## Handheld MSS: a rapidly growing market?

Many commentators have claimed that the handheld MSS market is growing rapidly. Indeed when announcing Inmarsat's collaboration with ACeS in September 2006, Andy Sukawaty, Inmarsat's CEO, asserted that "it's a market that's growing 30% a year" and valued handheld MSS voice as an estimated "\$650 million annual business". On its subsequent results calls Inmarsat was more cautious, giving an estimate of \$75M to \$90M per quarter in wholesale revenues for its handheld competitors. By our estimate handheld MSS services (both voice and data) generated roughly \$300M in total (wholesale) service revenues for Thuraya, Iridium and Globalstar during 2006 (\$100M, \$120M and \$80M respectively), a decline of almost 30% from revenues of \$420M in 2005 (\$240M, \$110M and \$70M from Thuraya, Iridium and Globalstar respectively). In fact during 2006 total MSS operator revenues for Inmarsat, Iridium, Globalstar and Thuraya fell for the first time on record, from \$1.14B in 2005 to \$1.01B in 2006, a decline of more than 11%.

Thuraya admitted that its performance in 2006 was not "as strong as expected"<sup>3</sup>, due at least in part both to delays in handset deliveries and interference experienced in the first half of 2006 (from a source in Libya). However, the scale of its difficulties and implications for growth in the handheld MSS market have not to our knowledge been widely publicized. Thuraya's revenues fell from \$322M in 2005 to a reported \$158M in 2006, a decline of 51% (although the magnitude of this decline is somewhat distorted by a \$122M bulk sale of prepaid cards to a major distributor which was recognized during 2005). Thuraya's revenue decline has continued into the first quarter of 2007, with revenues of \$33M compared to \$41M in the first quarter of 2006 (and \$56M in 2006Q4, when the first batch of 60,000 SO-2510 phones were sold). Subscriber numbers also fell to 230,000 compared to 246,000 at the end of March 2006<sup>4</sup>. While equipment sales have lagged as a result of delays in availability of Thuraya's new SG-2520 phone, service revenues have also continued to decline. Growth in the second half of 2007 is expected to improve as a result of new equipment sales, although the Thuraya's stotal revenues for the year are unlikely to exceed \$200M.



<sup>1</sup> See <a href="http://www.telecomseurope.net/article.php?id">http://www.telecomseurope.net/article.php?id</a> cat3=24&id article=2977

<sup>&</sup>lt;sup>2</sup> Inmarsat 2006Q3 results call, November 2006

<sup>&</sup>lt;sup>3</sup> See Yousef Al Sayed interview in Satellite Today, March 12, 2007

<sup>&</sup>lt;sup>4</sup> Information on Thuraya's revenues and subscribers is taken from public filings by a Thuraya investor

At the retail level, handheld MSS service revenues may have held up better in 2006, as the prepaid cards that Thuraya sold to a distributor in 2005 were purchased by end users. However, it seems probable that retail service revenues for handheld MSS were still no better than flat, given the loss of high usage Thuraya users to GSM in countries such as Iraq, and the stabilization of MSS usage (as opposed to equipment purchases) in North America following a spike after the 2005 hurricanes. In 2007, Thuraya's continued declines in revenues in the first quarter make it appear likely that there may also be little improvement in total retail service revenues for handheld MSS for the year as a whole, due to declines in Globalstar handheld service revenues (down about 10% year on year in the first half including independent gateway operators, and likely to show a further decline in the second half) which almost balance out Iridium's revenue gains during the period.

This is far from the rosy picture of handheld MSS that is often conveyed to the public. While handheld MSS subscriber numbers have continued to grow, and will expand in the future, an increasing proportion of formerly high usage customers have found that expanded coverage of GSM in many developing Asian and African countries has reduced the amount of time where they need to rely on MSS. As a result, overall handheld ARPUs have fallen significantly in the last few years.

Nevertheless, more attractive MSS handsets, such as the new Thuraya phones, are likely to make MSS an option for a wider range of occasional remote travelers in the future. Increased deployment of MSS phones for disaster preparedness has also been a significant stimulus to subscriber growth, particularly in North America. However, both types of user will produce relatively low ARPUs (except during occasional emergencies). As a result, in the absence of catastrophic hurricanes or earthquakes (or a major war), we believe that handheld MSS operators will rely increasingly on equipment sales to show continued revenue and profit growth.

In this context, the equipment pricing decisions of Iridium, Globalstar and Thuraya (who all make a margin of at least \$300 to \$500 per phone sold) appear far more logical than that of Inmarsat (who we believe to be selling their new handheld phone at close to its manufacturing cost, and appear to be subsidizing development costs for their next generation phone). Inmarsat is investing substantial sums in development of its handheld service, with a \$36.5M contract for Lockheed (for network upgrades) and a \$26.5M contract for EMS (for next generation handset development) announced in recent months. Inmarsat may be able to grow its handheld customer base by undercutting the handset prices of its competitors, but it is unclear whether the relatively low ARPUs of the handheld



customers it is likely to acquire will justify its investments in this business. On the other hand, if Inmarsat's entry into the handheld business makes it more difficult for Iridium and Globalstar to finance their next generation systems (and thereby reduces competition for Inmarsat's other services), then Inmarsat may consider this money well spent.

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This note is extracted from our September 2007 profile of Thuraya, which forms part of our MSS research service. To find out more visit www.tmfassociates.com/reports

