Why ESPN Wants to Start a Mobile Phone Company

The Emerging Market for Entertainment-Oriented MVNOs

Introduction

The 1990’s witnessed a frenzy of investment in telecommunications companies. Billions of dollars were invested in expanding wireless networks in the hopes of capturing as many customers as possible. Then, the crash: $750 billion\(^1\) of infrastructure and other investments went up in smoke. Investors fled telecom stocks, and companies either shut their doors forever or severely cut-back on employees and expansion plans.

So, why would a company like ESPN want to start their own wireless venture, in the face of heated competition and sustained losses by most of the major players? And more generally, why are there so many companies attempting to start their own wireless service offerings? The answer is less complicated (and less idiotic) than it may seem. As will be shown, all of the players stand to benefit by increasing the level of competition, and in fact the wireless industry overall may become more stable by introducing these new brands to consumers as wireless vendors. Why is this?

State of the Wireless Industry in the United States

The year 2004 will go down in history as a watershed year for the cellular telecommunications carriers in the United States. This was the year in which the industry finally

\(^1\) Malik, Om. *Broadbandits: Inside the $750 Billion Telecom Heist*. Wiley & Sons. May 2003.
participated in the consolidation of the national carriers it so badly needed. Prior to 2004, there were six national carriers; Verizon, Cingular, AT&T Wireless, Sprint PCS, T-Mobile, and Nextel. With the announced mergers of Cingular & AT&T Wireless and Sprint & Nextel, the market has now consolidated nationally to four carriers, with Alltel coming in fifth as a strong regional player in the Southeastern United States.

Figure 1 - U.S. Wireless Subscribers by Vendor, Assuming a Nextel/Sprint Merger

These carriers have evolved to handle massive scale of users, attempting to be all things to all people, spending heavily on national advertising and local in-store promotions. They are working to increase margins by driving down the cost of operations and trying to stem customer defections.

With the bulk of their networks built, they are trying to squeeze as many minutes as possible out of their systems, as the marginal cost of providing additional minutes of service falls to near zero. How can the carriers economically earn more from their sunk network investments? MVNOs could be the answer.

The MVNO Model (Mobile Virtual Network Operator)

**What is an MVNO?**

A mobile virtual network operator (MVNO) is an arrangement between a cellular carrier, who leases space on their network, and a company that wishes to be the customer-facing wireless brand, or virtual network operator. For example, I could lease space on a network and resell it to you, making me an MVNO. More generally, Gartner, a technology analysis firm, describes an MVNO as “…a company that does not own a mobile spectrum license but sells mobile services under its own brand name using a licensed mobile operator’s network.”\(^1\) An MVNO at its core is a basic reseller relationship.

The first MVNOs were driven largely by carriers to increase their distribution to non-traditional audiences in order to drive traffic onto their networks. Thus, Sprint PCS sought out the partnership with Virgin Mobile in the UK to bring the Virgin brand to the United States. Nextel similarly partnered with an Australian firm, Boost, to launch Boost Mobile in the United States. Both of these entities were designed to reach out to the non-traditional pre-paid and youth markets (both of which have credit challenges), to drive more traffic on the networks for non-peak times (late afternoon and early evening). These carriers both recognized that their MVNO partners had in-house marketing expertise that could accurately target and service these previously neglected market segments.

**Why Would a Carrier Want to Create an MVNO Partnership?**

At first glance, it is hard to understand why a carrier like Sprint would cede their customer base willingly to a competitor. As more MVNOs are introduced, the overall level of competition will increase, driving prices down and stealing customers from traditional carriers. From a strategic standpoint, this decision seems somewhat ludicrous. But, as will be shown, the economics in fact

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can be quite attractive. Are there any real strategic reasons to pursue an MVNO relationship for a national carrier?

As the United States reaches higher and higher levels of penetration, the carriers are finding it more and more difficult to continue their historic growth rates. The chart below shows just how much carrier subscriber growth rates are easing. If a customer really wanted wireless services, they would have already signed a contract with one of the national players, and as such are “unreachable” by the massively-scaled sales and distribution networks of the major carriers. MVNOs, by contrast, are able to bring their significant knowledge of their respective target customer niches to bear, thus allowing them to reach previously underserved markets.

**North America: Mobile Voice Connections and Growth, 2001-2008**

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In addition to reaching new segments of the un-served wireless population, some MVNOs can more economically reach some of the traditional wireless company’s less profitable or less attractive customers. By removing the customer service and support infrastructure expenditures

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dedicated to these customers, carriers can spend more time taking care of their high-value customers, and offload more “troublesome” subscribers to MVNO partners.

**The Long Tail – Reaching Previously Unprofitable Customers**

The concept of the “long tail,” currently being mentioned and analyzed on weblogs throughout the internet, helps contribute to the notion of why an MVNO is possible. Technology enables merchants to carry those products or provide those services that previously were unavailable due to the constraints of providing products or services due to limited shelf space or distribution. Now, a retailer like Amazon.com, with no physical presence but an unlimited electronic one, can provide those products in the “long tail” economically – in fact, more that 50% of their book revenue come from titles outside the top 130,000!\(^5\)

**Figure 2 - The Long Tail by Chris Anderson\(^6\)**

The “long tail” concept can be applied to cellular carriers in a slightly different way. The cost of providing network service to additional subscribers is essentially zero, but acquisition costs for carriers (CPGA, or cost per gross add) are still incredibly expensive, ranging from $274 for Verizon to $570 for Nextel.\(^7\) MVNOs do not require the investment in branded storefronts, choosing instead to partner with retailers like Target, surf-shops and other targeted retail outlets, resulting in CPGA for Boost of only $175.\(^8\) This allows the MVNOs to focus their energies on marketing and developing targeted products, while the carriers segment their network time amongst

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MVNOs who are able to reach previously underserved segments, like youth or credit-challenged individuals.

**The Economics of an MVNO**

When a carrier leases network time wholesale, a typical agreement is for $0.04-$0.05 per minute, while the marginal cost of a minute on the network is between $0.01-$0.02 per minute. So, at a minimum, a carrier could earn $0.02-$0.04 per minute per subscriber from an MVNO wholesale agreement. Given the fixed cost of providing cellular service, the carriers have every incentive to drive additional subs to their networks and grab the incremental revenue offered by the MVNOs.

The analysis by Deutsche Bank (Figure 3) attempts to strip out all expenses that an MVNO would cover (SG&A and equipment) to illustrate the marginal cost for Sprint to provide a minute of time on their network. As you can see, an incremental minute in 2005 will cost $0.02. Given that a carrier has excess capacity on their network, any leasing arrangement above $0.02 per minute is cash-flow positive for the carrier, and thus could represent a desirable operating model. In fact, Virgin Mobile is estimated to provide Sprint up to $0.10 per minute in wholesale revenue.

**Risks to Carriers of Partnering with an MVNO**

There are a number of risks to be considered when a carrier agrees to launch an MVNO with a partner. Most importantly, the carrier risks losing control over the customer experience. This problem becomes especially acute if the partner a carrier chooses has little customer service or

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billing expertise that could lead to customer dissatisfaction. If their partner turns out to be lousy, customers will churn which will reduce the value of leasing network space to the MVNO in the first place. Carriers would be wise to conduct significant due diligence on their potential partners to ensure a positive customer experience.

The other threats to the carriers are more of a macro-level issue. First, as more MVNOs begin to appear on the scene, prices are sure to come down overall in the industry. Even after the consolidation in 2004 to four national carriers, the emergence of MVNOs will ensure a healthy level of price competition, ultimately a win for consumers. The industry has excess capacity, and the marginal cost of providing this excess capacity is essentially zero, thus allowing for such precipitous price declines. Carriers need to be careful how they price their wholesale minutes to MVNO partners.

The second problem related to price competition is the general threat that MVNOs will steal customers from other national carriers as they offer consumers a differentiated, branded experience. As an industry, MVNOs are a threat, but to individual carriers, they present an opportunity. Sprint is the furthest along in leasing network space to MVNOs, and as such could emerge as a net winner in this marketplace at the expense of the rest of the industry.

**Who has already launched an MVNO?**

Although this sounds to many like a very new phenomenon, in fact there have been MVNOs for some time in the United States. One of the most well known is Tracfone, a unit of America Movil that has been selling handsets and prepaid wireless cards in 7-11 stores for the past few years. Now, MVNOs in the United States account for nearly 3% of total wireless subscribers (4.8M).[^12] Hardly numbers to scoff at, and this number will only continue to grow, as MVNOs are

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attracting 15-20% of net additions for the industry.\textsuperscript{13} And by 2010, the Yankee Group estimates that MVNO subscribers will make up more than 14% of all wireless subscribers, or 29 million total subs.\textsuperscript{14}

Taking a look at some MVNOs individually, there are two dominant ones currently in place in the United States – Boost Mobile, a partner of Nextel Communications, and Virgin Mobile, a partner of Sprint PCS. Boost Mobile is a prepaid brand that launched in 2003 to cater initially to the “surf culture” of Southern California, and is being rolled out nationally in stages. Boost has 1.5M subs as of Q1 2005.\textsuperscript{15}

Virgin Mobile was also launched around 2003 targeted more broadly at the overall youth segment, or “MTV generation.” Virgin is also a prepaid service, thus limiting the need for any credit checks, which opens up the service to a much wider potential customer base. Virgin has run promotions on MTV to appeal to its target audience, and is available nationally. Virgin Mobile has more than 3M subs as of Q1 2005.\textsuperscript{16}

The Opportunity for Emerging MVNOs

\textit{The Cellular Industry is Ripe for MVNO Growth}

So, why is now the right time to launch an MVNO? After the wave of consolidation in the United States wireless market, the landscape is dominated by four national players, all of whom are in competition for the same mass market of subscribers. At the same time, the RBOC-affiliated carriers, notably Cingular (owned by Bell South and SBC) and Verizon, are facing severe declines in their landline businesses as customers flock to mobile-only telecommunications service. As the

\textsuperscript{14} Mallinson, Keith. “MVNOs Will Segment the Market and Help Carriers Sustain Viability.” The Yankee Group. 27 April 2005.
\textsuperscript{16} Smith, Brad. “Virgin Mobile; From Doubt to MVNO Leader.” Wireless Week. 15 March 2005.
Figure 4 shows, the younger segments are most likely to cut the cord and go wireless only, which not only causes problems for the RBOCs today, but also means that a whole generation of consumers will grow up without landlines, further eroding their future prospects.

**Figure 4 - Cord-Cutting - Do you plan to abandon your local phone line for your mobile?**

Furthermore, Figure 5 shows more accurately just how much the RBOCs are feeling the pinch on their landline businesses. Specifically, by next year, the RBOCs are expected to have lost a cumulative 24M subscribers to wireless. Thus, you can expect the RBOCs will continue to fight for customers to stave off these declines.

**Figure 5 - Estimated Impact of Technology Substitution on RBOC Access Lines**

<table>
<thead>
<tr>
<th>U.S. Consumer Lines (000s)</th>
<th>2000</th>
<th>2001</th>
<th>2002</th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
</tr>
</thead>
<tbody>
<tr>
<td>Consumer Primary &amp; Resale/UNE-P Lines</td>
<td>100,451</td>
<td>100,482</td>
<td>96,011</td>
<td>95,254</td>
<td>92,886</td>
<td>89,316</td>
<td>65,259</td>
</tr>
<tr>
<td>Change (000s)</td>
<td>157</td>
<td>28</td>
<td>(2,402)</td>
<td>(1,754)</td>
<td>(3,399)</td>
<td>(3,570)</td>
<td>(6,056)</td>
</tr>
<tr>
<td>Change (%)</td>
<td>0.2%</td>
<td>0.0%</td>
<td>-2.5%</td>
<td>-1.8%</td>
<td>-3.0%</td>
<td>-3.9%</td>
<td>-4.5%</td>
</tr>
<tr>
<td>Cumulative Change Since 1999</td>
<td>197</td>
<td>225</td>
<td>(2,243)</td>
<td>(4,000)</td>
<td>(7,366)</td>
<td>(10,936)</td>
<td>(14,996)</td>
</tr>
<tr>
<td>Estimated Household Growth</td>
<td>2.0%</td>
<td>2.0%</td>
<td>2.0%</td>
<td>2.0%</td>
<td>2.0%</td>
<td>2.0%</td>
<td>2.0%</td>
</tr>
<tr>
<td>Cumulative Projected Change Since 1999 (000s)</td>
<td>2,005</td>
<td>4,050</td>
<td>6,136</td>
<td>8,264</td>
<td>10,435</td>
<td>12,648</td>
<td>14,906</td>
</tr>
<tr>
<td>(Assumes A/Ls grow with households)</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Gap Between Actual and Projected A/Ls</td>
<td>1,808</td>
<td>3,824</td>
<td>8,379</td>
<td>12,284</td>
<td>17,803</td>
<td>23,586</td>
<td>20,902</td>
</tr>
<tr>
<td>Less: Leases to Cable (non telephony sales)</td>
<td>0</td>
<td>1,523</td>
<td>2,212</td>
<td>2,413</td>
<td>2,622</td>
<td>3,395</td>
<td>5,411</td>
</tr>
<tr>
<td>Cumulative Lines “Lost” to Wireless Since 1999</td>
<td>1,808</td>
<td>2,301</td>
<td>8,167</td>
<td>11,871</td>
<td>15,781</td>
<td>20,194</td>
<td>25,491</td>
</tr>
</tbody>
</table>

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These challenges to the RBOCs indicate just how competitive the market for wireless is, and also illustrate that consumers have developed a significant and growing appetite for wireless services. The result is that consumers are becoming more and more comfortable in dropping their landline carrier, creating revenue opportunities for emerging MVNOs.

In addition, the concept of the “long tail” introduced earlier means that it is now more economical for the carriers to try and fill their networks with as many users as they can, and that it is now possible to take marketing segmentation to the extreme through the use of affiliated MVNO brands. These MVNOs essentially act as outsourced marketing organizations for the carriers, scouring the landscape for underserved wireless customers looking for something more from their wireless service. Carriers like Boost and Virgin opened the door for millions of underserved customers already. Now, a new generation of MVNOs that are tied to certain entertainment and other lifestyle brands stand to offer not only basic cellular service, but also valued-added content and hardware that is highly differentiated from the plain vanilla offering of the major carriers.

Cellphones have evolved from a symbol of status when they first launched, to a commodity product in the late 1990’s and early 2000’s, and are now becoming more and more of a status symbol once again. The launch and popularity in 2004 of Motorola’s V3 Razr phone symbolized the desire for many users to express themselves with their wireless handset. In addition, the service itself has become commoditized, so people in the US will increasingly look for value-added services to differentiate themselves. MVNOs are able to capitalize on this desire to express oneself through their mobile service, as many MVNOs will launch their own unique handsets. MVNOs in addition will create revenue opportunities by offering their own unique content and services, further
differentiating themselves and their customers. By 2010, the Yankee Group estimates that MVNO subscribers will make up more than 14% of all wireless subscribers, or 29 million total.\(^{19}\)

**ESPN Mobile’s Foray into Wireless**

ESPN Mobile is one of the highest-profile companies yet to announce they will offer MVNO service to their customers. In addition to the marketing and content that ESPN brings to bear on this market, ESPN subscribers are very attractive to a technology-oriented product or service provider, like ESPN Mobile. As you can see from a recent Forrester Research survey, those consumers that visit sports sites on a weekly basis make more money, are younger, male, entertainment motivated, and optimistic about technology – a prime market for any new technology product. This desirability of the ESPN core audience was likely one of the primary drivers for ESPN to entertain the idea of entering this market.

![Figure 6 - Online Sports Fans are Young, Higher-Income, Tech Optimists\(^{20}\)](image)

<table>
<thead>
<tr>
<th></th>
<th>Don't visit sports sites weekly</th>
<th>Visit sports sites weekly</th>
</tr>
</thead>
<tbody>
<tr>
<td>Percent of online HH</td>
<td>90.5%</td>
<td>9.5%</td>
</tr>
<tr>
<td>Male</td>
<td>47%</td>
<td>75%</td>
</tr>
<tr>
<td>Partnered</td>
<td>64%</td>
<td>67%</td>
</tr>
<tr>
<td>Have kids</td>
<td>37%</td>
<td>34%</td>
</tr>
<tr>
<td>Income</td>
<td>$62,814</td>
<td>$69,462</td>
</tr>
<tr>
<td>Average age</td>
<td>46.1</td>
<td>44.1</td>
</tr>
<tr>
<td>Career motivated</td>
<td>36%</td>
<td>40%</td>
</tr>
<tr>
<td>Entertainment motivated</td>
<td>29%</td>
<td>33%</td>
</tr>
<tr>
<td>Tech optimists</td>
<td>60%</td>
<td>71%</td>
</tr>
<tr>
<td>Have broadband</td>
<td>25%</td>
<td>35%</td>
</tr>
</tbody>
</table>

In addition to catering to an attractive audience, ESPN is motivated by the potential to deepen their customer relationships. According to Manish Jha, senior VP, ESPN Mobile, “We want


to create a fan experience that is more immersive, deeper and designed for sports fans. We want to be there with the most compelling content we have.”  

The hope for ESPN is to create long-lasting relationships, and to drive revenue from the content they have sitting on the shelf, thus creating incremental revenue opportunities for the business.

**Market Size and Economics for ESPN Mobile**

The total available market for ESPN Mobile includes a number of potential variables. There are currently over 94M people that interact with ESPN either online, on TV or in print every week. This is a strong group of potential subscribers, illustrated by the fact that ESPN ranked first in “brand resonance” among men out of 138 other brands. One could use this as a benchmark for sizing the available market for ESPN Mobile. However, I have decided to act a bit more conservatively and instead base an assumption on consumer research done by Forrester last year.

Forrester’s research surveyed households across North America in an attempt to find how many households regularly visit sports websites, and of those, how many are willing to pay for additional content such as voice or video. Forrester discovered that 9.5% of the population visits sites like ESPN regularly, and of that number about 8.5% would be willing to pay for content (I assumed approximately 50% of each segment to account for the fact that there is some overlap in the percent willing to pay for video and audio to arrive at the 8.5% value).

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21 Cuneo, Alice. “Brands Seek Higher Calling as 'Virtual' Cellphone Providers; ESPN to Disney, AARP Eye 80 Million Who Spend $50 Monthly on Service.” Advertising Age. 11 April 2005.


Figure 7 - Estimated Market Size and Revenue Opportunity for ESPN Mobile

<table>
<thead>
<tr>
<th>Source</th>
<th>Description</th>
<th>Value</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Total Mobile Population (2005)</strong></td>
<td></td>
<td>182,140,362</td>
</tr>
<tr>
<td>% online households regularly visit sports websites</td>
<td></td>
<td>9.50%</td>
</tr>
<tr>
<td>% willing to pay for sports video</td>
<td></td>
<td>8%</td>
</tr>
<tr>
<td>% willing to play for sports audio</td>
<td></td>
<td>9%</td>
</tr>
<tr>
<td>Assumption: 50% overlap</td>
<td></td>
<td>Estimate</td>
</tr>
<tr>
<td>% total willing to pay for sports content</td>
<td></td>
<td>8.5%</td>
</tr>
<tr>
<td><strong>Total market for sports fans willing to pay</strong></td>
<td></td>
<td>1,470,783</td>
</tr>
<tr>
<td>Estimated ARPU for ESPN Mobile</td>
<td></td>
<td>$60</td>
</tr>
<tr>
<td>Incremental ESPN Content Revenue</td>
<td></td>
<td>$5</td>
</tr>
<tr>
<td><strong>Total ESPN Monthly Revenue</strong></td>
<td></td>
<td>$65</td>
</tr>
<tr>
<td><strong>Total monthly revenue opportunity</strong></td>
<td></td>
<td>$95,600,923</td>
</tr>
<tr>
<td><strong>Annual revenue opportunity</strong></td>
<td></td>
<td>$1,147,211,070</td>
</tr>
<tr>
<td>Estimated penetration</td>
<td></td>
<td>50%</td>
</tr>
<tr>
<td>Estimated subscribers</td>
<td></td>
<td>735,392</td>
</tr>
<tr>
<td><strong>Estimated revenue</strong></td>
<td></td>
<td>$573,605,535</td>
</tr>
<tr>
<td>Subs as % of total mobile population</td>
<td></td>
<td>0.40%</td>
</tr>
</tbody>
</table>

Based on a total population of 182,140,362 wireless subscribers, we can use the survey results from Forrester Research to roughly estimate the number of wireless users that are willing to pay for sports content at 8.5% of the market, or 1.4M potential subscribers. Using an average ARPU estimate of $60, incremental ESPN-specific service revenue of $5, and an estimated 50% penetration of this market, we are looking at an annual revenue estimate of nearly $574M for ESPN.

Note that the subscribers I estimate ESPN will capture represents only 0.40% of the total wireless market, whereas Virgin Mobile already has 2% of all mobile subs. In fact, the Yankee Group

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24 Total number of wireless subscribers as reported by the Cellular Telecommunications and Industry Association (CTIA) on 26 May, 2005, via their website, [http://www.wow-com.com](http://www.wow-com.com).
recently estimated that ESPN would capture in excess of 1M subs, so my estimates here are conservative.\textsuperscript{28}

Next, we need to think of the cost of providing this service to ESPN to arrive at an estimate of net income. Part of the MVNO relationship is fact that ESPN will be responsible for all aspects of customer care and billing, as well as securing equipment and shelf space at the retailers of their choice. Below I have estimated that in a given month, ESPN will on average have 500 minutes of use per sub, translating into $25 of cost that Sprint will charge. Adding an SG&A cost of $15 and equipment of $10, plus an incremental $5 of non-voice revenue to the bottom line, ESPN will net just over $130M per year based on my conservative subscriber estimates.

**Figure 8 - ESPN’s Net Income Estimates**

<table>
<thead>
<tr>
<th>Source</th>
<th>Estimate</th>
</tr>
</thead>
<tbody>
<tr>
<td>Average MOU (minutes of use)</td>
<td>500</td>
</tr>
<tr>
<td>Cost</td>
<td>$0.02 Deutsche Bank</td>
</tr>
<tr>
<td>Total cost</td>
<td>$10.00</td>
</tr>
<tr>
<td>Wholesale price</td>
<td>$0.05 Deutsche Bank / estimate</td>
</tr>
<tr>
<td>Total revenue</td>
<td>$25.00</td>
</tr>
<tr>
<td><strong>Net income</strong></td>
<td><strong>$15.00</strong></td>
</tr>
<tr>
<td>ESPN cost</td>
<td>$25.00</td>
</tr>
<tr>
<td>Total ARPU</td>
<td>$60 Estimate</td>
</tr>
<tr>
<td>SG&amp;A</td>
<td>$15 Estimate</td>
</tr>
<tr>
<td>Equipment</td>
<td>$10 Estimate</td>
</tr>
<tr>
<td><strong>ESPN net income</strong></td>
<td><strong>$10.00</strong></td>
</tr>
<tr>
<td>ESPN incremental revenue</td>
<td>$5 Estimate - video/audio svcs</td>
</tr>
<tr>
<td>ESPN Total Net Income Opportunity</td>
<td>$15</td>
</tr>
<tr>
<td>ESPN Subscribers</td>
<td>735,392</td>
</tr>
<tr>
<td><strong>Annual Net Income</strong></td>
<td><strong>$132,370,508</strong></td>
</tr>
</tbody>
</table>

Recognizing that the SG&A and equipment line items are pure estimates, this model is sensitive to changes in the assumptions. A $5 increase in either SG&A or equipment cuts approximately $45M from the bottom line, however I believe this is a decent estimate of the opportunity ESPN is

looking at, otherwise Disney management would not have authorized an investment in starting this venture.

In addition, ESPN is likely modeling internally more than $5 in incremental data revenue, as they probably believe they have a high probability of extracting value from their subscribers. Also, they could be incorporating synergistic revenues from cross-selling on their cable and internet platforms, driving interactive content between the platforms.

**Economics for Sprint PCS**

Based on the above estimates, Sprint PCS stands to earn $15 per subscriber per month from ESPN Mobile, which translates into $10,901,250 per month, or $130,815,000 per year in incremental revenue to the carrier. The PCS division of Sprint is expected to post EBITDA of $4.7B in 2005, which means an ESPN deal would increase Sprint’s EBITDA by nearly 3% in 2005. Sprint PCS will also have an opportunity to cut some of their redundant customer service staff and possibly some retail outlets. These closures will become especially important after they close the merger with Nextel later this year and need to consolidate facilities. To the extent they can keep up the minutes of use on the network while reducing overhead costs, Sprint will continue to pursue deals like this. Net, this deal represents a solid financial opportunity for both sides.

**Beyond Revenue - Strategic Rationale for ESPN Mobile**

The economics clearly make sense for ESPN to offer this service, as shown above. But beyond the numbers, why would ESPN want to launch mobile service? ESPN is a content producer, and the company creates value when this content is monetized. TV and the internet have provided ESPN their primary revenue opportunities, and now they are looking to bring the content they have already produced to a new media. ESPN can deliver video and analysis to subscribers, thus giving ESPN a higher degree of “content utilization” across all their platforms, TV, internet

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and mobile. In addition, ESPN could deliver statistics and real-time data to subscribers, providing a potentially significant revenue stream to their members.

Moreover, ESPN currently relies on distribution networks in the form of the cable MSOs to reach their subscribers. ESPN Mobile will provide the company an opportunity to “own” the customer relationship, providing the direct link to customers they currently are lacking. In fact they will be able to learn more about their most valuable and loyal customers as they are the ones most likely to sign on with ESPN Mobile. ESPN stands to gain much in terms of knowledge of their customers, plus they can begin to engage them for new ideas regarding products and services, giving the company access to some of the best possible focus groups.

Some may ask, would ESPN be better off simply producing content for sale on all carrier networks, rather than creating their own? This might be a less expensive proposition, but they also stand to lose the per-minute revenue that an MVNO relationship will provide. If ESPN simply resells content, it becomes a business of one-off purchases, which seem much harder for the firm to sustain than if they had monthly, recurring revenue streams from a core customer base. Plus, ESPN would lose all of the customer relationships to another carrier, and wouldn’t stand to gain any additional knowledge of their customers. While this endeavor sounds expensive, ESPN can reach their target audience quickly and cheaply, by simply advertising to their base of 97 million viewers on television at virtually no cost to the company.

**Risks to ESPN Mobile**

As with any new venture, there are significant risks that need to be considered. First, the quality of the network they’ve chosen (Sprint PCS) could prove a negative, depending on how the merger with Nextel proceeds. Or, other carriers like Verizon could simply outspend Sprint in their

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network upgrades, which could result in less bandwidth for the services ESPN would like to provide. Second, the backend systems to manage an MVNO network could prove troublesome. As Lance Zingale, COO of StarTek, a vendor of business process outsourcing for wireless companies said, “MVNOs don’t really look at billing and CRM until sometime after deciding what network they will use.”  

If any of these systems don’t work, ESPN’s brand equity could be destroyed. Every time a customer drops a call, has a bad experience with customer service, or is upset about their bill, ESPN’s brand will suffer. In effect, ESPN is putting their brand in the hands of a service provider that could give them a black eye.

**Risks to Sprint PCS**

As mentioned earlier, any carrier that partners with an MVNO risks introducing new competitors in the marketplace that could ultimately drive down all prices. However, there are company-specific risks that need to be assessed, both with respect to the carrier and who the carrier chooses to partner with. In the case of Sprint PCS, their impending merger with Nextel could create internal resource-management conflicts as they try to bring MVNOs online. Moreover, Sprint has invested heavily in building-out a consumer-friendly retail store network that could become under-utilized if many customers begin to sign up with ESPN.

With respect to ESPN, Sprint also risks more than they do with Virgin Mobile, specifically in the amount of network traffic this deal will generate. ESPN is likely to want to deliver a variety of high-bandwidth video as well as frequent wireless-internet impressions. These services could put a lot of pressure on Sprint’s network that they may not be ready to absorb. It is likely that Sprint has

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thought through many of these issues already, so I don’t anticipate these to be huge issues, but they are something every carrier needs to think about when drafting an MVNO arrangement.

**Summary of the ESPN Opportunity**

ESPN looks to be the first MVNO play to rely on their existing customer base to capitalize on their extensive marketing expertise. Unlike Boost or Virgin, who catered to underserved, pre-paid wireless customers, ESPN is targeting their valuable customers, many of whom likely already have wireless service, and will offer them unique, branded content they can’t get anywhere else. ESPN certainly faces some challenges, but on balance this looks like a positive deal for the company. The more important issue here is that ESPN will simply be the first in a long-line of consumer and entertainment companies that are expected to launch MVNOs in the coming years.

**Another Entrant – Disney Mobile**

Disney, like its subsidiary ESPN, has announced that they are pursuing an MVNO arrangement with Sprint PCS as well. Disney, like ESPN, has more content in their libraries than they could leverage on their movie and TV networks, and as such an MVNO gives them another opportunity to monetize this content. In addition, Disney can further develop the relationship they have with families and kids, providing them with their favorite characters, games and video clips all the time. This will provide the company additional sources of revenue beyond their current library of ring tones sold by other carriers. Historically Disney has captured about $1-$2 per month from a subscriber that accesses Disney content via a mobile device on any given carrier. The company believes they can increase this amount to over $10.32 Disney is currently hiring a number of folks for

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positions in their mobile unit, including producers, business developers, marketers and financial analysts.\textsuperscript{33}

\section*{Conclusion}

Industry analysts have been calling for consolidation in the wireless industry for years. Just when they got their wish with the AT&T/Cingular and Sprint/Nextel mergers, it seems we are on the brink of an explosion of new carriers onto the landscape. ESPN, MTV, 7-11, Disney, Comcast, and Cablevision are all planning or thinking about becoming mobile carriers. Wal-Mart and Target could be close behind. Isn’t this trend a bad thing for the industry as a whole? It depends.

For consumers, clearly this is a positive step. More carriers means increased competition and lower prices overall. According to CTIA, the average monthly bill for a subscriber has actually been increasing over the last few years,\textsuperscript{34} so consumers will welcome any price competition. Moreover, MVNOs will begin to deliver value to consumers beyond basic voice services, providing entertainment and information that is relevant to their wants and needs.

As was said in the beginning of this paper, “all of the players stand to benefit by increasing the level of competition, and in fact the wireless industry overall may become more stable by introducing these new brands to consumers as wireless vendors.” It should be clear now that the companies who will (successfully) launch their own MVNOs bring something significant to the game that no one has done before; marketing expertise and segmentation that is unmatched by any national carrier.

\textsuperscript{33} The Walt Disney Company career site. \url{http://corporate.disney.go.com/careers/index.html}
\textsuperscript{34} CTIA’s semi-annual wireless industry survey shows that average monthly bills have increased from $39.43 in December 1998 to $50.64 in December 2004. \url{http://www.wow-com.com/research_statistics/statistics/index.cfm/AID/10030}
In the next five years, 20% of wireless subscribers will be from MVNOs, according to consulting firm Adventis. Furthermore, 80% of MVNO customers by that time will have come from other carriers, rather than introducing new users to wireless as is often the case today. Some carriers may believe that this 80% represents cannibalization of their business. Others, like Sprint, who have embraced the MVNO concept, see the trend as a means to outsourcing their marketing function to a slew of companies who know who their customers are, how to reach them, and what to price their products and services. The carriers who can benefit from MVNO arrangements can become leaner organizations, better able to focus on enterprise clients and leaving the consumer marketing to the experts. Indeed, this could make the industry overall more stable, by eliminating many of the expensive marketing programs the national carriers have undertaken.

If ESPN and others can pull off their MVNO strategies, these entertainment companies stand to benefit even more than the carriers. They are looking for new revenue streams and distribution channels for their content, which is now collecting dust, and an MVNO is a perfect way to do this. Technology makes it possible to create highly-segmented wireless consumer brands, to reach those customers that exist in the long tail. The question that remains is, will any old company make it as an MVNO? It is clear that companies like ESPN, Disney, or other entertainment companies, with valuable content, have a shot at making the MVNO model successful. Whether The Gap or other retail-focused brands can make it in the wireless market remains to be seen.

Regardless, anyone can give the MVNO model a shot. Simply point your web browser to www.sprint.com/business/program/wholesale/plsApplication.jsp to start your MVNO application.

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