

# PREPAID 2.0

Savings with no contracts are prompting subscribers to switch

By **Martin** Vilaboy

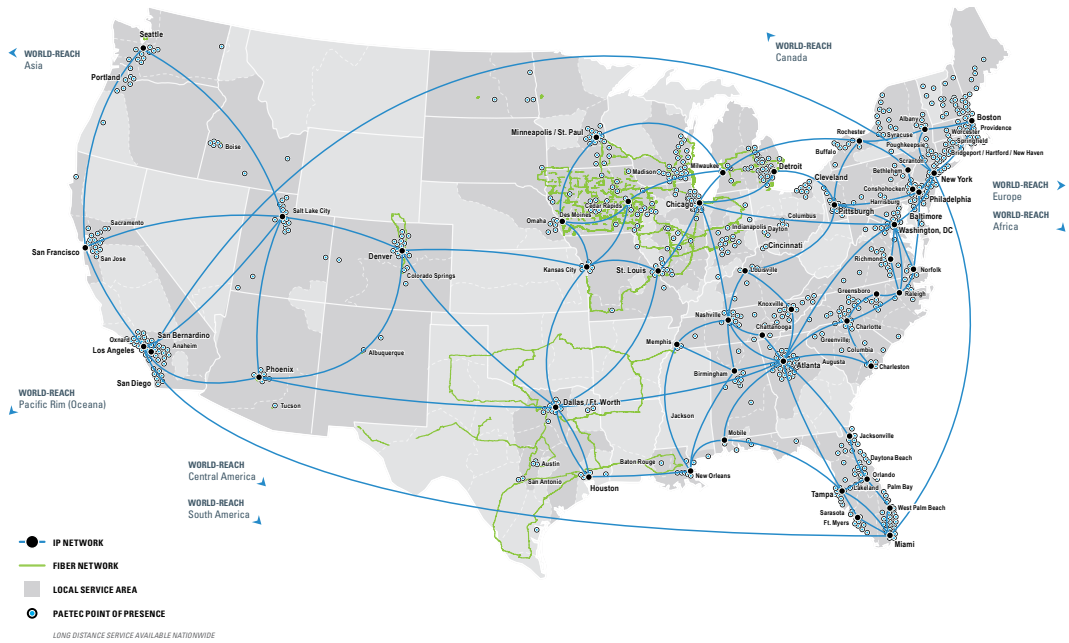


“Nobody likes prepaid,” quips Jeff Flynn, Boost Mobile senior manager. People, he explains, simply don’t like paying for services in advance. On the other hand, “people really don’t like contracts,” says Flynn, but commitments are signed, though often reluctantly, to achieve a savings.

And so it has gone for most of the history of wireless services, until now. The prepaid market has undergone a type of “re-birth,” says Pete Pattullo, CEO of NetworkIP, spurred by improvements in the offerings from prepaid providers as well as a fundamental change in the way consumers consume. And it’s possible that some of the mentality causing the move to prepaid platforms

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by different groups of consumers could encroach into the small business and “prosumer” spaces.

“Ten months ago it wasn’t cool to be frugal,” says Dennis Andrews, president and CEO of Emida. “And 12 months ago, prepaid wasn’t frugal.”

Charged by the onslaught of new “unlimited” voice and data plans for as low as \$40 a month – more and more often without hidden charges and roaming fees, as well as better coverage areas – the impact of prepaid’s new connection to “value” is being felt industry wide and can no longer be ignored by any distributor of wireless services.

“Making it frugal was the secret sauce,” says Andrews.

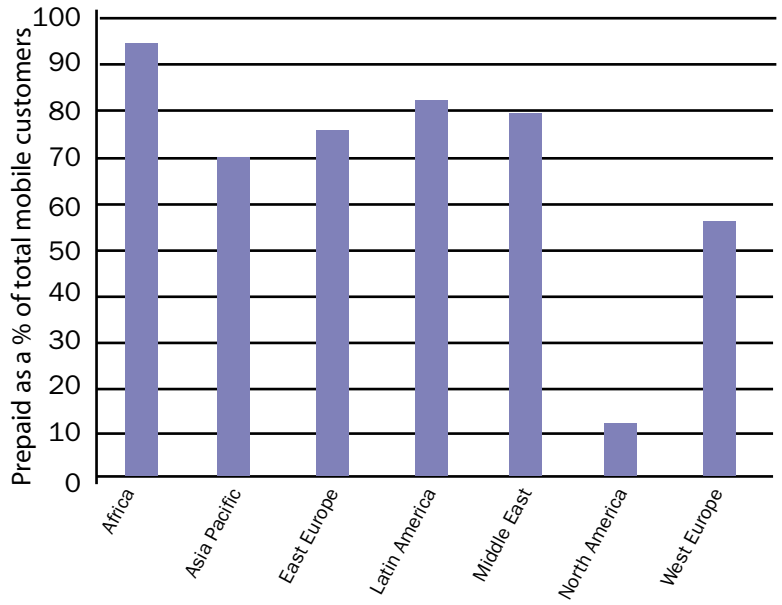
Certainly, prepaid still suffers from a stigma, at least in the U.S. Too often, it’s associated with high per-minute fees, cheap phones and the credit-challenged or “unbanked” customer. Basically, prepaid was about low-ARPU customers the major wireless providers didn’t want or couldn’t get to.

That’s not exactly a sentiment, mind you, shared by the rest of world. In most regions outside of North America, prepaid customers make up the vast majority of wireless subscribers, as much as 71 percent of all mobile subscriptions worldwide in 2008, according to Informa Telecoms & Media, which expects prepaid to account for 74 percent of global mobile subscribers by 2013.

In countries including Russia, Mexico, Italy and India, as well as most of Africa, prepaid penetration is near or above 90 percent, say Merrill Lynch figures. Penetration rates are above 80 percent in Latin America and the Middle East, while prepaid accounts for 70 percent of subscribers across the Asia-Pacific region, says Informa Telecoms & Media.

By comparison, prepaid mobile penetration in North America hovers in the teens, possibly approaching 20 percent or so in the U.S., but even in the U.S., prepaid is enjoying a new identity among some customers. Formerly known as a method for payment among the “credit

### Global Mobile Prepaid Penetration by Region, March 2008



Source: Informa Telecoms & Media

challenged,” it’s now being positioned as a “convenient and cost effective way to buy,” says Dennis Henderson, CEO of ReadyWireless, and that message is resonating.

For evidence of such, one simply needs to look at the record numbers of new prepaid accounts seen throughout most of this year, and it’s not just how much but also who is signing up.

According to Nielsen figures, for example, as much as 72 percent of all wireless subscriber additions in the first quarter of this year were prepaid accounts. That follows the previous quarter when more than half of U.S. subscriber additions were prepaid.

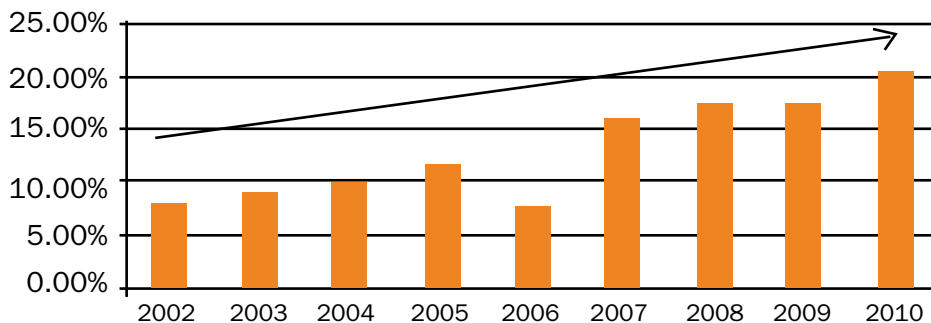
At T-Mobile specifically, prepaid constituted 61 percent of total net adds in the first quarter, up from 57 percent of net additions in the fourth quarter of 2008 and 25 percent in the first quarter of last year.

MetroPCS, meanwhile, picked up 1.4 million net additions in 2008, a record number for the prepaid wireless services provider during the peak of difficult economic times.

According to MetroPCS executives, by the way, more than 90 percent of its customers use PCS as their primary phones.

Indeed, we saw a type of inflection point in the first quarter of 2009, when for the first time the number of prepaid additions overtook the number of postpaid additions among the top four U.S. wireless providers. Whereas postpaid net additions at the

### Prepaid Percentage of U.S. Wireless Subscribers



Source: Merrill Lynch



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big four topped three-quarters of a million, more than 1 million prepaid subscriptions were added in the quarter, according to Morgan Stanley figures.

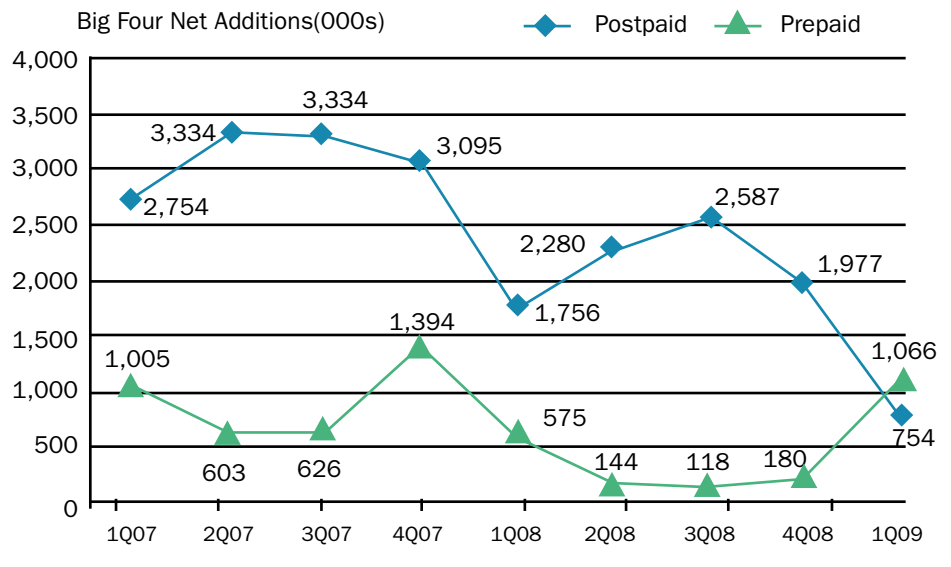
Along with the rise of affordable unlimited plans that have injected prepaid with a value and savings proposition, most contestants agree a big driver of demand has been the uncertainty over financial stability and especially employment, which has made avoiding contracts a lot more important to a lot more types of people. A tightening credit market only exacerbated the fears of locking into two-year deal.

There's also been a realization among lighter-use wireless subscribers that the buckets of minutes provided by the national operators carry a bit more than needed. More frequent use of text messaging also makes voice minutes less necessary for all types of end users, says Thomas Solomon, Incomm vice president.

Among those new subscribers, as much as 17 percent switched from contract plans in order to save money, say researchers at New Millennium Research Council. A recent J.D. Power and Associates survey of new and existing prepaid subscribers, meanwhile, found that 16 percent of all non-contracted subscribers had switched carriers in the past 12 month, and among those 51 percent previously had contract service. A full two-thirds of subscribers to the new breed of "prepaid monthly plans," which straddle the bridge between pre- and postpaid, have cut ties with a contracted services carrier, say the findings from J.D. Power and Associates. And prepaid monthly plans now account for more than 40 percent of all non-contract plans, compared with less than 30 percent in 2008.

Moving forward, the big question is what these types of users might do once the economy and job market fully stabilize and there is less need to cut cost and avoid credit.

### Prepaid Overtakes Postpaid Additions



Source: Morgan Stanley

Wireless analysts Chetan Sharma believes "it is quite likely that 50 percent to 60 percent of such consumers don't go back to postpaid."

"Service is becoming more like postpaid but without a contract," says Flynn.

Indeed, with prepaid providers increasingly offering wider selections of devices and payment plans, while incorporating lower prices and fewer restrictions, the possibility must be considered that more and more folks will find they can get along quite well with a prepaid account.

Whatever happens post-recovery, the recent growth in prepaid subscriptions has served to push the market toward the mainstream, argues Henderson. "Prepaid demographics are beginning to mirror postpaid."

Behavior is changing as well. Recent additions seen at Incomm, for example, are more likely to use data services, says Henderson.

J.D. Power and Associates present similar findings, at least among the emerging user group of the new monthly non-contract users. "The monthly prepaid plan user more closely resembles the contract plan user—desiring a large network, mid-range feature phones and messaging, but without the commitment or penalties of a contract," says the firm.

And it's not just consumers that appreciate the ability to save money without getting locked down. According to Jeff Auman, vice president of sales and distribution for Boost Mobile, 10-line or fewer small businesses also are responding to the company's new \$50 flat-rate unlimited voice and data plan.

### Prepaid Customer Satisfaction Factors

(in order of importance)

Performance and reliability	28%
Cost of service	19%
Account management	17%
Initial activation	15%
Offerings and promotions	12%
Customer service	9%

Source: J.D. Power and Associates

Such a customer could have seasonal or temporary staffing needs or, like many home owners, feel insecure about its immediate financial future.

It's also not hard to imagine small business owners gravitating to the new group of family plans that bundle a set of contracted mobile lines with a few prepaid handsets in the mix.

Elsewhere, mobile data card sales have stalled of late, as business owners question the expense of what's essentially a secondary access to the primary landline Internet connection in the office. An affordable pay-as-you-go data card service could alleviate some of the concern, while providing a more consistent option to random Wi-Fi hotspots and hotel per-day access charges.

Of course, reaching any real business penetration will require greater availability of smartphones and QWERTY keypads, but things already are moving quickly in this direction. We'd even bet that we'll soon see some of the smartest devices, or at least ones with comparable capabilities, among the selections of leading prepaid mobile providers.

That still leaves the issue of subsidies, and whether or not prepaid customers will be willing to go big upfront on expensive devices in order to gain flexibility and eventual savings. Here we must assume providers find ways to maintain the core values of convenience and affordability that got prepaid to the place it is today.

Even so, subsidies certainly work to sell devices, and mobile device sales certainly have become a larger part of wireless providers' business models. In the bigger picture, however, mobile devices increasingly are about more than just "communication services," suggesting a growing separation between the device, the voice provider it's brought from and the network on which it's bought to run.

One only need look to the app store phenomena to grasp the expanding possibilities of what people can do with a connected and capable device in the palm of their hands – one that's also, by the way, a camera, an organizer, a clock, a

navigational tool, a personal recorder and an mp3 player. As more and more activities grow prevalent, it stands to reason there will be less of a natural connection to any one service or product provider.

Prepaid, after all, is not a "service." It's a payment method, and as the services and plans wrapped around that payment method increasingly mirror those of postpaid platforms, it's likely a non-contracted option of paying, that also saves a few bucks, will appeal to an increasing number of both consumers and small businesses. □



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