more immediate efficiency gains in spectrum use for all parties – a “no brainer” as it were. However, if spectrum values for MSS/ATC spectrum rise over the next several years, this plan gives MSV a way to enhance appreciation for its owners by exercising options to increase its holdings – steps it is only likely to pursue if it gains enough to offset the Inmarsat payments. Likewise, from Inmarsat’s perspective, it



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gains some stake in MSV's success – both through direct ownership in stock but also by very substantial cash payments that are likely to occur to the extent MSV exercises its options. And, Inmarsat itself gains some optionality to effectively “put” spectrum to MSV in the event MSV exercises its first option but not the Phase 2 option (i.e., Inmarsat gets the option to exercise if MSV exercises accelerated contiguity under Phase 1). In the end, Inmarsat, which has always wanted an ATC play, gets participation in one with very little downside indeed.

Returning to our original question about the moves in stock prices, it all depends on what one thinks these options are worth. In any case, it's certainly good to see these companies cooperating to build value. So, while it may be premature to really celebrate at MSV and Inmarsat, this deal appears at least to be worth a few congratulatory toasts – with the real party to be deferred...

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