

WiFi – mergers ahead!

Gerbsman Partners 2003

About this report

Gerbsman Partners decided late in 2002 to expand its international business model to focus on and develop “Domain Expertise” in the worldwide Wireless and Technology market. Early research made clear to us that three areas of significant interest stood out among current wireless offerings – Premium SMS, WiFi and Wireless entertainment. As a part of our commitment, we spent the first half of 2003 visiting market leaders in each of these segments in the US, Europe and Israel. Observations, interviews, conversations and findings serve as the foundation for this White Paper. Gerbsman Partners is committed to continuing its efforts in wireless and is offering assistance to understand, navigate and execute business related to these three themes.

Summary

Nobody has been able to miss the buzz around WiFi the last 12 months. Large investments have dominated the deal flow and a mass of WiFi-related startups have launched new services or technologies. With recent cycles like the “Dot-com” era fresh in our memories, Gerbsman Partners has grown increasingly convinced that the US WiFi industry is a market segment that will look very different in just 6-12 months.

Early indicators are telling a tale of larger corporations buying the best of breed and incorporating their offerings into existing portfolios. With multiple providers in each segment, and an increasingly competitive market place, M&A activity is becoming a viable exit strategy for investors and founders alike. This white paper examines the current “hot zones” of the US WiFi market and offers a point of view on what segments represent the first wave of US WiFi mergers.

WiFi consists of related segments spanning from service to technology, therefore Gerbsman Partners has looked closer at this market and concentrated on two areas of significant interest – Hotspots (Service providers) and Access technology. By looking closer at both, we hope to provide a clear and compelling argument for Gerbsman Partners ability to assess your current portfolio or analyze potential future investments.

- **Consolidation ahead** – As the margin game has entered the marketplace, major players have the muscle to survive. Smaller companies will have to look at alternative ways to survive.
- **Wholesale WiFi** - Branded hotspots are changing their business models towards the independent wholesaler market.
- **Low profit margins** - Do not count on significant revenues from Hotspots, Customer loyalty and churn reduction might be wireless carriers argument for including hotspots into their offerings.

Introduction

WiFi, as a basic concept, wirelessly connects a user to broadband Internet, typically at Ethernet speeds, allowing use of maximum available bandwidth. The most common usage has proven to be in vertical enterprise applications such as warehouse ordering and inventory, hospitals and health care facilities, and public hotspots. As issues of security and privacy are getting appropriate attention, larger enterprise campuses and other localities suited for wireless are increasingly adopting and installing these networks.

Hardware mergers are happening

One big note is also that Microsoft has started a strong move into the WiFi space, recently announcing partnerships that include Swisscom, T-Mobile, Cometa Networks, Wayport and iPass. This is significant news since Microsoft seems to have learned from Intel and started to craft an eco-system, only in this case they will sell Windows XP instead of Intel's Centrino chip sets. Although it is too early to tell what impact these partnerships will have, one thing is clear – WiFi is gaining enterprise confidence.

The conclusion is that the larger companies are moving full speed ahead. As financial analysts predict an upbeat IT purchase trend beginning this fourth quarter of 03, the orders for end-to-end WiFi enterprise solutions are steadily picking up.

The plethora of access point and antenna technology providers has enjoyed an "easy" investment environment the last year and a half. However, with decreasing margins and dropping prices, they are beginning to feel a squeeze. One example is the decision by Intersil, a leader in WiFi chip sales, to sell its WiFi business to GlobespanVirata for \$365M.

Likewise, the \$500 M purchase of Linksys by Cisco provides a similar example. Cisco's massive enterprise customer portfolio trusts Cisco to provide larger installations. By incorporating Linksys's product portfolio, Cisco is now able to provide an end-to-end solution including networks as well as user access technology.

Intel's \$300 M investment in marketing of its Centrino product includes multiple eco-system-like investments where Centrino technology is at the epicenter of all offerings.

The disappearing margins and the increasingly competitive landscape, makes it interesting to take a close look at who might be on the other side of the equation. Companies like Lucent, Ericsson, Nortel Networks and Alcatel all offer professional services in addition to their infrastructure. The vast array of specialized telecom professional service companies all has to offer WiFi solutions to remain competitive..

Hotspot business models are changing

Pyramid Research has released a potentially fatal report, predicting that ARPU will decrease from an average \$30 today to \$3 in 2008. While the user base will grow with an average of 57% per year, economy of scale will become the only way to survive in the hotspot business. As a result, the Hotspot market is going through a complete change right now. The trend of going from being a branded provider to wholesale is evident at Wayport, Cometa and Boingo.

In earlier white papers (WiFi in the US, Aug. 03), Gerbsman Partners pointed out that a crucial component to hotspot growth will be roaming. Since then, the players on the US WiFi market has moved towards partnerships and collaboration in order to achieve just that. Wayport has shown the biggest movement by changing its business model from providing branded solutions offering roaming to wireless and landline carriers. Wayport has signed deals with AT&T Wireless, Verizon Wireless, SBC Communications and Sprint.

Cometa Networks entered the US market by offering WiFi access at McDonald's restaurants in New York City. A more compelling offering in urban Seattle will soon follow. By offering wholesale hotspots to multiple service providers in the same locations, Cometa hopes to create a niche for themselves as the backhaul one-stop-shop for WiFi service providers. Cometa has also signed a partnership with Sprint, enabling Sprint PCS customers access to Cometa's network. As AT&T is one of the founders of Cometa, AT&T is supplying Cometa with back end pipes and traffic management.

Boingo is the third big provider to enter the wholesale business. Fueled by its latest 2nd round investment of \$10M, Boingo continues to offer Boingo branded access points. This last spring Boingo launched its private brand offering targeted towards wireless carriers with T-Mobile as their biggest customer. Boingo announced in August that its network now has 2,600 access points/ hotspots. Boingo has also entered a formal collaboration with Earthlink to provide WiFi solutions..

The shift from operating a independent "new operator" business model to offer whole sale and roaming will enable the large to grow larger and put significant pressure on smaller providers to find ways to attract and keep customers.

As margins and ARPU are decreasing, and business models changing, the competitive landscape for Hotspots is about to radically change. The wireless carriers all consider offering their own WiFi service, either through a consolidated wholesaler or as a sole provider. This is very good news for the consumer since the prices will drop and access will inevitably become ubiquitous. But, as the market is full of independent providers, wireless carriers as well as ISP's will move towards acquisitions.

Conclusions

As the US WiFi market forms into a clear eco system and larger entities are packaging and bundling services, US WiFi will continue to grow. Whether it will be offered by independent service providers or consolidated aggregators, the ubiquitous nature of access will enable profit and success by utilizing economies of scale. Also, as location is at the core of the issue, revenues will probably flex between premium locations or free access at obscure places. Companies offering roaming and neutral access will prosper. Smaller, independent providers will, on the other hand, have a hard time ahead with limited ability to provide roaming or offer connection outside their primary coverage zones.

Gerbsman Partners has the unique ability to maximize shareholder value by fostering a merger or acquisition process within the US WiFi market. Our extensive experience and specific domain expertise enables us to assist our clients in a rapid and structured manner.

About Gerbsman Partners

As a result of Gerbsman Partners' 23 years of maximizing enterprise value and specific domain expertise in technology related intellectual property, we have developed an established, proven and responsive distribution channel for our clients. Our channel reaches International and US institutional investors, venture capital funds, investment bankers, lawyers and accountants, as well as leveraging Gerbsman Partners' direct relationships with major wireless and technology companies.

Gerbsman Partners, supported by its International Board of Intellectual Capital, has been involved in over \$1 billion of transactions worldwide and has assisted in M&A, restructuring, licensing, partnership and capital formation for numerous companies and their Intellectual Property.

Our international business and technical team, which includes European and Israeli based sales and technical personnel, looks forward to earning the right to be a resource for you.

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- Premium SMS: www.gerbsmanpartners.com/premiumsmswp.pdf
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For additional information, please call or email:

Steven R. Gerbsman
+1 415 456 0628
steve@gerbsmanpartners.com

Patric Carlsson
+1 415 244 5018
patric@gerbsmanpartners.com

Gunnar Ostergren
+1 415 205 5700
gunnar@gerbsmanpartners.com

Jason Gerbsman
+1 646 326 9716
jason@gerbsmanpartners.com

Motti Abramovitz
+972 54 774 762
motti@gerbsmanpartners.com